INTERMEDIATE (IPC) COURSE

PRACTICE MANUAL

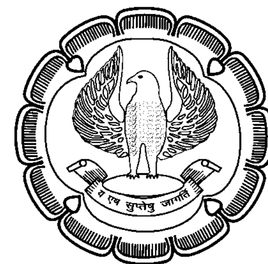
PAPER 4 : TAXATION

Part - I : Income-tax

[As amended by the Finance Act, 2016]

Assessment Year 2017-18

[Relevant for May, 2017 & November, 2017 Examinations]



BOARD OF STUDIES
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

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This Practice Manual has been prepared by the faculty of the Board of Studies. The objective of the Practice Manual is to provide teaching material to the students to enable them to obtain knowledge and skills in the subject. In case students need any clarifications or have any suggestions to make for further improvement of the material contained herein, they may write to the Director of Studies.

All care has been taken to provide interpretations and discussions in a manner useful for the students. However, the Practice Manual has not been specifically discussed by the Council of the Institute or any of its Committees and the views expressed herein may not be taken to necessarily represent the views of the Council or any of its Committees.

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A WORD ABOUT PRACTICE MANUAL

The Board of Studies has been instrumental in imparting theoretical education for the students of Chartered Accountancy Course. The distinctive characteristic of the course i.e., distance education, has emphasized the need for bridging the gap between the students and the Institute and for this purpose, the Board of Studies has been providing a variety of educational inputs for the students. Bringing out a series of subject-wise Practice Manuals is one of the quality services provided by the Institute. These Practice Manuals are highly useful to the students preparing for the examinations, since they are able to get answers for all important questions relating to a subject at one place and that too, grouped chapter-wise.

Income-tax constitutes Part I of Intermediate (IPC) Paper 4: Taxation. Practice Manual of Part I: Income-tax, is divided into ten chapters in line with the Study Material on Income-tax. This will help the students to correlate the Practice Manual with the Study Material and facilitate in complete revision of each chapter. This Practice Manual has been prepared on the basis of the provisions of law as amended by the Finance Act, 2016, and applicable for A.Y.2017-18.

In this edition of the Practice Manual, all the questions have been adapted and answered on the basis of the provisions of income-tax law as amended by the Finance Act, 2016, which are relevant for the A.Y.2017-18, being the assessment year applicable for students appearing in May, 2017 and November, 2017 examinations.

This Practice Manual contains a wide range of questions on income-tax and includes questions set at the past examinations at PE-II, PCC & IPCC levels as well as other important questions. Solving questions in the Practice Manual would, therefore, facilitate in thorough understanding of the manner of application of the provisions discussed in the Study Material. In this edition of the Practice Manual, “Key Points” have been included at the beginning of each chapter, which would aid the students in answering the questions and solving the problems contained in that chapter. It would also facilitate quick revision of the chapter.

The Practice Manual also contains a matrix showing the topic-wise distribution of examination questions to make the students aware of the weightage given to the various chapters in the examination. The Practice Manual will serve as a useful and handy reference guide while preparing for Intermediate (IPC) Examination. It will guide the students to improve their performance in the examinations and also help them to work upon their grey areas and plan a strategy to tackle problems in income-tax. For further clarification/guidance, students may send their queries at priya@icai.in or aparna.chauhan@icai.in.

Happy Reading and Best Wishes!

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Paper – 4: Taxation

Statement showing topic-wise distribution of Examination Questions along with Marks

Chapter			Term of Examination																				Total Marks	Avg. Marks
			Nov. 2011		May 2012		Nov 2012		May 2013		Nov 2013		May 2014		Nov 2014		May 2015		Nov 2015		May 2016			
			Q	M	Q	M	Q	M	Q	M	Q	M	Q	M	Q	M	Q	M	Q	M	Q	M		
PART-I : INCOME TAX																								
1	Basic Concepts										7(a)	**4**									2(a)(i)	**4**	**8**	**.8**
2	Residence and Scope of Total Income		6(a)(i)	**4**					2(a)	**8**					2(a)	**8**	2(a)	**8**	2(a)	**8**	2(a)(ii)	**4**	**40**	**4.0**
3	Incomes which do not form Part of Total Income										4(b)(ii) 5(a) 7(b)	**2** **4** **8**			3(a)(ii)	**4**	3(a)	**8**			3(a)(i) 3(a)(ii) 7(iii)(A)	**4** **4** **2**	**36**	**3.6**
4	Heads of Income						6(a)	**8**	7(a)(iii)	**4**													**12**	**1.2**
	Unit-1	Income from Salaries	2(a)	**8**	7(a)	**8**			3(a)	**8**	3(a)	**8**	3(A)	**8**	4(a)	**8**	4(a)	**8**					**56**	**5.6**
	Unit-2	Income from House Property			2(a)(iii)	**4**					2(a)	**8**	4(A)	**8**					6(a)	**8**			**28**	**2.8**
	Unit-3	Profits and Gains of Business or Profession	1(a) 4(a) 7(a)(i)	**5** **8** **4**	6(a)	**8**	4(a)	**8**	7(a)(ii)	**4**	5(b)	**4**	2(A)	**8**	3(a)(i) 5(a)	**4** **8**			5(a)	**8**	5(a)	**8**	**77**	**7.7**

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	Unit-4	Capital Gains	3(a)	**8**	3(a)	**8**	3(a) 7(a)(iii)	**8** **4**	6(a)	**8**	4(a)	**4**	5(A)	**8**			5(a)	**8**	3(a)	**8**			**64**	**6.4**
	Unit-5	Income from Other Sources	6(a)(ii)	**4**							4(b)(i)	**2**									4(a) 7(iii)(B)	**8** **2**	**16**	**1.6**
5	Income of other Persons included in Assessee's Total Income		1(a)	**5**	2(a)(ii) 5(a)	**4** **8**	2(a)	**8**	5(a)	**8**					6(a) (ii)	**4**	6(a) (ii)	**4**					**41**	**4.1**
6	Set-off and Carry Forward of Losses		4(a)	**8**			5(a)	**8**	4(a)	**8**	6(a)	**8**	6(A)	**4**							6(a)	**8**	**44**	**4.4**
7	Deductions from Gross Total Income		5(a)	**8**									6(B)	**4**	6(a) (i)	**4**	6(a) (i)	**4**					**20**	**2**
8	Computation of Total Income and Tax Payable		1(b)	**5**	1(a) 4(a)	**10** **8**	1(a)	**10**	1(a)	**10**	1(a)	**10**	1(A)	**10**	1(a)	**10**	1(a)	**10**	1(a) 4(a)	**10** **8**	1(a)	**10**	**111**	**11.1**
9	Provisions concerning Advance Tax and TDS		7(a)(ii)	**4**			7(a)(i)	**4**	7(a)(i)	**4**			7(A) (1)/ (3)	**4** **2**	7(a (i)	**4**	7(a) (ii) &(iii)	**8**	7(a)(i) 7(a)(ii)	**4** **4**	7(a)(i) 7(a)(ii)	**4** **4**	**46**	**4.6**
10	Provisions for filing of Return of Income		7(a)(iii)	**4**	2(a)(i)	**4**	7(a)(ii)	**4**					7(A) (2)	**4**	7(a) (ii)& (iii)	**8**	7(a) (i)	**4**	7(a)(iii)	**4**			**32**	**3.2**

Note: 'Q' represents question numbers as they appeared in the question paper of respective examination. 'M' represents the marks which each question carries.

The question papers of all the past attempts of IPCE/Intermediate (IPC) Examinations can be accessed from the BOS Knowledge Portal on the Institute's website www.icai.org

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Annexure : Text of Income Computation and Disclosure Standards (ICDSs) notified on 29.9.2016 to be applicable from A.Y.2017-18 and the significant changes in the ICDSs notified on 29.9.2016 *vis-a-vis* ICDSs notified earlier on 31.3.2015 (since rescinded).

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1 Basic Concepts

Introduction

Components of income-tax law

The income-tax law, which governs the levy of income-tax in India, has the following components –

(1) Income-tax Act, 1961

- The main source of income-tax law is the Income-tax Act, 1961.
- The Act is divided into sections; the sections are grouped under Chapters. The Act also contains Schedules.
- Many of the sections are further divided into sub-sections, clauses and sub-clauses, which are denoted within brackets.

  For example, if we have to refer to section 80D, sub-section (2) clause (b), the same should be written as section 80D(2)(b).

(2) Income-tax Rules, 1962

- Rules are necessary for carrying out the purposes of the Act.
- The Act gives power to the authority responsible for implementation of the Act to make appropriate rules.
- The Central Board of Direct Taxes (CBDT) governs the administration of Income-tax Act, 1961 in India, for which purpose it frames rules from time to time.
- These rules together form the Income-tax Rules, 1962.

(3) **Annual Finance Act**

- The Finance Bill is introduced in the Parliament every year for implementing the tax proposals in the Union Budget.
- When the Finance Bill is approved by the Parliament and gets the assent of the President, it becomes the Finance Act.
- The amendments are made every year to the Income-tax Act, 1961 and other tax laws by the Finance Act.
- The First Schedule to the Finance Act contains four parts which specify the rates of tax –

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- Part I of the First Schedule to the Finance Act specifies the rates of tax applicable for the current Assessment Year.
- Part II specifies the rates at which tax is deductible at source for the current Financial Year.
- Part III gives the rates for calculating income-tax for deducting tax from income chargeable under the head "Salaries" and computation of advance tax.
- Part IV gives the rules for computing net agricultural income.

(4) Circulars/Notifications

- Circulars are issued by the CBDT to clarify the meaning and scope of certain provisions contained in the Act.
- Notifications are issued by the Central Government to give effect to the provisions of the Act.

  For example, under section 10(15)(iv)(h), interest payable by any public sector company in respect of such bonds or debentures and subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in this behalf would be exempt. Therefore, the bonds and debentures, interest on which would qualify for exemption under this section are specified by the Central Government through Notifications.

(5) Case law decisions

- The various issues which arise out of the provisions of the Act are decided by judicial forums.
- The decisions of the Courts interpreting the provisions of the law also form an important constituent of income-tax law.

***Note** – Case laws, are however, dealt with only at the Final level and not at the Intermediate (IPC) level.*

<u>Fundamental concepts of income-tax law</u>

<u>Income</u>

The concept of "income" under the Income-tax Act, 1961, is not the same as what is generally understood as "income" in common parlance.

An exhaustive definition is one which confines the scope to what is contained in the definition, whereas an inclusive definition does not limit the scope to what is mentioned in the definition.

The definition of "income" as per section 2(24) of the Income-tax Act, 1961, begins as "income includes ……". The definition of "income" is, therefore, inclusive and not exhaustive. This implies that the scope of income is not confined only to the income which are mentioned in section 2(24).

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	In Common Parlance	Under the Income-tax Act, 1961
(1)	Income is understood as a regular monetary return from specified sources.	Income also includes casual income like winnings from lotteries, crossword puzzles etc.
(2)	Normally, only revenue receipts are considered as income.	Capital gains on transfer of assets are specifically included in the definition of income.
(3)	Income means the actual income i.e., gross receipts less expenditure incurred.	Income is also calculated applying a presumptive rate on gross receipts, in certain cases, for example, an individual carrying on civil construction business with gross receipts of, say, ₹ 80 lakh, can calculate his income by applying the presumptive rate of 8% on ₹ 80 lakh, even though his actual income may be higher.
(4)	Income generally refers to real income.	Even notional income is treated as income, if specifically provided under the Act i.e. annual value of a property which is not actually let out but is deemed to be let out is chargeable to income-tax.
(5)	Income connotes the gross receipts after deducting actual expenditure incurred to earn such receipts.	The deductions specifically provided for under the Income-tax Act, 1961 can alone be reduced to compute income. Also, if there are any restrictions on the quantum of deduction allowable under the Act, the deduction would be allowed subject to such limits. For instance, in case of salary income, transport allowance is allowable as deduction only up to ₹ 1,600 per month, even though the employee may have actually incurred more than ₹ 1,600 p.m. and may be getting a higher transport allowance. Sometimes, deduction may be allowed for a higher sum than actually incurred. For example, weighted deduction @200% is allowable in respect of in-house scientific research expenditure incurred by a company.
(6)	Income is generally considered to belong to the person who receives the same.	The Income-tax Act, 1961 has specific provisions including the income of one person in the hands of the other, in certain circumstances, like including income of a minor child in the hands of the parent.

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Previous Year & Assessment Year

Assessment year (A.Y.) means the period of twelve months commencing on the 1st April every year. Assessment year is the financial year following the previous year.

Previous year (P.Y.) is the financial year immediately preceding the assessment year, i.e., it is the financial year ending on 31st March, in which the income has accrued/received. In case of a newly set-up business, the previous year would be the period beginning with the date of setting up of the business or profession or, as the case may be, the date on which the source of income newly came into existence, and ending on 31st March.

Income earned during the previous year is chargeable to tax in the Assessment year. For example, income earned during the P.Y. 2016-17 is chargeable to tax in the A.Y. 2017-18. Therefore, for the A.Y.2017-18, the relevant previous year is P.Y.2016-17.

Person [Section 2(31)]

The levy of income-tax is on every "person". The definition of "person" is, again, inclusive. It includes an individual, a Hindu Undivided Family (HUF, in short), a company, a firm, an association of persons (AOP) or a body of individuals (BOI), whether incorporated or not, a local authority and every artificial juridical person.

Assessee [Section 2(7)]

"Assessee" means a person by whom tax or any other sum of money is payable under the Income-tax Act, 1961. In addition, it includes –

- Every person in respect of whom any proceeding under the Act has been taken for the assessment of –
  - his income; or
  - the income of any other person in respect of which he is assessable; or
  - the loss sustained by him or by such other person; or
  - the amount of refund due to him or to such other person.
- Every person who is deemed to be an assessee under any provision of this Act;
- Every person who is deemed to be an assessee-in-default under any provision of this Act.

Question 1

Write short note on "Income accruing" and "Income due". Can an income which has been taxed on accrual basis be assessed again on receipt basis?

Answer

'Accrue' refers to the right to receive income, whereas 'due' refers to the right to enforce payment of the same. For e.g. salary for work done in December will 'accrue' throughout the month, day to day, but will become 'due' on the salary bill being passed on 31st December or 1st January. Similarly, on Government securities, interest payable on specified dates arise during

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the period of holding, day to day, but will become 'due' for payment on the specified dates.

Income which has been taxed on accrual basis cannot be assessed again on receipt basis, as it will amount to double taxation. For example, when interest on bank deposit is offered on accrual basis, amounts received on maturity of such deposit including interest thereon cannot be treated as income again.

Question 2

An employee instructs his employer to pay a certain portion of his salary to a charity and claims it as exempt as it is diverted by over riding charge / title – Comment.

Answer

In the instant case, it is an application of income and in the nature of foregoing of salary. According to the Supreme Court judgment in *CIT v. L.W. Russel (1964) 52 ITR 91*, the salary which has been foregone after its accrual in the hands of the employee is taxable. Hence, the amount paid by the employer to a charity as per the employee's directions is taxable in the hands of the employee.

Question 3

Describe average rate of tax and maximum marginal rate under section 2(10) and 2(29C) of the Income-tax Act, 1961.

Answer

As per section 2(10), **"Average Rate of tax"** means the rate arrived at by dividing the amount of income-tax calculated on the total income, by such total income.

Section 2(29C) defines **"Maximum marginal rate"** to mean the rate of income-tax (including surcharge on the income-tax, if any) applicable in relation to the highest slab of income in the case of an individual, AOP or BOI, as the case may be, as specified in Finance Act of the relevant year.

Question 4

Who is an "Assessee"? Who is a "Deemed Assessee"? Who is an "Assessee in Default"? Explain with suitable examples.

Answer

Assessee

As per section 2(7), assessee means a person by whom tax or any other sum of money is payable under the Income-tax Act, 1961.

In addition, the term includes –

- Every person in respect of whom any proceeding under the Act has been taken for the assessment of –
  - his income; or

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- the income of any other person in respect of which he is assessable; or
- the loss sustained by him or by such other person; or
- the amount of refund due to him or to such other person.

- Every person who is deemed to be an assessee under any provision of this Act;
- Every person who is deemed to be an assessee in default under any provision of this Act.

Deemed Assessee

Assessee includes every person who is deemed to be an assessee under the provisions of the Act. For example, section 160(1) defines “Representative assessee”. Section 160(2) states that, every representative assessee shall be deemed to be an assessee for the purposes of the Act.

Assessee in default

A person is said to be an assessee in default if he fails to comply with the duties imposed upon him under the Income-tax Act, 1961. Suppose an employer who pays salary or other person who pays interest, commission, professional fees etc. but does not deduct tax at source and deposit into government treasury, then, he shall be deemed to be an assessee in default. Likewise, under section 218, if a person does not pay advance tax, then, he shall be deemed to be an assessee-in-default.

Question 5

State any four instances where the income of the previous year is assessable in the previous year itself instead of the assessment year.

Answer

The income of an assessee for a previous year is charged to income-tax in the assessment year following the previous year. However, in a few cases, the income is taxed in the previous year in which it is earned. These exceptions have been made to protect the interests of revenue. The exceptions are as follows:

(i) Where a ship, belonging to or chartered by a non-resident, carries passengers, livestock, mail or goods shipped at a port in India, the ship is allowed to leave the port only when the tax has been paid or satisfactory arrangement has been made for payment thereof. 7.5% of the freight paid or payable to the owner or the charterer or to any person on his behalf, whether in India or outside India on account of such carriage is deemed to be his income which is charged to tax in the same year in which it is earned.

(ii) Where it appears to the Assessing Officer that any individual may leave India during the current assessment year or shortly after its expiry and he has no present intention of returning to India, the total income of such individual for the period from the expiry of the respective previous year up to the probable date of his departure from India is chargeable to tax in that assessment year.

(iii) If an AOP/BOI etc. is formed or established for a particular event or purpose and the

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Assessing Officer apprehends that the AOP/BOI is likely to be dissolved in the same year or in the next year, he can make assessment of the income up to the date of dissolution as income of the relevant assessment year.

(iv) During the current assessment year, if it appears to the Assessing Officer that a person is likely to charge, sell, transfer, dispose of or otherwise part with any of his assets to avoid payment of any liability under this Act, the total income of such person for the period from the expiry of the previous year to the date, when the Assessing Officer commences proceedings under this section is chargeable to tax in that assessment year.

(v) Where any business or profession is discontinued in any assessment year, the income of the period from the expiry of the previous year up to the date of such discontinuance may, at the discretion of the Assessing Officer, be charged to tax in that assessment year.

Exercise

1. *The basic source of income-tax law is -*

   (a). Income-tax Act, 1961

   (b). Circulars/Notifications issued by CBDT

   (c). Judgments of Courts

2. *A domestic company means -*

   (a). Only an Indian company

   (b). Only a foreign company which has made the prescribed arrangements for declaration and payment of dividends in India

   (c). Indian company and a foreign company which has made the prescribed arrangements for declaration and payment of dividends in India

3. *The rates of income tax are mentioned in -*

   (a). Income-tax Act, 1961

   (b). The Annual Finance Acts

   (c). Both in the Income-tax Act, 1961 and the Annual Finance Acts.

4. *The surcharge applicable in the case of an individual is -*

   (a). 10% of tax payable if total income exceeds ₹ 1 crore

   (b). 12% of tax payable if total income exceeds ₹ 1 crore

   (c). 15% of tax payable if total income exceeds ₹ 1 crore

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5. *In respect of a resident assessee, who is of the age of 60 years or more but less than 80 years at any time during the previous year 2016-17, -*

   (a). Higher basic exemption of ₹ 2,50,000 is available

   (b). Higher basic exemption of ₹ 3,00,000 is available

   (c). Higher basic exemption of ₹ 5,00,000 is available.

6. *The rate of tax applicable to a domestic company for A.Y. 2017-18, where turnover/gross receipts does not exceed ₹ 5 crore during the P.Y. 2014-15, is -*

   (a). 29%

   (b). 25%

   (c). 30%

7. *The surcharge applicable to a domestic company for A.Y. 2017-18 is -*

   (a). 5%, if total income exceeds ₹ 1 crore.

   (b). 7%, if the total income exceeds ₹ 1 crore but does not exceed ₹ 10 crore, and 15%, if the total income exceeds ₹ 10 crore.

   (c). 7%, if the total income exceeds ₹ 1 crore but does not exceed ₹ 10 crore, and 12%, if the total income exceeds ₹ 10 crore.

8. *The surcharge applicable to a foreign company for A.Y. 2017-18 is -*

   (a). 5%, if the total income exceeds ₹ 1 crore.

   (b). 2%, if the total income exceeds ₹ 1 crore but does not exceed ₹ 10 crore and 5% if the total income exceeds ₹ 10 crore.

   (c). 2%, if the total income exceeds ₹ 10 crore.

9. *The rate of tax applicable to a firm for A.Y. 2017-18 is -*

   (a). 30%

   (b). 35%

   (c) 40%

10. *Where the total income of an artificial juridical person is ₹ 3,10,000, the income-tax payable is ₹ …………… and surcharge payable is ₹ …………..*

    (a) ₹ 6,000; surcharge – nil.

    (b) ₹ 11,000; surcharge – ₹ 1100.

    (c) ₹ 93,000; surcharge – ₹ 4650.

11. *Define the following terms under the Income-tax Act, 1961 -*

    (i) Assessee

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(ii) Person

(iii) Previous year

12. *Write short notes on the following -*

    (i) Year of accrual of dividend

    (ii) Marginal relief

13. *"Income of a previous year will be charged to tax in the assessment year following the previous year"- Discuss the exceptions to this general rule.*

14. *Explain the concept of "Marginal Relief" under the Income-tax Act, 1961.*

Answers

1. a; **2**. c; **3.** c; **4.** c; **5.** b; **6.** a; **7.** c; **8.** b; **9.** a., **10.** a.

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2 RESIDENCE AND SCOPE OF TOTAL INCOME

<table>
<tr><th colspan="4">Key Points</th></tr>
<tr><td colspan="4"><u>Section 6 [Residence in India]</u></td></tr>
<tr><td rowspan="3">(i)</td><td colspan="3"><u>Individuals [Resident and ordinarily resident / Resident but not ordinarily resident / non-resident].</u> The residential status of an individual is determined on the basis of the period of his stay in India.
Basic conditions:
(i) Must be present in India for a period of 182 days or more during the previous year
(ii) Must be present in India for a period of 60 days or more during the previous year and 365 days or more during the 4 years immediately preceding the previous year.
However, the second condition is not applicable in the following cases:
(1) An Indian citizen who leaves India during the previous year for the purpose of employment outside India or as a member of the crew of an Indian ship;
(2) An Indian citizen or a person of Indian origin who, being outside India, comes on a visit to India during the previous year.
Additional conditions:
(i) He is a resident in at least 2 out of 10 previous years preceding the relevant previous year;
(ii) His stay in India in the last 7 years preceding the relevant previous year is 730 days or more.</td></tr>
<tr><th>Resident and ordinarily resident</th><th>Resident but not ordinarily resident</th><th>Non-resident</th></tr>
<tr><td>Must satisfy at least one of the basic conditions and both the additional conditions.</td><td>Must satisfy at least one of the basic conditions and one or none of the additional conditions.</td><td>Must not satisfy either of the basic conditions.</td></tr>
<tr><td>(ii)</td><td colspan="3"><u>HUFs [Resident and ordinarily resident / Resident but not ordinarily resident / non-resident]</u>
(i) A HUF would be resident in India if the control and management of its affairs is situated wholly or partly in India.</td></tr>
</table>

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	(ii) If the **control and management** of the affairs is situated **wholly outside India**, it would become a **non-resident**. (iii) If the HUF is resident, then the **status of the Karta** would determine whether the HUF is **resident and ordinarily resident** or **resident but not ordinarily resident** If the karta is resident and ordinarily resident, then the HUF would be a resident and ordinarily resident and if the karta is resident but not ordinarily resident, then the HUF would be a resident but not ordinarily resident.
(iii)	**Firms & AOPs [Resident / Non-resident]** (i) A firm or AOP would be **resident in India** if the **control and management** of its affairs is situated **wholly or partly in India**. (ii) If the **control and management** of the affairs is situated **wholly outside India,** it would become a **non-resident**.
(iv)	**Companies [Resident / Non-resident]** (i) A company would be **resident in India** in any previous year if it is an Indian Company or its place of effective management (POEM) in that year is in India. (ii) If the company is not an Indian Company and its POEM is also not in India in that year, it would become a non-resident for that year.

Section 5 [Scope of Total Income]

Resident And Ordinarily Resident	Resident But Not Ordinarily Resident	Non-Resident
Income received/ deemed to be received/ accrued or arisen/ deemed to accrue or arise in or outside India In short, the global income is taxable.	Income which is received/ deemed to be received/ accrued or arisen/ deemed to accrue or arise in India; **AND** Income which accrues or arises outside India being derived from a business controlled from or profession set up in India.	Income received/ deemed to be received/ accrued or arisen/deemed to accrue or arise in India.

Question 1

Mr. Ramesh & Mr. Suresh are brothers and they earned the following incomes during the financial year 2016-17. Mr. Ramesh settled in Canada in the year 1995 and Mr. Suresh settled in Delhi. Compute the total income for the assessment year 2017-18.

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Sr. No.	*Particulars*	*Mr. Ramesh (₹)*	*Mr. Suresh (₹)*
1.	*Interest on Canada Development Bonds (only 50% of interest received in India)*	*35,000*	*40,000*
2.	*Dividend from British company received in London*	*28,000*	*20,000*
3.	*Profit from a business in Nagpur, but managed directly from London*	*1,00,000*	*1,40,000*
4.	*Short term capital gain on sale of shares of an Indian company received in India*	*60,000*	*90,000*
5.	*Income from a business in Chennai*	*80,000*	*70,000*
6.	*Fees for technical services rendered in India, but received in Canada*	*1,00,000*	*----*
7.	*Interest on savings bank deposit in UCO Bank, Delhi*	*7,000*	*12,000*
8.	*Agricultural income from a land situated in Andhra Pradesh*	*55,000*	*45,000*
9.	*Rent received in respect of house property at Bhopal*	*1,00,000*	*60,000*
10.	*Life insurance premium paid*	*---*	*30,000*

Answer

Computation of total income of Mr. Ramesh & Mr. Suresh for the A.Y. 2017-18

S. No.	Particulars	Mr. Ramesh (Non-Resident) (₹)	Mr. Suresh (Resident) (₹)
1.	Interest on Canada Development Bond **(See Note 2)**	17,500	40,000
2.	Dividend from British Company received in London **(See Note 3)**	-	20,000
3.	Profit from a business in Nagpur but managed directly from London **(See Note 2)**	1,00,000	1,40,000
4.	Short term capital gain on sale of shares of an Indian company received in India **(See Note 2)**	60,000	90,000
5.	Income from a business in Chennai **(See Note 2)**	80,000	70,000
6.	Fees for technical services rendered in India, but received in Canada **(See Note 2)**	1,00,000	-
7.	Interest on savings bank deposit in UCO Bank, Delhi **(See Note 2)**	7,000	12,000

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8.	Agricultural income from a land in Andhra Pradesh **(See Note 4)**	-	-
9.	Income from house property at Bhopal **(See Note 5)**	70,000	42,000
	Gross Total income	**4,34,500**	**4,14,000**
	Less: Deduction under chapter VIA-		
	Section 80C-Life insurance premium paid	-	30,000
	Section 80TTA **(See Note 6)**	7,000	10,000
	Total Income	**4,27,500**	**3,74,000**

Notes:

1. Mr. Ramesh is a non-resident since he has been living in Canada since 1995. Mr. Suresh, who is settled in Delhi, is a resident.

2. In case of a resident, his global income is taxable as per section 5(1). However, as per section 5(2), in case of a non-resident, only the following incomes are chargeable to tax:

(i) Income received or deemed to be received in India; and

(ii) Income accruing or arising or deemed to accrue or arise in India.

Therefore, fees for technical services rendered in India would be taxable in the hands of Mr. Ramesh, even though he is a non-resident.

The income referred to in Sl. No. 3,4,5 and 7 are taxable in the hands of both Mr. Ramesh and Mr. Suresh since they accrue or arise in India.

Interest on Canada Development Bond would be fully taxable in the hands of Mr. Suresh, whereas only 50% which is received in India is taxable in the hands of Mr. Ramesh.

3. Dividend received from British company in London by Mr. Ramesh is not taxable since it accrues and is received outside India. However, dividend received by Mr. Suresh is taxable, since he is a resident. Exemption under section 10(34) would not be available in respect of dividend received from a foreign company.

4. Agricultural income from a land situated in India is exempt under section 10(1) in the case of both non-residents and residents.

5. Income from house property-

	Mr. Ramesh	**Mr. Suresh**
	(₹)	**(₹)**
Rent received	1,00,000	60,000
Less: Deduction under section 24 @ 30%	30,000	18,000
Net income from house property	**70,000**	**42,000**

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The net income from house property in India would be taxable in the hands of both Mr. Ramesh and Mr. Suresh, since the accrual and receipt of the same are in India.

6. In case of an individual, interest upto ₹ 10,000 from savings account with, *inter alia*, a bank is allowable as deduction under section 80TTA.

Question 2

Mrs. Geetha and Mrs. Leena are sisters and they earned the following income during the Financial Year 2016-17. Mrs. Geetha is settled in Malaysia since 1986 and visits India for a month every year. Mrs. Leena is settled in Indore since her marriage in 1994. Compute the total income of Mrs. Geetha and Mrs. Leena for the assessment year 2017-18:

Sl. No.	*Particulars*	*Mrs. Geetha ₹*	*Mrs. Leena ₹*
(i)	*Income from Profession in Malaysia, (set up in India) received there*	*15,000*	-
(ii)	*Profit from business in Delhi, but managed directly from Malaysia*	*40,000*	-
(iii)	*Rent (computed) from property in Malaysia deposited in a Bank at Malaysia, later on remitted to India through approved banking channels.*	*1,20,000*	-
(iv)	*Dividend from PQR Ltd., an Indian Company*	*5,000*	*9,000*
(v)	*Dividend from a Malaysian company received in Malaysia*	*15,000*	*8,000*
(vi)	*Cash gift received form a friend on Mrs. Leena's 50th birthday*	-	*51,000*
(vii)	*Agricultural income from land in Maharashtra*	*7,500*	*4,000*
(viii)	*Past foreign untaxed income brought to India*	*5,000*	-
(ix)	*Fees for technical services rendered in India received in Malaysia*	*25,000*	-
(x)	*Income from a business in Pune (Mrs. Geetha receives 50% of the income in India)*	*12,000*	*15,000*
(xi)	*Interest on debentures in an India company (Mrs. Geetha received the same in Malaysia)*	*18,500*	*14,000*
(xii)	*Short-term capital gain on sale of shares of an Indian company*	*15,000*	*25,500*
(xiii)	*Interest on savings account with SBI*	*12,000*	*8,000*
(xiv)	*Life insurance premium paid to LIC*	-	*30,000*

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Answer

The residential status of Mrs. Geetha and Mrs. Leena has to be determined on the basis of the number of days of their stay in India. Since Mrs. Geetha is settled in Malaysia since 1986, she would be a non-resident for A.Y.2017-18. Her visit to India for a month every year would not change her residential status. However, Mrs. Leena would be resident and ordinarily resident for A.Y.2017-18, since she is settled in India permanently since 1994.

Based on their residential status, the total income of Mrs. Geetha and Mrs. Leena would be determined as follows:

Computation of total income of Mrs. Geetha & Mrs. Leena for the A.Y. 2017-18

S. No.	Particulars	Mrs. Geetha (Non-Resident) (₹)	Mrs. Leena (Resident) (₹)
1.	Income from profession in Malaysia (set up in India) received there (***Note 1)***	-	-
2.	Profit from business in Delhi, but managed directly from Malaysia (***Note 1)***	40,000	-
3.	Rent (computed) from property in Malaysia deposited in a Bank at Malaysia, later on remitted to India through approved banking channels (***Note 1)***	-	-
4.	Dividend from PQR Ltd. an Indian Company ***[Exempt under section 10(34)]***	-	-
5.	Dividend from Malaysian Company received in Malaysia (***Note 1)***	-	8,000
6.	Cash gift received from a friend on Mrs. Leena's 50th birthday ***Note:*** *As per section 56(2)(vii), cash gifts received from a non-relative would be taxable, if the amount exceeds ₹ 50,000 in aggregate during the previous year.*	-	51,000
7.	Agricultural income from land in Maharashtra ***[Exempt under section 10(1), both in the hands of non-resident and resident].***	-	-
8.	Past foreign untaxed income brought to India ***[Not taxable, since it does not represent income of the P.Y.2016-17].***	-	-
9.	Fees for technical services rendered in India, but received in Malaysia ***(Note 1)***	25,000	-

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10.	Income from a business in Pune (Mrs. Geetha receives 50% of the income in India) ***(Note 2)***	12,000	15,000
11.	Interest on debentures in an Indian company (Mrs. Geetha received the same in Malaysia) ***(Note 2)***	18,500	14,000
12.	Short-term capital gain on sale of shares of an Indian company ***(Note 2)***	15,000	25,500
13.	Interest on savings account with SBI ***(Note 2)***	12,000	8,000
Gross Total income		**1,22,500**	**1,21,500**
Less: Deductions under Chapter VIA			
	- Section 80C [Life insurance premium paid] [Assuming that premium paid is within the specified percentage (10% /20%, as the case may be) of capital sum assured]	-	30,000
	- Section 80TTA (In case of an individual, interest upto ₹ 10,000 from savings account with, inter alia, a bank is allowable as deduction under section 80TTA)	10,000	8,000
	Total Income	**1,12,500**	**83,500**

Notes:

(1) As per section 5(1), global income is taxable, in case of a resident. However, as per section 5(2), only the following incomes are chargeable to tax, in case of a non-resident:

(i) Income received or deemed to be received in India; and

(ii) Income accruing or arising or deemed to accrue or arise in India.

Therefore, income from profession in Malaysia, rent from property in Malaysia and dividend from Malaysian company received in Malaysia by Mrs. Geetha, a non-resident, would not be taxable in India, since both the accrual and receipt are outside India.

However, profit from business in Delhi would be taxable in India in the hands of Mrs. Geetha, even though it is managed directly from Malaysia.

Further, by virtue of section 9(1)(vii), fees for technical services rendered in India would also be taxable in the hands of Mrs. Geetha, since it is deemed to accrue or arise in India.

(2) The income referred to in S. No. 10, 11, 12 and 13 are taxable in the hands of both Mrs. Geetha and Mrs. Leena due to their accrual/deemed accrual in India, even though a part of income from business in Pune and the entire interest on debentures in Indian company is received by Mrs. Geetha outside India.

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Question 3

Discuss the correctness or otherwise of the statement- "Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fees for technical services is to be taxed irrespective of territorial nexus".

Answer

This statement is correct.

As per *Explanation* to section 9, income by way of interest, royalty or fee for technical services which is deemed to accrue or arise in India by virtue of clauses (v), (vi) and (vii) of section 9(1), shall be included in the total income of the non-resident, whether or not -

(i) non-resident has a residence or place of business or business connection in India; or

(ii) the non-resident has rendered services in India.

In effect, the income by way of fee for technical services, interest or royalty from services utilised in India would be deemed to accrue or arise in India in case of a non-resident and be included in his total income, whether or not such services were rendered in India and irrespective of whether the non-resident has a residence or place of business or business connection in India.

Question 4

Mr. David, a Government employee serving in the Ministry of External Affairs, left India for the first time on 31.03.2016 due to his transfer to High Commission of Canada. He did not visit India any time during the previous year 2016-17. He has received the following income for the Financial Year 2016-17:

S.No.	*Particulars*	₹
(i)	*Salary*	*5,00,000*
(ii)	*Foreign Allowance*	*4,00,000*
(iii)	*Interest on fixed deposit from bank in India*	*1,00,000*
(iv)	*Income from agriculture in Pakistan*	*2,00,000*
(v)	*Income from house property in Pakistan*	*2,50,000*

Compute his gross total income for Assessment Year 2017-18.

Answer

As per section 6(1), Mr. David is a non-resident for the A.Y. 2017-18, since he was not present in India at any time during the previous year 2016-17.

As per section 5(2), a non-resident is chargeable to tax in India only in respect of following incomes:

(i) Income received or deemed to be received in India; and

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(ii) Income accruing or arising or deemed to accrue or arise in India.

In view of the above provisions, income from agriculture in Pakistan and income from house property in Pakistan would not be chargeable to tax in the hands of David, assuming that the same were received in Pakistan.

Income from 'Salaries' payable by the Government to a citizen of India for services rendered outside India is deemed to accrue or arise in India as per section 9(1)(iii). Hence, such income is taxable in the hands of Mr. David, even though he is a non-resident. It has been assumed that Mr. David is a citizen of India.

However, allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India for rendering service outside India is exempt under section 10(7). Hence, foreign allowance of ₹ 4,00,000 is exempt under section 10(7).

Gross Total Income of Mr. David for A.Y. 2017-18

Particulars	₹
Salaries	5,00,000
Income from other sources (Interest on fixed deposit in India)	1,00,000
Gross Total Income	**6,00,000**

Question 5

Brett Lee, an Australian cricket player visits India for 100 days in every financial year. This has been his practice for the past 10 financial years. Find out his residential status for the assessment year 2017-18.

Answer

Determination of Residential Status of Mr. Brett Lee for the A.Y. 2017-18:-

Period of stay during previous year 2016-17 = 100 days.

Calculation of period of stay during 4 preceding previous years (100 x 4=400 days)

2015-16	100 days
2014-15	100 days
2013-14	100 days
2012-13	100 days
Total	400 days

Mr. Brett Lee has been in India for a period more than 60 days during previous year 2016-17 and for a period of more than 365 days during the 4 immediately preceding previous years. Therefore, since he satisfies one of the basic conditions under section 6(1), he is a resident for the assessment year 2017-18.

Computation of period of stay during 7 preceding previous years = 100 x 7=700 days

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2015-16	100 days
2014-15	100 days
2013-14	100 days
2012-13	100 days
2011-12	100 days
2010-11	100 days
2009-10	100 days
Total	**700 days**

Since his period of stay in India during the past 7 previous years is less than 730 days, he is a not-ordinarily resident during the assessment year 2017-18. (See Note below)

Therefore, Mr. Brett Lee is a resident but not ordinarily resident during the previous year 2016-17 relevant to the assessment year 2017-18.

Note: *A not-ordinarily resident person is one who satisfies any one of the conditions specified under section 6(6), i.e.,*

(i) If such individual has been non-resident in India in any 9 out of the 10 previous years preceding the relevant previous year, or

(ii) If such individual has during the 7 previous years preceding the relevant previous year been in India for a period of 729 days or less.

In this case, since Mr. Brett Lee satisfies condition (ii), he is a not-ordinary resident for the A.Y. 2017-18.

Question 6

Miss Vivitha paid a sum of 5000 USD to Mr. Kulasekhara, a management consultant practising in Colombo, specializing in project financing. The payment was made in Colombo. Mr. Kulasekhara is a non-resident. The consultancy is related to a project in India with possible Ceylonese collaboration. Is this payment chargeable to tax in India in the hands of Mr. Kulasekhara, since the services were used in India?

Answer

A non-resident is chargeable to tax in respect of income received outside India only if such income accrues or arises or is deemed to accrue or arise to him in India.

The income deemed to accrue or arise in India under section 9 comprises, *inter alia*, income by way of fees for technical services, which includes any consideration for rendering of any managerial, technical or consultancy services. Therefore, payment to a management consultant relating to project financing is covered within the scope of "fees for technical services".

The *Explanation* below section 9(2) clarifies that income by way of, *inter alia*, fees for technical

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services, from services utilized in India would be deemed to accrue or arise in India in case of a non-resident and be included in his total income, whether or not such services were rendered in India or whether or not the non-resident has a residence or place of business or business connection in India.

In the instant case, since the services were utilized in India, the payment received by Mr. Kulasekhara, a non-resident, in Colombo is chargeable to tax in his hands in India, as it is deemed to accrue or arise in India.

Question 7

Mr. Ram, an Indian citizen, left India on 22.09.2016 for the first time to work as an officer of a company in Germany.

Determine the residential status of Ram for the assessment year 2017-18 and explain the conditions to be fulfilled for the same under the Income-tax Act, 1961.

Answer

Under section 6(1), an individual is said to be resident in India in any previous year if he satisfies any one of the following conditions -

(i) He has been in India during the previous year for a total period of 182 days or more, or

(ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

In the case of Indian citizens leaving India for employment, the period of stay during the previous year must be 182 days instead of 60 days given in (ii) above.

During the previous year 2016-17, Mr. Ram, an Indian citizen, was in India for 175 days only (i.e 30+31+30+31+31+22 days). Thereafter, he left India for employment purposes.

Since he does not satisfy the minimum criteria of 182 days, he is a non-resident for the A.Y. 2017-18.

Question 8

From the following particulars of income furnished by Mr. Anirudh pertaining to the year ended 31.3.2017, compute the total income for the assessment year 2017-18, if he is:

(i) Resident and ordinary resident;

(ii) Resident but not ordinarily resident;

(iii) Non-resident

	Particulars	***₹***
(a)	*Short term capital gain on sale of shares in Indian Company received in Germany*	*15,000*
(b)	*Dividend from a Japanese Company received in Japan*	*10,000*

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(c)	*Rent from property in London deposited in a bank in London, later on remitted to India through approved banking channels*	*75,000*
(d)	*Dividend from RP Ltd., an Indian Company*	*6,000*
(e)	*Agricultural income from lands in Gujarat*	*25,000*

Answer

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

Particulars	Resident & ordinarily resident	Resident but not ordinarily resident	Non-Resident
1) Short term capital gain on sale of shares of an Indian company, received in Germany	15,000	15,000	15,000
2) Dividend from a Japanese company, received in Japan	10,000	-	-
3) Rent from property in London deposited in a bank in London [See Note (i) below]	52,500	-	-
4) Dividend from RP Ltd., an Indian Company [See Note (ii) below]	-	-	-
5) Agricultural income from land in Gujarat [See Note (iii) below]	-	-	-
Total Income	**77,500**	**15,000**	**15,000**

Notes:

(i) It has been assumed that the rental income is the gross annual value of the property. Therefore, deduction @30% under section 24, has been provided and the net income so computed is taken into account for determining the total income of a resident and ordinarily resident.

Rent received (assumed as gross annual value)	75,000
Less: Deduction under section 24 (30% of ₹ 75,000)	22,500
Income from house property	52,500

(ii) Dividend from Indian company is exempt under section 10(34).

(iii) Agricultural income is exempt under section 10(1).

Question 9

Discuss the provisions relating to determination of residential status of Hindu undivided family, partnership firm and company.

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Answer

Residential status of a HUF:

A HUF would be resident in India if the control and management of its affairs is situated wholly or partly in India during the relevant previous year. If the control and management of its affairs is situated wholly outside India during the relevant previous year, it would be considered as a non-resident.

If the HUF is resident, then the status of its Karta determines whether it is resident and ordinarily resident or resident but not ordinarily resident.

Residential status of a firm:

A firm would be resident in India if the control and management of its affairs is situated wholly or partly in India during the relevant previous year. Where the control and management of the affairs is situated wholly outside India during the relevant previous year, the firm would be considered as a non-resident.

Residential status of a company:

A company is said to be resident in India in any previous year if :

(a) it is an Indian company, or

(b) its place of effective management, in that year, is in India.

Question 10

Mr. Dey, a non-resident, residing in US since 1990, came back to India on 1.4.2015 for permanent settlement. What will be his residential status for assessment years 2016-17 and 2017-18?

Answer

Mr. Dey is a resident in A.Y.2016-17 and A.Y.2017-18 since he has stayed in India for a period of 365 days (more than 182 days) during the P.Y.2015-16 and P.Y.2016-17, respectively.

As per section 6(6), a person will be "Not ordinarily Resident" in India in any previous year, if such person:

(a) has been a non-resident in 9 out of 10 previous years preceding the relevant previous year; or

(b) has during the 7 previous years immediately preceding the relevant previous year been in India for 729 days or less.

If he does not satisfy either of these conditions, he would be a resident and ordinarily resident.

In the instant case, applying the above, the status of Mr. Dey for the previous year 2015-16 (A.Y. 2016-17) will be "Resident but not ordinarily resident".

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For the previous year 2016-17 (A.Y. 2017-18) his status would continue to be Resident but not ordinarily resident since he was non-resident in 9 out of 10 previous years immediately preceding the previous year and also had stayed for less than 729 days in 7 previous years immediately preceding the previous year.

Therefore, his status for

A.Y. 2016-17 – "Resident but not ordinarily resident"

A.Y. 2017-18 – "Resident but not ordinarily resident"

Question 11

State the activities and operations, income from which is not deemed to accrue or arise in India.

Answer

Explanation 1 to section 9(1)(i) lists out income which shall not be deemed to accrue or arise in India. They are given below:

(1) In the case of a business, in respect of which all the operations are not carried out in India [*Explanation 1(a)* to section 9(1)(i)]

In the case of a business of which all the operations are not carried out in India, the income of the business deemed to accrue or arise in India shall be only such part of income as is reasonably attributable to the operations carried out in India. Therefore, it follows that such part of income which cannot be reasonably attributed to the operations in India, is not deemed to accrue or arise in India.

(2) Purchase of goods in India for export [*Explanation 1(b)* to section 9(1)(i)]

In the case of a non-resident, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export.

(3) Collection of news and views in India for transmission out of India [*Explanation 1(c)* to section 9(1)(i)]

In the case of a non-resident, being a person engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be deemed to accrue or arise in India to him through or from activities which are confined to the collection of news and views in India for transmission out of India.

(4) Shooting of cinematograph films in India [*Explanation 1(d)* to section 9(1)(i)]

In the case of a non-resident, no income shall be deemed to accrue or arise in India through or from operations which are confined to the shooting of any cinematograph film in India, if such non-resident is :

(i) an individual, who is not a citizen of India or

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(ii) a firm which does not have any partner who is a citizen of India or who is resident in India; or

(iii) a company which does not have any shareholder who is a citizen of India or who is resident in India.

Question 12

When is an individual and HUF said to be "Resident and ordinarily Resident" under the Income-tax Act, 1961?

Answer

Individual – An individual is said to be a resident in India in any previous year if he fulfills any one of the following two basic conditions:

(i) He is in India during the previous year for a period or periods amounting in all to 182 days or more.

(ii) He is in India for a period or periods amounting in all to 60 days or more during the previous year and 365 days or more during 4 years immediately preceding the relevant previous year.

Exception – If an Indian citizen leaves India for the purpose of employment or as a member of crew of an Indian ship or if an Indian citizen or person of Indian origin who is residing outside India comes to India on a visit in any previous year, he would be considered as resident in India in that year only if he has been in India in that year for 182 days or more instead of 60 days referred to in, (ii) above.

Resident and Ordinarily Resident: If an individual satisfies any one of the basic conditions and none of the following additional conditions, he will be treated as "resident and ordinarily resident".

Additional conditions:

(i) He has been a non-resident in India in 9 out of 10 previous years preceding the relevant previous year; or

(ii) He has been in India for a period of 729 days or less during 7 previous years immediately preceding the relevant previous year.

Thus in brief, an individual fulfilling any one of the basic conditions and none of the additional conditions will be "resident and ordinarily resident".

HUF: If the control and management of the affairs of the HUF is wholly or partly situated in India and if the manager of the HUF does not satisfy either of the following two additional conditions, the HUF shall be considered as "resident and ordinarily resident" –

(i) He has been non resident in India in 9 out of 10 previous years preceding the relevant previous year;

(ii) He has been in India for a period of 729 days or less during the 7 previous years preceding the relevant previous year.

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Question 13

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

(a) Only individuals and HUFs can be resident, but not ordinarily resident in India; firms can be either a resident or non-resident.

(b) Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fee for technical services is taxable in India irrespective of territorial nexus.

(c) Mr. X, Karta of HUF, claims that the HUF is non-resident as the business of HUF is transacted from UK and all the policy decisions are taken there.

Answer

(a) True: A person is said to be "not-ordinarily resident" in India if he satisfies either of the conditions given in sub-section (6) of section 6. This sub-section relates to only individuals and Hindu Undivided Families. Therefore, only individuals and Hindu Undivided Families can be resident, but not ordinarily resident in India. All other classes of assessees can be either a resident or non-resident for the purpose of income-tax. Firms and companies can, therefore, either be a resident or non-resident.

(b) True: *Explanation* below section 9(2) clarifies that income by way of interest, royalty or fee for technical services which is deemed to accrue or arise in India by virtue of clauses (v), (vi) and (vii) of section 9(1), shall be included in the total income of the non-resident, whether or not :

(i) non-resident has a residence or place of business or business connection in India; or

(ii) the non-resident has rendered services in India

(c) True: A HUF is considered to be a non-resident where the control and management of its affairs are situated wholly outside India. In the given case, since all the policy decisions of HUF are taken from UK, the HUF is a non-resident.

Question 14

Miss Charlie, an American national, got married to Mr. Radhey of India in USA on 2.03.2016 and came to India for the first time on 16.03.2016. She remained in India up till 19.9.2016 and left for USA on 20.9.2016. She returned to India again on 27.03.2017. While in India, she had purchased a show room in Mumbai on 22.04.2016, which was leased out to a company on a rent of ₹ 25,000 p.m. from 1.05.2016 She had taken loan from a bank for purchase of this show room on which bank had charged interest of ₹ 97,500 upto 31.03.2017. She had received the following gifts from her relatives and friends during 1.4.2016 to 30.6.2017:

- From parents of husband	*₹*	*51,000*
- From married sister of husband	*₹*	*11,000*
- From two very close friends of her husband, ₹ 1,51,000 and ₹ 21,000	*₹*	*1,72,000*

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Determine her residential status and compute the total income chargeable to tax along with the amount of tax payable on such income for the Assessment Year 2017-18.

Answer

Under section 6(1), an individual is said to be resident in India in any previous year, if he satisfies any one of the following conditions:

(i) He has been in India during the previous year for a total period of 182 days or more, or

(ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

If an individual satisfies any one of the conditions mentioned above, he is a resident. If both the above conditions are not satisfied, the individual is a non-resident.

Therefore, the residential status of Miss Charlie, an American National, for A.Y.2017-18 has to be determined on the basis of her stay in India during the previous year relevant to A.Y. 2017-18 i.e. P.Y.2016-17 and in the preceding four assessment years.

Her stay in India during the previous year 2016-17 and in the preceding four years are as under:

P.Y. 2016-17

01.04.2016 to 19.09.2016	-	172 days
27.03.2017 to 31.03.2017	-	5 days
Total		177 days

Four preceding previous years

P.Y.2015-16 [1.4.2015 to 31.3.2016]	-	16 days
P.Y.2014-15 [1.4.2014 to 31.3.2015]	-	Nil
P.Y.2013-14 [1.4.2013 to 31.3.2014]	-	Nil
P.Y.2012-13 [1.4.2012 to 31.3.2013]	-	Nil
Total		16 days

The total stay of the assessee during the previous year in India was less than 182 days and during the four years preceding this year was for 16 days. Therefore, due to non-fulfillment of any of the two conditions for a resident, she would be treated as non-resident for the Assessment Year 2017-18.

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

Particulars	₹	₹
Income from house property		
Show room located in Mumbai remained on rent from 01.05.2016 to 31.03.2017 @ ₹ 25,000/- p.m.	2,75,000	

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Gross Annual Value [25,000 x 11] (See Note 1 below)			
Less: Municipal taxes		Nil	
Net Annual Value (NAV)		**2,75,000**	
Less: Deduction under section 24			
30% of NAV	82,500		
Interest on loan	97,500	1,80,000	95,000
Income from other sources			
Gifts received from non-relatives is chargeable to tax as per section 56(2)(vii) if the aggregate value of such gifts exceeds ₹ 50,000.			
- ₹ 50,000 received from parents of husband would be exempt, since parents of husband fall within the definition of relatives and gifts from a relative are not chargeable to tax.		Nil	
- ₹ 11,000 received from married sister of husband is exempt, since sister-in-law falls within the definition of relative and gifts from a relative are not chargeable to tax.		Nil	
- Gift received from two friends of husband ₹ 1,51,000 and ₹ 21,000 aggregating to ₹ 1,72,000 is taxable under section 56(2)(vii) since the aggregate of ₹ 1,72,000 exceeds ₹ 50,000. (See Note 2 below)		1,72,000	1,72,000
Total income			**2,67,000**

Computation of tax payable by Miss Charlie for the A.Y. 2017-18

Particulars	₹
Tax on total income of ₹ 2,67,000	1,700
Add: Education cess@2%	34
Add : Secondary and higher education cess @1%	17
Total tax payable	**1,751**

Notes:

1. Actual rent received has been taken as the gross annual value in the absence of other information (i.e. Municipal value, fair rental value and standard rent) in the question.
2. If the aggregate value of taxable gifts received from non-relatives exceeds ₹ 50,000 during the year, the entire amount received (i.e. the aggregate value of taxable gifts received) is taxable. Therefore, the entire amount of ₹ 1,72,000 is taxable under section 56(2)(vii).

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3. Since Miss Charlie is a non-resident for the A.Y. 2017-18, rebate under section 87A would not be available to her, even though her total income is less than ₹ 5 lacs.

Question 15

Determine the taxability of income of US based company Heli Ltd., in India on entering into the following transactions during the financial year 2016-17:

(i) ₹ 5 lacs received from an Indian domestic company for providing technical knowhow in India.

(ii) ₹ 6 lacs from an Indian firm for conducting the feasibility study for the new project in Finland. The payment for the same was made in Finland.

(iii) ₹ 4 lacs from a non-resident for use of patent for a business in India.

(iv) ₹ 8 lacs from a non-resident Indian for use of know how for a business in Singapore. Such amount was received in U.S.

(v) ₹ 10 lacs for supply of manuals and designs for the business to be established in Singapore. No payment for the same was made in India.

Answer

A non-resident is chargeable to tax in India in respect of following incomes:

(i) Income received or deemed to be received in India; and

(ii) Income accruing or arising or deemed to accrue or arise in India.

In view of the above provisions, taxability of income is determined in following manner:

S. No.	Particulars	₹ (in lacs)
(i)	Amount received from an Indian domestic company for providing technical knowhow in India is deemed to accrue or arise in India and is, therefore, taxable in India.	5
(ii)	Conducting the feasibility study for the new project in Finland for the Indian firm is not taxable in India as the income accrues outside India since such study is done for a business outside India.	Nil
(iii)	Income received from a non-resident for use of patent for a business in India is taxable in India as it is deemed to accrue or arise in India.	4
(iv)	Income received from a non-resident Indian for use of knowhow for a business in Singapore. It is not taxable in India since it does not accrue or arise in India nor is it deemed to accrue or arise in India,	Nil
(v)	Income received for supply of manuals and designs for the business to be established in Singapore is not taxable in India,	Nil

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	since it does not accrue or arise in India nor is it deemed to accrue or arise in India.	
	Total Income	**9**

Question 16

State with reasons whether the following transactions attract income-tax in India in the hands of recipients:

(i) Salary paid by Central Government to Mr. John, a citizen of India ₹ 7,00,000 for the services rendered outside India.

(ii) Interest on moneys borrowed from outside India ₹ 5,00,000 by a non-resident for the purpose of business within India say, at Mumbai.

(iii) Post office savings bank interest of ₹ 12,000 received by a resident assessee, Mr. Ram.

(iv) Royalty paid by a resident to a non-resident in respect of a business carried on outside India.

(v) Legal charges of ₹ 5,00,000 paid to a lawyer of United Kingdom who visited India to represent a case at the Delhi High Court.

Answer

	Taxable / Not Taxable	**Amount liable to tax (₹)**	**Reason**
(i)	Taxable	7,00,000	As per section 9(1)(iii), salaries payable by the Government to a citizen of India for service rendered outside India shall be deemed to accrue or arise in India. Therefore, salary paid by Central Government to Mr. John for services rendered outside India would be deemed to accrue or arise in India since he is a citizen of India.
(ii)	Taxable	5,00,000	As per section 9(1)(v)(c), interest payable by a non-resident on moneys borrowed and used for the purposes of business carried on by such person in India shall be deemed to accrue or arise in India in the hands of the recipient.
(iii)	Partly Taxable	Nil	The interest on Post Office Savings Bank Account, would be exempt under section 10(15)(i), only to the extent of ₹ 3,500 in case of an individual account. The remaining ₹ 8,500, being less than ₹ 10,000, would be allowed as deduction under section 80TTA from Gross Total Income.
(iv)	Not Taxable	-	Royalty paid by a resident to a non-resident in respect of a business carried outside India would not be taxable in the hands of the non-resident provided the same is not

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			received in India. This has been provided as an exception to deemed accrual mentioned in section 9(1)(vi)(b).
(v)	Taxable	5,00,000	In case of a non-resident, any income which accrues or arises in India or which is deemed to accrue or arise in India or which is received in India or is deemed to be received in India is taxable in India. Therefore, legal charges paid in India[1] to a non-resident lawyer of UK, who visited India to represent a case at the Delhi High Court would be taxable in India. ***Note*** *– This question can also be answered on the rationale that existence of professional connection tantamounts to existence of business connection, and hence, legal charges paid to a non-resident lawyer would be deemed to accrue or arise in India by virtue of section 9(1)(i).*

Question 17

(a) (i) Explain with reasons whether the following transactions attract income-tax in India in the hands of recipients :

(a) Salary paid to Mr. David, a citizen of India ₹ 15,00,000 by the Central Government for the services rendered in Canada.

(b) Legal charges of ₹ 7,50,000 paid to Mr. Johnson, a lawyer of London, who visited India to represent a case at the Supreme Court.

(c) Royalty paid to Rajeev, a non-resident by Mr. Mukesh, a resident for a business carried on in Sri Lanka.

(ii) Ms. Bindu, a non-resident, residing in New York since 1990, came back to India on 19-02-2015 for permanent settlement in India. Explain the residential status of Ms. Bindu for the Assessment Year 2017-18 in accordance with the various provisions of Income-tax Act, 1961.

Answer

(i) Taxability of certain receipts under the Income-tax Act, 1961

Sl. No.	**Taxable/Not Taxable**	**Amount liable to tax (₹)**	**Reason**
1	**2**	**3**	**4**
(a)	Taxable	15,00,000	Salaries payable by the Government to a citizen

[1] Since the payment is in Indian currency, it is logical to assume that the same has been paid in India.

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			of India for service rendered outside India shall be deemed to accrue or arise in India as per section 9(1)(iii). Mr. David is a citizen of India. Therefore, salary paid by the Central Government to him for services rendered in Canada would be deemed to accrue or arise in India in his hands.
(b)	Taxable	7,50,000	In case of a non-resident, any income which accrues or arises in India or which is deemed to accrue or arise in India or which is received in India or is deemed to be received in India is taxable in India. Therefore, legal charges paid in India[2] to Mr. Johnson, a non-resident lawyer of London, who visited India to represent a case at the Supreme Court would be taxable in India. ***Note*** – *This question can also be answered on the rationale that existence of professional connection tantamounts to existence of business connection, and hence, legal charges paid to a non-resident lawyer would be deemed to accrue or arise in India by virtue of section 9(1)(i).*
(c)	Not Taxable	-	Royalty paid by a resident to a non-resident in respect of a business carried on outside India would not be taxable in the hands of the non-resident, as the same would **not** be deemed to accrue or arise in India as per the exception mentioned in section 9(1)(vi)(b). Therefore, royalty paid by Mukesh, a resident, to Rajeev, a non-resident, for a business carried on in Sri Lanka would **not** be deemed to accrue or arise in India. ***Note*** - *It is assumed that the royalty was not received in India.*

(ii) Determination of residential status of Ms. Bindu for the A.Y. 2017-18

Ms. Bindu is a resident since she has stayed in India for 365 days during the P.Y.2016-17. Therefore, she satisfies the condition of stay in India for a period of 182 days or more in the relevant previous year as per the requirement under section 6(1).

As per section 6(6), an individual is said to be "not ordinarily resident" in India in any

[2] Since the payment is in Indian currency, it is logical to assume that the same has been paid in India.

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previous year, if he has:

(a) been a non-resident in India in nine out of ten previous years preceding the relevant previous year; or

(b) during the seven previous years immediately preceding the relevant previous year, been in India for a period of, or periods amount in all to, 729 days or less.

Ms. Bindu must, therefore, satisfy either of the conditions to qualify as a not-ordinarily resident.

Ms. Bindu was a non-resident in India up to A.Y.2015-16.

She was resident in India only for P.Y. 2015-16 (A.Y.2016-17) out of the ten previous years preceding P.Y. 2016-17 (A.Y.2017-18). This implies that she has been a non-resident in India in nine out of ten previous years preceding P.Y. 2016-17 (A.Y. 2017-18).

Further, she was in India only for a period of 406 days [i.e., 10 days in February, 2015 + 31 days in March 2015 + 365 days during the P.Y.2015-16] in the seven previous years preceding P.Y. 2016-17 (A.Y.2017-18).

Therefore, since Ms. Bindu satisfies both the conditions for "not-ordinarily resident", her residential status for A.Y.2017-18 would be "Resident but not ordinarily resident"

Question 18

An individual, who is an Indian resident, is allowed to hold two different citizenships simultaneously. Is the citizenship a determining factor for residential status of an individual?

Answer

Citizenship of a country and residential status of that country are separate concepts. A person may be an Indian national /citizen, but may not be a resident in India. On the other hand, a person may be a foreign national /citizen, but may be a resident in India. The citizenship of an individual has no role in determining the residential status of an individual.

The residential status of resident, non-resident, etc. are determined on the basis of number of days an individual actually stays in India during the previous year.

The provisions of section 6 of the Income-tax Act, 1961 are the determining factor of residential status of an individual.

Question 19

Mr. Soham, an Indian Citizen, left India on 20-04-2014 for the first time to setup a software firm in Singapore. On 10-04-2016, he entered into an agreement with LK Limited, an Indian Company, for the transfer of technical documents and designs to setup an automobile factory in Faridabad. He reached India along with his team to render the requisite services on 15-05-2016 and was able to complete his assignment on 20-08-2016. He left for Singapore on 21-08-2016. He charged ₹ 50 lakhs for his services from LK Limited.

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Determine the residential status of Mr. Soham for the Assessment Year 2017-18 and explain as to the taxability of the fees charged from LK Limited as per the Income-tax Act, 1961.

Answer

Determination of residential status of Mr. Soham

As per section 6(1), an individual is said to be resident in India in any previous year if he satisfies the conditions:-

(i) He has been in India during the previous year for a total period of 182 days or more, or

(ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

In the case of an Indian citizen leaving India for the purposes of employment outside India during the previous year or an Indian citizen, who being outside India, comes on a visit to India in any previous year, the period of stay during the previous year in condition (ii) above, to qualify as a resident, would be 182 days instead of 60 days.

In this case, Mr. Soham is an Indian citizen who left India to set up a software firm in Singapore on 20.04.2014. Therefore, he is an Indian citizen living in Singapore, who comes on a visit to India during the P.Y.2016-17. His stay in India during the period of his visit is only 99 days (i.e., 17+30+31+21 days). Since his stay in India during the previous year 2016-17 is only 99 days, he does not satisfy the minimum criterion of 182 days stay in India for being a resident. Hence, his residential status for A.Y.2017-18 is Non-Resident.

Taxability of income

As per section 5(2), in case of a non-resident, only income which accrues or arises or which is deemed to accrue or arise to him in India or which is received or deemed to be received in India in the relevant previous year is taxable in India.

In this case, Mr. Soham, a non-resident, charges fees from LK Ltd., an Indian company, for transfer of technical documents and designs to set up an automobile factory in Faridabad. He renders the requisite services in India for which he stays in India for 99 days during the P.Y.2016-17.

Explanation 2 to section 9(1)(vi) defines “royalty” to mean consideration for transfer of all or any rights in respect of, inter alia, a design and also for the rendering of services in connection with such activity. As per Explanation 4 to section 9(1)(vi), transfer of rights in the above definition includes transfer of right for use or right to use a computer software also. Therefore, the fees received by Mr. Soham for transfer of technical documents and designs and rendering of requisite services in relation thereto would fall within the meaning of “royalty”.

As per section 9(1)(vi), income by way of royalty payable by a person who is a resident (in this case, LK Limited, an Indian company) would be deemed to accrue or arise in India in the hands of the non-resident (Mr. Soham, in this case), except where such royalty is payable in

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respect of any right or property or information used or for services utilized for the purpose of a business carried on by such person outside India or for the purposes of making or earning income from any source outside India.

In this case, since the royalty is payable by an Indian company to Mr. Soham, a non-resident, in respect of services utilized for a business in India (namely, for setting up an automobile factory in Faridabad), the same is deemed to accrue or arise in India and is hence, taxable in India in the hands of Mr. Soham, a non-resident for the A.Y. 2017-18.

Question 19

How is the residential status of a company determined for the purposes of Income-tax Act, 1961, for the assessment year 2017-18?

Answer

Determination of residential status of a company for A.Y.2017-18

As per section 6(3), a company is said to be resident in India in any previous year, if -

(a) it is an Indian company

(b) its place of effective management, in that year, is in India.

Accordingly, all Indian companies are resident in India for A.Y.2017-18. However, a company other than an Indian company would be resident in India for A.Y.2017-18, only if its place of effective management (POEM), in the P.Y.2016-17, is in India.

"Place of effective management" means a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance, made.

Exercise

1. *If Anirudh has stayed in India in the P.Y. 2016-17 for 181 days, and he is non-resident in 9 out of 10 years immediately preceding the current previous year and he has stayed in India for 365 days in all in the 4 years immediately preceding the current previous year and 420 days in all in the 7 years immediately preceding the current previous year, his residential status for the A.Y.2017-18 would be -*

   a) Resident and ordinarily resident

   b) Resident but not ordinarily resident

   c) Non-resident

2. *Raman was employed in Hindustan Lever Ltd. He received a salary at ₹ 40,000 p.m. from 1.4.2016 to 27.9.2016. He resigned and left for Dubai for the first time on 1.10.2016 and got salary of rupee equivalent of ₹ 80,000 p.m. from 1.10.2016 to 31.3.2017. His salary for October to December 2016 was credited in his Dubai bank account and the salary for January to March 2017 was credited in his Bombay account directly. He is liable to tax in respect of -*

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a) Income received in India from Hindustan Lever Ltd;

b) Income received in India and in Dubai;

c) Income received in India from Hindustan Lever Ltd. and income directly credited in India;

3. *A company, other than an Indian company, would be a resident in India for the P.Y.2016-17 if, during that year,*

   a) its POEM is in India.

   b) its control and management is wholly or partly in India.

   c) majority of its directors are resident in India.

4. *Income accruing in London and received there is taxable in India in the case of -*

   a) resident and ordinarily resident only

   b) both resident and ordinarily resident and resident but not ordinarily resident

   c) both resident and non-resident

5. *When is an individual said to be "Resident and ordinarily resident" under the Income-tax Act, 1961?*

6. *Define royalty as per section 9 of the Income-tax Act, 1961?*

7. *Write short notes on -*

   a) Business connection

   b) Income deemed to accrue or arise in India.

8. *Discuss the provisions relating to determination of residential status of individuals.*

9. *When are the following income deemed to accrue or arise in India?*

   a) Interest

   b) Fees for technical services.

10. *Discuss the correctness or otherwise of the statement – "Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fees for technical services is to be taxed irrespective of territorial nexus."*

11. *Explain the term "Business Connection" under section 9(1).*

Answers

1. b; **2.** b; **3.** a; **4.** a.

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3 Incomes which do not Form Part of Total Income

<table>
<tr><th colspan="4">Key Points</th></tr>
<tr><th>Section</th><th colspan="3">Particulars</th></tr>
<tr><td>10(1)</td><td colspan="3">Agricultural income is exempt under section 10(1).
However, agricultural income has to be aggregated with non-agricultural income for determining the rate at which non-agricultural income would be subject to tax, in case of individuals, HUFs, AOP & BOIs etc., where the –
• agricultural income exceeds ₹ 5,000 p.a. and
• non-agricultural income exceeds basic exemption limit.
The following are the steps to be followed in computation of tax -
Step 1: Tax on non-agricultural income plus agricultural income
Step 2: Tax on agricultural income plus basic exemption limit
Step 3: Tax payable by the assessee = Step 1 – Step 2
Step 4: Add Surcharge/Deduct Rebate under section 87A, if applicable.
Step 5: Add Education cess@2% and SHEC@1%.</td></tr>
<tr><td>10(2)</td><td colspan="3">Since the HUF is taxed in respect of its income, the share income is exempt from tax in the hands of the member under section 10(2).</td></tr>
<tr><td>10(2A)</td><td colspan="3">The partner's share in the total income of the firm or LLP is exempt from tax.</td></tr>
<tr><td>10(10BC)</td><td colspan="3">Compensation received by an individual or his legal heir on account of any disaster is exempt, if the same has been granted by the Central Government, State Government or a local authority.</td></tr>
<tr><td rowspan="2">10(10D)</td><td colspan="3">Any sum received under a life insurance policy, including the sum allocated by way of bonus on such policy is exempt provided that –</td></tr>
<tr><td>In case of a policy issued between 1.4.2003 and 31.3.2012, the premium paid does not exceed 20% of the actual capital sum assured.</td><td>In case of a policy issued on or after 1.4.2012, the premium paid does not exceed 10% of the actual capital sum assured.</td><td>In case of a policy issued on or after 1.4.2013, the premium paid does not exceed 15% of the actual capital sum assured, if the insurance is on the life of a person with disability referred to in section 80U. In all other cases, the limit would be 10%.</td></tr>
</table>

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	Any sum received under a Keyman insurance policy is, however, not exempt. Further, "keyman insurance policy" includes a policy which has been assigned to any person during its term, with or without consideration. Consequently, the sum received by the keyman on such policies would not be exempt under section 10(10D).
10(11A)	Any payment from Sukanya Samriddhi Account.
10(18)	Pension received by individual who has been awarded "Param Vir Chakra" or "Maha Vir Chakra" or "Vir Chakra" such other gallantry award as the Central Government notifies is exempt from tax. Family pension received by any member of the family of such individual is also exempt from tax.
10(23BBH)	Any income of the Prasar Bharati established under section 3(1) of the Prasar Bharati Act, 1990 is exempt from tax.
10(26AAA)	Income from any source in the state of Sikkim, dividend income and interest on securities is exempt in the hands of a Sikkimese individual. This exemption is not available to a Sikkimese woman who, on or after 1st April, 2008, marries a non-Sikkimese individual.
10AA	Tax holiday for newly established units in Special Economic Zones (SEZs), which has begun or begins to manufacture or produce articles or things or computer software or provide any service on or after 1.4.2005 in any SEZ for 15 consecutive assessment years in respect of its profits from exports. Amount of exemption = Profits from business of the undertaking being the unit $\times$ $\left(\frac{\text{Export turnover of the undertaking of such articles or things or computer software}}{\text{Total turnover of the business carried on by the undertaking}}\right)$ 100% of such profits would be exempt in the first five years, 50% in the next five years and in the last five years, 50% subject to transfer to special reserve.
11 to 13, 2(15) & 115BBC	**(i)** Income derived from property held under trust wholly for public charitable or public religious purposes is exempt from tax under section 11 subject to fulfillment of the following conditions – (1) the trust should be registered with the Commissioner of Income-tax under section 12AA;

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		(2) the accounts of the trust should be audited, if the total income, before giving effect to the exemption under sections 11 and 12, exceeds the basic exemption limit; (3) at least 85% of the income is applied for the approved purposes; and (4) the unapplied income and the money accumulated or set apart should be invested or deposited in the specified forms and modes.
	(ii)	**<u>Charitable purpose [Section 2(15)]</u>** The definition of "charitable purpose" under section 2(15) includes relief of the poor, education, Yoga, medical relief, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest, and the advancement of any other object of general public utility. "Advancement of any other object of general public utility" shall, however, not be a charitable purpose, if it involves the carrying on of any activity in the nature of trade, commerce or business or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application or retention, of the income from such activity. However, "advancement of any other object of general public utility" would continue to be a "charitable purpose", if the aggregate receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed 20% of the total receipts of the trust or institution undertaking such activity or activities for the previous year.
	(iii)	**<u>Anonymous donations [Section 115BBC]</u>** Anonymous donations received by charitable trusts/institutions would be subject to tax@30% of the amount in excess of, 5% of the total donations received or Rs.1 lakh, whichever is higher, as per section 115BBC. The exemption provisions under section 11 and 12 would not apply to such anonymous donations. Section 115BBC does not, however, apply to a trust or institution created or established wholly for religious purposes. Further, anonymous donations received by partly charitable

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		and partly religious trusts would be taxable under section 115BBC only if the same is made with a specific direction that such donation is for any university or other educational institution or any hospital or other medical institution run by such trust or institution.
13A	Any income from house property, income from other sources, capital gains and income by way of voluntary contributions received by the political parties from any person is exempt under section 13A, subject to satisfaction of the following conditions - (i) maintenance of such books and other documents as would enable the Assessing Officer to properly deduce the income of the political party; (ii) maintenance of record in respect of each such voluntary contribution in excess of ₹ 20,000; (iii) audit of accounts by a chartered accountant; and (iv) submission of a report under section 29C(3) of the Representation of People Act, 1951 for every financial year.	

Question 1

State whether the following are chargeable to tax and the amount liable to tax:

(i) Arvind received ₹ 20,000 as his share from the income of the HUF.

(ii) Mr. Xavier, a 'Param Vir Chakra' awardee, who was formerly in the service of the Central Government, received a pension of ₹ 2,20,000 during the financial year 2016-17.

(iii) A political party registered under section 29A of the Representation of the People Act, 1951 earned rental income of ₹ 6,00,000 by letting out premises.

(iv) Agricultural income to a resident of India from a land situated in Malaysia.

(v) Allowance received by an employee working in a transport system at ₹ 10,000 per month to meet his personal expenditure while on duty. He is not receiving any daily allowance.

(vi) Amount withdrawn from Public Provident Fund as per relevant rules.

(vii) Rent of ₹ 72,000 received for letting out agricultural land for a movie shooting.

Answer

S.No.	Taxable/Not Taxable	Amount liable to tax (₹)	Reason
(i)	Not Taxable	-	Share received by member out of the income of the HUF is exempt under section 10(2).

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(ii)	Not Taxable	-	Pension received by Mr. Xavier, a former Central Government employee who is a 'Param Vir Chakra' awardee, is exempt under section 10(18).
(iii)	Not Taxable	-	Any income of a political party registered under section 29A of the Representation of the People Act, 1951 which is chargeable, *inter alia*, under the head "Income from house property" is exempt under section 13A provided the political party maintains such books of account as would enable the Assessing Officer to properly deduce its income therefrom and the accounts are audited by a chartered accountant.
(iv)	Taxable	-	Agricultural income from a land in any foreign country is taxable in the case of a resident taxpayer as income under the head "Income from other sources". Exemption under section 10(1) is not available in respect of such income.
(v)	Partly taxable	36,000	Under section 10(14), any allowance granted to an employee working in a transport system to meet his personal expenditure during his duty is exempt, provided he is not in receipt of daily allowance. The exemption is 70% of such allowance (i.e., ₹ 7,000 per month, being 70% of ₹ 10,000) or ₹ 10,000 per month, whichever is less. Hence, ₹ 84,000 (i.e., ₹ 7,000 × 12) is allowable as deduction under section 10(14). Balance ₹ 36,000 (₹ 1,20,000 - ₹ 84,000) shall be taxable.
(vi)	Not taxable	-	Any amount withdrawn from public provident fund as per relevant rules is not exigible to tax. Such exemption is provided in section 10(11).
(vii)	Taxable	72,000	Agricultural income is exempt from tax as per section 10(1). Agricultural income means, *inter alia*, any rent or revenue derived from land which is situated in India and is used for agricultural purposes. In the present case, rent is being derived from letting out of agricultural land for a movie shoot, which is not an agricultural purpose. In effect, the land is not being put to use for agricultural purposes. Therefore, ₹ 72,000, being rent received from letting out of agricultural land for movie shooting, is not exempt under section 10(1). The same is chargeable to tax under the head "Income from other sources".

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Question 2

Discuss the taxability of agricultural income under the Income-tax Act, 1961. How will income be computed where an individual derives agricultural and non-agricultural income?

Answer

Agricultural income is exempt from tax as per section 10(1). However, aggregation of agricultural and non-agricultural income is to be done to determine the rate at which the non-agricultural income shall be chargeable to tax. In case the agricultural income is not more than ₹ 5,000 or the tax-payer has non-agricultural income less than the basic exemption limit, then no such aggregation needs to be done. Further, such aggregation has to be done only if the tax-payer is an individual, HUF, AOP, BOI or an artificial judicial person, since the Finance Act prescribes slab rates of income-tax for these assessees. In the case of other assessees such as partnership firms, companies etc, whose income is chargeable to tax at a flat rate, aggregation of agricultural income would have no effect.

Since the second part of the question requires the manner of computation of income where an individual derives agricultural and non-agricultural income, the same can be answered on the basis of Rules 7A, 7B and 8 of the Income-tax Rules, 1962 dealing with composite income.

Rule	Particulars	Business Income	Agricultural Income
Rule 7A	Income from manufacture of rubber in India	35%	65%
Rule 7B	Income from manufacture of coffee		
	- grown and cured by the seller in India	25%	75%
	- grown, cured, roasted and grounded by the seller in India	40%	60%
Rule 8	Income from manufacture of tea in India	40%	60%

Thereafter, income-tax shall be computed by aggregating the agricultural income and the non-agricultural income in the manner described below:

(1) Aggregate the agricultural income with non-agricultural income and determine tax payable on such amount.

(2) Aggregate the agricultural income with the basic exemption limit of the assessee i.e., ₹ 2,50,000 /₹ 3,00,000 /₹ 5,00,000, as the case may be, and determine tax on such amount.

(3) Compute the difference between the tax computed in Step (1) and Step (2), which shall be the tax payable in respect of non-agricultural income.

(4) The tax payable so computed in step (3) shall be increased by surcharge @15%, if the total income exceeds ₹ 1 crore or reduced by rebate under section 87A, if the total income does not exceed ₹ 5 lakh. Thereafter, education cess of 2% and secondary and higher education cess of 1% has to be added to compute the total tax liability.

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Question 3

Whether the income derived from saplings or seedlings grown in a nursery is taxable under the Income-tax Act, 1961?

Answer

As per *Explanation 3* to section 2(1A) of the Act, income derived from saplings or seedlings grown in a nursery shall be deemed to be agricultural income and exempt from tax, whether or not the basic operations were carried out on land.

Question 4

State with reasons in brief whether the following statements are true or false with reference to the provisions of the Income-tax Act, 1961:

(i) Exemption is available to a Sikkimese individual, only in respect of income from any source in the State of Sikkim.

(ii) Where it is noticed that the income of the charitable trust is applied for the benefit of the author of the trust, the Principal Commissioner of Income-tax can cancel the registration by passing an order in writing.

(iii) In respect of voluntary contributions in excess of ₹ 20,000 received by a political party, exemption under section 13A is available where proper details about the donations are maintained; there is no need to maintain books of account.

(iv) Pension received by a recipient of gallantry award is exempt from income-tax.

(v) Mr. A, a member of a HUF, received ₹ 10,000 as his share from the income of the HUF. The same is to be included in his chargeable income.

(vi) Mr. Roy received a sum of ₹ 20 lakh on 31.3.2017 from Life Insurance Corporation of India in respect of a policy, where the sum assured was ₹ 15 lakh, taken on 1.10.2003 and for which a one time premium of ₹ 10 lakh was paid. Mr. Roy claims that the amount is totally exempt under section 10(10D)(c) of the Income-tax Act, 1961.

(vii) Voluntary contributions received by charitable trusts, universities and educational institutions are not taxable as the definition of income in section 2(24) does not cover the same.

(viii) Compensation on account of disaster received from a local authority by an individual or his/her legal heir is taxable.

(ix) Mr. P, a shareholder of a closely held company, holding 16% shares, received advances from that company which is to be deemed as dividend from an Indian Company, hence exempted under section 10(34) of the Income-tax Act, 1961.

(x) Payment of ₹ 10 lakh from an approved superannuation fund made by XYZ Ltd. by way of transfer to the account of Mr. Satish, an employee, under Atal Pension Yojana is taxable in the hands of Mr. Satish.

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Answer

(i) False: Exemption under section 10(26AAA) is available to a Sikkimese individual not only in respect of the said income, but also in respect of income by way of dividend or interest on securities.

(ii) True: As per section 12AA(4), the Commissioner or the Principal Commissioner has power to cancel the registration of the trust, by passing a written order, where it is noticed that, *inter alia,* the income of the trust is applied for the benefit of specified persons, including the author of the trust. However, the registration shall not be cancelled if the trust proves that there was reasonable cause for application of income in such manner.

(iii) False: The obligation under section 13A to maintain proper details of voluntary contributions in excess of ₹ 20,000 is over and above the obligation to maintain such books of account and other documents as would enable the Assessing Officer to properly deduce its income therefrom.

(iv) True: Section 10(18) exempts any income by way of pension received by individual who has been awarded "Param Vir Chakra" or "Maha Vir Chakra" or "Vir Chakra" or such other gallantry award as the Central Government, may, by notification in the Official Gazette, specify in this behalf.

(v) False: Section 10(2) exempts any sum received by an individual as a member of a HUF where such sum has been paid out of the income of the family. Therefore, ₹ 10,000 should not be included in Mr. A's chargeable income.

(vi) False: As per section 10(10D)(c), any sum received under an insurance policy issued on or after 1.4.2003 but before 31.03.2012, in respect of which the premium payable for any year during the term of the policy exceeds 20% of actual capital sum assured, shall not be exempt from tax. Hence, the contention of Mr. Roy is not correct since the one-time premium of ₹ 10 lakh paid by him is in excess of 20% of the sum assured [i.e. it exceeds ₹ 3 lakh, being 20% of ₹ 15 lakh]. Further, tax is deductible @1% under section 194DA on such sum paid to Roy, since the same is not exempt under section 10(10D).

(vii) False: Section 2(24) defining the term 'income' includes voluntary contributions received by any trust, university or educational institution. Hence, the statement is not correct.

(viii) False : As per section 10(10BC), any amount received or receivable as compensation by an individual or his/her legal heir on account of any disaster from the Central Government, State Government or a local authority is exempt from tax. However, the exemption is not available to the extent such individual or legal heir has already been allowed a deduction under this Act on account of such loss or damage caused by such disaster.

(ix) False: As per section 10(34), only income by way of dividend referred to in section 115-O shall be exempt in the hands of shareholders. Corporate dividend tax under section 115-O is not leviable on deemed dividend under section 2(22)(e) and hence, such deemed dividend is not exempt under section 10(34).

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(x) False: Any payment from an approved superannuation fund made by way of transfer to the account of an employee under a notified pension scheme referred to in section 80CCD is exempt under section 10(13). Since Atal Pension Yojana is a notified pension scheme under section 80CCD, the payment of Rs.10 lakhs made by XYZ Ltd. by way of transfer from an approved superannuation fund to Mr. Satish's account under such scheme is exempt under section 10(13).

Question 5

Explain the provisions regarding exemption of compensation received on account of disaster under section 10(10BC) of the Income-tax Act, 1961.

Answer

Exemption of compensation received on account of disaster under section 10(10BC)

(i) Section 10(10BC) exempts any amount received or receivable as compensation by an individual or his / her legal heir on account of any disaster.

(ii) Such compensation should be granted by the Central or State Government or by a local authority.

(iii) Exemption would not be available in respect of the compensation for alleviating any damage or loss, which has already been allowed as deduction under the Act.

(iv) "Disaster" means a catastrophe, mishap, calamity or grave occurrence in any area, arising from natural or man made causes, or by accident or negligence.

(v) It should have the effect of causing substantial loss of life or human suffering, or damage to, and destruction of, property, or damage to, or degradation of, environment.

(vi) It should be of such a nature or magnitude, which is beyond the coping capacity of the community of the affected area.

Question 6

Nathan Aviation Ltd. is running two industrial undertakings one in a SEZ (Unit S) and another in a normal area (Unit N). The brief summarized details for the year ended 31.3.2017 are as follows:

Particulars	*₹ (in lacs)*	
	S	***N***
Domestic turnover	*10*	*100*
Export turnover	*120*	*Nil*
Gross profit	*20*	*10*
Less: Expenses and depreciation	*7*	*6*
Profits derived from the unit	*13*	*4*

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The brought forward business loss pertaining to Unit N is ₹ 2 lacs. Briefly compute the business income of the assessee.

Assume F.Y. 2016-17 falls within the first 5 year period commencing from the year of manufacture or production of articles or things or provisions of services by the Unit S.

Answer

Computation of business income of Nathan Aviation Ltd.

Particulars	₹ (in lacs)
Total profit derived from Units S & N (₹ 13 lacs + ₹ 4 lacs)	17
Less: Exemption under section 10AA [**See Working Note below**]	12
	5
Less: Brought forward business loss	2
	3

Working Note

Computation of exemption under section 10AA in respect of Unit S located in a SEZ

Particulars	₹ (in lacs)
Domestic turnover of Unit S	10
Export turnover of Unit S	120
Total turnover of Unit S	**130**
Profit derived from Unit S	13
Exemption under section 10AA	
Profit of Unit S x $\frac{\text{Export turnover of unit S}}{\text{Total turnover of Unit S}} = 13 \times \frac{120}{130} =$	12

Question 7

Y Ltd. furnishes you the following information for the year ended 31.3.2017:

Particulars	*₹ (in lacs)*
Total turnover of Unit A located in Special Economic Zone	*100*
Profit of the business of Unit A	*30*
Export turnover of Unit A	*50*
Total turnover of Unit B located in Domestic Tariff Area (DTA)	*200*
Profit of the business of Unit B	*20*

Compute deduction under section 10AA for the A.Y. 2017-18.

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Answer

100% of the profit derived from export of articles or things or services is eligible for deduction under section 10AA, assuming that F.Y.2016-17 falls within the first five year period commencing from the year of manufacture or production of articles or things or provision of services by the Unit in SEZ. As per section 10AA(7), the profit derived from export of articles or things or services shall be the amount which bears to the profits of the business of the undertaking, being the Unit, the same proportion as the export turnover in respect of articles or things or services bears to the total turnover of the business carried on by the undertaking.

Deduction under section 10AA

$$= \text{Profit of the business of Unit A x } \frac{\text{Export Turnover of Unit A}}{\text{Total Turnover of Unit A}}$$

$$= ₹\ 30 \text{ lakhs x } \frac{50}{100}$$

= ₹ 15 lakhs

Question 8

MNO Ltd. has one undertaking at Special Economic Zone (SEZ) and another at Domestic Tariff Area (DTA). Following are the details given to you for the financial year 2016-17:

₹ in lakhs

	Unit in SEZ	*Unit in Domestic Tariff Area (DTA)*
Total Sales	*200*	*100*
Export Sales	*150*	*80*
Net Profit	*40*	*10*

Compute the quantum of eligible deduction under section 10AA for the A.Y.2017-18 in the following situations:

(i) Both the units were set up and began manufacturing from 25-07-2009.

(ii) Both the units were set up and began manufacturing from 10-04-2013

Answer

As per section 10AA, in computing the total income of MNO Ltd. from its unit located in a Special Economic Zone (SEZ), which begins to manufacture or produce any article or thing on or after 1.04.2005, there shall be allowed a deduction of 100% of the profit derived from export of such article or thing for the first five year period commencing from the year of manufacture or production of articles or things by the Unit in SEZ and 50% of such profits for further five years subject to fulfillment of other conditions specified in section 10AA.

(i) <u>If Unit in SEZ were set up and began manufacturing from 25-07-2009:</u>

Since it is the 8th year of operation of the eligible unit, it shall be eligible for deduction

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upto 50% of the profit of such unit assuming all the other conditions specified in section 10AA are fulfilled.

$$= \text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \times 50\%$$

$$= 40 \text{ lakhs} \times \frac{150 \text{ lakhs}}{200 \text{ lakhs}} \times 50\% = 15 \text{ lakhs}$$

(ii) <u>If Unit in SEZ were set up and began manufacturing from 10.04.2013:</u>

Since it is 4th year of operation of the eligible unit, it shall be eligible for deduction upto 100% of profit of such unit.

$$= \text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \times 100\%$$

$$= 40 \text{ lakhs} \times \frac{150 \text{ lakhs}}{200 \text{ lakhs}} \times 100\% = 30 \text{ lakhs}$$

Question 9

Rudra Ltd. has one unit at Special Economic Zone (SEZ) and other unit at Domestic Tariff Area (DTA). The company provides the following details for the previous year 2016-17.

Particulars	*Rudra Ltd. (₹)*	*Unit in DTA (₹)*
Total Sales	*6,00,00,000*	*2,00,00,000*
Export Sales	*4,60,00,000*	*1,60,00,000*
Net Profit	*80,00,000*	*20,00,000*

Calculate the eligible deduction under section 10AA of the Income-tax Act, 1961, for the Assessment Year 2017-18, in the following situations:

(i) If both the units were set up and start manufacturing from 22-05-2010.

(ii) If both the units were set up and start manufacturing from 14-05-2014.

Answer

Computation of deduction under section 10AA of the Income-tax Act, 1961

As per section 10AA, in computing the total income of Rudra Ltd. from its unit located in a Special Economic Zone (SEZ), which begins to manufacture or produce articles or things or provide any services during the previous year relevant to the assessment year commencing on or after 01.04.2006 but before 1st April 2021, there shall be allowed a deduction of 100% of the profit and gains derived from export of such articles or things or from services for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or

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things or provide services, as the case may be, and 50% of such profits for further five assessment years subject to fulfillment of other conditions specified in section 10AA.

Computation of eligible deduction under section 10AA [See Working Note below]:

(i) **<u>If Unit in SEZ was set up and began manufacturing from 22-05-2010:</u>**

Since A.Y. 2017-18 is the 7th assessment year from A.Y. 2011-12, relevant to the previous year 2010-11, in which the SEZ unit began manufacturing of articles or things, it shall be eligible for deduction of 50% of the profits derived from export of such articles or things, assuming all the other conditions specified in section 10AA are fulfilled.

$$= \text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \times 50\%$$

$$= 60 \text{ lakhs} \times \frac{300 \text{ lakhs}}{400 \text{ lakhs}} \times 50\% = ₹\ 22.50 \text{ lakhs}$$

(ii) **<u>If Unit in SEZ was set up and began manufacturing from 14-05-2014:</u>**

Since A.Y.2017-18 is the 3rd assessment year from A.Y. 2015-16, relevant to the previous year 2014-15, in which the SEZ unit began manufacturing of articles or things, it shall be eligible for deduction of 100% of the profits derived from export of such articles or things, assuming all the other conditions specified in section 10AA are fulfilled.

$$= \text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \times 100\%$$

$$= 60 \text{ lakhs} \times \frac{300 \text{ lakhs}}{400 \text{ lakhs}} \times 100\% = ₹\ 45 \text{ lakhs}$$

The unit set up in Domestic Tariff Area is not eligible for the benefit of deduction under section 10AA in respect of its export profits, in both the situations.

Working Note:

Computation of total sales, export sales and net profit of unit in SEZ

Particulars	Rudra Ltd. (₹)	Unit in DTA (₹)	Unit in SEZ (₹)
Total Sales	6,00,00,000	2,00,00,000	**4,00,00,000**
Export Sales	4,60,00,000	1,60,00,000	**3,00,00,000**
Net Profit	80,00,000	20,00,000	**60,00,000**

Question 10

Mr. Suresh has set up an undertaking in SEZ (Unit A) and another undertaking in DTA (Unit B) in the financial year 2011-12. In the previous year 2016-17, total turnover of the Unit A is ₹ 180 lacs and total turnover of Unit B is ₹ 120 lacs. Export turnover of Unit A for the year is ₹ 150 lacs and the profit for the Unit A is ₹ 60 lacs.

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Calculate the deduction available, if any, to Mr. Suresh under section 10AA of the Income-tax Act, 1961, for the Assessment year 2017-18, if Unit A had started manufacturing in the financial year 2011-12.

Answer

Computation of deduction available under section 10AA to Mr. Suresh for A.Y.2017-18

As per section 10AA, in computing the total income of an assessee from its unit located in a Special Economic Zone (SEZ), which begins to manufacture or produce articles or things or provide any services during the previous year relevant to the assessment year commencing on or after 01.04.2006, there shall be allowed a deduction of 100% of the profit and gains derived from export of such articles or things or from services for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, and 50% of such profits for further five assessment years subject to fulfillment of other conditions specified in section 10AA.

Mr. Suresh has set up an undertaking in SEZ (Unit A) and started manufacturing in the financial year 2011-12. For A.Y. 2017-18, being the 6th year of operation, he will be eligible for deduction of 50% of the profit of such unit, assuming all the other conditions specified in section 10AA are fulfilled.

$$= \text{Profits of Unit in SEZ x } \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unitin SEZ}} \times 50\%$$

$$= \text{60 lacs x } \frac{\text{150 lacs}}{\text{180 lacs}} \times 50\%$$

= ₹ 25 lacs

Mr. Suresh is not eligible for deduction under section 10AA in respect of Unit B set up in DTA.

Question 11

Explain the meaning of expression "advancement of any other object of general public utility" in the context of "Charitable Purpose" defined under section 2(15) of the Act. Discuss its tax implication as well.

Answer

The expression "advancement of any other object of general public utility" includes any object which will be beneficial even to a segment of society and not necessarily to the whole mankind. However, the object should not be for the benefit of specified individuals.

The proviso to section 2(15) of the Act provides that “advancement of any other object of general public utility" shall not be a charitable purpose, if it involves carrying on of -

(i) any activity in the nature of trade, commerce or business, or

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(ii) any activity of rendering of any service in relation to any trade, commerce or business,

for a cess or fee or any other consideration, irrespective of the nature of use or application of the income from such activity or the retention of such income, by the concerned entity. However, "advancement of any other object of general public utility" would continue to be a "charitable purpose", if such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility and the aggregate receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business does not exceed 20% of the total receipts of the trust or institution undertaking such activity or activities of that previous year.

Question 12

Can a political party claim exemption of its income under section 13A of the Income-tax Act, 1961?

Answer

Under section 13A, a political party registered under section 29A of the Representation of the People Act, 1951, can claim exemption under the following heads - Income from house property, capital gains and income from other sources. Income by way of voluntary contributions received by such political party is also exempt under section 13A.

These exemptions are subject to the following conditions:-

(i) The political party must keep and maintain such books of account and other documents as would enable the Assessing Officer to properly deduce its income therefrom.

(ii) The political party should keep and maintain a record of each such voluntary contribution in excess of ₹ 20,000 and the names and addresses of such contributors, the date of receipt and such other details as may be relevant or appropriate.

(iii) The accounts of the political party must be audited by a chartered accountant.

(iv) A report under section 29C(3) of the Representation of People Act, 1951 has to be submitted by the treasurer of such political party or any other person authorised by the political party in this behalf for every financial year.

Exercise

1. *The maximum ceiling limit for exemption under section 10(10) in respect of gratuity for employees covered by the Payment of Gratuity Act, 1972 is -*

   (a) ₹ 3,50,000

   (b) ₹ 10,00,000

   (c) ₹ 5,00,000

2. *The maximum ceiling limit for exemption under section 10(10C) with respect to compensation received on voluntary retirement is -*

   (a) ₹ 3,00,000

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(b) ₹ 3,50,000

(c) ₹ 5,00,000

3. The HRA paid to an employee residing in Patna is exempt up to the lower of actual HRA, excess of rent paid over 10% of salary and -

   (a) 40% of salary

   (b) 50% of salary

   (c) 60% of salary

4. Anirudh stays in New Delhi. His basic salary is ₹ 10,000 p.m., D.A. (60% of which forms part of pay) is 6,000 p.m., HRA is ₹ 5,000 p.m. and he is entitled to a commission of 1% on the turnover achieved by him. Anirudh pays a rent of ₹ 5,500 p.m. The turnover achieved by him during the current year is 12 lakhs. The amount of HRA exempt under section 10(13A) is –

   (a) ₹ 48,480

   (b) ₹ 45,600

   (c) ₹ 49,680

5. In case of a trade union registered under the Trade Unions Act, 1926 formed for regulating relations between workmen and employers or between workmen and workmen, the following incomes are exempt from tax -

   (a) Capital gains and Income from other sources.

   (b) Income from house property and capital gains.

   (c) Income from house property and income from other sources.

6. Voluntary contributions received by electoral trusts during the P.Y.2016-17 is -

   (a) Fully taxable

   (b) Fully exempt from tax

   (c) Exempt only if the trust distributes to a registered political party during the year, 95% of the aggregate donations received by it

7. The income derived from property held under trust wholly for charitable or religious purpose is exempt from tax under section 11 subject to fulfillment of certain conditions. One of the conditions is that -

   (a) At least 75% of the income is required to be applied for the approved purposes.

   (b) At least 85% of the income is required to be applied for the approved purposes.

   (c) The entire income is required to be applied for the approved purposes.

8. Income by way of voluntary contributions of political parties is exempt provided -

   (a). the political party keeps and maintains a record of each such voluntary contribution in excess of ₹ 10,000 and of the name and address of the person who made such contribution;

   (b). the political party keeps and maintains a record of each such voluntary contribution in

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excess of ₹ 20,000 and of the name and address of the person who made such contribution;

(c) the political party keeps and maintains a record of each such voluntary contribution in excess of ₹ 30,000 and of the name and address of the person who made such contribution;

9. *(a) Discuss the exemption available under the Income-tax Act in respect of specified income arising from any international sporting event in India.*

   (b) What are the exemptions available under section 10 in respect of companies engaged in the business of generation or transmission or distribution of power and subsidiaries of such companies? What are the conditions to be fulfilled to avail such exemptions?

10. *When can a charitable trust avail benefits under section 11 & 12 of the Income-tax Act, 1961?*

11. *Write short notes on:*

    (i) Exemption for retrenchment compensation under section 10(10B).

    (ii) Exceptions under section 10(10D) as regards exemption of any sum received under a life insurance policy.

    (iii) 'Encashment of Earned Leave' and its taxability under the Act.

12. *State the provisions relating to the exemption in respect of long-term capital gains on transfer of listed equity shares.*

13. *What are the conditions to be fulfilled by a Charitable Trust under section 12A for applicability of exemption provisions contained in sections 11 and 12?*

14. *Briefly explain the exemption available under section 10(48) of the Income-tax Act, 1961 in respect of income received by certain foreign companies from sale of crude oil.*

Answers

1. b; **2.** c; **3.** a; **4.** a; **5.** c; **6.** c; **7.** b; **8.** b

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4 Unit 1 : Income From Salaries

<table>
<tr><th colspan="3">Key Points</th></tr>
<tr><td colspan="3"><u>Basis of Charge [Section 15]</u></td></tr>
<tr><td>(i)</td><td colspan="2">Salary is chargeable to tax either on ‘due’ basis or on ‘receipt’ basis, whichever is earlier.</td></tr>
<tr><td>(ii)</td><td colspan="2">However, where any salary, paid in advance, is assessed in the year of payment, it cannot be subsequently brought to tax in the year in which it becomes due.</td></tr>
<tr><td>(iii)</td><td colspan="2">If the salary paid in arrears has already been assessed on due basis, the same cannot be taxed again when it is paid.</td></tr>
<tr><td colspan="3"><u>Taxability/Exemption of certain Allowances</u></td></tr>
<tr><th>Section</th><th>Allowance</th><th>Exemption</th></tr>
<tr><td>10(13A)</td><td>House Rent Allowance</td><td>Least of the following is exempt:
(a) HRA actually received
(b) Rent paid less 10% of salary
(c) 50% of salary, if accommodation is located in Mumbai, Kolkata, Delhi or Chennai
40% of salary, if the accommodation is located in any other city.</td></tr>
<tr><td>10(14)(ii)</td><td>Children education allowance</td><td>₹ 100 per month per child upto maximum of two children</td></tr>
<tr><td></td><td>Transport allowance for commuting between the place of residence and the place of duty.</td><td>₹ 1,600 per month (₹ 3,200 per month for an employee who is blind or deaf or dumb or orthopaedically handicapped)</td></tr>
<tr><td></td><td>Hostel expenditure of employee’s children</td><td>₹ 300 per month per child up to a maximum of two children</td></tr>
</table>

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Exemption of Terminal Benefits

Section	Component of salary	Category of employee	Particulars [Taxability / Exemption under section 10]
10(10)	**Gratuity**	Government	Fully exempt u/s 10(10)(i)
		Non-Government	Least of the following is exempt : (i) ₹ 10 lacs (ii) Gratuity actually received (iii) **In case of employees covered by the Payment of Gratuity Act, 1972** 15/26 x last drawn salary x number of completed years or part in excess of six months **In case of employees not covered by the Payment of Gratuity Act, 1972** 1/2 x average salary of last 10 months x number of completed years of service (fraction to be ignored).
10(10A)	**Pension** Uncommuted pension	Government & Non-Government	Fully taxable.
	Commuted pension	Government/ local authorities/ statutory corporation/ members of Civil services / All-India services / Defence Services.	Fully exempt under section 10(10A)(i)
		Other Employees	**If the employee is in receipt of gratuity** The amount exempt would be one-third of the amount of commuted pension which he would have received had he commuted his entire pension. **If the employee is not in receipt of gratuity** The amount exempt would be one-half of the amount of commuted pension which he would have received had he commuted his entire pension.

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10(10AA)	**Leave Salary**		
	Received during service	Government & Non-Government	Fully taxable
	Received at the time of retirement, (whether on superannuation or otherwise)	Government	Fully exempt (at the time of retirement)
		Non-Government	Least of the following is exempt : (i) ₹ 3,00,000 (ii) Leave salary actually received (iii) Cash equivalent of leave standing at the credit of the employee [based on on average salary of last 10 months] (maximum 30 days for every year of service) (iv) 10 months salary (based on average salary of last 10 months)
10(10B)	Retrenchment Compensation		Least of the following is exempt : (i) Compensation actually received. (ii) ₹ 5,00,000 (iii) 15/26 × Average salary of last 3 months × Completed years of service and part thereof in excess of 6 months
10(10C)	Voluntary Retirement Compensation	Central and State Government, Public sector company, any other company, local authority, co-operative society, IIT etc.	Least of the following is exempt : (i) Compensation actually received (ii) ₹ 5,00,000 (iii) Last drawn salary x 3 months x completed years of service (iv) Last drawn salary x remaining months of service

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Section 10(5) [Leave Travel Concession]

Exemption is available for 2 trips in a block of 4 calendar years.

S. No.	Journey performed by	Exemption
1	Air	Amount not exceeding air economy fare by the shortest route.
2	Any other mode :	
(i)	Where rail service is available	Amount not exceeding air conditioned first class rail fare by the shortest route.
(ii)	Where rail service is not available	
	a) and public transport does not exist	Amount equivalent to air conditioned first class rail fares by the shortest route
	b) but public transport exists.	Amount not exceeding the first class or deluxe class fare by the shortest route.

Provident Funds - Exemption & Taxability provisions

Particulars	Recognized PF	Unrecognized PF	Statutory PF	Public PF
Employer's Contribution	Amount in excess of 12% of salary is taxable	Not taxable yearly	Fully exempt	N.A.
Employee's Contribution	Eligible for deduction u/s 80C	Not eligible for deduction	Eligible for deduction u/s 80C	Eligible for deduction u/s 80C
Interest Credited	Amount in excess of 9.5% p.a. is taxable	Not taxable yearly	Fully exempt	Fully exempt
Amount received on retirement, etc.	Exempt from tax if employee served a continuous period of 5 years or more or retires before rendering 5 years of service because of reason beyond the control of the employee. In other case, it will be taxable.	Employer's contribution and interest thereon is taxable as salary. Employee's contribution is not taxable. Interest on employee's contribution is taxable under income from other source.	Fully exempt u/s 10(11)	Fully exempt u/s 10(11)

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<table>
<tr><td colspan="4"><u>Valuation of Perquisites [Section 17(2) read with Rule 3]</u></td></tr>
<tr><td colspan="4">(A) Rent-free residential accommodation</td></tr>
<tr><th>S. No. (A)</th><th>Category of Employee (B)</th><th>Unfurnished accommodation (C)</th><th>Furnished accommodation (D)</th></tr>
<tr><td>1</td><td>Government employee</td><td>License fee determined as per government rules as reduced by the rent actually paid by the employee.</td><td>Value determined under column (C)
Add: 10% p.a. of the furniture cost.

However, if the furniture is hired, then hire charges payable/paid should be added to the value determined under column (C), as reduced by charges recovered from employee.</td></tr>
<tr><td>2</td><td>Non-government employee</td><td><u>Where accommodation is owned by employer</u>
<table>
<tr><th>Location</th><th>Perquisite value</th></tr>
<tr><td>In cities having a population > 25 lacs as per 2001 census.</td><td>15% of salary</td></tr>
<tr><td>In cities having a population > 10 lacs ≤ 25 lacs as per 2001 census.</td><td>10% of salary</td></tr>
<tr><td>In other areas</td><td>7.5% of salary</td></tr>
</table>
The perquisite value should be arrived at by reducing the rent, if any, actually paid by the employee, from the above value.</td><td>Value determined under column (C)
Add: 10% p.a. of the furniture cost.

However, if the furniture is hired, then hire charges payable/paid should be added to the value determined under column (C), as reduced by charges recovered from employee.</td></tr>
</table>

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		Where the accommodation is taken on lease or rent by employer Lower of the following is taxable: (a) actual amount of lease rent paid or payable by employer or (b) 15% of salary The lower of the above should be reduced by the rent, actually paid by the employee, to arrive at the perquisite value.	Value determined under column (C) *Add:* 10% p.a. of the furniture cost. However, if the furniture is hired, then hire charges payable/paid should be added to the value determined under column (C), as reduced by charges recovered from employee.

(B) Interest free or concessional loan

In respect of any loan given by employer to employee or any member of his household (excluding for medical treatment for specified ailments or where loans amount in aggregate does not exceed ₹ 20,000), the interest at the rate charged by SBI as on the first day of the relevant previous year at maximum outstanding monthly balance (aggregate outstanding balance for each loan as on the last day of each month) as reduced by the interest, if any, actually paid by him or any member of his household.

(D) Use of movable assets by employee/ any member of his household

(i)	10% p.a. of actual cost of asset owned by the employer or the amount of hire charges incurred by the employer for the asset hired would be the perquisite value.
(ii)	There would, however, be no perquisite for use of laptops and computers.

(E) Transfer of movable assets

Perquisite value would be the depreciated value of the asset computed by applying the rates of depreciation mentioned in the following table, as reduced by any amount paid by or recovered from the employee.

S. No.	Assets	Rate of depreciation
1	Computers and electronic items	50% of WDV for each completed year of usage
2	Motor cars	20% of WDV for each completed year of usage
3	Other assets	10% on SLM for each completed year of usage

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(F) Motor car

S. No.	Car owned/ hired by	Expenses met by	Wholly official use	Wholly personal use	Partly personal use
1	Employer	Employer	Not a perquisite	Running and maintenance expenses, wear and tear or hire charges, driver salary less amount charged from the employee for such use.	**cc of engine** / **Perquisite value**: upto 1.6 litres – ₹ 1,800 p.m.; above 1.6 litres – ₹ 2,400 p.m. If chauffeur is also provided, ₹ 900 p.m should be added to the above value.
2	Employee	Employer	Not a perquisite	Actual amount of expenditure incurred.	Actual amount of expenditure incurred by the employer as reduced by the perquisite value arrived at in (2) above.
3	Employer	Employee	Not a perquisite	Wear and tear or hire charges, driver salary.	**cc of engine** / **Perquisite value**: upto 1.6 litres – ₹ 600 p.m.; above 1.6 litres – ₹ 900 p.m. If chauffeur is also provided, ₹ 900 p.m should be added to the above value.

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Meaning of Salary:

S. No.	Calculation of exemption of Allowance / Terminal benefit / Valuation of perquisite	Meaning of salary
1	Gratuity (in case of non-Government employees covered by the Payment of Gratuity Act, 1972)	Basic salary and dearness allowance.
2	a) Gratuity (in case of non-Government employee not covered by Payment of Gratuity Act, 1972) b) Leave Salary c) House Rent Allowance d) Recognized Provident Fund e) Voluntary Retirement Compensation	Basic salary and dearness allowance, if provided in terms of employment, and commission calculated as a fixed percentage of turnover.
3	Rent free accommodation and concessional accommodation	All pay, allowance, bonus or commission or any monetary payment by whatever name called but excludes- (1) Dearness allowance not forming part of computation of superannuation or retirement benefit (2) employer's contribution to the provident fund account of the employee; (3) allowances which are exempted from the payment of tax; (4) value of the perquisites specified in section 17(2); (5) any payment or expenditure specifically excluded under the proviso to section 17(2) i.e., medical expenditure/payment of medical insurance premium specified therein. (6) lump-sum payments received at the time of termination or service or superannuation or voluntary retirement.

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<table>
<tr><td colspan="3"><u>Deductions from gross salary [Section 16]</u></td></tr>
<tr><td rowspan="4">(1)</td><td colspan="2">Entertainment allowance (allowable only in the case of government employees) [Section 16(ii)]
Least of the following is allowed as deduction:</td></tr>
<tr><td>(1)</td><td>₹ 5,000</td></tr>
<tr><td>(2)</td><td>1/5th of basic salary</td></tr>
<tr><td>(3)</td><td>Actual entertainment allowance received</td></tr>
<tr><td>(2)</td><td colspan="2">Profession tax [Section 16(iii)]
Any sum paid by the assessee on account of tax on employment is allowable as deduction.
In case profession tax is paid by employer on behalf of employee, the amount paid shall be included in gross salary as a perquisite and then deduction can be claimed.</td></tr>
<tr><td colspan="3"><u>Relief when salary is paid in arrears or in advance [Section 89]</u></td></tr>
<tr><td rowspan="3">Step 1</td><td colspan="2">Calculate tax payable of the previous year in which the arrears/advance salary is received by considering:</td></tr>
<tr><td>(a)</td><td>Total Income inclusive of additional salary</td></tr>
<tr><td>(b)</td><td>Total Income exclusive of additional salary</td></tr>
<tr><td>Step 2</td><td colspan="2">Compute the difference the tax calculated in Step 1 and Step 2 i.e., (a) – (b)</td></tr>
<tr><td rowspan="3">Step 3</td><td colspan="2">Calculate the tax payable of every previous year to which the additional salary relates:</td></tr>
<tr><td>(a)</td><td>On total income including additional salary of that particular previous year</td></tr>
<tr><td>(b)</td><td>On total income excluding additional salary.</td></tr>
<tr><td>Step 4</td><td colspan="2">Calculate the difference between (a) and (b) in Step 3 for every previous year to which the additional salary relates and aggregate the same.</td></tr>
<tr><td>Step 5</td><td colspan="2">Relief u/s 89(1) = Amount calculated in Step 2 – Amount calculated in Step 4</td></tr>
</table>

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Question 1

Mr. Harish, aged 52 years, is the Production Manager of XYZ Ltd. From the following details, compute the taxable income for the assessment year 2017-18.

Basic salary	*₹ 50,000 per month*
Dearness allowance	*40% of basic salary*
Transport allowance (for commuting between place of residence and office)	*₹ 3,000 per month*
Motor car running and maintenance charges fully paid by employer (The motor car is owned by the company and driven by the employee. The engine cubic capacity is above 1.60 litres. The motor car is used for both official and personal purpose by the employee.)	*₹ 60,000*
Expenditure on accommodation in hotels while touring on official duties met by the employer	*₹ 80,000*
Loan from recognized provident fund (maintained by the employer)	*₹ 60,000*
Lunch provided by the employer during office hours.	
Cost to the employer	*₹ 24,000*
Computer (cost ₹ 35,000) kept by the employer in the residence of Mr. Harish from 1.06.2016	
Mr. Harish made the following payments:	
Medical insurance premium: Paid in Cash	*₹ 4,800*
Paid by account payee crossed cheque	*₹ 25,700*

Answer

Computation of taxable income of Mr. Harish for the A.Y.2017-18

Particulars	₹	₹
Basic salary (₹ 50,000 x 12)		6,00,000
Dearness allowance @ 40% of basic salary		2,40,000
Transport allowance (₹ 3,000 x 12)	36,000	
Less : Exemption under section 10(14) (₹ 1,600 x 12)	19,200	16,800
Motor car running & maintenance charges paid by employer **(See Note-1)**		28,800
Expenditure on accommodation in hotels while touring on official duty is not a perquisite in the hands of employee and hence not chargeable to tax		Nil
Loan from recognized provident fund – not chargeable to tax		Nil

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Value of lunch provided during office hours	24,000	
Less: Exempt under Rule 3(7)(iii) **(See Note-2)**	15,000	9,000
Computer provided in the residence of employee by the employer – not chargeable to tax [Rule 3(7)(vii)]		Nil
Gross Salary		**8,94,600**
Less : Deduction under Chapter VI-A		
Deduction under section 80D in respect of medical insurance premium paid by cheque amounting to ₹ 25,700 but restricted to ₹25,000 **(See Note-3)**		25,000
Taxable income		**8,69,600**

Notes:

1. As per Rule 3(2), if the motor car (whose engine cubic capacity is above 1.60 litres) is owned by the employer and is used for both official and personal purpose by the employee, then, the value of perquisite for use of motor car would be ₹ 2,400 per month.

   Therefore, value of perquisite for use of motor car would be ₹ 2,400 x 12 = ₹ 28,800

2. As per Rule 3(7)(iii), lunch provided by the employer during office hours is not considered as perquisite upto ₹ 50 per meal. Since, the number of working days is not given in the question, it is assumed to be 300 days during the F.Y. 2016-17. Therefore, ₹ 15,000 (i.e. 300 x ₹ 50) would be exempt and the balance ₹ 9,000 (i.e. ₹ 24,000 - ₹ 15,000) would be taxable.

3. Medical insurance premium paid in cash of ₹ 4,800 is not allowable as deduction under section 80D. Further, deduction for medical insurance premium paid through cheque is restricted to ₹ 25,000, which is the maximum deduction allowable.

Question 2

Mr. Balaji, employed as Production Manager in Beta Ltd., furnishes you the following information for the year ended 31.03.2017:

(i) Basic salary upto 31.10.2016 ₹ 50,000 p.m.
Basic salary from 01.11.2016 ₹ 60,000 p.m.
Note: Salary is due and paid on the last day of every month.

(ii) Dearness allowance @ 40% of basic salary.

(iii) Bonus equal to one month salary. Paid in October 2016 on basic salary plus dearness allowance applicable for that month.

(iv) Contribution of employer to recognized provident fund account of the employee@16% of basic salary.

(v) Profession tax paid ₹ 3,000 of which ₹ 2,000 was paid by the employer.

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(vi) Facility of laptop and computer was provided to Balaji for both official and personal use. Cost of laptop ₹ 45,000 and computer ₹ 35,000 were acquired by the company on 01.12.2016.

(vii) Motor car owned by the employer (cubic capacity of engine exceeds 1.60 litres) provided to the employee from 01.11.2016 meant for both official and personal use. Repair and running expenses of ₹ 45,000 from 01.11.2016 to 31.03.2017, were fully met by the employer. The motor car was self-driven by the employee.

(viii) Leave travel concession given to employee, his wife and three children (one daughter aged 7 and twin sons aged 3). Cost of air tickets (economy class) reimbursed by the employer ₹ 30,000 for adults and ₹ 45,000 for three children. Balaji is eligible for availing exemption this year to the extent it is permissible in law.

Compute the salary income chargeable to tax in the hands of Mr. Balaji for the assessment year 2017-18.

Answer

Computation of Taxable Salary of Mr. Balaji for A.Y. 2017-18

Particulars	₹
Basic salary [(₹ 50,000 × 7) + (₹ 60,000 × 5)]	6,50,000
Dearness Allowance (40% of basic salary)	2,60,000
Bonus (₹ 50,000 + 40% of ₹ 50,000) (**See Note 1**)	70,000
Employers contribution to recognised provident fund in excess of 12% of salary = 4% of ₹ 6,50,000 (**See Note 4**)	26,000
Professional tax paid by employer	2,000
Perquisite of Motor Car (₹ 2,400 for 5 months) (**See Note 5**)	12,000
Gross Salary	**10,20,000**
Less: Deduction under section 16	
Professional tax (**See Note 6**)	3,000
Taxable Salary	**10,17,000**

Notes:

1. Since bonus was paid in the month of October, the basic salary of ₹ 50,000 for the month of October is considered for its calculation.
2. As per Rule 3(7)(vii), facility of use of laptop and computer is an exempt perquisite, whether used for official or personal purpose or both.
3. Mr. Balaji can avail exemption under section 10(5) on the entire amount of ₹ 75,000 reimbursed by the employer towards Leave Travel Concession since the same was availed for himself, his wife and three children and the journey was undertaken by economy class airfare. The restriction imposed for two children is not applicable in case of multiple births which take place after the first child.

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It is assumed that the Leave Travel Concession was availed for journey within India.

4. It is assumed that dearness allowance does not form part of salary for computing retirement benefits.

5. As per the provisions of Rule 3(2), in case a motor car (engine cubic capacity exceeding 1.60 liters) owned by the employer is provided to the employee without chauffeur for personal as well as office use, the value of perquisite shall be ₹ 2,400 per month. The car was provided to the employee from 01.11.2016, therefore the perquisite value has been calculated for 5 months.

6. As per section 17(2)(iv), a "perquisite" includes any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the assessee. Therefore, professional tax of ₹ 2,000 paid by the employer is taxable as a perquisite in the hands of Mr. Balaji. As per section 16(iii), a deduction from the salary is provided on account of tax on employment i.e. professional tax paid during the year.

Therefore, in the present case, the professional tax paid by the employer on behalf of the employee ₹ 2,000 is first included in the salary and deduction of the entire professional tax of ₹ 3,000 is provided from salary.

Question 3

From the following details, find out the salary chargeable to tax for the A.Y.2017-18 -

Mr. X is a regular employee of Rama & Co., in Gurgaon. He was appointed on 1.1.2016 in the scale of 20,000-1,000-30,000. He is paid 10% D.A. & Bonus equivalent to one month pay based on salary of March every year. He contributes 15% of his pay and D.A. towards his recognized provident fund and the company contributes the same amount.

He is provided free housing facility which has been taken on rent by the company at ₹ 10,000 per month. He is also provided with following facilities:

(i) Facility of laptop costing ₹ 50,000.

(ii) Company reimbursed the medical treatment bill of his brother of ₹ 25,000, who is dependent on him.

(iii) The monthly salary of ₹ 1,000 of a house keeper is reimbursed by the company.

(iv) A gift voucher of ₹ 10,000 on the occasion of his marriage anniversary.

(v) Conveyance allowance of ₹ 1,000 per month is given by the company towards actual reimbursement.

(vi) He is provided personal accident policy for which premium of ₹ 5,000 is paid by the company.

(vii) He is getting telephone allowance @ ₹ 500 per month.

(viii) Company pays medical insurance premium of his family of ₹ 10,000.

Answer

Computation of taxable salary of Mr. X for A.Y. 2017-18

Particulars	₹
Basic pay [(₹ 20,000×9) + (₹ 21,000×3)] = ₹ 1,80,000 + ₹ 63,000	2,43,000
Dearness allowance [10% of basic pay]	24,300
Bonus	21,000
Employer's contribution to Recognized Provident Fund in excess of 12% (15%-12% =3% of ₹ 2,67,300) [See Note 1 below]	8,019
Taxable allowances	
Telephone allowance	6,000
Taxable perquisites	
Rent-free accommodation [See Note 1 & 2 below]	44,145
Medical reimbursement (₹ 25,000 - ₹ 15,000) [See Note 4 below]	10,000
Reimbursement of salary of housekeeper	12,000
Gift voucher [See Note 6 below]	10,000
Salary income chargeable to tax	**3,78,464**

Notes:

1. It has been assumed that dearness allowance forms part of salary for retirement benefits and accordingly, the perquisite value of rent-free accommodation and employer's contribution to recognized provident fund have been worked out.

2. Where the accommodation is taken on lease or rent by the employer, the value of rent-free accommodation provided to employee would be actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower.

   For the purposes of valuation of rent free house, salary includes:

   (i) Basic salary i.e., ₹ 2,43,000

   (ii) Dearness allowance (assuming that it is included for calculating retirement benefits) i.e. ₹ 24,300

   (iii) Bonus i.e., ₹ 21,000

   (iv) Telephone allowance i.e., ₹ 6,000

   Therefore, salary works out to

   2,43,000 + 24,300 + 21,000 +6,000 = 2,94,300.

   15% of salary = 2,94,300 × 15/100 = 44,145

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Value of rent-free house = Lower of rent paid by the employer (i.e. ₹ 1,20,000) or 15% of salary (i.e., ₹ 44,145).

Therefore, the perquisite value is ₹ 44,145.

3. Facility of use of laptop is not a taxable perquisite.
4. Clause (v) of the proviso to section 17(2) exempts any sum paid by the employer in respect of any expenditure actually incurred by the employee on his medical treatment or treatment of any member of his family to the extent of ₹ 15,000. Therefore, in this case, the balance of ₹ 10,000 (i.e., ₹ 25,000 – ₹ 15,000) is a taxable perquisite. Medical insurance premium paid by employer is exempt.
5. Conveyance allowance is exempt since it is based on actual reimbursement for official purposes.
6. The value of any gift or voucher or token in lieu of gift received by the employee or by member of his household below ₹ 5,000 in aggregate during the previous year is exempt. In this case, the gift voucher was received on the occasion of marriage anniversary and the sum exceeds the limit of ₹ 5,000.

   Therefore, the entire amount of ₹ 10,000 is liable to tax as perquisite.

   Note - *An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000.*
7. Premium of ₹ 5,000 paid by the company for personal accident policy is not liable to tax.

Question 4

From the following details, find out the salary chargeable to tax of Mr. Anand for the assessment year 2017-18:

Mr. Anand is a regular employee of Malpani Ltd. in Mumbai. He was appointed on 01-03-2016 in the scale of 25,000-2,500-35,000. He is paid dearness allowance (which forms part of salary for retirement benefits) @ 15% of basic pay and bonus equivalent to one and a half month's basic pay as at the end of the year. He contributes 18% of his salary (basic pay plus dearness allowance) towards recognized provident fund and the Company contributes the same amount.

He is provided free housing facility which has been taken on rent by the Company at ₹ 15,000 per month. He is also provided with following facilities:

(i) The Company reimbursed the medical treatment bill of ₹ 40,000 of his daughter, who is dependent on him.

(ii) The monthly salary of ₹ 2,000 of a house keeper is reimbursed by the Company.

(iii) He is getting telephone allowance @ ₹ 1,000 per month.

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(iv) A gift voucher of ₹ 4,700 was given on the occasion of his marriage anniversary.

(v) The Company pays medical insurance premium to effect an insurance on the health of Mr. Anand ₹ 12,000.

(vi) Motor car running and maintenance charges of ₹ 36,600 fully paid by employer. (The motor car is owned and driven by Mr. Anand. The engine cubic capacity is below 1.60 litres. The motor car is used for both official and personal purpose by the employee.)

(vii) Value of free lunch provided during office hours is ₹ 2,200.

Answer

Computation of taxable salary of Mr. Anand for A.Y. 2017-18

Particulars	₹
Basic pay [(₹ 25,000×11) + (₹ 27,500×1)] = ₹ 2,75,000 + ₹ 27,500	3,02,500
Dearness allowance [15% of basic pay]	45,375
Bonus [₹ 27,500 × 1.5]	41,250
Employer's contribution to Recognized Provident Fund in excess of 12% (18% - 12% = 6% of ₹ 3,47,875)	20,873
Taxable allowances	
Telephone allowance	12,000
Taxable perquisites	
Rent-free accommodation **[See Note 1 below]**	60,169
Medical reimbursement (₹ 40,000 - ₹ 15,000) **[See Note 2 below]**	25,000
Reimbursement of salary of housekeeper [₹ 2,000 × 12]	24,000
Gift voucher [**See Note 4 below]**	-
Motor car owned and driven by employee, running and maintenance charges borne by the employer [₹ 36,600 - ₹ 21,600 (i.e., ₹ 1,800 × 12)]	15,000
Value of free lunch facility [**See Note 5 below]**	-
Salary income chargeable to tax	**5,46,167**

Notes:

1. Where the accommodation is taken on lease or rent by the employer, the value of rent-free accommodation provided to employee would be actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower.

   For the purposes of valuation of rent free house, salary includes:

(i)	Basic salary	₹ 3,02,500
(ii)	Dearness allowance	₹ 45,375
(iii)	Bonus	₹ 41,250
(iv)	Telephone allowance	₹ 12,000
	Total	₹ 4,01,125

   15% of salary = ₹ 4,01,125 × 15/100 = ₹ 60,169

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	Value of rent-free house will be - Actual amount of lease rental paid by employer (i.e. ₹ 1,80,000) or - 15% of salary (i.e., ₹ 60,169), whichever is lower. Therefore, the perquisite value is ₹ 60,169.
2.	Any sum paid by the employer in respect of any expenditure actually incurred by the employee on his medical treatment or treatment of any member of his family is exempt to the extent of ₹ 15,000. Therefore, in this case, the balance of ₹ 25,000 (i.e., ₹ 40,000 – ₹ 15,000) is a taxable perquisite.
3.	Medical insurance premium paid by the employer to effect an insurance on the health of the employee is fully exempt.
4.	If the value of any gift or voucher or token in lieu of gift received by the employee or by member of his household is less than ₹ 5,000 in aggregate during the previous year, the perquisite value is Nil. In this case, the gift voucher was received on the occasion of marriage anniversary and the sum is less than ₹ 5,000. Therefore, the perquisite value of gift voucher, is Nil.
5.	Free lunch provided by the employer during office hours is not a perquisite, assuming that the value does not exceed ₹ 50 per meal.

Question 5

Shri Hari is the General Manager of ABC Ltd. From the following details, compute the taxable income for the Assessment year 2017-18:

Basic salary	*₹ 20,000 per month*
Dearness allowance	*30% of basic salary*
Transport allowance (for commuting between place of residence and office)	*₹ 2,000 per month*
Motor car running and maintenance charges fully paid by employer	*₹ 36,000*
(The motor car is owned and driven by employee Hari. The engine cubic capacity is below 1.60 litres. The motor car is used for both official and personal purpose by the employee)	
Expenditure on accommodation in hotels while touring on official duties met by the employer.	*₹ 30,000*
Loan from recognised provident fund (maintained by the employer)	*₹ 40,000*
Lunch provided by the employer during office hours.	
Cost to the employer	*₹ 12,000*
Computer (cost ₹ 50,000) kept by the employer in the residence of Hari from 1.10.2016	
Hari made the following payments:	
Medical insurance premium : Paid in cash	*₹ 3,000*
Paid by cheque	*₹ 27,000*

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Answer

Computation of taxable income of Shri Hari for the A.Y. 2017-18

Particulars	₹	₹
Basic salary (₹ 20,000 x 12)		2,40,000
Dearness allowance @ 30%		72,000
Transport allowance (₹ 2,000 x 12)	24,000	
Less: Exemption under section 10(14) (read with Rule 2BB @ ₹ 1,600 p.m.)	19,200	4,800
Motor car maintenance borne by employer [₹ 36,000 - ₹ 21,600 (i.e., ₹ 1,800 × 12)]		14,400
Expenditure on accommodation while on official duty not a perquisite and hence not chargeable to tax		Nil
Loan from recognized provident fund – not chargeable to tax		Nil
Value of lunch provided during working hours (not chargeable to tax as per rule 3(7)(iii)-free food provided by the employer during working hours is not treated as perquisite provided that the value thereof does not exceed fifty rupees per meal)		Nil
Computer provided in the residence of employee by the employer – not chargeable to tax [Rule 3(7)(vii)]		Nil
Gross Salary		**3,31,200**
Less: Deduction under Chapter VI-A		
Deduction under section 80D in respect of medical insurance premium paid by cheque, restricted to ₹ 25,000	25,000	
Premium paid in cash not eligible for deduction	Nil	25,000
Taxable income		**3,06,200**

Question 6

Mr. Vignesh, Finance Manager of KLM Ltd., Mumbai, furnishes the following particulars for the financial year 2016-17:

(i) Salary ₹ 46,000 per month

(ii) Value of medical facility in a hospital maintained by the company ₹ 7,000

(iii) Rent free accommodation owned by the company

(iv) Housing loan of ₹ 6,00,000 given on 01.04.2016 at the interest rate of 6% p.a. (No repayment made during the year). The rate of interest charged by State Bank of India (SBI) as on 01.04.2016 in respect of housing loan is 10%.

(v) Gifts in kind made by the company on the occasion of wedding anniversary of Mr. Vignesh ₹ 4,750.

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(vi) A wooden table and 4 chairs were provided to Mr. Vignesh at his residence (dining table). This was purchased on 1.5.2013 for ₹ 60,000 and sold to Mr. Vignesh on 1.8.2016 for ₹ 30,000.

(vii) Personal purchases through credit card provided by the company amounting to ₹ 10,000 was paid by the company. No part of the amount was recovered from Mr. Vignesh.

(viii) An ambassador car which was purchased by the company on 16.7.2013 for ₹ 2,50,000 was sold to the assessee on 14.7.2016 for ₹ 80,000.

Other income received by the assessee during the previous year 2016-17:

	Particulars	***₹***
(a)	*Interest on Fixed Deposits with a company*	*5,000*
(b)	*Income from specified mutual fund*	*3,000*
(c)	*Interest on bank fixed deposits of a minor married daughter*	*3,000*

(ix) Contribution to LIC towards premium under section 80CCC ₹ 1,00,000

(x) Deposit in PPF Account made during the year 2016-17 ₹ 40,000

Compute the taxable income of Mr. Vignesh and the tax thereon for the Assessment year 2017-18.

Answer

Computation of taxable income of Mr. Vignesh for the Assessment Year 2017-18

	Particulars	**₹**	**₹**
(a)	Income from salaries (See Working Note below)		7,62,800
(b)	Income from other sources		
	(i) Interest on fixed deposit with a company	5,000	
	(ii) Income from specified mutual fund exempt under section 10(35)	Nil	
	(iii) Interest on Fixed Deposit received by minor daughter (₹ 3,000 - ₹ 1500)	1,500	6,500
Gross total income			**7,69,300**
	Less: Deductions under Chapter VI-A		
	Section 80C – PPF	40,000	
	Section 80CCC	1,00,000	1,40,000
Total Income			**6,29,300**
	Tax on total income		50,860
	Add: Education cess @ 2%		1,017

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	Add : Secondary and Higher Education cess @ 1%		509
	Total tax liability		**52,386**
	Total tax liability (rounded off)		**52,390**

Working Note:

Computation of salary income of Mr. Vignesh for the Assessment Year 2017-18

Particulars		₹
Income under the head "salaries"		
Salary [₹ 46,000 x 12]		5,52,000
Medical facility [in the hospital maintained by the company is exempt]		–
Rent free accommodation		
15% of salary is taxable (i.e. ₹ 5,52,000 × 15% as per Rule 3(1))		82,800
Use of dining table for 4 months		
[₹ 60,000 x 10 /100 x 4 /12]		2,000
Valuation of perquisite of interest on loan		
[Rule 3(7)(i)] – 10% is taxable which is to be reduced by actual rate of interest charged i.e. [10% - 6% = 4%]		24,000
Gift given on the occasion of wedding anniversary ₹ 4,750 is exempt, since its value is less than ₹ 5,000		-
Perquisite on sale of dining tables		
Cost	60,000	
Less: Depreciation on straight line method @ 10% for 3 years	18,000	
Written Down Value	42,000	
Less: Amount paid by the assessee	30,000	12,000
Purchase through credit card – not being a privilege but covered by section 17(2)(iv)		10,000
Perquisite on sale of car		
Original cost of car	2,50,000	
Less: Depreciation from 16.7.2013 to 15.7.2014 @ 20%	50,000	
	2,00,000	
Less: Depreciation from 16.7.2014 to 15.7.2015 @ 20%	40,000	
Value as on 14.07.2015- being the date of sale to employee	1,60,000	
Less: Amount received from the assessee on 14.07.2016	80,000	80,000
Income from Salaries		**7,62,800**

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Note: Under Rule 3(7)(viii), while calculating the perquisite value of benefit to the employee arising from the transfer of any movable asset, the normal wear and tear is to be calculated in respect of each completed year during which the asset was put to use by the employer. In the given case the third year of use of ambassador car is completed on 15.7.2016 where as the car was sold to the employee on 14.7.2016. The solution worked out above provides for wear and tear for only two years.

Question 7

Mrs. Lakshmi aged about 66 years is a Finance Manager of M/s. Lakshmi & Co. Pvt. Ltd., based at Calcutta. She is in continuous service since 1975 and receives the following salary and perks from the company during the year ending 31.03.2017:

(i) Basic Salary (₹ 50,000 x 12) = ₹ 6,00,000

(ii) D.A. (₹ 20,000 x 12) = ₹ 2,40,000 (forms part of pay for retirement benefits)

(iii) Bonus – 2 months basic pay.

(iv) Commission – 0.1% of the turnover of the company. The turnover for the F.Y. 2016-17 was ₹ 15.00 crores.

(v) Contribution of the employer and employee to the recognized provident fund Account ₹ 3,00,000 each.

(vi) Interest credited to Recognized Provident Fund Account at 9.5% - ₹ 60,000.

(vii) Rent free unfurnished accommodation provided by the company for which the company pays a rent of ₹ 70,000 per annum.

(viii) Entertainment Allowance – ₹ 30,000.

(ix) Hostel allowance for three children – ₹ 5,000 each.

She makes the following payments and investments :

(i) Premium paid to insure the life of her major son – ₹ 15,000.

(ii) Medical Insurance premium for self – ₹ 6,000 ; Spouse – ₹ 6,000.

(iii) Donation to a public charitable institution registered under 80G ₹ 2,00,000 by way of cheque.

(iv) LIC Pension Fund – ₹ 50,000.

Determine the tax liability for the Assessment Year 2017-18.

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Answer

Computation of Total Income of Mrs. Lakshmi for A.Y. 2017-18

Particulars	₹	₹
Income from salary		
Basic salary		6,00,000
Dearness allowance		2,40,000
Bonus		1,00,000
Commission (calculated as percentage of turnover)		1,50,000
Entertainment allowance		30,000
Children's hostel allowance	15,000	
Less : Exemption (₹ 300 x 12 x 2)	7,200	7,800
Interest credited to recognized provident fund account (exempt)		-
Rent free unfurnished accommodation (Refer Working Note 1)		70,000
Excess contribution to PF by employer (Refer Working Note 2)		1,81,200
Gross salary		**13,79,000**
Less : Deduction under section 80C		
Life insurance premium paid for insurance of major son	15,000	
Contribution to recognized provident fund	3,00,000	
	3,15,000	
Restricted to	1,50,000	
Deduction under section 80CCC in respect of LIC pension fund	50,000	
	2,00,000	
Deduction limited to ₹ 1,50,000 as per section 80CCE		1,50,000
Deduction under section 80D		12,000
Total income before deduction under section 80G		12,17,000
Deduction under section 80G :		
50% of ₹ 1,21,700 (10% total income) (Refer Working Note 3)		60,850
Total income		**11,56,150**
Tax on total income [20,000 + 1,00,000 + (11,56,150 -10,00,000) x 30%]		1,66,845
Add : Education cess @ 2%		3,337
Add : Secondary and higher education cess @ 1%		1,668
Total tax liability		**1,71,850**

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Working Notes:

1. **Value of rent free unfurnished accommodation**

Particulars	₹
Basic salary	6,00,000
Dearness allowance	2,40,000
Bonus	1,00,000
Commission @ 0.1% of turnover	1,50,000
Entertainment allowance	30,000
Children's hostel allowance	7,800
Gross Salary	11,27,800
15% of salary	1,69,170
Actual rent paid by the company	70,000
The least of the above is chargeable perquisite.	

2. **Employer's contribution to P.F. in excess of 12% of salary**

Employer's contribution	₹ 3,00,000
Less : 12% of basic salary, dearness allowance & commission	
12% of ₹ 9,90,000	₹ 1,18,800
	₹ 1,81,200

3. No deduction shall be allowed under section 80G in respect of any sum exceeding ₹ 10,000 unless such sum is paid by any mode other than cash. Here, since the donation of ₹ 2,00,000 is made by cheque, the same is allowed.

Question 8

Mr. M is an area manager of M/s N. Steels Co. Ltd. During the financial year 2016-17, he gets the following emoluments from his employer:

Basic Salary	
Up to 31.8.2016	*₹ 20,000 p.m.*
From 1.9.2016	*₹ 25,000 p.m.*
Transport allowance	*₹ 2,000 p.m.*
Contribution to recognised provident fund	*15% of basic salary*
Children education allowance (Total)	*₹ 500 p.m. for two children*
City compensatory allowance	*₹ 300 p.m.*
Hostel expenses allowance (Total)	*₹ 380 p.m. for two children*
Tiffin allowance (actual expenses ₹ 3,700)	*₹ 5,000 p.a.*
Tax paid on employment	*₹ 2,500*

Compute taxable salary of Mr. M for the Assessment year 2017-18.

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Answer

Computation of taxable salary of Mr. M. for the Assessment Year 2017-18

Particulars	₹	₹
Basic Salary (₹ 20,000 x 5) +(₹ 25,000 x 7)		2,75,000
Transport allowance (₹ 2,000 x 12)	24,000	
Less : Exempt under section 10(14) (₹ 1,600 x 12)	19,200	4,800
Children education allowance (₹ 500 x 12)	6,000	
Less: Exempt under section 10(14) (₹ 100 x 2 x 12)	2,400	3,600
City Compensatory Allowance (₹ 300 x 12)		3,600
Hostel Expenses Allowance (₹ 380 x 12)	4,560	
Less: Exempt under section 10(14) (₹ 300 x 2 x 12 i.e. ₹ 7,200 but restricted to the actual allowance of ₹ 4,560)	4,560	Nil
Tiffin allowance (fully taxable)		5,000
Tax paid on employment [See Note Below]		2,500
Employer's contribution to recognized provident fund in excess of 12% of salary (i.e., 3% of ₹ 2,75,000)		8,250
Gross Salary		**3,02,750**
Less : Tax on employment under section 16(iii)		2,500
Taxable salary		**3,00,250**

Note: *Professional tax paid by employer should be included in the salary of Mr. M as a perquisite since it is discharge of monetary obligation of the employee by the employer. Thereafter, deduction of professional tax paid is allowed to the employee from his gross salary.*

Question 9

From the following details furnished by Mr. Dinesh, a marketing manager of XL Corporation Ltd., Delhi, compute the gross total income for the Assessment Year 2017-18.

Particulars	***Amount (₹)***
Salary including Dearness Allowance	*6,50,000*
Conveyance allowance of ₹ 900 p.m.	*10,800*
Bonus	*50,000*
Salary of servant provided by the employer	*48,000*
Bills paid by the employer for gas, electricity and water provided free of cost at the residence of Mr. Dinesh	*82,000*

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Dinesh purchased a flat in a co-operative housing society in Dwarka, Delhi for self occupation for ₹ 35,00,000 in April 2013, which was financed by a loan from Bank of India of ₹ 20,00,000 @ 11% interest and his own savings of ₹ 5,00,000 and a deposit of ₹ 10,00,000 from Bank of Baroda, to whom he let out his another house in Rohini, Delhi on lease for ten years. The rent payable by Bank of Baroda is ₹ 35,000 per month. Other relevant particulars are given below:

(i) Municipal taxes paid by Dinesh for his flat in Dwarka are ₹ 18,000 per annum and for his house in Rohini are ₹ 12,000 per annum.

(ii) Principal loan amount outstanding as on 01-04-2016 was ₹ 18,50,000.

(iii) He also paid ₹ 8,000 towards insurance of both the houses.

(iv) In the financial year 2015-16, he had gifted ₹ 40,000 each to his wife and minor son. The gifted amounts were advanced to Mr. Sandeep, who is paying interest @ 18% per annum.

(v) Mr. Dinesh's son is studying in a school run by the employer company throughout the financial year 2016-17. The education facility was provided free of cost. The cost of such education in similar school is ₹ 2,500 per month.

(vi) Dinesh also received gifts of ₹ 45,000 each from his two friends during the financial year 2016-17.

Answer

Computation of gross total income of Mr. Dinesh for the A.Y. 2017-18

Particulars	₹	₹
Salaries		
Salary including dearness allowance		6,50,000
Bonus		50,000
Conveyance allowance (Fully exempt under section 10(14)(i) read with Rule 2BB(1)(c), assuming that it is granted to meet the expenditure actually incurred on conveyance in performance of duties of an office or employment of profit).		Nil
Value of perquisites:		
(i) Salary of servant [Rule 3(3)]	48,000	
(ii) Free gas, electricity and water [Rule 3(4)]	82,000	
(iii) Cost of free education provided by employer (₹ 2,500 x 12) is fully taxable, since the cost of education exceeds ₹ 1,000 per month [Rule 3(5)].	30,000	1,60,000
Income chargeable under the head "Salaries"		**8,60,000**

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Income from house property		
Let-out property (At Rohini)		
Gross Annual Value (GAV) (Lease rental is taken as GAV in the absence of other information) (₹ 35,000 × 12)	4,20,000	
Less: Municipal taxes paid	12,000	
Net Annual Value (NAV)	4,08,000	
Less: Deduction under section 24(a): 30% of NAV[1]	1,22,400	
(A)	2,85,600	
Self-occupied property (At Dwarka)		
Net Annual Value (NAV) [Since the property is self-occupied]	Nil	
Less: Deduction under section 24(a)		
Interest on loan from Bank of India @11% of ₹ 18,50,000 restricted to 2,03,500	(2,00,000)	
(B)	(2,00,000)	
Income from house property **[A - B]**		**85,600**
Income from Other Sources		
(i) Interest earned by minor son from advances made out of money gifted to him by his father, Mr. Dinesh, is includible in the hands of Dinesh as per section 64(1A), since all income arising to a minor child is includible in the hands of parent[2] whose total income (before including the income of minor child) is greater (₹ 40,000 x 18%)	7,200	
Less: Exempt under section 10(32)	1,500	
	5,700	
(ii) Interest income earned by Dinesh's wife from advances made out of money gifted to her by her husband, Mr. Dinesh, has to be included in the total income of Mr. Dinesh as per section 64(1) (₹ 40,000 x 18%)	7,200	
(iii) Gift received from two friends [taxable under section 56(2)(vii)] since the aggregate amount received during the year exceeds ₹ 50,000 (₹ 45,000 x 2)	90,000	1,02,900
Gross Total Income		**10,48,500**

[1] No separate deduction is allowable in respect of insurance.

[2] It is assumed that Mr. Dinesh's total income before including the income of minor child is higher than his wife's total income.

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Question 10

Mr. Anand, an employee of XYZ Co. Ltd. at Mumbai and covered by Payment of Gratuity Act, retires at the age of 64 years on 31-12-2016 after completing 33 years and 7 months of service. At the time of retirement, his employer pays ₹ 20,51,640 as Gratuity and ₹ 6,00,000 as accumulated balance of Recognised Provident fund. He is also entitled for monthly pension of ₹ 8,000. He gets 75% of pension commuted for ₹ 4,50,000 on 1st February, 2017.

Determine the salary chargeable to tax for Mr. Anand for the Assessment Year 2017-18 with the help of following information:

	₹
Basic Salary (₹ 80,000 x 9)	*7,20,000*
Bonus	*36,000*
House Rent Allowance (₹ 15,000 x 9)	*1,35,000*
Rent paid by Mr. Anand (₹ 10,000 x 12)	*1,20,000*
Employer contribution towards Recognized Provident Fund	*1,10,000*
Professional Tax paid by Mr. Anand	*2,000*

Note: *Salary and Pension falls due on the last day of each month.*

Answer

Computation of taxable salary of Mr. Anand for the Assessment Year 2017-18

Particulars	₹
Basic Salary (₹ 80,000 x 9)	7,20,000
Bonus	36,000
House Rent Allowance ***(Working Note 1)***	1,17,000
Employer's contribution towards recognized provident fund in excess of 12% of salary [i.e., ₹ 1,10,000 – ₹ 86,400 (12% of ₹ 7,20,000)]	23,600
Gratuity ***(Working Note 2)***	10,51,640
Uncommuted Pension [(₹ 8,000 x 1) + (₹ 2,000 x 2)]	12,000
Commuted Pension ***(Working Note 3)***	2,50,000
Gross Salary	**22,10,240**
Less: Professional tax paid by Mr. Anand [deductible under section 16(iii)]	2,000
Taxable salary	**22,08,240**

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Working Notes:

	Particulars		₹	₹
(1)	**Taxable House Rent Allowance**			
	Actual HRA Received			1,35,000
	As per section 10(13A), least of the following is exempt:			
	(i) Actual HRA received		1,35,000	
	(ii) Excess of rent paid over 10% of salary (basic pay, in this case)			
	- Rent paid (₹ 10,000 x 9)	₹ 90,000		
	- *Less*: 10% of salary (i.e., 10% of ₹ 7,20,000)	₹ 72,000	18,000	
	(iii) 50% of salary (i.e., 50% of ₹ 7,20,000)		3,60,000	
	Least of the above			18,000
	Taxable HRA			**1,17,000**
(2)	**Taxable Gratuity**			
	Actual Gratuity received			20,51,640
	As per section 10(10), least of the following is exempt:			
	(i) Statutory limit		10,00,000	
	(ii) Actual gratuity received		20,51,640	
	(iii) 15 days salary for each completed year of service or part thereof in excess of 6 months i.e., 15/26 x 80,000 x 34		15,69,231	
	Least of the above			10,00,000
	Taxable Gratuity			**10,51,640**
(3)	**Commuted Pension**			
	Since Mr. Anand is a non-government employee in receipt of gratuity, exemption under section 10(10A), would be available to the extent of 1/3rd of the amount of the pension which he would have received had he commuted the whole of the pension.			
	Amount received (Commuted value of 75% of pension)			4,50,000
	Amount exempt from tax = (₹ 4,50,000 x 100/75) x 1/3			2,00,000
	Taxable amount			**2,50,000**
(4)	**Accumulated balance of Recognized Provident Fund (RPF)**			
	₹ 6 lakh, representing the accumulated balance of RPF, received on retirement is exempt since Mr. Anand has rendered a continuous service for a period of 5 years or more (33 years and 7 months) in XYZ Ltd.			

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Question 11

Mr. X retired from the services of M/s Y Ltd. on 31.01.2017, after completing service of 30 years and one month. He had joined the company on 1.1.1987 at the age of 30 years and received the following on his retirement:

(i) Gratuity ₹ 6,00,000. He was covered under the Payment of Gratuity Act, 1972.

(ii) Leave encashment of ₹ 3,30,000 for 330 days leave balance in his account. He was credited 30 days leave for each completed year of service.

(iii) As per the scheme of the company, he was offered a car which was purchased on 01.02.2014 by the company for ₹ 5,00,000. Company has recovered ₹ 2,00,000 from him for the car. Company depreciates the vehicles at the rate of 15% on Straight Line Method.

(iv) An amount of ₹ 3,00,000 as commutation of pension for 2/3 of his pension commutation.

(v) Company presented him a gift voucher worth ₹ 6,000 on his retirement.

(vi) His colleagues also gifted him a Television (LCD) worth ₹ 50,000 from their own contribution.

Following are the other particulars:

(i) He has drawn a basic salary of ₹ 20,000 and 50% dearness allowance per month for the period from 01.04.2016 to 31.01.2017.

(ii) Received pension of ₹ 5,000 per month for the period 01.02.2017 to 31.03.2017 after commutation of pension.

Compute his gross total income from the above for Assessment Year 2017-18.

Answer

Computation of Gross Total Income of Mr. X for A.Y. 2017-18

Particulars	₹
Basic Salary = ₹ 20,000 x 10	2,00,000
Dearness Allowance = 50% of basic salary	1,00,000
Gift Voucher **(See Note - 1)**	6,000
Transfer of car **(See Note - 2)**	56,000
Gratuity **(See Note - 3)**	80,769
Leave encashment **(See Note - 4)**	1,30,000
Uncommuted pension (₹ 5000 x 2)	10,000
Commuted pension **(See Note - 5)**	1,50,000
Taxable Salary /Gross Total Income	**7,32,769**

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Notes:

(1) As per Rule 3(7)(iv), the value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the amount was received on his retirement and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 6,000 is liable to tax as perquisite.

Note - *An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 1,000 and gross taxable income would be ₹ 7,27,769.*

(2) **Perquisite value of transfer of car:** As per Rule 3(7)(viii), the value of benefit to the employee, arising from the transfer of an asset, being a motor car, by the employer is the actual cost of the motor car to the employer as reduced by 20% of such cost for each completed year during which such motor car was put to use by the employer on a written down value basis. Therefore, the value of perquisite on transfer of motor car, in this case, would be:

Particulars	₹
Purchase price (1.2.2014)	5,00,000
Less: Depreciation @ 20%	1,00,000
WDV on 31.1.2015	4,00,000
Less: Depreciation @ 20%	80,000
WDV on 31.1.2016	3,20,000
Less: Depreciation @ 20%	64,000
WDV on 31.1.2017	2,56,000
Less: Amount recovered	2,00,000
Value of perquisite	**56,000**

The rate of 15% as well as the straight line method adopted by the company for depreciation of vehicle is not relevant for calculation of perquisite value of car in the hands of Mr. X.

(3) **Taxable gratuity**

Particulars	₹
Gratuity received	6,00,000
Less : Exempt under section 10(10) - Least of the following:	
(i) Notified limit = ₹ 10,00,000	

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(ii) Actual gratuity = ₹ 6,00,000	
(iii) 15/26 x 30,000 x 30 = ₹ 5,19,231	5,19,231
Taxable Gratuity	**80,769**

(4) **Taxable leave encashment**

Particulars	₹
Leave Salary received	3,30,000
Less : Exempt under section 10(10AA) - Least of the following:	
(i) Notified limit ₹ 3,00,000	
(ii) Actual leave salary ₹ 3,30,000	
(iii) 10 months x ₹ 20,000 ₹ 2,00,000 (assuming that dearness allowance does not form part of pay for retirement benefit)	
(iv) Cash equivalent of leave to his credit ₹ 2,20,000 $\left(\frac{330}{30} \times 20,000\right)$	2,00,000
Taxable Leave encashment	**1,30,000**

Note – *It has been assumed that dearness allowance does not form part of salary for retirement benefits. In case it is assumed that dearness allowance forms part of pay for retirement benefits, then, the third limit for exemption under section 10(10AA) in respect of leave encashment would be ₹ 3,00,000 (i.e. 10 x ₹ 30,000) and the fourth limit ₹ 3,30,000, in which case, the taxable leave encashment would be ₹ 30,000 (₹ 3,30,000 -₹ 3,00,000). In such a case, the gross total income would be ₹ 6,32,769.*

(5) **Commuted Pension**

Since Mr. X is a non-government employee in receipt of gratuity, exemption under section 10(10A) would be available to the extent of 1/3rd of the amount of the pension which he would have received had he commuted the whole of the pension.

Particulars	₹
Amount received	3,00,000
Exemption under section 10(10A) = $\frac{1}{3} \times \left[3,00,000 \times \frac{3}{2}\right]$	1,50,000
Taxable amount	**1,50,000**

(6) The taxability provisions under section 56(2)(vii) are not attracted in respect of television received from colleagues, since television is not included in the definition of property therein.

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Question 12

Mr. Narendra, who retired from the services of Hotel Samode Ltd., on 31.1.2017 after putting on service for 5 years, received the following amounts from the employer for the year ending on 31.3.2017:

- *Salary @ ₹ 16,000 p.m. comprising of basic salary of ₹ 10,000, Dearness allowance of ₹ 3,000, City compensatory allowance of ₹ 2,000 and Night duty allowance of ₹ 1,000.*
- *Pension @ 30% of basic salary from 1.2.2017.*
- *Leave salary of ₹ 75,000 for 225 days of leave accumulated during 5 years @ 45 days leave in each year. He has not availed any earned leave during his tenure of 5 years and utilized only his casual leave.*
- *Gratuity of ₹ 50,000.*

Compute the total income of Mr. Narendra for the assessment year 2017-18.

Answer

Computation of total income of Mr. Narendra for A.Y. 2017-18

Particulars	₹	₹
Income from Salaries		
Gross salary received during 1.4.2016 to 31.1.2017 @ ₹ 16,000 p.m. (₹ 16,000 x 10)		1,60,000
Pension for 2 months @ 30% of the basic salary of ₹ 10,000 p.m.		6,000
Leave Salary	75,000	
Less: Exempt under section 10(10AA) (Note1)	50,000	25,000
Gratuity	50,000	
Less: Exempt under section 10(10) (Note2)	25,000	25,000
Total Income		**2,16,000**

Notes:

1. Leave encashment is exempt to the extent of least of the following:

	Particulars	₹
(i)	Statutory limit	3,00,000
(ii)	Cash equivalent of leave for 30 days for 5 years (₹ 10,000 ×150/30)	50,000
(iii)	10 months average salary (10 x ₹ 10,000)	1,00,000
(iv)	Actual amount received	75,000

Therefore, ₹ 50,000 is exempt under section 10(10AA).

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2. Assuming that the employee is not covered under the Payment of Gratuity Act, 1972, Gratuity is exempt to the extent of least of the following :

	Particulars	₹
(i)	Statutory limit	10,00,000
(ii)	Half month's salary for 5 years of service (5 x ₹ 5,000)	25,000
(iii)	Actual gratuity received	50,000

Therefore, ₹ 25,000 is exempt under section 10(10).

3. It has been assumed that dearness allowance does not form part of salary for retirement benefits and therefore, not included in "Salary" for the purpose of computation of leave encashment and gratuity.

Question 13

Mr. Mohit is employed with XY Ltd. on a basic salary of ₹ 10,000 p.m. He is also entitled to dearness allowance @ 100% of basic salary, 50% of which is included in salary as per terms of employment. The company gives him house rent allowance of ₹ 6,000 p.m. which was increased to ₹ 7,000 p.m. with effect from 1.01.2017. He also got an increment of ₹ 1,000 p.m. in his basic salary with effect from 1.02.2017. Rent paid by him during the previous year 2016-17 is as under:

April and May, 2016 - Nil, as he stayed with his parents

June to October, 2016 - ₹ 6,000 p.m. for an accommodation in Ghaziabad

November, 2016 to March, 2017 - ₹ 8,000 p.m. for an accommodation in Delhi.

Compute his gross salary for assessment year 2017-18.

Answer

Computation of gross salary of Mr. Mohit for A.Y. 2017-18

Particulars	₹
Basic salary [(₹ 10,000 × 10) + (₹ 11,000 × 2)]	1,22,000
Dearness Allowance (100% of basic salary)	1,22,000
House Rent Allowance (See Note below)	21,300
Gross Salary	**2,65,300**

Note: Computation of Taxable House Rent Allowance (HRA)

Particulars	April-May (₹)	June-Oct (₹)	Nov-Dec (₹)	Jan (₹)	Feb-March (₹)
Basic salary per month	10,000	10,000	10,000	10,000	11,000
Dearness allowance (included in salary as per terms of					

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employment) (50% of basic salary)	5,000	5,000	5,000	5,000	5,500
Salary per month for the purpose of computation of house rent allowance	15,000	15,000	15,000	15,000	16,500
Relevant period (in months)	**2**	**5**	**2**	**1**	**2**
Salary for the relevant period (Salary per month × relevant period)	30,000	75,000	30,000	15,000	33,000
Rent paid for the relevant period	Nil	30,000 (₹6,000×5)	16,000 (₹8,000×2)	8,000 (₹8,000×1)	16,000 (₹ 8,000×2)
House rent allowance (HRA) received during the relevant period **(A)**	12,000 (₹6,000×2)	30,000 (₹6,000×5)	12,000 (₹6,000×2)	7,000 (₹7,000×1)	14,000 (₹7,000×2)
Least of the following is exempt [u/s 10(13A)]					
1. Actual HRA received	12,000	30,000	12,000	7,000	14,000
2. Rent paid – 10% of salary	N.A.	22,500	13,000	6,500	12,700
3. 40% of salary (Residence at Ghaziabad–June to Oct, 2016)	N.A.	30,000 (40% × ₹ 75,000)			
50% of salary (Residence at Delhi– Nov'16- March'17)			15,000 (50% × ₹30,000)	7,500 (50% × ₹15,000)	16,500 (50% × ₹33,000)
Exempt HRA (B)	**Nil**	**22,500**	**12,000**	**6,500**	**12,700**
Taxable HRA (Actual HRA – Exempt HRA) **(A-B)**	12,000	7,500	Nil	500	1,300

Taxable HRA (total) = ₹ 12,000 + ₹ 7,500 + ₹ 500 + ₹ 1,300 = ₹ 21,300

Question 14

(i) Mr. Khanna, an employee of IOL, New Delhi, a private sector company, received the following for the financial year 2016-17:

Sl. No.	*Particulars*	*₹*
1.	*Basic pay*	*1,20,000*

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2.	*House rent allowance*	*1,00,000*
3.	*Special allowance*	*30,000*

Mr. Khanna was residing at New Delhi and was paying a rent of ₹ 10,000 a month.

Compute the eligible exemption under section 10(13A) of the Income-tax Act, 1961, in respect of house rent allowance received.

(ii) If Mr. Khanna opts for rent free accommodation whereby IOL would be paying a rent of ₹ 10,000 per month to the landlord and recovers a sum of ₹ 2,500 per month from Mr. Khanna which was in excess of his entitlement, what will be the perquisite value in respect of such rent free accommodation?

(iii) Which of the above would be beneficial to Mr. Khanna i.e., house rent allowance or rent free accommodation?

Answer

(i) The eligible exemption under section 10(13A) in respect of house rent allowance received would be least of the following:

	Particulars	**₹**	**₹**
(a)	Actual house rent allowance (HRA) received		1,00,000
(b)	Excess of rent paid over 10% of basic salary		
	Rent paid (10,000 x 12)	1,20,000	
	Less: 10% of basic pay (i.e. 10% of ₹ 1,20,000)	12,000	1,08,000
(c)	50% of salary (i.e. 50% of ₹ 1,20,000)		60,000

Least of the above is ₹ 60,000.

The house rent allowance received by Mr. Khanna would be exempt to the extent of ₹ 60,000 under section 10(13A). The balance of ₹ 40,000 is includible in his total income.

(ii) Perquisite value in respect of concessional accommodation

As per rule 3(1), where the accommodation is taken on lease or rent by the employer, the actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower, as reduced by the rent, if any, actually paid by the employee is the value of the perquisite.

(a) Actual rent paid by the employer = ₹ 10,000 x 12 = ₹ 1,20,000

(b) 15% of salary = 15% of basic pay plus special allowance =

15% of ₹ 1,50,000 = ₹ 22,500

Lower of the above is ₹ 22,500, which should be reduced by the rent of ₹ 30,000 paid by the employee (i.e.,2,500 × 12 = ₹ 30,000). The perquisite value is, therefore, nil.

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(iii) We have to see the cash flow from both the options to find out which is more beneficial.

Particulars	₹	₹
Option 1: HRA		
Cash inflows [Basic Pay + HRA + Special Allowance]		2,50,000
Less: Cash outflows:		
Rent paid	1,20,000	
Tax (See Working Note 1 below)	Nil	1,20,000
Net cash flow		1,30,000
Option 2: Concessional Accommodation		
Cash inflows [Basic Pay + Special Allowance]		1,50,000
Less: Cash outflows:		
Rent recovery	30,000	
Tax (See Working Note 2 below)	Nil	30,000
Net cash flow		1,20,000

Since the net cash flow is higher in Option 1, Mr. Khanna should opt for HRA, which would be more beneficial to him.

Working Notes:

1. Computation of tax under Option 1 (HRA):

Particulars	₹
Salary:	
Basic Pay	1,20,000
HRA (taxable)	40,000
Special allowance	30,000
Total salary	1,90,000
Tax on ₹ 1,90,000 (including cess)	Nil

2. Computation of tax under Option 2 (Concessional accommodation)

Particulars	₹
Salary:	
Basic Pay	1,20,000
Special allowance	30,000
Concessional accommodation	Nil
Total salary	1,50,000
Tax on ₹ 1,50,000	Nil

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Question 15

Mr. X and Mr. Y are working for M/s. Gama Ltd. As per salary fixation norms, the following perquisites were offered:

(i) For Mr. X, who engaged a domestic servant for ₹ 500 per month, his employer reimbursed the entire salary paid to the domestic servant i.e. ₹ 500 per month.

(ii) For Mr. Y, he was provided with a domestic servant @ ₹ 500 per month as part of remuneration package.

You are required to comment on the taxability of the above in the hands of Mr. X and Mr. Y, who are not specified employees.

Answer

In the case of Mr. X, it becomes an obligation which the employee would have discharged even if the employer did not reimburse the same. Hence, the perquisite will be covered under section 17(2)(iv) and will be taxable in the hands of Mr. X. This is taxable in the case of all employees.

In the case of Mr. Y, it cannot be considered as an obligation which the employee would meet. The employee might choose not to have a domestic servant. This is taxable only in the case of specified employees covered by section 17(2)(iii). Hence, there is no perquisite element in the hands of Mr. Y.

Question 16

The following benefits have been granted by Ved Software Ltd. to one of its employees Mr. Badri:

(i) Housing loan @ 6% per annum. Amount outstanding on 1.4.2016 is ₹ 6,00,000. Mr. Badri pays ₹ 12,000 per month towards principal, on 5th of each month.

(ii) Air-conditioners purchased 4 years back for ₹ 2,00,000 have been given to Mr. Badri for ₹ 90,000.

Compute the chargeable perquisite in the hands of Mr. Badri for the A.Y. 2017-18.

The lending rate of State Bank of India as on 1.4.2016 for housing loan may be taken as 10%.

Answer

Perquisite value for housing loan: The value of the benefit to the assessee resulting from the provision of interest-free or concessional loan made available to the employee or any member of his household during the relevant previous year by the employer or any person on his behalf shall be determined as the sum equal to the interest computed at the rate charged per annum by the State Bank of India (SBI) as on the 1st day of the relevant previous year in respect of loans for the same purpose advanced by it. This rate should be applied on the

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maximum outstanding monthly balance and the resulting amount should be reduced by the interest, if any, actually paid by him.

"Maximum outstanding monthly balance" means the aggregate outstanding balance for loan as on the last day of each month.

The perquisite value for computation is 10% - 6% = 4%

Month	Maximum outstanding balance as on last date of month (₹)	Perquisite value at 4% for the month (₹)
April, 2016	5,88,000	1,960
May, 2016	5,76,000	1,920
June, 2016	5,64,000	1,880
July, 2016	5,52,000	1,840
August, 2016	5,40,000	1,800
September, 2016	5,28,000	1,760
October, 2016	5,16,000	1,720
November, 2016	5,04,000	1,680
December, 2016	4,92,000	1,640
January, 2017	4,80,000	1,600
February, 2017	4,68,000	1,560
March, 2017	4,56,000	1,520
	Total value of this perquisite	**20,880**

Perquisite Value of Air Conditioners

Particulars	₹
Original cost	2,00,000
Depreciation on SLM basis for 4 years @10% i.e. ₹ 2,00,000 x10% x 4	80,000
Written down value	**1,20,000**
Amount recovered from the employee	90,000
Perquisite value	**30,000**

Chargeable perquisite in the hands of Mr. Badri for the assessment year 2017-18

Particulars	₹
Housing loan	20,880
Air Conditioner	30,000
Total	**50,880**

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Question 17

Shri Bala employed in ABC Co. Ltd. as Finance Manager gives you the list of perquisites provided by the company to him for the entire financial year 2016-17:

(i) Medical facility given to his family in a hospital maintained by the company. The estimated value of benefit because of such facility is ₹ 40,000.

(ii) Domestic servant was provided at the residence of Bala. Salary of domestic servant is ₹ 1,500 per month. The servant was engaged by him and the salary is reimbursed by the company (employer).

In case the company has employed the domestic servant, what is the value of perquisite?

(iii) Free education was provided to his two children Arthy and Ashok in a school maintained and owned by the company. The cost of such education for Arthy is computed at ₹ 900 per month and for Ashok at ₹ 1,200 per month. No amount was recovered by the company for such education facility from Bala.

(iv) The employer has provided movable assets such as television, refrigerator and air-conditioner at the residence of Bala. The actual cost of such assets provided to the employee is ₹ 1,10,000.

(v) A gift voucher worth ₹ 10,000 was given on the occasion of his marriage anniversary. It is given by the company to all employees above certain grade.

(vi) Telephone provided at the residence of Shri Bala and the bill aggregating to ₹ 25,000 paid by the employer.

State the taxability or otherwise of the above said perquisites and compute the total value of taxable perquisites.

Answer

Taxability of perquisites provided by ABC Co. Ltd. to Shri Bala

(i) Medical facility to employees' family in a hospital maintained by the employer is not a taxable perquisite. Regardless of the estimated value of benefit arising from such facility to the employee, it is exempt from tax. Therefore, the value of perquisite is Nil.

(ii) Domestic servant was employed by the employee and the salary of such domestic servant was paid/reimbursed by the employer. It is taxable as perquisite for all categories of employees.

Taxable perquisite value = ₹ 1,500 × 12 = ₹ 18,000.

If the company had employed the domestic servant and the facility of such servant is given to the employee, then the perquisite is taxable only in the case of specified employees. The value of the taxable perquisite in such a case also would be ₹ 18,000.

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(iii) Where the educational institution is owned by the employer, the value of perquisite in respect of free education facility shall be determined with reference to the reasonable cost of such education in a similar institution in or near the locality. However, there would be no perquisite if the cost of such education per child does not exceed ₹ 1,000 per month.

Therefore, there would be no perquisite in respect of cost of free education provided to his child Arthy, since the cost does not exceed ₹ 1,000 per month.

However, the cost of free education provided to his child Ashok would be taxable, since the cost exceeds ₹ 1,000 per month. The taxable perquisite value would be ₹ 14,400 (₹ 1,200 × 12).

Note – *An alternate view possible is that only the sum in excess of ₹ 1,000 per month is taxable. In such a case, the value of perquisite would be ₹ 2,400.*

(iv) Where the employer has provided movable assets to the employee or any member of his household, 10% per annum of the actual cost of such asset owned or the amount of hire charges incurred by the employer shall be the value of perquisite. However, this will not apply to laptops and computers. In this case, the movable assets are television, refrigerator and air conditioner and actual cost of such assets is ₹ 1,10,000.

The perquisite value would be 10% of the actual cost i.e., ₹ 11,000, being 10% of ₹ 1,10,000.

(v) The value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the amount was received on the occasion of marriage anniversary and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 10,000 is liable to tax as perquisite.

Note - *An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001 that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000.*

Total value of taxable perquisite = ₹ 53,400 [i.e. ₹ 18,000 + 14,400 + 11,000 + 10,000].

(v) Telephone provided at the residence of the employee and payment of bill by the employer is a tax free perquisite.

Note *- In case the alternate views are taken for items (iii) & (v), the total value of taxable perquisite would be ₹ 36,400 [i.e., ₹ 18,000 + 2,400 + 11,000 + 5,000].*

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Question 18

Ms. Rakhi is an employee in a private company. She receives the following medical benefits from the company during the previous year 2016-17:

			₹
1	*Reimbursement of following medical expenses incurred by Ms. Rakhi*		
	(A)	*On treatment of her self employed daughter in a private clinic*	*4,000*
	(B)	*On treatment of herself by family doctor*	*8,000*
	(C)	*On treatment of her mother-in-law dependent on her, in a nursing home*	*5,000*
2	*Payment of premium on Mediclaim Policy taken on her health*		*7,500*
3	*Medical Allowance*		*2,000 per month*
4	*Medical expenses reimbursed on her son's treatment in a government hospital*		*5,000*
5	*Expenses incurred by company on the treatment of her minor son abroad*		*1,05,000*
6	*Expenses in relation to foreign travel and stay of Rakhi and her son abroad for medical treatment (Limit prescribed by RBI for this is ₹ 2,00,000)*		*1,20,000*

Discuss about the taxability of above benefits and allowances in the hands of Rakhi.

Answer

Tax treatment of medical benefits, allowances and mediclaim premium in the hands of Ms. Rakhi for A.Y. 2017-18

	Particulars	
1.	**Reimbursement of medical expenses incurred by Ms. Rakhi**	
	(A)	The amount of ₹ 4,000 reimbursed by her employer for treatment of her self-employed daughter in a private clinic qualifies for exclusion from perquisite, subject a maximum of ₹ 15,000 as per clause (v) of the first proviso to section 17(2), since daughter falls within the definition of "family", even though she is not a dependent. As per the definition of family, the condition of dependency is relevant only for parents, brothers and sisters of the individual and not for spouse and children.
	(B)	The amount of ₹ 8,000 reimbursed by the employer for treatment of Ms. Rakhi by family doctor qualifies for exclusion from perquisite, subject to a maximum of ₹ 15,000 under clause (v) of the first proviso to section 17(2).

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	(C) The amount of ₹ 5,000 reimbursed by her employer for treatment of her dependant mother-in-law in a nursing home **does not qualify for exclusion** upto ₹ 15,000, since mother-in-law does not fall within the definition of "family", even though she is dependent on Ms. Rakhi. Therefore, the aggregate sum of ₹ 12,000, specified in (A) and (B) above, reimbursed by the employer would be excluded from perquisite [since the same is less than the maximum permissible limit of ₹ 15,000]. However, the sum of ₹ 5,000 specified in (C) above is a taxable perquisite.
2.	Medical insurance premium of ₹ 7,500 paid by the employer for insuring health of Ms. Rakhi is an exempt perquisite as per clause (iii) of the first proviso to section 17(2).
3.	Medical allowance of ₹ 2,000 per month i.e., ₹ 24,000 p.a. is a fully taxable allowance.
4.	As per clause (ii)(a) of the first proviso to section 17(2), reimbursement of medical expenses of ₹ 5,000 on her son's treatment in a hospital maintained by the Government is an exempt perquisite.
5. & 6.	As per clause (vi) of the first proviso to section 17(2), the following expenditure incurred by the employer would be excluded from perquisite subject to certain conditions – (i) Expenditure on medical treatment of the employee, or any member of the family of such employee, outside India **[₹ 1,05,000, in this case];** (ii) Expenditure on travel and stay abroad of the employee or any member of the family of such employee for medical treatment and one attendant who accompanies the patient in connection with such treatment **[₹ 1,20,000, in this case].** The conditions subject to which the above expenditure would be exempt are as follows - (i) The expenditure on medical treatment and stay abroad would be excluded from perquisite to the extent permitted by Reserve Bank of India; (ii) The expenditure on travel would be excluded from perquisite only in the case of an employee whose gross total income, as computed before including the said expenditure, does not exceed ₹ 2 lakh. Assuming that the limit of ₹ 2 lakh prescribed by RBI pertains to both expenditure on medical treatment of minor son as well as expenditure on stay abroad of Ms. Rakhi and her minor son, such expenditure would be excluded from perquisite subject to a maximum of ₹ 2 lakh. If such expenditure is less than ₹ 2 lakh, it would be fully excluded. The foreign travel expenditure of Ms. Rakhi and her minor son borne by the employer would be excluded from perquisite only if the gross total income of Ms. Rakhi, as computed before including the said expenditure, does not exceed ₹ 2 lakh.

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Question 19

AB Co. Ltd. allotted 1000 sweat equity shares to Sri Chand in June 2016. The shares were allotted at ₹ 200 per share as against the fair market value of ₹ 300 per share on the date of exercise of option by the allottee viz. Sri Chand. The fair market value was computed in accordance with the method prescribed under the Act.

(i) What is the perquisite value of sweat equity shares allotted to Sri Chand?

(ii) In the case of subsequent sale of those shares by Sri Chand, what would be the cost of acquisition of those sweat equity shares?

Answer

(i) As per section 17(2)(vi), the value of sweat equity shares chargeable to tax as perquisite shall be the fair market value of such shares on the date on which the option is exercised by the assessee as reduced by the amount actually paid by, or recovered from, the assessee in respect of such shares.

Particulars	₹
Fair market value of 1000 sweat equity shares @ ₹ 300 each	3,00,000
Less: Amount recovered from Sri Chand 1000 shares @ ₹ 200 each	2,00,000
Value of perquisite of sweat equity shares allotted to Sri Chand	**1,00,000**

(ii) As per section 49(2AA), where capital gain arises from transfer of sweat equity shares, the cost of acquisition of such shares shall be the fair market value which has been taken into account for perquisite valuation under section 17(2)(vi).

Therefore, in case of subsequent sale of sweat equity shares by Sri Chand, the cost of acquisition would be ₹ 3,00,000.

Question 20

Mr. Shah an Accounts Manager has retired from JK Ltd. on 15.1.2017, after rendering services for 30 years 7 months. His salary is ₹ 25,000/- p.m. upto 30.09.2016 and ₹ 27,000/- thereafter. He also gets ₹ 2,000/- p.m. as dearness allowance (55% of it is a part of salary for computing retirement benefits). He is not covered by the Payment of Gratuity Act, 1972. He has received ₹ 8 Lacs as gratuity from the employer company. Compute the gratuity taxable in the hands of Mr. Shah.

Answer

Computation of gratuity taxable in the hands of Mr. Shah for the P.Y. 2016-17

As per section 10(10)(iii), gratuity received by an employee would be exempt upto the least of the following limits –

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S.No.	Particulars	₹
(i)	Gratuity received	8,00,000
(ii)	Half-month's salary for every year of completed service **(See Note below)**	4,00,500
(iii)	Monetary limit	10,00,000

Therefore, ₹ 4,00,500 would be exempt under section 10(10)(iii). The balance ₹ 3,99,500 (i.e.₹ 8,00,000 – ₹ 4,00,500) would be taxable.

Note: One of the limits for calculation of gratuity exempt under section 10(10)(iii) is one-half-month's salary for each year of completed service (fraction of a year to be ignored), {{on the basis of average salary for the ten months immediately preceding the month of retirement. In this case, the month of retirement is January, 2017. Therefore, average salary for the months of March 2016 to December 2016 has to be considered. The salary is ₹ 25,000 p.m. upto 30.9.2016 and ₹ 27,000 p.m. from 1.10.2016. Hence, average salary would be ₹ 26,700 {[(₹ 25,000 × 7) + (₹ 27,000 × 3) + (2000× 55%×10)]/10}.

Further, half-month's salary should be multiplied by the number of years of completed service and any fraction of a year has to be ignored. Therefore, in this case, half-month's salary should be multiplied by 30 and the fraction of 7 months should be ignored.

Computation of average salary	₹
Basic salary March 2016 to December 2016 (25,000×7+27,000×3)	2,56,000
Dearness allowance (2,000 × 10 × 55%)	11,000
	2,67,000
Average salary = 2,67,000/10 = ₹ 26,700	
Half-month's salary for every year of completed service (fraction is to be ignored) [30 × 26,700/2]	4,00,500

Question 21

Mr. Alok, a Government employee, retired from service on 31-7-2016 after rendering service of 25 years and 7 months. He received gratuity of ₹ 7,00,000. His salary at the time of retirement was as under:

Basic salary ₹ 16,000 p.m.; Dearness Allowance ₹ 8,000 p.m. (eligible for retirement benefits)

(i) Compute the taxable portion of gratuity.

(ii) If Mr. Alok is not a Government employee but covered by Payment of Gratuity Act, 1972 determine the taxable and exempt portion of gratuity.

Answer

(a) (i) As per section 10(10), gratuity received by a Government employee on retirement is fully exempt from tax. Since Mr. Alok is a government employee, gratuity amounting to ₹ 7,00,000 received would be fully exempt. The taxable portion of gratuity shall be Nil.

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(ii) If Mr. Alok is not a Government employee but covered by the Payment of Gratuity Act, 1972, then, gratuity received by him would be exempt upto least of the following :

Particulars	₹
(i) Statutory limit	10,00,000
(ii) Actual gratuity received	7,00,000
(iii) 15/26 x last drawn salary x years of service (including part of the year in excess of 6 months) 15/26 x ₹ 24,000 x 26 years	3,60,000

Therefore, ₹ 3,60,000 is exempt under section 10(10).

Therefore, taxable portion of gratuity = ₹ 7,00,000 – ₹ 3,60,000 = ₹ 3,40,000

Note: Salary, for the purpose of computation of exempt gratuity, means basic salary plus dearness allowance i.e. ₹ 24,000 (₹ 16,000 + ₹ 8,000).

Question 22

Distinguish between foregoing of salary and surrender of salary.

Answer

Foregoing of salary – Waiver by an employee of his salary is foregoing of salary. Once salary accrues, subsequent waiver does not absolve him from liability to income-tax.

Surrender of salary – If any employee surrenders his salary to the Central Government under the Voluntary Surrender of Salaries (Exemption from Taxation) Act, 1961, the surrendered salary would not be included in computing his taxable income, whether he is a private sector/public sector or Government employee.

Question 23

How is advance salary taxed in the hands of an employee? Is the tax treatment same for loan or advance against salary?

Answer

Advance Salary: Advance salary is taxable when it is received by the employee, irrespective of the fact whether it is due or not.

It may so happen that when advance salary is included and charged in a particular previous year, the rate of tax at which the employee is assessed may be higher than the normal rate of tax to which he would have been assessed. Section 89(1) provides for relief in these types of cases.

Loan or Advance against salary: Loan is different from salary. When an employee takes a loan from his employer, which is repayable in certain specified installments, the loan amount cannot be brought to tax as salary of the employee.

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Similarly, advance against salary is different from advance salary. It is an advance taken by the employee from his employer. This advance is generally adjusted against his salary over a specified time period. It cannot be taxed as salary.

Question 24

Mr. Ashok, an employee of a PSU, furnishes the following particulars for the previous year ending 31.03.2017:

Particulars	₹
(i) Salary income for the year	*7,25,000*
(ii) Salary for financial year 2009-10 received during the year	*80,000*
(iii) Assessed income for the financial year 2009-10	*2,40,000*

You are requested by the assessee to compute relief under section 89 of the Income-tax Act, 1961 and the tax payable for assessment year 2017-18.

The rates of income tax for the assessment year 2010-11 are:

	Tax rate (%)
On first ₹ 1,60,000	*Nil*
On ₹ 1,60,000 – ₹ 3,00,000	*10*
On ₹ 3,00,000 – ₹ 5,00,000	*20*
Above ₹ 5,00,000	*30*
Education cess	*3*

Answer

Computation of relief under section 89 of Mr. Ashok for the A.Y. 2017-18

Particulars				₹	₹
Assessment year 2017-18					
Salary Income for the year excluding arrears					7,25,000
Add: Arrears relating to Financial Year 2009-10					80,000
Total Income (including arrears)					8,05,000
Tax on ₹ 8,05,000					
	First	₹ 2,50,000	Nil	Nil	
	Next	₹ 2,50,000	10%	25,000	
	Balance	₹ 3,05,000	20%	61,000	
		₹ 8,05,000		86,000	

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Add: Education cess @ 2%	1,720	
Secondary and higher education cess @1%	860	
Tax on total income (including arrears) (A)	**88,580**	
Total Income excluding arrears		7,25,000
Tax on ₹ 7,25,000		
First ₹ 2,50,000 Nil	Nil	
Next ₹ 2,50,000 10%	25,000	
Balance ₹ 2,25,000 20%	45,000	
₹ 7,25,000	70,000	
Add : Education cess @ 2%	1,400	
Secondary and higher education cess @ 1%	700	
Tax on total income (excluding arrears) (B)	**72,100**	
Difference between A & B (I)		**16,480**
Assessment Year 2010-11		
Total Income assessed		2,40,000
Add: Arrears relating to Financial year 2009-10		80,000
Total income (including arrears)		3,20,000
Tax on ₹ 3,20,000	18,000	
Add: Education Cess @ 2%	360	
Secondary and higher education cess @1%	180	
Tax on total income (including arrears) (C)	**18,540**	
Total Income excluding arrears		2,40,000
Tax on ₹ 2,40,000	8,000	
Add: Education Cess @ 2%	160	
Secondary and higher education cess @1%	80	
Tax on total income (excluding arrears) (D)	**8,240**	
Difference between C & D (II)		**10,300**
Relief under section 89 (I – II)		**6,180**

Note: *It has been assumed that salary income of ₹ 7,25,000 for the year, as given in the question, does not include salary of ₹ 80,000 for the F.Y. 2009-10 received during the year.*

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Exercise

1. *Where there is a decision to increase the D.A. in March, 2017 with retrospective effect from 1.4.2016, and the increased D.A. is received in April, 2017, the increase is taxable -*
   (a) *in the previous year 2016-17*
   (b) *in the previous year 2017-18*
   (c) *in the respective years to which they relate.*
2. *The entertainment allowance received by a Government employee is exempt up to the lower of the actual entertainment allowance received, 1/5th of basic salary and -*
   (a). *₹ 4,000*
   (b). *₹ 6,000*
   (c). *₹ 5,000.*
3. *Rajesh is provided with a rent free unfurnished accommodation, which is owned by his employer, XY Pvt. Ltd., in New Delhi. The value of perquisite in the hands of Rajesh is -*
   (a). *20% of salary*
   (b). *15% of salary*
   (c). *10% of salary*
4. *Anirudh is provided with furniture to the value of ₹ 70,000 along with house from February, 2016. The actual hire charges paid by his employer for hire of furniture is ₹ 5,000 p.a.. The value of furniture to be included along with value of unfurnished house for A.Y.2017-18 is-*
   (a) *₹ 5,000*
   (b) *₹ 7,000*
   (c) *₹ 14,000*
5. *Employer's contribution to superannuation fund during the previous year 2016-17 is -*
   (a) *subject to fringe benefits in the hands of the employer*
   (b) *fully taxable as perquisite in the hands of the employee*
   (c) *taxable as perquisite in the hands of the employee if it exceeds ₹ 1.50 lakh.*
6. *Write short notes on -*
   (a) *Profits in lieu of salary*
   (b) *Specified employees*
7. *Is retrenchment compensation received by workmen taxable under the Act? If yes, to what extent is it taxable?*
8. *When is provision of medical facilities or assistance by an employer not treated as a perquisite in the hands of the employee? Discuss.*
9. *Can an assessee claim relief under section 89 in respect of VRS compensation of ₹ 6 lakh received by him from his employer, if he has claimed exemption of ₹ 5 lakh in respect of the same under section 10(10C)? Discuss.*
10. *Explain the term "Profit in lieu of salary".*

Answers

1. a; **2.** c; **3.** b; **4.** a; **5.** c

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4 Unit 2 : Income From House Property

Key Points			
Section 22 [Basis of Charge]			
(i)	Determination of annual value of the property is the first step in computation of income under the head "Income from house property".		
(ii)	The annual value of any property comprising of building or land appurtenant thereto, of which the assessee is the owner, is chargeable to tax under the head "Income from house property".		
	(i)	Property should consist of any building or land appurtenant thereto	
		(a)	Buildings include residential buildings as well as factory buildings, offices etc.
		(b)	Land appurtenant means land connected with the building.
		(c)	Income from letting out of vacant land is, however, taxable under the head "Income from other sources
	(ii)	Assessee must be the owner of the property	
		(a)	Owner is the person who is entitled to receive income from the property in his own right.
		(b)	The requirement of registration of the sale deed is not warranted.
		(c)	Ownership includes both free-hold and lease-hold rights.
		(d)	Ownership includes deemed ownership
		(e)	The person who owns the building need not also be the owner of the land upon which it stands.
		(f)	The assessee must be the owner of the house property during the previous year. It is not material whether he is the owner in the assessment year.
	(iii)	The property may be used for any purpose, but it should not be used by the owner for the purpose of any business or profession carried on by him, the profit of which is chargeable to tax.	

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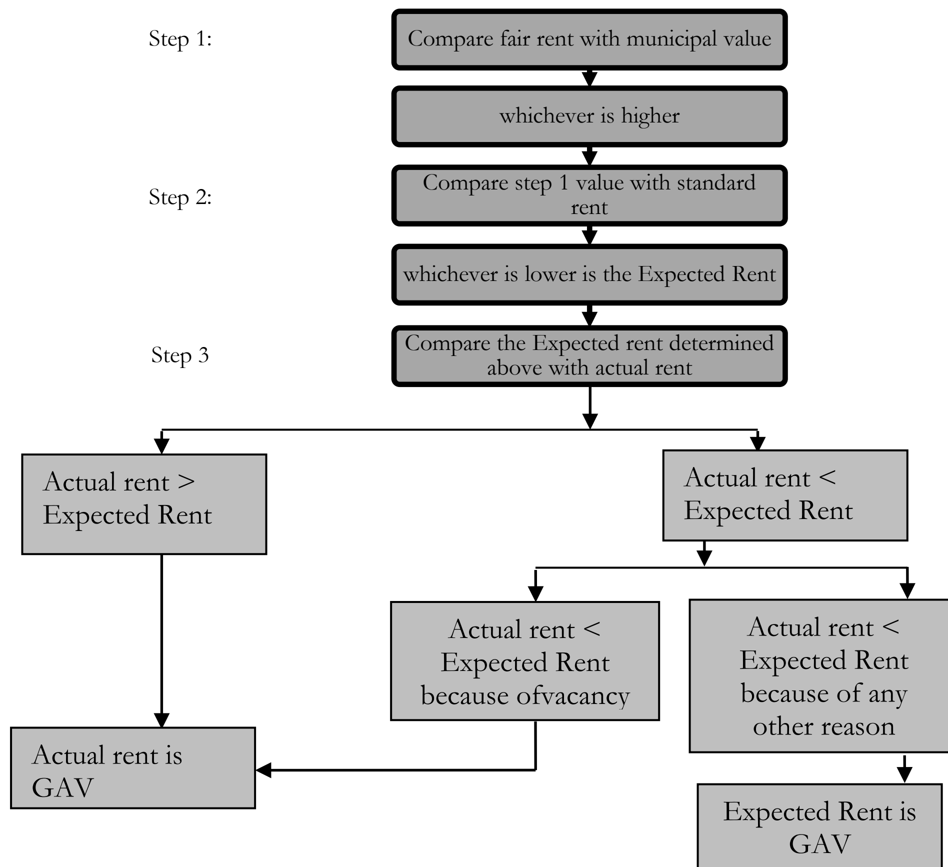
	(iv)	Property held as stock-in-trade etc. Annual value of house property will be charged under the head "Income from house property" in the following cases also –		
		(a)	Where it is held by the assessee as stock-in-trade of a business;	
		(b)	Where the assessee is engaged in the business of letting out of property on rent;	
			Exceptions:	
			(1)	If letting out is supplementary to the main business, the income will be assessed as business income.
			(2)	If letting out of building along with other facilities, like machinery and the two lettings are inseparable, the income will either be assessed as business income or as income from other sources, as the case may be.

Section 23(1) [Determination of Gross Annual Value(GAV) of Let-out Property]



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Computation of "Income from house property" in case of property let out throughout the previous year	
Particulars	**Amount**
Gross Annual Value (GAV) [Calculated as per the chart given above]	A
Less: Municipal taxes (paid by the owner during the previous year)	B
Net Annual Value (NAV) = (A-B)	C
Less: **Deductions under section 24**	
(a) 30% of NAV (irrespective of the actual expenditure incurred) D	
(b) Interest on borrowed capital (actual without any ceiling limit) (See conditions given below) E	
Income from house property (C-D-E)	F

Allowability of interest on borrowed capital under section 24(b)

(a)	Interest payable on loans borrowed can be claimed as deduction.
(b)	Interest payable on a fresh loan taken to repay the original loan is also admissible as deduction.
(c)	Interest payable on borrowed capital for the period prior to the previous year in which the property has been acquired or constructed, can be claimed as deduction over a period of 5 years in equal annual installments commencing from the year of acquisition or completion of construction.
(d)	Interest related to year of completion of construction can be fully claimed irrespective of completion date.

Computation of income from self-occupied property or property unoccupied due to employment, business in another place

Particulars	**Amount**
Annual value under section 23(2)	Nil
Less: **Deduction under section 24** **Interest on borrowed capital** Interest on loan taken for acquisition or construction of house on or after 1.4.99 and same was completed within 5 years from the end of the financial year in which capital was borrowed, interest paid or payable subject to a maximum of ₹ 2,00,000 (including apportioned pre-construction interest).	X

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	In case of loan for acquisition or construction taken prior to 1.4.99 or loan taken for repair, renovation or reconstruction at any point of time, interest paid or payable subject to a maximum of ₹ 30,000.	
Income from house property		(-)X
Other important points		
(i)	If the assessee has occupied more than one house for his own residential purposes, only one house (according to his own choice) is treated as self-occupied and all other houses will be "deemed to be let out".	
(ii)	In case of a house property which is deemed to be let-out, the Expected Rent would be the gross annual value. All deductions permissible to a let-out property would be allowable in case of a "deemed to be let out" property.	
(iii)	If a portion of a property is let-out and a portion is self-occupied, then, the income will be computed separately for let out and self occupied portion.	
Taxability of recovery of unrealised rent & arrears of rent received [New Section 25A]		
(i)	Taxable in the year of receipt/realisation	
(ii)	Deduction@30% of rent received/realised	
(iii)	Taxable even if assessee is not the owner of the property in the financial year of receipt/realisation.	

Question 1

Mr. Vaibhav own five houses at Cochin, all of which are let out. Compute the gross annual value of each house from the information given below: **(₹)**

	House-I	*House-II*	*House-III*	*House-IV*	*House-V*
Municipal value	*1,20,000*	*2,40,000*	*1,10,000*	*90,000*	*75,000*
Fair rent	*1,50,000*	*2,40,000*	*1,14,000*	*84,000*	*80,000*
Standard rent	*1,08,000*	*N.A.*	*1,44,000*	*N.A.*	*78,000*
Actual rent received / receivable	*1,80,000*	*2,10,000*	*1,20,000*	*1,08,000*	*72,000*

Answer

As per section 23(1) Gross Annual Value (GAV) is the higher of Expected rent and actual rent received. Expected rent is higher of municipal value and fair rent but restricted to standard rent.

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Computation of GAV of each house owned by Mr. Vaibhav

(₹)

	Particulars	House-I	House-II	House-III	House-IV	House-V
(i)	Municipal Value	1,20,000	2,40,000	1,10,000	90,000	75,000
(ii)	Fair rent	1,50,000	2,40,000	1,14,000	84,000	80,000
(iii)	**Higher of (i) & (ii)**	**1,50,000**	**2,40,000**	**1,14,000**	**90,000**	**80,000**
(iv)	Standard rent	1,08,000	N.A.	1,44,000	N.A.	78,000
(v)	**Expected rent [Lower of (iii) & (iv)]**	**1,08,000**	**2,40,000**	**1,14,000**	**90,000**	**78,000**
(vi)	Actual rent received/receivable	1,80,000	2,10,000	1,20,000	1,08,000	72,000
	GAV [Higher of (v) & (vi)]	**1,80,000**	**2,40,000**	**1,20,000**	**1,08,000**	**78,000**

Question 2

Two brothers Arun and Bimal are co-owners of a house property with equal share. The property was constructed during the financial year 1998-1999. The property consists of eight identical units and is situated at Cochin.

During the financial year 2016-17, each co-owner occupied one unit for residence and the balance of six units were let out at a rent of ₹ 12,000 per month per unit. The municipal value of the house property is ₹ 9,00,000 and the municipal taxes are 20% of municipal value, which were paid during the year. The other expenses were as follows:

		₹
(i)	*Repairs*	*40,000*
(ii)	*Insurance premium (paid)*	*15,000*
(iii)	*Interest payable on loan taken for construction of house*	*3,00,000*

One of the let out units remained vacant for four months during the year.

Arun could not occupy his unit for six months as he was transferred to Chennai. He does not own any other house.

The other income of Mr. Arun and Mr. Bimal are ₹ 2,90,000 and ₹ 1,80,000, respectively, for the financial year 2016-17.

Compute the income under the head 'Income from House Property' and the total income of two brothers for the assessment year 2017-18.

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Answer

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

Particulars	Arun (₹)	Bimal(₹)
Income from house property		
I. Self-occupied portion (25%)		
Annual value	Nil	Nil
Less: Deduction under section 24(b)		
Interest on loan taken for construction ₹ 37,500 (being 25% of ₹ 1.5 lakh) restricted to maximum of ₹ 30,000 for each co-owner since the property was constructed before 1.04.1999	30,000	30,000
Loss from self occupied property	(30,000)	(30,000)
II. Let-out portion (75%) – See Working Note below	1,25,850	1,25,850
Income from house property	**95,850**	**95,850**
Other Income	2,90,000	1,80,000
Total Income	**3,85,850**	**2,75,850**

Working Note – Computation of income from let-out portion of house property

Particulars	₹	₹
Let-out portion (75%)		
Gross Annual Value		
(a) Municipal value (75% of ₹ 9 lakh)	6,75,000	
(b) Actual rent [(₹ 12000 x 6 x 12) – (₹ 12,000 x 1 x 4)] = ₹ 8,64,000 - ₹ 48,000	8,16,000	
- whichever is higher		8,16,000
Less: Municipal taxes 75% of 1,80,000 (20% of ₹ 9 lakh)		1,35,000
Net Annual Value (NAV)		6,81,000
Less: Deduction under section 24		
(a) 30% of NAV	2,04,300	
(b) Interest on loan taken for the house [75% of ₹ 3 lakh]	2,25,000	4,29,300
Income from let-out portion of house property		2,51,700
Share of each co-owner (50%)		1,25,850

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Question 3

Mr. Raman is a co-owner of a house property along with his brother holding equal share in the property.

Particulars	*₹*
Municipal value of the property	*1,60,000*
Fair rent	*1,50,000*
Standard rent under the Rent Control Act	*1,70,000*
Rent received	*15,000 p.m.*

The loan for the construction of this property is jointly taken and the interest charged by the bank is ₹ 25,000, out of which ₹ 21,000 has been paid. Interest on the unpaid interest is ₹ 450. To repay this loan, Raman and his brother have taken a fresh loan and interest charged on this loan is ₹ 5,000.

The municipal taxes of ₹ 5,100 have been paid by the tenant.

Compute the income from this property chargeable in the hands of Mr. Raman for the A.Y. 2017-18.

Answer

Computation of income from house property of Shri Raman for A.Y. 2017-18

Particulars	₹	₹
Gross Annual Value (See Note 1 below)		1,80,000
Less: Municipal taxes – paid by the tenant, hence not deductible		Nil
Net Annual Value (NAV)		1,80,000
Less: Deductions under section 24		
(i) 30% of NAV	54,000	
(ii) Interest on housing loan (See Note 2 below)		
- Interest on loan taken from bank	25,000	
- Interest on fresh loan to repay old loan for this property	5,000	84,000
Income from house property		**96,000**
50% share taxable in the hands of Shri Raman (See Note 3 below)		**48,000**

Notes:

1. **Computation of Gross Annual Value (GAV)**

   GAV is the higher of Expected rent and actual rent received. Expected rent is the higher of municipal value and fair rent, but restricted to standard rent.

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Particulars	₹	₹	₹	₹
(a) Municipal value of property	1,60,000			
(b) Fair rent	1,50,000			
(c) Higher of (a) and (b)		1,60,000		
(d) Standard rent		1,70,000		
(e) Expected rent [lower of (c) and (d)]			1,60,000	
(f) Actual rent [15,000 x 12]			1,80,000	
(g) Gross Annual Value [higher of (e) and (f)]				1,80,000

2. Interest on housing loan is allowable as a deduction under section 24 on accrual basis. Further, interest on fresh loan taken to repay old loan is also allowable as deduction. However, interest on unpaid interest is not allowable as deduction under section 24.

3. Section 26 provides that where a house property is owned by two or more persons whose shares are definite and ascertainable, the share of each such person in the income of house property, as computed in accordance with sections 22 to 25, shall be included in his respective total income. Therefore, 50% of the total income from the house property is taxable in the hands of Mr. Raman since he is an equal owner of the property.

Question 4

Mr. Krishna owns a residential house in Delhi. The house is having two identical units. First unit of the house is self-occupied by Mr. Krishna and another unit is rented for ₹ 12,000 p.m. The rented unit was vacant for three months during the year. The particulars of the house for the previous year 2016-17 are as under:

Standard Rent	*₹ 2,20,000 p.a.*
Municipal Valuation	*₹ 2,44,000 p.a.*
Fair Rent	*₹ 2,35,000 p.a.*
Municipal tax paid by Mr. Krishna	*12% of the Municipal Valuation*
Light and water charges	*₹ 800 p.m.*
Interest on borrowed capital	*₹ 2,000 p.m.*
Insurance charges	*₹ 3,500 p.a.*
Painting expenses	*₹ 16,000 p.a.*

Compute income from house property of Mr. Krishna for the A.Y.2017-18.

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Answer

Computation of Income from house property of Mr. Krishna for A.Y. 2017-18

	Particulars	₹	₹
(A)	**Rented unit (50% of total area)**		
	Step I - Computation of Expected Rent		
	Municipal valuation (₹ 2,44,000 x ½)	1,22,000	
	Fair rent (₹ 2,35,000 x ½)	1,17,500	
	Standard rent (₹ 2,20,000 x ½)	1,10,000	
	Expected Rent is higher of municipal valuation and fair rent, but restricted to standard rent	1,10,000	
	Step II - Actual Rent		
	Rent receivable for the whole year (₹ 12,000 x 12)	1,44,000	
	Step III – Computation of Gross Annual Value		
	Actual rent received owing to vacancy (₹ 1,44,000 – ₹ 36,000)	1,08,000	
	Since, owing to vacancy, the actual rent received is lower than the Expected Rent, the actual rent received is the Gross Annual value		
	Gross Annual Value (GAV)		**1,08,000**
	Less: Municipal taxes (12% of ₹ 1,22,000)		14,640
	Net Annual Value (NAV)		**93,360**
	Less : Deductions under section 24		
	(a) 30% of NAV	28,008	
	(b) Interest on borrowed capital (₹ 1,000 x 12)	12,000	40,008
	Taxable income from let out portion		**53,352**
(B)	**Self occupied unit (50% of total area)**		
	Annual value	Nil	
	Less : Deduction under section 24:		
	Interest on borrowed capital (₹ 1,000 x 12)	12,000	(12,000)
	Income from house property		**41,352**

Note: *No deduction will be allowed separately for light and water charges, insurance charges and painting expenses.*

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Question 5

Mrs. Rohini Ravi, a citizen of the U.S.A., is a resident and ordinarily resident in India during the financial year 2016-17. She owns a house property at Los Angeles, U.S.A., which is used as her residence. The annual value of the house is $20,000. The value of one USD ($) may be taken as ₹ 60.

She took ownership and possession of a flat in Chennai on 1.7.2016, which is used for self-occupation, while she is in India. The flat was used by her for 7 months only during the year ended 31.3.2017. The municipal valuation is ₹ 32,000 p.m. and the fair rent is ₹ 4,20,000 p.a. She paid the following to Corporation of Chennai :

Property Tax	*₹ 16,200*
Sewerage Tax	*₹ 1,800*

She had taken a loan from Standard Chartered Bank for purchasing this flat. Interest on loan was as under:

	₹
Period prior to 1.4.2016	*49,200*
1.4.2016 to 30.6.2016	*50,800*
1.7.2016 to 31.3.2017	*1,31,300*

She had a house property in Bangalore, which was sold in March, 2014. In respect of this house, she received arrears of rent of ₹ 60,000 in March, 2017. This amount has not been charged to tax earlier.

Compute the income chargeable from house property of Mrs. Rohini Ravi for the assessment year 2017-18, exercising the most beneficial option available.

Answer

Since the assessee is a resident and ordinarily resident in India, her global income would form part of her total income i.e., income earned in India as well as outside India will form part of her total income.

She possesses a self-occupied house at Los Angeles as well as at Chennai. At her option, one house shall be treated as self-occupied, whose annual value will be nil. The other self-occupied house property will be treated as "deemed let out property”.

The annual value of the Los Angeles house is ₹ 12,00,000 and the Chennai flat is ₹ 3,15,000. Since the annual value of Los Angeles house is obviously more, it will be beneficial for her to opt for choosing the same as self-occupied. The Chennai house will, therefore, be treated as "deemed let out property".

As regards the Bangalore house, arrears of rent will be chargeable to tax as income from house property in the year of receipt under section 25A. It is not essential that the assessee should continue to be the owner. 30% of the arrears of rent shall be allowed as deduction.

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Accordingly, the income from house property of Mrs. Rohini Ravi will be calculated as under:

	Particulars	₹	₹
1.	**Self-occupied house at Los Angeles**		
	Annual value	Nil	
	Less: Deduction under section 24	Nil	
	Chargeable income from this house property		Nil
2.	**Deemed let out house property at Chennai**		
	Annual value (Higher of municipal value and fair rent) [4,20,000 x 9/12]		3,15,000
	Less: Municipal Taxes (Property tax + Sewerage tax)		18,000
	Net Annual Value (NAV)		2,97,000
	Less: Deductions under section 24		
	30% of NAV	89,100	
	Interest on borrowed capital (See Note below)	1,91,940	2,81,040
			15,960
3.	**Arrears in respect of Bangalore property(Section 25A)**		
	Arrears of rent received	60,000	
	Less: Deduction @ 30%u/s 25A(2)	18,000	42,000
Income chargeable under the head"Income from house property"			**57,960**

Note : Interest on borrowed capital	₹
Interest for the current year (₹ 50,800 + ₹ 1,31,300)	1,82,100
Add: 1/5th of pre-construction interest (₹ 49,200 x 1/5)	9,840
Interest deduction allowable under section 24	**1,91,940**

Question 6

Mr. A and Mr. B constructed their houses on a piece of land purchased by them at New Delhi. The built up area of each house was 1,000 sq.ft. ground floor and an equal area in the first floor. A started construction on 1-04-2015 and completed on 1-04-2016. B started the construction on 1-04-2015 and completed the construction on 30-06-2016. A occupied the entire house on 01-04-2016. B occupied the ground floor on 01-07-2016 and let out the first floor for a rent of ₹ 15,000 per month. However, the tenant vacated the house on 31-12-2016 and B occupied the entire house during the period 01-01-2017 to 31-03-2017.

Following are the other information

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(i)	*Fair rental value of each unit (ground floor /first floor)*	*₹ 1,00,000 per annum*
(ii)	*Municipal value of each unit (ground floor / first floor)*	*₹ 72,000 per annum*
(iii)	*Municipal taxes paid by*	*A – ₹ 8,000* *B – ₹ 8,000*
(iv)	*Repair and maintenance charges paid by*	*A – ₹ 28,000* *B – ₹ 30,000*

A has availed a housing loan of ₹ 20 lakhs @ 12% p.a. on 01-04-2015. B has availed a housing loan of ₹ 12 lakhs @ 10% p.a. on 01-07-2015. No repayment was made by either of them till 31-03-2017. Compute income from house property for A and B for the previous year 2016-17 (A.Y. 2017-18).

Answer

Computation of income from house property of Mr. A for A.Y. 2017-18

Particulars	₹	₹
Annual value is nil (since house is self occupied)		Nil
Less : Deduction under section 24(b)		
Interest paid on borrowed capital ₹ 20,00,000 @ 12%	2,40,000	
Pre-construction interest ₹ 2,40,000 / 5	48,000	
	2,88,000	
As per second proviso to section 24(b), interest deduction restricted to		2,00,000
Loss under the head "Income from house property" of Mr. A		(2,00,000)

Computation of income from house property of Mr. B for A.Y. 2017-18

Particulars	Ground floor (Self occupied)	First floor
Gross annual value (See Note below)	Nil	90,000
Less :Municipal taxes (for first floor)	____	4,000
Net annual value(A)	Nil	86,000
Less : Deduction under section 24		
(a) 30% of net annual value		25,800
(b) interest on borrowed capital		
Current year interest		
₹ 12,00,000 x 10% = ₹ 1,20,000	60,000	60,000
Pre-construction interest		

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₹ 12,00,000 x 10% x 9/12 = ₹ 90,000 ₹ 90,000 allowed in 5 equal installments ₹ 90000 / 5 = ₹ 18,000 per annum	9,000	9,000
Total deduction under section 24(B)	69,000	94,800
Income from house property (A)-(B)	(69,000)	(8,800)
Loss under the head "Income from house property" of Mr.B (both ground floor and first floor)	(77,800)	

Note :Computation of Gross Annual Value (GAV) of first floor of B's house

If a single unit of property (in this case the first floor of B's house) is let out for some months and self-occupied for the other months, then the Expected Rent of the property shall be taken into account for determining the annual value. The Expected Rent shall be compared with the actual rent and whichever is higher shall be adopted as the annual value. In this case, the actual rent shall be the rent for the period for which the property was let out during the previous year.

The Expected Rent is the higher of fair rent and municipal value. This should be considered for 9 months since the construction of property was completed only on 30.6.2016.

Expected rent	= ₹ 75,000 being higher of -
	Fair rent = 1,00,000 x 9 /12 = ₹ 75,000
	Municipal value = 72,000 x 9/12 = ₹ 54,000
Actual rent =	₹ 90,000 (₹ 15,000 p.m. for 6 months from July to December, 2016)

Gross Annual Value = ₹ 90,000 (being higher of Expected Rent of ₹ 75,000 and actual rent of ₹ 90,000)

Question 7

Mr. Vikas owns a house property whose Municipal Value, Fair Rent and Standard Rent are ₹ 96,000, ₹ 1,26,000 and ₹1,08,000 (per annum), respectively.

During the Financial Year 2016-17, one-third of the portion of the house was let out for residential purpose at a monthly rent of ₹ 5,000. The remaining two-third portion was self-occupied by him. Municipal tax @ 11 % of municipal value was paid during the year.

The construction of the house began in June, 2009 and was completed on 31-5-2012.

Vikas took a loan of ₹ 1,00,000on 1-7-2009 for the construction of building.

He paid interest on loan @ 12% per annum and every month such interest was paid.

Compute income from house property of Mr. Vikas for the Assessment Year 2017-18.

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Answer

Computation of income from house property of Mr. Vikas for the A.Y. 2017-18

Particulars		₹	₹
Income from house property			
I. Self-occupied portion (Two third)			
Net Annual value			Nil
Less: Deduction under section 24(b)			
Interest on loan (See Note below) (₹ 18,600 x 2/3)			12,400
Loss from self occupied property			**(12,400)**
II. Let-out portion (One third)			
Gross Annual Value			
(a) Actual rent received (₹ 5,000 x 12)	₹ 60,000		
(b) Expected rent [higher of municipal valuation (i.e., ₹ 96,000) and fair rent (i.e.,₹ 1,26,000) but restricted to standard rent(i.e., ₹ 1,08,000)] = ₹ 1,08,000 x 1/3	₹ 36,000		
Higher of (a) or (b)		60,000	
Less: Municipal taxes (₹ 96,000 x 11% x 1/3)		3,520	
Net Annual Value		**56,480**	
Less: Deductions under section 24			
(a) 30% of NAV		16,944	
(b) Interest on loan (See Note below) (₹ 18,600 x 1/3)		6,200	**33,336**
Income from house property			**20,936**

Note: Interest on loan taken for construction of building

Interest for the year (1.4.2016 to 31.3.2017) = 12% of ₹ 1,00,000 = ₹ 12,000

Pre-construction period interest = 12% of ₹ 1,00,000 for 33 months (from 1.07.2009 to 31.3.2012) = ₹ 33,000

Pre-construction period interest to be allowed in 5 equal annual installments of ₹ 6,600 from the year of completion of construction i.e. from F.Y. 2012-13 till F.Y. 2016-17.

Therefore, total interest deduction under section 24 = ₹ 12,000 + ₹ 6,600 = ₹ 18,600.

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Question 8

Mr. X owns one residential house in Mumbai. The house is having two identical units. First unit of the house is self occupied by Mr. X and another unit is rented for ₹ 8,000 p.m. The rented unit was vacant for 2 months during the year. The particulars of the house for the previous year 2016-17 are as under:

Standard rent	*₹ 1,62,000 p.a.*
Municipal valuation	*₹ 1,90,000 p.a.*
Fair rent	*₹ 1,85,000 p. a*
Municipal tax (Paid by Mr. X)	*15% of municipal valuation*
Light and water charges	*₹ 500 p.m.*
Interest on borrowed capital	*₹ 1,500 p.m.*
Lease money	*₹ 1,200 p.a.*
Insurance charges	*₹ 3,000 p.a.*
Repairs	*₹ 12,000 p.a.*

Compute income from house property of Mr. X for the A.Y. 2017-18.

Answer

Computation of Income from house property for A.Y. 2017-18

Particulars	₹	₹
(A) Rented unit (50% of total area – See Note 1 below)		
Step I - Computation of Expected Rent		
Municipal valuation (₹ 1,90,000 x ½)	95,000	
Fair rent (₹ 1,85,000 x ½)	92,500	
Standard rent (₹ 1,62,000 x ½)	81,000	
Expected Rent is higher of municipal valuation and fair rent, but restricted to standard rent	81,000	
Step II - Actual Rent		
Rent receivable for the whole year (₹ 8,000 x 12)	96,000	
Step III – Computation of Gross Annual Value		
Actual rent received owing to vacancy (₹ 96,000 – ₹ 16,000)	80,000	
Since, owing to vacancy the actual rent received is lower than the Expected Rent, the actual rent received is the Gross Annual Value		
Gross Annual Value		**80,000**
Less: Municipal taxes (15% of ₹ 95,000)		14,250

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Net Annual value		**65,750**
Less : Deductions under section 24 -		
(i) 30% of net annual value	19,725	
(ii) Interest on borrowed capital (₹ 750 x 12)	9,000	28,725
Taxable income from let out portion		**37,025**
(B) Self occupied unit (50% of total area – See Note 1 below)		
Annual value	Nil	
Less : Deduction under section 24 -		
Interest on borrowed capital (₹ 750 x 12)	9,000	9,000
Income from house property		**28,025**

Note: No deduction will be allowed separately for light and water charges, lease money paid, insurance charges and repairs.

Question 9

Mrs. Indu, a resident individual, owns a house in U.S.A. She receives rent @ $ 2,000 per month. She paid municipal taxes of $ 1,500 during the financial year 2016-17. She also owns a two storied house in Mumbai, ground floor is used for her residence and first floor is let out at a monthly rent of ₹ 10,000. Standard rent for each floor is ₹ 11,000 per month and fair rent is ₹ 10,000 per month. Municipal taxes paid for the house amounts to ₹ 7,500. Mrs. Indu had constructed the house by taking a loan from a nationalised bank on 20.6.2010. She repaid the loan of ₹ 54,000 including interest of ₹ 24,000. The value of one dollar is to be taken as ₹ 60.

Compute total income from house property of Mrs. Indu.

Answer

Computation of Income from House Property of Mrs. Indu for the A.Y.2017-18

Particulars	₹	₹
House property in USA		
GAV– Rent received {treated as fair rent} ($2,000 p.m. x ₹ 60per USD x 12 months)	14,40,000	
Less : Municipal taxes paid ($1,500 x ₹ 60per USD)	90,000	
Net Annual Value (NAV)	**13,50,000**	
Less : Deduction under section 24		
30% of NAV	4,05,000	9,45,000
House property in Mumbai (Let-out portion - First Floor)		

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Expected rent **(lower of standard rent and fair rent)**			
Standard Rent (₹ 11,000 x 12)₹ 1,32,000			
Fair rent (₹ 10,000 x 12)₹ 1,20,000		1,20,000	
Actual rent received (10,000 × 12)		1,20,000	
Gross Annual Value (higher of Expected rent and actual rent)		1,20,000	
Less : Municipal taxes paid (50% of ₹ 7,500)		3,750	
Net Annual Value (NAV)		**1,16,250**	
Less : Deduction under section 24			
30% of NAV	₹ 34,875		
Interest on housing loan (50% of ₹ 24,000)	₹ 12,000	46,875	69,375
Income from House property in Mumbai (Self-occupied portion - Ground Floor)			
Gross annual value		Nil	
Less: Municipal taxes		Nil	
Net Annual Value (NAV)		Nil	
Less : Deduction under section 24			
30% of NAV		Nil	
Interest on housing loan (50% of ₹ 24,000)		12,000	(-) 12,000
Income from house property			**10,02,375**

Question 10

Nisha has two houses, both of which are self-occupied. The particulars of these are given below:

	(Value in ₹)	
Particulars	***House - I***	***House - II***
Municipal Valuation per annum	*1,20,000*	*1,15,000*
Fair Rent per annum	*1,50,000*	*1,75,000*
Standard rent per annum	*1,00,000*	*1,65,000*
Date of completion	*31-03-1999*	*31-03-2001*
Municipal taxes payable during the year (paid for House II only)	*12%*	*8%*
Interest on money borrowed for repair of property during current year	*-*	*55,000*

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Compute Nisha's income from house property for the Assessment Year 2017-18 and suggest which house should be opted by Nisha to be assessed as self-occupied so that her tax liability is minimum.

Answer

In this case, Nisha has more than one house property for self-occupation. As per section 23(4), Nisha can avail the benefit of self-occupation (i.e., benefit of "Nil" Annual Value) only in respect of one of the house properties, at her option. The other house property would be treated as "deemed let-out" property, in respect of which the Expected rent would be the gross annual value. Nisha should, therefore, consider the most beneficial option while deciding which house property should be treated by her as self-occupied.

OPTION 1 [House I – Self-occupied and House II – Deemed to be let out]

If House I is opted to be self-occupied, Nisha's income from house property for A.Y.2017-18 would be –

Particulars	Amount in ₹
House I (Self-occupied) [Annual value is Nil]	Nil
House II (Deemed to be let-out) ***[See Working Note below]***	54,060
Income from house property	**54,060**

OPTION 2 [House I – Deemed to be let out and House II – Self-occupied]

If House II is opted to be self-occupied, Nisha's income from house property for A.Y.2017-18 would be –

Particulars	Amount in ₹
House I (Deemed to be let-out) ***[See Working Note below]***	70,000
House II (Self-occupied) [Annual value is Nil, but interest deduction would be available, subject to a maximum of ₹30,000. In case of money borrowed for **repair of self-occupied property**, the interest deduction would be restricted to ₹30,000, irrespective of the date of borrowal].	(30,000)
Income from house property	**40,000**

Since Option 2 is more beneficial, Nisha should opt to treat House - II as Self-occupied and House I as Deemed to be let out, in which case, her income from house property would be ₹ 40,000 for the A.Y. 2017-18.

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Working Note:

Computation of income from House I and House II assuming that both are deemed to be let out

Particulars	Amount in Rupees	
	House I	House II
Gross Annual Value (GAV)		
Expected rentis the GAV of house property		
Expected rent= Higher of Municipal Value and Fair Rent but restricted to Standard Rent	1,00,000	1,65,000
Less: Municipal taxes (paid by the owner during the previous year)	Nil	9,200
Net Annual Value (NAV)	**1,00,000**	**1,55,800**
***Less:* Deductions under section 24**		
(a) 30% of NAV	30,000	46,740
(b) Interest on borrowed capital (allowed in full in case of deemed let out property)	-	55,000
Income from deemed to be let-out house property	**70,000**	**54,060**

Question 11

Mr. Raphael constructed a shopping complex. He had taken a loan of ₹ 25 lakhs for construction of the said property on 01-08-2014 from SBI @ 10% for 5 years. The construction was completed on 30-06-2015. Rental income received from shopping complex ₹ 30,000 per month-let out for the whole year. Municipal taxes paid for shopping complex ₹ 8,000.

Arrears of rent received from shopping complex ₹ 1,20,000

Interest paid on loan taken from SBI for purchase of house for use as own residence for the period 2016-2017, ₹ 3 lakhs.

You are required to compute income from house property of Mr. Raphael for AY 2017-2018 as per Income-tax Act, 1961.

Answer

Computation of income from house property of Mr. Raphael for A.Y.2017-18

	Particulars	₹	₹
1.	**Shopping complex**		
	Gross Annual Value [₹ 30,000 × 12][1]		3,60,000

[1] Rent received has been taken as the annual value in the absence of information relating to municipal value, fair rent and standard rent.

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	Less: Municipal Taxes		8,000
	Net Annual Value (NAV)		3,52,000
	Less: Deductions under section 24		
	30% of NAV	1,05,600	
	Interest on borrowed capital **(See Working Note below)**	2,83,333	3,88,933
			(36,933)
	Arrears of rent received taxable under section 25A	1,20,000	
	Less: Deduction@30%	36,000	84,000
			47,067
2.	**Self-occupied residential house**		
	Annual value (since the house property is self-occupied)[2]	Nil	
	Less: Deduction under section 24 Interest on loan from SBI ₹ 3 lakhs, restricted to	2,00,000	
	Chargeable income from this house property		(2,00,000)
	Income chargeable under the head "Income from house property"		**(1,52,933)**

Working Note : Interest on borrowed capital (Shopping Complex)	₹
Interest for the current year (10% of ₹ 25 lakhs)	2,50,000
Add: 1/5th of pre-construction interest (interest for the period from 1.8.2014 to 31.3.2015 for 8 months (₹ 1,66,667 x 1/5)	33,333
Interest deduction allowable under section 24	**2,83,333**

Note:

(1) In case all the conditions specified in Section 80EE are satisfied, out of the remaining interest of ₹ 1 lakh (₹ 3 lakh – ₹ 2 lakh) Mr. Raphael can claim deduction of ₹ 50,000 towards interest paid for acquisition of self occupied resident house.

(2) It has been assumed that loan of ₹ 25 lakhs has to be repaid after the five year period. Hence, there has been no repayment upto 31.3.2017. Interest computation has been made accordingly.

[2] As per section 23(2)

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Question 12

Explain the treatment of unrealized rent and its recovery in subsequent years under the provisions of Income-tax Act, 1961.

Answer

Unrealised rent refers to the rent payable but not paid by the tenant and which the owner is also not able to realize from the tenant. As per *Explanation* below section 23(1), the amount of rent which the owner cannot realize shall not be included in the actual rent while determining the annual value of the property, subject to fulfillment of following conditions prescribed under Rule 4 of the Income-tax Rules, 1962:

(a) the tenancy must be bonafide;

(b) the defaulting tenant has vacated the property or steps have been taken to compel him to vacate the property;

(c) the defaulting tenant does not occupy any other property of the assessee; and

(d) the assessee has taken all reasonable steps to institute legal proceedings for the recovery of unpaid rent or satisfies the Assessing Officer that the legal proceedings would be useless.

If the conditions mentioned above are satisfied, then, the actual rent should be reduced by the unrealized rent and thereafter, compared with the Expected rent (being the higher of fair rent and municipal value, but restricted to standard rent) for computing the gross annual value.

As per section 25A, the unrealised rent, when realised in any subsequent year, shall be deemed to be the income chargeable under the head 'Income from house property' in the previous year in which such rent is realised, whether or not the assessee is the owner of the property in that previous year. A sum of 30% of the unrealized rent shall be allowed as deduction.

Question 13

Explain briefly the applicability of section 22 for chargeability of income-tax for:

(i) House property situated in foreign country and

(ii) House property with disputed ownership.

Answer

Applicability of section 22 for chargeability of income-tax for –

(i) House property situated in foreign country

A resident assessee is taxable under section 22 in respect of annual value of a house property situated in foreign country. A resident but not ordinarily resident or a non resident is taxable in respect of income from such property if the income is received in India during the previous year. Once incidence of tax is attracted under section 22, the annual value will be computed as if the property is situated in India.

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(ii) House property with disputed ownership

If the title of ownership of the house property is under dispute in a court of law, the decision about who is the owner lies with the Income tax Department. The assessment cannot be held up for such dispute. Generally, a person who receives the income or who enjoys the possession of the house property as owner, though his claim is under dispute, is assessable to tax under section 22.

Question 14

Ownership itself is the criteria for assessment under the head income from house property. Discuss.

Answer

Section 27 enumerates certain cases, where the legal ownership may vest with one person whereas the taxability is cast on another person who is deemed to be the owner.

In these specific cases, the charge of tax is on the deemed owner and not on the legal owner. The exceptions are given below:

(i) In case of transfer of house property to spouse (not being a transfer in connection with an agreement to live apart) or minor child (not being a married daughter) without adequate consideration - transferor is the deemed owner.

(ii) Holder of an impartible estate – shall be deemed to be the individual owner of all the properties comprised in the estate.

(iii) A member of a co-operative society/company/AOP to whom a building or part thereof is allotted or leased under a house building scheme – shall be deemed to be the owner of building or part thereof.

(iv) A person who is allowed to take or retain possession of any building or part thereof is the deemed owner of such building or part thereof if such possession is obtained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882.

(v) A person who acquires any rights (excluding any rights by way of a lease from month to month or for a period not exceeding one year) in or with respect to any building or part thereof, by virtue of any such transaction as is referred to in section 269UA(f).

Therefore, legal ownership itself is not the criteria for assessment of income under the head "Income from house property".

Also, the provisions of section 25A dealing with receipt of unrealised rent and arrears of rent also fall in this category. The receipt is considered as income under the head 'house property' though the recipient may not have legal ownership of the property to which the receipt relates.

Question 15

Discuss the following issues relating to Income from house property:

(i) Income earned by residents from house properties situated in foreign countries.

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(ii) Properties which are used for agricultural purposes.

Answer

(i) In case of resident individual, his global income is taxable in India. Therefore, income earned by residents from house properties situated in foreign countries is taxable in India.

If the income from house properties situated outside India is chargeable to tax in India the annual value of such property would be computed as if the property is situated in India. Further, municipal taxes paid under the laws of that country can also be deducted while arriving at the Annual Value of the property. The Madras High Court in *CIT v. Venugopala Reddiar [1965] 58 ITR 439* observed that while computing taxable income, no distinction should be made between a house property situated in India and a house property situated abroad.

(ii) If the property is used for agricultural purposes, the annual value of such property would be treated as "Agricultural Income" as per section 2(1A)(c) and it is exempt under section 10(1) of the Act. However, if the house property is used for purpose other than agriculture the annual value of such property cannot be treated as agricultural income.

Question 16

(1) X let out his property to Y. Y sublets it. How is sub-letting receipt to be assessed in the hands of Y?

(2) Y has built a house on a leasehold land. He has let out the property and claims that the income therefrom is chargeable under the head "Income from other sources". He has deducted expenses on repairs, security charges, insurance and collection charges in all amounting to 40% of receipts. Is Mr. Y's claim valid?

(3) Z uses his property for his own business. Would the annual value be subject to tax under the head "Income from house property"?

Answer

(1) Sub-letting receipt in the hands of Y can be assessed as "Income from Other Sources" or as "Profits and gains from business or profession" depending upon the facts and circumstances of each case. It is not assessable as income from house property.

(2) No, Mr. Y's claim is not valid. The income from letting out of house built on leasehold land is assessable as "Income from house property" since ownership of land is not a pre-requisite for assessment of income under this head. 30% of Net Annual Value is allowed as deduction under section 24.

(3) Where the assessee uses his property for business, it is not assessable under the head " Income from house property". He is entitled to depreciation under section 32(1)(ii) on the building.

Question 17

Discuss the tax liability in respect of arrears of rent and unrealized rent.

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Answer

As per section 25A, where the assessee receives any amount by way of arrears of rent or realizes unrealized rent in respect of any property consisting of buildings or land appurtenant thereto of which he is the owner, the amount so received shall be chargeable to tax under the head "Income from House Property". It shall be charged to tax as the income of the previous year in which such rent is received even if the assessee is no longer the owner of such property. In computing the income chargeable to tax in respect of the arrears of rent and unrealized rent so received, 30% shall be allowed as a deduction, irrespective of the actual expenditure incurred.

Question 18

Mr. Kalpesh borrowed a sum of ₹ 30 lakhs from the National Housing Bank towards purchase of a residential flat. The loan amount was disbursed directly to the flat promoter by the bank. Though the construction was completed in May, 2017, repayments towards principal and interest had been made during the year ended 31.3.2017.

In the light of the above facts, state:

(i) Whether Mr. Kalpesh can claim deduction under section 24 in respect of interest for the assessment year 2017-18?

(ii) Whether deduction under Section 80C can be claimed for the above assessment year, even though the construction was completed only after the closure of the year?

Answer

(i) Interest on borrowed capital is allowed as deduction under section 24(b)

As per section 24(b), Interest payable on loans borrowed for the purpose of acquisition, construction, repairs, renewal or reconstruction of house property can be claimed as deduction. Interest payable on borrowed capital for the period prior to the previous year in which the property has been acquired or constructed, can be claimed as deduction over a period of 5 years in equal annual installments commencing from the year of acquisition or completion of construction.

It is stated that the construction is completed only in May, 2017. Hence, deduction in respect of interest on housing loan cannot be claimed in the assessment year 2017-18.

(ii) Clause (xviii) of section 80C is attracted where there is any payment for the purpose of purchase or construction of a residential house property, the income from which is chargeable to tax under the head 'Income from house property'. Such payment covers repayment of any amount borrowed from the National Housing Bank.

However, deduction is *prima facie* eligible only if the income from such property is chargeable to tax under the head "Income from House Property". During the assessment year 2017-18, there is no such income chargeable under this head. Hence, deduction under section 80C cannot be claimed for A.Y. 2017-18.

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Exercise

1. *Ganesh is a member of a house building co-operative society. The society is the owner of the flats constructed by it. One of the flats is allotted to Ganesh. The income from that flat will be assessed in the hands of*
   - *(a) Co-operative Society*
   - *(b) Ganesh*
   - *(c) Neither of the above.*
2. *Vacant site lease rent is taxable as*
   - *(a). Income from house property*
   - *(b). Business income*
   - *(c) Income from other sources or business income, as the case may be*
3. *Treatment of unrealized rent for determining income from house property*
   - *(a) To be deducted from expected rent*
   - *(b) To be deducted from actual rent*
   - *(c) To be deducted under section 24 from annual value*
4. *Municipal taxes to be deducted from GAV should be*
   - *(a) Paid by the tenant during the previous year*
   - *(b) Paid by the owner during the previous year*
   - *(c) Accrued during the previous year*
5. *Deduction under section 24(a) is*
   - *(a) 1/3rd of NAV*
   - *(b) repairs actually incurred by the owner*
   - *(c) 30% of NAV*
6. *Interest on borrowed capital accrued up to the end of the previous year prior to the year of completion of construction is allowed*
   - *(a) as a deduction in the year of completion of construction*
   - *(b) in 5 equal annual installments from the year of completion of construction*
   - *(c) In the respective year in which the interest accrues*
7. *The ceiling limit of deduction under section 24(b) in respect of interest on loan taken on 1.4.2016 for repairs of a self-occupied house is*
   - *(a) ₹ 30,000 p.a.*
   - *(b) ₹ 1,50,000 p.a.*
   - *(c) ₹ 2,00,000 p.a.*
   - *(d) No limit*
8. *Where an assessee has two house properties for self-occupation, the benefit of nil annual value will be available in respect of -*

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(a) *Both the properties*

(b) *The property which has been acquired/constructed first*

(c) *Any one of the properties, at the option of the assessee*

9. *Leena received ₹ 30,000 as arrears of rent during the P.Y. 2016-17. The amount taxable under section 25A would be -*

   (a) *30,000*

   (b) *21,000*

   (c) *20,000*

10. *Vidya received ₹ 90,000 in May, 2016 towards recovery of unrealised rent, which was deducted from actual rent during the P.Y. 2015-16 for determining annual value. The amount taxable under section 25A for A.Y.2017-18 would be -*

    (a) *90,000*

    (b) *63,000*

    (c) *60,000*

11. *Ganesh and Rajesh are co-owners of a self-occupied property. They own 50% share each. The interest paid by each co-owner during the previous year on loan (taken for acquisition of property during the year 2004) is ₹ 2,05,000. The amount of allowable deduction in respect of each co-owner is –*

    (a) *2,05,000*

    (b) *1,02,500*

    (c) *2,00,000*

    (d) *1,00,000*

12. *An assessee, who was deriving income from house property, realised a sum of ₹ 52,000 on account of display of advertisement hoardings of various concerns on the roof of the building. He claims that this amount should be considered under the head "Income from house property" and not "Income from other sources". How do you deal with the following issue under the provisions of the Income-tax Act, 1961?*

13. *Ram owned a house property at Chennai which was occupied by him for the purpose of his residence. He was transferred to Mumbai in June, 2016 and therefore, he let out the property w.e.f. 1.7.2016 on a monthly rent of ₹ 8,000. The corporation tax payable in respect of the property was ₹ 2,000 of which 50% was paid by him before 31.3.2017. Interest on money borrowed for the construction of the property amounted to ₹ 12,000. Compute the income from house property for the A.Y.2017-18.*

14. *What do you understand by "Composite Rent"? What is the tax treatment of Composite Rent under the Income-tax Act, 1961?*

Answers

1. b; **2.** c; **3.** b; **4.** b; **5.** c; **6.** b; **7.** a; **8.** c; **9.** b; **10.**b; **11.** c, **13.**₹ 37,700

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4 Unit 3 : Profits and Gains of Business or Profession

Key Points	
Method of Accounting [Section 145]	
Income chargeable under this head shall be computed in accordance with the method of accounting regularly and consistently employed by the assessee either cash or mercantile basis.	
Income chargeable under this head [Section 28]	
(i)	The profits and gains of any business or profession carried on by the assessee at any time during the previous year.
(ii)	Any compensation or other payment due to or received by a person, at or in connection with - (a) Termination of his management or modification of the terms and conditions relating thereto, in case the person is managing the whole or substantially the whole of the affairs of an Indian company. (b) Termination of his office or modification of the terms and conditions relating thereto, in case the person is managing the whole or substantially the whole of the affairs in India of any other company. (c) Termination of agency or modification of the terms and conditions relating thereto, in case the person is holding an agency in India for any part of the activities relating to the business of any other person. (d) Vesting in the Government or in any corporation owned and controlled by the Government, under any law for the time being in force, of the management of any property or business.
(iii)	Income derived by a trade, professional or similar association from specific services performed for its members.
(iv)	In the case of an assessee carrying on export business, the following incentives – (a) Profit on sale of import entitlements; (b) Cash assistance against exports under any scheme of GoI; (c) Customs duty or excise re-paid or repayable as drawback;

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	(d) Profit on transfer of Duty Free Replenishment Certificate.
(v)	Value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of profession.
(vi)	Any interest, salary, bonus, commission or remuneration due to, or received by, a partner of a firm from such firm (to the extent allowed as deduction in the hands of the firm).
(vii)	Any sum, received or receivable, in cash or kind under an agreement for – (a) not carrying out any activity in relation to any business or profession; or (b) not sharing any know-how, patent, copyright, trademark, licence, franchise or any other business of commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision of services.
(viii)	Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.
(ix)	Any sum, whether received or receivable, in cash or kind, on account of any capital asset (other than land or goodwill or financial instrument) being demolished, destroyed, discarded or transferred, in respect of which the whole of the expenditure had been allowed as deduction under section 35AD.

Computation of income under the head "Profits and gains of business or profession"

The income referred to in section 28 has to be computed in accordance with the provisions contained in sections 30 to 43D.

Admissible Deductions

Section	Deduction
30	Amount paid on account of rent, rates, taxes, repairs (not including expenditure in the nature of capital expenditure) and insurance for buildings used for the purpose of business or profession. In case the premises are occupied by the assessee as a tenant, the amount of repairs would be allowed as deduction only if he has undertaken to bear the cost of repairs to the premises.
31	Amount paid on account for current repairs and insurance of machinery, plant and furniture used for the purpose of business or profession.
32	**Depreciation** Depreciation is mandatorily allowable as deduction.

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Conditions for claiming depreciation

- Asset must be used for the purpose of business or profession at any time during the previous year.

  Note: If the asset is acquired during the previous year and is put to use for less than 180 days during **that** previous year then, only 50% of the depreciation calculated at the rates prescribed will be allowed.
- The asset should be owned (wholly or partly) by the assessee.
- The depreciation shall be allowed on the written down value of **block of assets** at the **prescribed rates** (except in the case of assets of power generating units, in respect of which depreciation has to be calculated as a percentage of actual cost).

  As per section 2(11), **block of assets** means a group of assets falling within a class of assets comprising:

  (a) buildings, machinery, plant or furniture being tangible assets,

  (b) know-how, patents, copyrights, trade marks, licences, franchises or any other business or commercial rights of similar nature being intangible assets;

  in respect of which, the same rate of depreciation is prescribed.

Written Down Value of Assets (W.D.V.) [Section 43(6)]

(1)	W.D.V. of the block of assets on 1st April of the previous year	xxxx
(2)	*Add:* Actual cost of assets acquired during the previous year	xxxx
(3)	Total (1) + (2)	xxxx
(4)	*Less:* Money receivable in respect of any asset falling within the block which is sold, discarded, demolished or destroyed during that previous year	xxxx
(5)	W.D.V at the end of the year (on which depreciation is allowable) [(3) – (4)]	xxxx
(6)	Depreciation at the prescribed rate (Rate of Depreciation × WDV arrived at in (5) above)	xxxx

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Block of Assets	Depreciation (% of WDV)
Tangible Assets	
Building	
Mainly used for residential purposes except hotels and boarding houses	5%
Buildings other than those mainly used for residential purposes	10%
Purely temporary erections such as wooden structures	100%
Furniture and fittings (including electrical fittings)	10%
Plant and Machinery	
General rate	15%
Motor cars, motor lorries and motor taxis used in the business of running them on hire	30%
Motor cars other than those used in a business of running them on hire	15%
Specified Air Control Pollution Equipments/Water Control Pollution Equipments	100%
Computers including computer software	60%
Books owned by assessees carrying on profession, other than annual publications	60%
Books, being annual publications, owned by assesses carrying on a profession	100%
Books owned by assesses carrying on business in running lending libraries	100%
Ships	20%
Intangible Assets	
Know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature	25%

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32(1)(iia)	**Additional depreciation** at the rate of 20% of actual cost of plant or machinery acquired and installed after 31.03.2005 by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation, transmission or distribution of power, shall be allowed. If plant and machinery is acquired and put to use for the purpose of business or profession for less than 180 days during the previous year in which it is acquired, additional depreciation will get restricted to 50% of the depreciation allowable. The balance 50% of additional depreciation will be allowed in the immediately succeeding previous year. However, additional depreciation will not be allowed on the following plant or machinery: • Ships, aircraft, road transport vehicles, office appliances; • Machinery previously used by any other person; • Machinery installed in any office premises, residential accommodation, or guest house; • Machinery in respect of which, the whole of the actual cost is fully allowed as deduction (whether by way of depreciation or otherwise) of any one previous year. In order to encourage acquisition and installation of plant and machinery for setting up of manufacturing units in the notified backward areas of the States of Andhra Pradesh, Bihar, Telangana and West Bengal, a proviso has been inserted to section 32(1)(iia) to allow higher additional depreciation at the rate of 35% (instead of 20%) in respect of the actual cost of new machinery or plant (other than a ship and aircraft) acquired and installed during the period between 1st April, 2015 and 31st March, 2020 by a manufacturing undertaking or enterprise which is set up in the notified backward areas of these specified States on or after 1st April, 2015. Such additional depreciation shall be restricted to 17.5% (i.e., 50% of 35%), if the new plant and machinery acquired is put to use for the purpose of business for less than 180 days in the year of acquisition and installation. The balance 50% of additional depreciation (i.e., 50% of 35%) would, however, be allowed in the immediately succeeding financial year.
32AC	Manufacturing companies investing more than ₹ 25 crore in new plant and machinery in any previous year during the period from 1.4.2014 to 31.3.2017 entitled to deduction@15% under section 32AC(1A). Where the installation of the new plant and machinery is in a year other than the year of acquisition, the deduction under section 32AC(1A) shall be allowed in the year in which the new plant and machinery is installed, provided the installation is on or before 31.3.2017

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32AD	(i) In order to encourage the setting up of industrial undertakings in the backward areas of the States of Andhra Pradesh, Bihar, Telangana and West Bengal, new section 32AD has been inserted to provide for a deduction of an amount equal to 15% of the actual cost of new plant and machinery acquired and installed in the assessment year relevant to the previous year in which such plant and machinery is installed, if the following conditions are satisfied by the assessee - (a) The assessee sets up an undertaking or enterprise for manufacture or production of any article or thing on or after 1st April, 2015 in any backward area notified by the Central Government in the State of Andhra Pradesh or Bihar or Telangana or West Bengal; and (b) the assessee acquires and installs new plant and machinery for the purposes of the said undertaking or enterprise during the period between 1st April, 2015 and 31st March, 2020 in the said backward areas. (ii) Where the assessee is a company, deduction under section 32AD would be available over and above the existing deduction available under section 32AC, subject to the satisfaction of conditions thereunder. Accordingly, if an undertaking is set up in the notified backward areas in the States of Andhra Pradesh or Bihar or Telangana or West Bengal **by a company**, it shall be eligible to claim deduction under section 32AC as well as under section 32AD, if it fulfills the conditions specified in section 32AC and the conditions specified under section 32AD.
35	**Expenditure on Scientific Research** **<u>Expenditure incurred by assessee</u>** • Any revenue and capital expenditure (other than cost of acquisition of land) on scientific research for in house research related to its business is allowable as deduction **[Section 35(1)(i) & Section 35(1)(iv) read with section 35(2)].** • Deduction is also allowed in respect of any such expenditure incurred during 3 years immediately preceding the year of commencement of business. Such deduction is allowed in the year in which it has commenced its business **[Section 35(1)(i)/Section 35(2)]**. • In case of companies engaged in the business of bio-technology or manufacture or production of article or thing, deduction of 200% of expenditure incurred on scientific research on in-house research and development facility is allowed (other than expenditure on cost of land or building) **[Section 35(2AB)]**.

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Contributions to Outsiders

Contributions made by any assessee to certain specified/ approved institutions shall be entitled to weighted deduction as follows:

Section	Contribution made to	Deduction (as a % of contribution made)
35(1)(ii)	Research Association for scientific research	175%
35(1)(iia)	Company for scientific research	125%
35(1)(iii)	Research association for research in social science or statistical research	125%
35(2AA)	National Laboratory / University / IIT	200%

35AD

This section provides for investment-linked tax deduction in respect of the following specified businesses -

- setting-up and operating 'cold chain' facilities for specified products;
- setting-up and operating warehousing facilities for storing agricultural produce;
- laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network;
- building and operating a hotel of two-star or above category, anywhere in India;
- building and operating a hospital, anywhere in India, with at least 100 beds for patients;
- developing and building a housing project under a scheme for slum redevelopment or rehabilitation framed by the Central Government or a State Government, as the case may be, and notified by the CBDT in accordance with the prescribed guidelines;
- developing and building a housing project under a notified scheme for affordable housing framed by the Central Government or State Government;
- production of fertilizer in India;
- setting up and operating an inland container depot or a container freight station notified or approved under the Customs Act, 1962;
- bee-keeping and production of honey and beeswax;
- setting up and operating a warehousing facility for storage of sugar;
- laying and operating a slurry pipeline for transportation of iron-ore; and

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	• setting up and operating a semiconductor wafer fabrication manufacturing unit, if such unit is notified by the Board in accordance with the prescribed guidelines. 100% of the capital expenditure incurred during the previous year, wholly and exclusively for the above businesses would be allowed as deduction from the business income. However, expenditure incurred on acquisition of any land, goodwill or financial instrument would not be eligible for deduction. Further, the expenditure incurred, wholly and exclusively, for the purpose of specified business prior to commencement of operation would be allowed as deduction during the previous year in which the assessee commences operation of his specified business, provided the amount incurred prior to commencement has been capitalized in the books of account of the assessee on the date of commencement of its operations. In respect of the following specified businesses, weighted deduction @150% of investment made is allowable, if the operations have been commenced on or after 1st April, 2012: 1. setting up and operating a cold chain facility. 2. setting up and operating a warehouse facility for storage of agricultural produce. 3. building and operating anywhere in India, a new hospital with at least 100 beds. 4. business of developing and building a housing project under a scheme for affordable housing framed by the Central or State Government and notified by CBDT. 5. business of production of fertilizer in India. An assessee availing investment-linked tax deduction under section 35AD in respect of any specified business in any assessment year, is not eligible for claiming profit-linked deduction under Chapter VI-A or section 10AA for the same or any other assessment year in respect of such specified business. Any asset in respect of which a deduction is claimed and allowed under section 35AD shall be used only for the specified business, for a period of eight years beginning with the previous year in which such asset is acquired or constructed. If such asset is used for any purpose other than the specified business, the total amount of deduction so claimed and allowed in any previous year in respect of such asset, as reduced by the depreciation allowable under section 32 as if no deduction had been allowed under section 35AD, shall be deemed to be the business income of the assessee of the previous year in which the asset is so used.

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35CCC	150% of expenditure incurred by an assessee on notified agricultural extension project in accordance with the prescribed guidelines.
35CCD	150% of expenditure (other than expenditure in nature of cost of any land or building) incurred by a company on notified skill development project.
35D	Preliminary expenditure incurred by Indian companies and other resident non-corporate assessees shall be allowed as deduction over a period of 5 years beginning with the previous year in which business commences or in which extension of the undertaking is completed. Maximum aggregate amount of the qualifying expenses that can be amortized is 5% of the cost of project. In case of an Indian company, 5% of the cost of project or at its option, 5% of the capital employed by the company, whichever is higher.
35DD	One-fifth of the expenditure incurred by an Indian company wholly and exclusively for the purpose of amalgamation or demerger, shall be allowed as deduction for five successive previous years beginning with the previous year in which the amalgamation or demerger has taken place.
35DDA	One-fifth of the expenditure incurred by an assessee-employer in any previous year in the form of payment to any employee in connection with his voluntary retirement in accordance with a scheme of voluntary retirement, shall be allowed as deduction in that previous year and the balance in four equal installments in the immediately four succeeding previous years.
36(1)(iii)	Interest paid in respect of capital borrowed for the purposes of business or profession. However, any interest paid for acquisition of an asset (whether capitalized in the books of account or not) for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction.
36(1)(iv)	Any sum paid by the assessee as an employer by way of contribution towards a recognized provident fund or approved superannuation fund, subject to prescribed limits.
36(1)(iva)	Any sum paid by the assessee as an employer by way of contribution towards a pension scheme referred to in section 80CCD, to the extent of 10% of salary of any employee. Salary includes dearness allowance, if the terms of employment so provide. Correspondingly, section 40A(9) disallows the sum paid in excess of 10% of the salary of any employee.

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<table>
<tr><td>36(1)(vii)</td><td colspan="2">Any bad debts written off as irrecoverable in the accounts of the assessee for the previous year, provided the debt has been taken into account in computing the income of the previous year or any earlier previous year. Amount of debt taken into account in computing the income of the assessee on the basis of notified ICDSs to be allowed as deduction in the previous year in which such debt or part thereof becomes irrecoverable. If a debt, which has not been recognized in the books of account as per the requirement of the accounting standards but has been taken into account in the computation of income as per the notified ICDSs, has become irrecoverable, it can still be claimed as bad debts under section 36(1)(vii) since it shall be deemed that the debt has been written off as irrecoverable in the books of account by virtue of the second proviso to section 36(1)(vii).

In the case of an assessee eligible for deduction under section 36(1)(viia), the amount of deduction under section 36(1)(vii) shall be limited to the amount by which such debt or part thereof exceeds the credit balance in the provision for bad and doubtful debts made under section 36(1)(viia).</td></tr>
<tr><td rowspan="6">36(1)(viia)</td><td colspan="2">Provision for bad and doubtful debts made by certain banks and financial institutions.</td></tr>
<tr><th>Bank / Financial Institution</th><th>Maximum deduction</th></tr>
<tr><td>Scheduled Bank or a Non-scheduled bank or a Co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank</td><td>7.5% of gross total income + 10% of aggregate average advances made by rural branches of the bank</td></tr>
<tr><td>Foreign Bank</td><td>5% of gross total income</td></tr>
<tr><td>Public Financial Institution/State Financial Corporation/State Industrial Investment Corporation</td><td>5% of gross total income</td></tr>
<tr><td>A Non-Banking Financial Company</td><td>5% of gross total income</td></tr>
<tr><td>36(1)(viii)</td><td colspan="2">In respect of any special reserve created and maintained by a specified entity (banking company, specified financial corporations etc.), an amount not exceeding 20% of the profits derived from the eligible business (industrial or agricultural development, development of infrastructure facility in India, development of housing in India) computed under this head and carried to such reserve account.

Where the aggregate of the amounts carried to such reserve account from time to time exceeds twice the amount of paid up share capital and of the general reserves of the specified entity, no deduction is allowable in respect of such excess.</td></tr>
</table>

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36(1)(ix)	Any bona fide expenditure incurred by a **company** for the purpose of promoting family planning amongst its employees. In case the expenditure or part thereof is of capital nature, one-fifth of such expenditure shall be deducted for the previous year in which it was incurred; and the balance in four equal installments in four succeeding previous years.
36(1)(xv)	An amount equal to the securities transaction tax (STT) paid by the assessee in respect of taxable securities transactions entered into in the course of his business during the previous year, if the income arising from such taxable securities transactions is included in the income computed under the head "Profits and gains of business or profession".
36(1)(xvi)	An amount equal to commodities transaction tax (CTT) paid in respect of taxable commodities transactions entered into the course of business during the previous year, 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".
General	
37(1)	An expenditure shall be allowed under section 37**,** provided: • it is not in the nature of expenditure described under sections 30 to 36; • it is not in the nature of capital expenditure; • it is not a personal expenditure of the assessee; • it is laid out and expended wholly and exclusively for the purpose of business/ profession; • it is not incurred for any purpose which is an offence or which is prohibited by law; and • it is not an expenditure incurred by the assessee on CSR activities referred to in section 135 of the Companies Act, 2013.
37(2B)	Any expenditure incurred for advertisement in any souvenir, brochure, tract, pamphlet etc. published by a political party is not allowable as deduction.
Amounts not deductible	
Section	**Particulars**
40(a)(i)	Any interest, royalty, fees for technical services or other sum chargeable under the Act, which is payable outside India or in India to a **non corporate non-resident or to a foreign company**, on which tax deductible at source has not been deducted or after deduction has not been paid on or before the due date specified under section 139(1).

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	However, if such tax has been deducted in any subsequent year or has been deducted in the previous year but paid in the subsequent year after the due date specified under section 139(1), such sum shall be allowed as deduction in computing the income of the previous year in which such tax is paid.
40(a)(ia)	30% of any sum payable to a resident on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction has not been paid on or before the due date for filing of return of income under section 139(1). However, if such tax has been deducted in any subsequent year or has been deducted in the previous year but paid in the subsequent year after the due date specified under section 139(1), 30% of such sum shall be allowed as deduction in computing the income of the previous year in which such tax is paid.
	Where such person responsible for deducting tax is not deemed to be an assessee-in-default on account of payment of taxes by the resident payee, it shall be deemed that the payer has deducted and paid the tax on such sum on the date of furnishing return of income by the resident payee. Since the date of furnishing the return of income by the resident payee is taken to be the date on which the payer has deducted tax at source and paid the same, the expenditure/payment in respect of which the payer has failed to deduct tax at source shall be disallowed under section 40(a)(ia) in the year in which the said expenditure is incurred. Such expenditure will be allowed as deduction in the subsequent year in which the return of income is furnished by the resident payee, since tax is deemed to have been deducted and paid by the payer in that year.
40(a)(ii)/ (iia)	Any sum paid on account of income-tax or wealth-tax
40(a)(iib)	Any amount paid by way of royalty, licence fee, service fee, privilege fee, service charge, or any other fee or charge, which is levied exclusively on, or any amount appropriated, directly or indirectly, from a State Government undertaking, by the State Government.
40(a)(iii)	Any payment chargeable under the head "Salaries", if it is payable outside India or to a non-resident, if tax has not been paid thereon nor deducted therefrom
40(a)(v)	Tax paid by the employer on non-monetary perquisites provided to its employees, which is exempt under section 10(10CC) in the hands of the employee.
40(b)	In case of partnership firms or LLPs - (i) Salary, bonus, commission or remuneration, by whatever name called, paid to any partner who is not a working partner;

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	(ii)	Payment of remuneration or interest to a working partner, which is not – • authorized by the partnership deed; or • in accordance with the terms of the partnership deed.
	(iii)	Payment of remuneration or interest to a working partner authorized by and in accordance with the terms of the partnership deed, but relates to a period falling prior to the date of such partnership and is not authorized by the earlier partnership deed.
	(iv)	Payment of interest to any partner authorised by and in accordance with the terms of the partnership deed and falling after the date of the partnership deed to the extent of the excess of the amount calculated at 12% simple interest per annum.
	(v)	Payment of remuneration to a working partner which is authorized by and in accordance with the partnership deed to the extent the aggregate of such payment to working partners exceed the following limits -
		(a) On the first ₹ 3,00,000 of the book-profit or in case of a loss — ₹ 1,50,000 or 90% of the book-profit, whichever is more. (b) On the balance of book-profit — 60%

Expenses or payments not deductible in certain circumstances

Section	Particulars
40A(2)	Any expenditure incurred in respect of which a payment is made to a related person or entity, to the extent it is excessive or unreasonable by the Assessing Officer. Few examples of related persons are as under:

Assessee	Related Person
Individual	Any relative of the individual
Firm	Any partner of the firm or relative of such partner and the member of the family or association
HUF or AOP	Any member of the AOP or HUF or any relative of such member
Company	Director of the company or any relative of the director
Any assessee	Any individual who has a substantial interest (20% or more voting power or beneficial entitlement to 20% of profits) in the business or profession of the assessee; or A relative of such individual.

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40A(3)	Any expenditure, in respect of which a **payment or aggregate of payments** made to a person in a single day otherwise than by account payee cheque or account payee bank draft exceeds ₹ 20,000. In case of payments made to transport operator for plying, hiring or leasing goods carriages, an enhanced limit of ₹ 35,000 shall apply. If the payment/payments exceed this limit, the entire expenditure would be disallowed. However, disallowance would not be attracted if the cases and circumstances in which payment is made otherwise than by way of an account payee cheque or bank draft are covered in Rule 6DD.
40A(3A)	Where an expenditure has been allowed as deduction on accrual basis in any previous year, and payment is made in a subsequent previous year and such payment (or aggregate of payments made to a person in a day is made in a subsequent previous year) is in excess of the limits of ₹ 20,000/₹ 35,000 specified above, the payment/aggregate of payments so made shall be deemed as profits and gains of the business or profession and charged to tax as income of the subsequent previous year. However, the deeming provision will not apply in the cases and circumstances covered in Rule 6DD.
40A(7)	Provision for payment of gratuity to employees. However, disallowance would not be attracted if provision is made for contribution to approved gratuity fund or for payment of gratuity that has become payable during the year.
Profits chargeable to tax [Section 41]	
41(1)	Where deduction was allowed in respect of loss, expenditure or trading liability for any year and subsequently, during any previous year, the assessee or successor of the business has obtained any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained or the value of benefit accrued shall be deemed to be income.
41(3)	Amount realized on transfer of an asset used for scientific research is taxable as business income to the extent of deduction allowed under section 35 in the year in which transfer takes place.
41(4)	Any amount recovered by the assessee against bad debt earlier allowed as deduction shall be taxed as income in the year in which it is received.
Certain Deductions to be allowed only on Actual Payment [Section 43B]	
In respect of the following sums payable by an assessee, deduction is allowable only if the sum is actually paid on or before the due date of filing of return under section 139(1). (i) Tax, duty, cess or fee, under any law for the time being in force; or	

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(ii)	Contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees; or
(iii)	Bonus or commission for services rendered by employees, where such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission; or
(iv)	Interest on any loan or borrowing from any public financial institution or a State Financial Corporation or a State Industrial Investment Corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing; or
(v)	Interest on any loan or advance from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan or advances; or
(vi)	Payment in lieu of any leave at the credit of his employee.
(vii)	Any sum payable to the Indian Railways for use of Railway assets.

Other Provisions

Section	Particulars		
43CA	Where the consideration for the transfer of an asset (other than capital asset), being land or building or both, is less than the stamp duty value, the value so adopted or assessed or assessable (i.e., the stamp duty value) shall be deemed to be the full value of the consideration for the purposes of computing income under the head "Profits and gains of business or profession". Further, where the date of an agreement fixing the value of consideration for the transfer of the asset and the date of registration of the transfer of the asset are not same, the stamp duty value may be taken as on the date of the agreement for transfer instead of on the date of registration for such transfer, provided at least a part of the consideration has been received by any mode other than cash on or before the date of the agreement.		
44AA	**Maintenance of accounts by certain persons carrying on profession or business**		
	Class of Persons	**Threshold limit of gross receipts/total income**	**Requirement**
	Every person carrying on a specified profession, namely, legal, medical, engineering, architectural profession or the professionof accountancy or technical consultancy or interior decoration or any other notified profession[i.e., authorised representative, film artist, company secretary and information technology].	If his total gross receipts from profession does not exceed ₹ 1,50,000 in any one of the three years immediately preceding the previous year, or Where the profession has been newly set up in the previous year, his total gross receipts in the profession for that year does not exceed ₹ 1,50,000.	Maintenance of such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Act

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	Every person carrying on a specified profession, namely, legal, medical, engineering, architectural profession or the profession of accountancy or technical consultancy or interior decoration or authorised representative or film artist.	If his total gross receipts from profession exceeds ₹ 1,50,000 in any one of the three years immediately preceding the previous year, or Where the profession has been newly set up in the previous year, his total gross receipts in the profession for that year exceeds ₹ 1,50,000.	Maintenance of such books of account and other documents referred to in sub-rule (2), namely, cash book, journal, if accounts are maintained according to the mercantile system of accounting, a ledger, carbon copies of bills for sums exceeding ₹ 25, original bills and receipts (payment vouchers in case the expenditure does not exceed ₹ 50).
	Every person carrying on a non-specified profession or business.	(i) If his total sales, turnover or gross receipts from business or profession exceeds ₹ 10,00,000 in any one of the three years immediately preceding the previous year, or his income from business or profession exceeds ₹ 1,20,000 in any one of the three years immediately preceding the previous year.	Maintenance of such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Act.
		(ii) Where the business or profession has been newly set up in the previous year, his total sales, turnover or gross receipts for that year is likely to exceed ₹ 10,00,000 or his income from business or profession for that year is likely to exceed ₹ 1,20,000 in that year.	

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		(iii) Where the profits and gains from business are deemed to be the profits and gains of the assessee under section 44AE, 44BB, 44BBB and the assesssee has claimed his income to be lower than the deemed profits. (iv) Where the provisions of section 44AD(4) are applicable in an assessee's case and his income exceeds the basic exemption limit	

44AB	**Mandatory audit of accounts of certain persons**	
	Category of person	**Condition for applicability of section 44AB**
	Every person carrying on business	Total sales, turnover or gross receipts in business > ₹ 1 crore in any previous year
	Every person carrying on profession	Gross receipts in profession > ₹ 50 lakh in any previous year
	Every person carrying on a business, where deemed profits are taxed on presumptive basis under section 44AE, 44BB and 44BBB.	Income is claimed to be lower than the deemed profits under the respective sections
	Every person carrying on a profession, where 50% of the gross receipts are deemed to be the profits under section 44ADA.	Income is claimed to be lower than the deemed profits and such income exceeds the basic exemption limit.
	Every person who declared profit on presumptive bassi under section 44AD for any previous year and thereafter, declares profits for any five consecutive assessment years relevant to the previous year succeeding such previous year not in accordance with presumptive tax provisions of section 44AD(1).	Income cannot be computed on the basis of presumptive tax provisions under section 44AD for five assessment years subsequent to the assessment year relevant to the previous year in which profits have not been declared under section 44AD(1) and whose income exceeds the basic exemption limit in that year.

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Presumptive taxation provisions		
Section	**Particulars**	**Deemed profits and gains**
44AD	Any individual, HUF or firm who is a resident (other than LLP) who has not claimed deduction under section 10AA or Chapter VI-A under the heading "C - Deductions in respect of certain incomes" engaged in any business (except the business of plying, hiring or leasing goods carriages referred to in section 44AE) and whose total turnover or gross receipts in the previous year does not exceed ₹ 2 crore. However, this section will not apply to – (i) a person carrying on specified professions referred to in section 44AA(1), (ii) a person earning income in the nature of commission or brokerage; (iii) a person carrying on agency business.	8% of gross receipts or total turnover
44ADA	An assessee, being a resident in India, who is engaged - in any profession referred to in section 44AA(1) such as legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other profession as is notified by the Board in the Official Gazette; and - whose total gross receipts does not exceed ₹ 50 lakhs in a previous year.	50% of the gross receipts.
44AE	Any assessee who owns not more than ten goods carriages at any time during the previous year and who is engaged in the business of plying, hiring and leasing goods carriages.	For each goods vehicle, whether heavy goods vehicle or other than heavy goods vehicle, ₹ 7,500 per month or part of a month during which such vehicle is owned by the assessee or an amount claimed to have been actually earned from such vehicle, whichever is higher.

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Taxability in case of composite income

In cases where income is derived from the sale of rubber manufactured or processed from rubber plants grown by the seller in India, coffee (grown and cured/grown, cured, roasted and grounded) or tea grown and manufactured in India, the income shall be computed as if it were income derived from business, and a specified percentage of such income, as given in the table below, shall be deemed to be income liable to tax -

Rule	Nature of composite income	Business income (Taxable)	Agricultural Income (Exempt)
7A	Income from the manufacture of rubber	35%	65%
7B	Income from the manufacture of coffee		
	- sale of coffee grown and cured	25%	75%
	- sale of coffee grown, cured, roasted and grounded	40%	60%
8	Income from the manufacture of tea	40%	60%

Notification of new income computation and disclosure standards to be applicable from A.Y.2017-18 [Notification No.S.O. 3079(E) dated 29-09-2016]

Under section 145(1), income chargeable under the heads "Profits and gains of business or profession" or "Income from other sources" shall be computed in accordance with either the cash or mercantile system of accounting regularly employed by the assessee. Section 145(2) empowers the Central Government to notify in the Official Gazette from time to time, **income computation and disclosure standards** to be followed by any class of assessees or in respect of any class of income. Accordingly, the Central Government has, in exercise of the powers conferred under section 145(2), notified ten income computation and disclosure standards (ICDSs) to be followed by **all assessees (other than an individual or a Hindu undivided family who is not required to get his accounts of the previous year audited in accordance with the provisions of section 44AB), following the mercantile system of accounting, for the purposes of computation of income chargeable to income-tax under the head "Profit and gains of business or profession" or " Income from other sources" for A.Y.2017-18 and subsequent assessment years.**

Refer to Annexure at the end of the Practice Manual wherein the text of the ICDSs notified on 29.9.2016 to be applicable from A.Y.2017-18 has been given. Also, a comparison between the initially notified ICDS (notified on 31.3.2015 – since rescinded) and the newly notified ICDSs (applicable from A.Y.2017-18) has been given to facilitate an easy understanding of the changes which have been made in the newly notified ICDSs.

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Question 1

A car purchased by Dr. Soman on 10.08.2014 for ₹ 5,25,000 for personal use is brought into professional use on 1.07.2016 by him, when its market value was ₹ 2,50,000.

Compute the actual cost of the car and the amount of depreciation for the assessment year 2017-18 assuming the rate of depreciation to be 15%.

Answer

As per section 43(1), the expression "actual cost" would mean the actual cost of asset to the assessee.

The purchase price of ₹ 5,25,000 is, therefore, the actual cost of the car to Dr. Soman. Market value (i.e. ₹ 2,50,000) on the date when the asset is brought into professional use is not relevant.

Therefore, amount of depreciation on car as per section 32 for the A.Y.2017-18 would be ₹ 78,750, being ₹ 5,25,000 x 15%.

Note : *Explanation 5 to section 43(1) providing for reduction of notional depreciation from the date of acquisition of asset for personal use to determine actual cost of the asset is applicable only in case of building which is initially acquired for personal use and later brought into professional use. It is not applicable in respect of other assets.*

Question 2

Venus Ltd., engaged in manufacture of pesticides, furnishes the following particulars relating to its manufacturing unit at Chennai, for the year ending 31-3-2017:

	(₹ in lacs)
Opening WDV of Plant and Machinery	*20*
New machinery purchased on 1-9-2016	*10*
New car purchased on 1-12-2016	*8*
Computer purchased on 3-1-2017	*4*

Additional information:

- *All assets were put to use immediately.*
- *Computer has been installed in the office.*
- *During the year ended 31-3-2016, a new machinery had been purchased on 31-10-2015, for ₹ 10 lacs. Additional depreciation, besides normal depreciation, had been claimed thereon.*
- *Depreciation rate for machinery may be taken as 15%.*

Compute the depreciation available to the assessee as per the provisions of the Income-tax Act, 1961 and the WDV of different blocks of assets as on 31-3-2017.

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Answer

Computation of written down value of block of assets of Venus Ltd. as on 31.3.2017

Particulars	Plant & Machinery (₹ in lacs)	Computer (₹ in lacs)
Opening written down value (as on 01.04.2016)	**20**	**Nil**
Add: Actual cost of new assets acquired during the year		
New machinery purchased on 1.9.2016	10	-
New car purchased on 1.12.2016	8	-
Computer purchased on 3.1.2017	-	4
	38	4
Less: Assets sold/discarded/destroyed during the year	Nil	Nil
Closing Written Down Value (as on 31.03.2017)	**38**	**4**

Computation of Depreciation for A.Y. 2017-18

	Particulars	Plant & Machinery (₹ in lacs)	Computer (₹ in lacs)
I.	**Assets put to use for more than 180 days, eligible for 100% depreciation calculated applying the eligible rate of normal depreciation and additional depreciation**		
	Normal Depreciation		
	- Opening WDV of plant and machinery (₹ 20 lacs x 15%)	3.00	-
	- New Machinery purchased on 1.9.2016 (₹ 10 lacs x 15%)	1.50	-
	(A)	4.50	-
	Additional Depreciation		
	New Machinery purchased on 1.9.2016 (₹ 10 lacs x 20%) (B)	2.00	-
	Balance additional depreciation in respect of new machinery purchased on 31.10.2015 and put to use for less than 180 days in the –P.Y. 2015-16 (Rs. 10 lakhs)	1.00	

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II.	**Assets put to use for less than 180 days, eligible for 50% depreciation calculated applying the eligible rate of normal depreciation and additional depreciation**		
	Normal Depreciation		
	New car purchased on 1.12.2016 [₹ 8 lacs x 7.5% (i.e., 50% of 15%)]	0.60	-
	Computer purchased on 3.1.2017 [₹ 4 lacs x 30% (50% of 60%)]	-	1.20
	(C)	0.60	1.20
	Total Depreciation (A+B+C)	**8.10**	**1.20**

Notes:

(1) As per section 32(1)(iia), additional depreciation is allowable in the case of any new machinery or plant acquired and installed after 31.3.2005, by an assessee engaged, *inter alia,* in the business of manufacture or production of any article or thing, at the rate of 20% of the actual cost of such machinery or plant.

However, additional depreciation shall not be allowed in respect of, *inter alia*, –

(i) any office appliances or road transport vehicles;

(ii) any machinery or plant installed in, *inter alia*, office premises.

In view of the above provisions, additional depreciation cannot be claimed in respect of -

(i) Car purchased on 1.12.2016 and

(ii) Computer purchased on 3.1.2017, installed in office.

(2) The Finance Act, 2015 has inserted third proviso to section 32(1)(ii) with effect from A.Y.2016-17, to provide that balance 50% of additional depreciation on new plant or machinery acquired and put to use for less than 180 days in the year of acquisition which has not been allowed in that year, shall be allowed in the immediately succeeding previous year.

Hence, in this case, the balance 50% additional depreciation (i.e., ₹ 1 lacs, being 10% of ₹ 10 lacs) in respect of new machinery which had been purchased during the previous year 2015-16 and put to use for less than 180 days in that year can be claimed in P.Y. 2016-17 being immediately succeeding previous year.

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Question 3

M/s. Dollar Ltd., a manufacturing concern, furnishes the following particulars:

		₹
(i)	*Opening writing down value of plant and machinery (1.4.2016) (15% block)*	*5,00,000*
(ii)	*Purchase of plant and machinery (put to use before 01.10.2016)*	*2,00,000*
(iii)	*Sale proceeds of plant and machinery which became obsolete- the plant and machinery was purchased on 01-04-2014 for ₹ 5,00,000.*	*5,000*

Further, out of purchase of plant and machinery:

(a) Plant and machinery of ₹ 20,000 has been installed in office.

(b) Plant and machinery of ₹ 20,000 was used previously for the purpose of business by the seller.

Compute depreciation and additional depreciation as per Income-tax Act, 1961 for the Assessment Year 2017-18.

Answer

Computation of written down value of Plant and Machinery of M/s. Dollar Ltd. as on 31.3.2017

Particulars	₹
Opening written down value (as on 01.04.2016)	5,00,000
Add: Purchase of plant and machinery during the previous year	2,00,000
	7,00,000
Less: Sale proceeds of obsolete plant and machinery sold during the year	5,000
Closing Written Down Value (as on 31.03.2017)	**6,95,000**

Computation of Depreciation and Additional Depreciation for A.Y. 2017-18 as per section 32 of the Income-tax Act, 1961

Particulars	₹
Normal Depreciation (₹ 6,95,000 x 15%)	1,04,250
Additional Depreciation (Refer Note 2)(₹ 2,00,000 – ₹ 20,000 - ₹ 20,000) x 20%	32,000
Depreciation on Plant and Machinery	**1,36,250**

Notes:-

(1) Since the new plant and machinery was purchased and put to use before 1.10.2016, it was put to use for more than 180 days in the year. Hence, full depreciation is allowable for A.Y. 2017-18.

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(2) As per section 32(1)(iia), additional depreciation is allowable in the case of any new machinery or plant acquired and installed after 31.3.2005 by an assessee engaged, *inter alia,* in the business of manufacture or production of any article or thing, at the rate of 20% of the actual cost of such machinery or plant.

However, additional depreciation shall not be allowed in respect of, *inter alia*, –

(i) any machinery or plant which, before its installation by the assessee, was used either within or outside India by any other person;

(ii) any machinery or plant installed in office premises, residential accommodation or in any guest house.

In view of the above provisions, additional depreciation cannot be claimed in respect of -

(i) Plant and machinery of ₹ 20,000 used previously for the purpose of business by the seller.

(ii) Plant and machinery of ₹ 20,000, installed in office.

Therefore, in the given case additional depreciation has to be provided only on ₹ 1,60,000 (i.e., ₹ 2,00,000 - ₹ 40,000).

Question 4

Mr. Abhimanyu is engaged in the business of generation and distribution of electric power. He always opts to claim depreciation on written down value for income-tax purposes. From the following details, compute the depreciation allowable as per the provisions of the Income-tax Act, 1961 for the assessment year 2017-18:

		(₹ in lacs)
(i)	*Opening WDV of block (15% rate)*	*42*
(ii)	*New machinery purchased on 12-10-2016*	*10*
(iii)	*Machinery imported from Colombo on 12-4-2016.* *This machine had been used only in Colombo earlier and the assessee is the first user in India.*	*9*
(iv)	*New computer installed in generation wing of the unit on 15-7-2016*	*2*

Answer

Computation of depreciation under section 32 for A.Y.2017-18

Particulars	₹	₹
Normal Depreciation		
Depreciation@15% on ₹ 51,00,000, being machinery (put to use for more than 180 days) [Opening WDV of ₹ 42,00,000 + Purchase cost of imported machinery of ₹ 9,00,000]	7,65,000	

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Depreciation@7.5% on ₹ 10,00,000, being new machinery put to use for less than 180 days	75,000	
	8,40,000	
Depreciation@60% on computers purchased ₹ 2,00,000	1,20,000	9,60,000
Additional Depreciation (Refer Note below)		
Additional Depreciation@10% of ₹ 10,00,000 [being actual cost of new machinery purchased on 12-10-2016]	1,00,000	
Additional Depreciation@20% on new computer installed in generation wing of the unit [20% of ₹ 2,00,000]	40,000	1,40,000
Depreciation on Plant and Machinery		**11,00,000**

Note:-

The benefit of additional depreciation is available to new plant and machinery acquired and installed in power sector undertakings. Accordingly, additional depreciation is allowable in the case of any new machinery or plant acquired and installed by an assessee engaged, *inter alia,* in the business of generation or generation and distribution of power, at the rate of 20% of the actual cost of such machinery or plant.

Therefore, new computer installed in generation wing of the unit is eligible for additional depreciation@20%.

Since the new machinery was purchased only on 12.10.2016, it was put to use for less than 180 days during the previous year, and hence, only 10% (i.e., 50% of 20%) is allowable as additional depreciation in the A.Y. 2017-18. The balance additional depreciation would be allowed in the next year.

However, additional depreciation shall not be allowed in respect of, *inter alia*, any machinery or plant which, before its installation by the assessee, was used either within or outside India by any other person. Therefore, additional depreciation is not allowable in respect of imported machinery, since it was used in Colombo, before its installation by the assessee.

Question 5

Harish Jayaraj Pvt. Ltd. is converted into Harish Jayaraj LLP on 1.1.2017. The following particulars are available to you:

S. No.	*Particulars*	₹
(i)	*Cost of land*	*5,00,000*
(ii)	*WDV of machinery as on 1.4.2016*	*3,30,000*
(iii)	*Patents acquired on 1.6.2016*	*3,00,000*
(iv)	*Building acquired on 12.3.2015 for which deduction was allowed*	*7,00,000*

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	under section 35AD.	
(v)	*Above building was revalued as on the date of conversion into LLP as*	*12,00,000*
(vi)	*Unabsorbed business loss as on 1.4.2016 (Related to A.Y. 2013-14)*	*9,00,000*

Though the conversion into LLP took place on 1.1.2017, there was disruption of business and the assets were put into use by the LLP only from 1st March, 2017 onwards.

The company earned profits of ₹ 8 lacs prior to computation of depreciation.

Assuming that the necessary conditions laid down in section 47(xiiib) of the Income-tax Act, 1961 have been complied with, explain the tax treatment of the above in the hands of the LLP.

Answer

Tax treatment of depreciation and unabsorbed business loss of a private company on its conversion into a LLP

1. Depreciation

The aggregate depreciation allowable to the predecessor company and successor LLP shall not exceed, in any previous year, the depreciation calculated at the prescribed rates as if the conversion had not taken place. Such depreciation shall be apportioned between the predecessor company and the successor LLP in the ratio of the number of days for which the assets were used by them [Fifth proviso to Section 32(1)]

Therefore, depreciation has to be first calculated as if the conversion had not taken place and then apportioned between the company and the LLP in the ratio of the number of days for which the assets were used by them.

		₹		₹
Block I	Machinery	3,30,000	15%	49,500
Block II	Patents	3,00,000	25%	75,000
				1,24,500

Allocation of depreciation

Depreciation on machinery and patents have to be apportioned between the company and the LLP in the ratio of the number of days for which the **assets were used by them**. Since patents were acquired only on 1.6.2016, it could have been used by the company for 214 days only. Therefore, the depreciation on assets has to be allocated between the company and LLP as follows –

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		Company		LLP	
Asset	**Total depreciation for the year**	**No. of days of usage**	**Depreciation**	**No. of days of usage**	**Depreciation**
Machinery	49,500	275	44,485	31	5,015
Patents	75,000	214	65,510	31	9,490
	1,24,500		**1,09,995**		**14,505**

Therefore, depreciation to be allowed in the hands of the company is ₹ 1,09,995 and depreciation to be allowed in the hands of the LLP is ₹ 14,505.

2. **Unabsorbed business loss to be carried forward by the LLP**:

Particulars	₹
Profits of the company before depreciation	8,00,000
Less: Current year depreciation	1,09,995
Business income of the company after depreciation	6,90,005
Brought forward business loss	9,00,000
Unabsorbed business loss as on 31.12.2016 to be carried forward by the LLP	**2,09,995**

The LLP would be allowed to carry forward and set-off the unabsorbed business loss and unabsorbed depreciation of the predecessor company [Section 72A(6A)].

3. **Actual cost of assets to the LLP**

(1) The actual cost of the block of assets in case of the LLP shall be the WDV of the block of assets as in the case of the company on the date of conversion. The WDV as on 1.1.2017 for Machinery and Patents are ₹ 2,85,515 and ₹ 2,34,490, respectively, which would be the actual cost in the case of the LLP.

WDV of Machinery as on 1.1.2017 = ₹ 3,30,000 – ₹ 44,485 = ₹ 2,85,515

WDV of Patents as on 1.1.2017 = ₹ 3,00,000 – ₹ 65,510 = ₹ 2,34,490

(2) Land is not a depreciable asset. The cost of acquisition of land to the LLP would be the cost for which the company acquired it, as increased by the cost of improvement.

(3) In respect of the building, deduction had been allowed in the earlier year under section 35AD. Hence, there is no question of depreciation during the current year. The actual cost of the building to the LLP would be Nil. [Explanation 13 to Section 43(1)]

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Question 6

Sai Ltd. has a block of assets carrying 15% rate of depreciation, whose written down value on 01.04.2016 was ₹ 40 lacs. It purchased another asset (second-hand plant and machinery) of the same block on 01.11.2016 for ₹ 14.40 lacs and put to use on the same day. Sai Ltd. was amalgamated with Shirdi Ltd. with effect from 01.01.2017.

You are required to compute the depreciation allowable to Sai Ltd. & Shirdi Ltd. for the previous year ended on 31.03.2017 assuming that the assets were transferred to Shirdi Ltd. at ₹ 60 lacs.

Answer

Statement showing computation of depreciation allowable to Sai Ltd. & Shirdi Ltd. for A.Y. 2017-18

Particulars	₹
Written down value (WDV) as on 1.4.2016	40,00,000
Addition during the year (used for less than 180 days)	14,40,000
Total	**54,40,000**
Depreciation on ₹ 40,00,000 @ 15%	6,00,000
Depreciation on ₹ 14,40,000 @ 7.5%	1,08,000
Total depreciation for the year	**7,08,000**
Apportionment between two companies:	
(a) Amalgamating company, Sai Ltd.	
₹ 6,00,000 × 275/365	4,52,055
₹ 1,08,000 × 61/151	43,629
	4,95,684
(b) Amalgamated company, Shirdi Ltd.	
₹ 6,00,000 × 90/365	1,47,945
₹ 1,08,000 × 90/151	64,371
	2,12,316

Notes:

(1) The aggregate deduction, in respect of depreciation allowable to the amalgamating company and amalgamated company in the case of amalgamation shall not exceed in any case, the deduction calculated at the prescribed rates as if the amalgamation had not taken place. Such deduction shall be apportioned between the amalgamating company and the amalgamated company in the ratio of the number of days for which the assets were used by them.

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(2) The price at which the assets were transferred, i.e., ₹ 60 lacs, has no implication in computing eligible depreciation.

Question 7

Mr. Gopi carrying on business as proprietor converted the same into a limited company by name Gopi Pipes (P) Ltd. from 01-07-2016. The details of the assets are given below:

	₹
Block - I WDV of plant & machinery (rate of depreciation @ 15%)	*12,00,000*
Block - II WDV of building (rate of depreciation @ 10%)	*25,00,000*

The company Gopi Pipes (P) Ltd. acquired plant and machinery in December 2016 for ₹ 10,00,000. It has been doing the business from 01-07-2016.

Compute the quantum of depreciation to be claimed by Mr. Gopi and successor Gopi Pipes (P) Ltd. for the assessment year 2017-18.

Note: Ignore additional depreciation.

Answer

Computation of depreciation allowable to Mr. Gopi for A.Y. 2017-18

Particulars	₹	₹
Block 1 Plant and Machinery (15% rate)		
WDV as on 1.4.2016	12,00,000	
Depreciation@15%		1,80,000
Block 2 Building (10% rate)		
WDV as on 1.4.2016	25,00,000	
Depreciation@10%		2,50,000
Total depreciation for the year		**4,30,000**
Proportionate depreciation allowable to Mr. Gopi for 91 days (i.e., from 1.4.2016 to 30.6.2016) [i.e., 91/365 x ₹ 4,30,000)		1,07,205

Computation of depreciation allowable to Gopi Pipes (P) Ltd. for A.Y.2017-18

Particulars	₹
(i) Depreciation on building and plant and machinery Proportionately for 274 days (i.e. from 1.7.2016 to 31.3.2017) (274/365 x 4,30,000)	3,22,795
(ii) Depreciation@ 50% of 15% on ₹ 10 lakh, being the value of plant and machinery purchased after conversion, which was put to use for less than 180 days during the P.Y. 2016-17	75,000
Depreciation allowable to Gopi Pipes (P) Ltd.	**3,97,795**

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Note: *As per the fifth proviso to section 32(1), in the case of conversion of sole proprietary concern into a company as per section 47(xiv), the depreciation should be first calculated for the whole year as if no succession had taken place. Thereafter, the depreciation should be apportioned between the sole proprietary concern and the company in the ratio of the number of days for which the assets were used by them. It is assumed that in this case, the conditions specified in section 47(xiv) are satisfied.*

Question 8

M/s Sidhant & Co., a sole proprietary concern is converted into a company, Sidhant Co. Ltd. with effect from November 29, 2016. The written down value of assets as on April 1, 2016 is as follows:

Items	*Rate of Depreciation*	*WDV as on 1st April, 2016*
Building	*10%*	*₹ 3,50,000*
Furniture	*10%*	*₹ 50,000*
Plant and Machinery	*15%*	*₹ 2,00,000*

Further, on October 15, 2016, M/s Sidhant & Co. purchased a plant for ₹ 1,00,000 (rate of depreciation 15%). After conversion, the company added another plant worth ₹ 50,000 (rate of depreciation 15%).

Compute the depreciation available to (i) M/s Sidhant & Co. and (ii) Sidhant Co. Ltd. for Assessment Year 2017-18.

Answer

In the case of conversion of sole proprietary concern into a company as per section 47(xiv), the depreciation should be first calculated for the whole year assuming that no succession had taken place. Thereafter, the depreciation should be apportioned between the sole proprietary concern and the company in the ratio of the number of days for which the assets were used by them. It is assumed that in this case, the conditions specified in section 47(xiv) are satisfied.

Computation of depreciation allowable to M/s Sidhant & Co. for A.Y.2017-18

Particulars	₹	₹
Building		
WDV as on 1.4.2016	3,50,000	
Depreciation@10%		35,000
Furniture		
WDV as on 1.4.2016	50,000	
Depreciation@10%		5,000

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Plant and Machinery		
WDV as on 1.4.2016	2,00,000	
Add: Additions during the year (purchased on 15.10.2016)	1,00,000	
	3,00,000	
Less: Depreciation for the year		
(15% of ₹ 2,00,000 + 50% of 15% of ₹ 1,00,000)		37,500
(₹ 30,000 + ₹ 7,500)		
(Depreciation on new machinery is restricted to 50% of eligible depreciation, since the asset is put to use for less than 180 days in that year)		
Total depreciation for the year		**77,500**
Proportionate depreciation allowable to M/s Sidhant & Co. for 242 days		
On existing assets (i.e. 1.4.2016 to 28.11.2016) (i.e. 242/365 x ₹ 70,000)	46,411	
On new machine for 45 days i.e., 45/168 × ₹ 7,500	2,009	**48,420**

Computation of depreciation allowable to M/s Sidhant Co. Ltd. for A.Y.2017-18

	Particulars	₹
(i)	Depreciation on the assets on conversion	
	Proportionately for 123 days i.e. after conversion period	
	(123/365 x ₹ 70,000)+ (123/168 × ₹ 7,500) = ₹ 23,589 + ₹ 5,491	29,080
(ii)	Depreciation @ 50% of normal rate of 15% on ₹ 50,000, being the value of plant purchased after conversion, which was put to use for less than 180 days	3,750
Depreciation allowable to Sidhant Co. Ltd.		**32,830**

Note: *Since it has not been specifically mentioned that M/s Sidhant & Co. and Sidhant Co. Ltd. are manufacturing concerns or companies engaged in the business of generation, transmission or distribution of power, additional depreciation is not provided for.*

Question 9

What are intangible assets? Give four examples. What is the rate of depreciation on a block of intangible assets?

Answer

Intangible assets are assets which are not corporeal i.e., not capable of being touched. Such assets are represented by rights of the persons through them.

According to Explanation 3(b) to section 32(1), the following are intangible assets :

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(a) Know-how
(b) Patents
(c) Copyrights
(d) Trade Marks
(e) Licences
(f) Franchises
(g) any other business or commercial rights of similar nature.

They are to be depreciated at the rate of 25%.

Question 10

Gopichand Industries furnishes you the following information:

		(₹)
Block I	*WDV of Plant and machinery (consisting of 10 looms)*	*5,00,000*
	Rate of depreciation 15%	
Block II	*WDV of Buildings (consisting of 3 buildings)*	*12,50,000*
	Rate of depreciation 10%	
Acquired on 5-07-2016 – 5 looms for		*4,00,000*
Sold on 7-12-2016 – 15 looms for		*10,00,000*
Acquired on 10-01-2017 – 2 looms for		*3,00,000*

Compute depreciation claim for the Assessment year 2017-18.

Answer

Computation of depreciation for Gopichand Industries for A.Y.2017-18

Particulars	₹	₹
Block 1 : Plant & machinery (Rate of depreciation – 15%)		
WDV as on 1st April (10 looms)	5,00,000	
Add: Additions during the year		
- 5 looms acquired on 5th July	4,00,000	
- 2 looms acquired on 10th January	3,00,000	
	12,00,000	
Less : Assets sold during the year		
- 15 looms sold on 7th December	10,00,000	
W.D.V. as on 31st March (2 looms)	2,00,000	
Depreciation on ₹ 2 lakhs @ 15% (limited to 50%)		15,000

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Block II: Buildings (Rate of depreciation – 10%)		
WDV as on 1st April (3 buildings)	12,50,000	
Depreciation on ₹ 12,50,000 @ 10%		1,25,000
Total depreciation for the year		**1,40,000**

Notes:

1. Closing balance of Block 1: Plant and machinery represents the looms acquired on 10th January. These looms have been put to use or less than 180 days during the previous year, and therefore, only 50% of normal depreciation is permissible.
2. No additional depreciation @ 20% of the cost of new plant and machinery is provided for assuming that all conditions contained in the section 32(1)(iia) have not been fulfilled.

Question 11

M/s. QQ & Co., a sole proprietary concern, was converted into a company on 1.9.2016. Before the conversion, the sole proprietary concern had a Block of Plant and Machinery (Rate of depreciation 15%), whose WDV as on 1.4.2016 was ₹ 3,00,000. On 1st April itself, a new plant of the same block was purchased for ₹ 1,20,000. After the conversion, the company has purchased the same type of Plant on 1.1.2017 for ₹ 1,60,000.

Compute the depreciation that would be allocated between the sole proprietary concern and the successor company.

***Note**: Ignore additional depreciation.*

Answer

Computation of depreciation in the case of transfer of business:

Depreciation is to be calculated as if there is no succession.	(₹)
WDV as on 1st April	3,00,000
Add : Additions made before succession	1,20,000
	4,20,000
Less : Sale consideration of the asset sold	Nil
	4,20,000
Depreciation @ 15%	63,000

Allocation of depreciation between sole proprietary concern and the successor company:

The depreciation of ₹ 63,000 is to be allocated in the ratio of number of days the assets were used by the sole proprietary concern and the company.

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Ex–sole proprietary concern

1st April to 31st August = 153 days ₹ 63,000 x 153 / 365 = ₹ 26,408

Successor company

₹ 63,000 - ₹ 26,408 = ₹ 36,592 (i.e. ₹ 63,000 x 212 /365)

The depreciation of ₹ 12,000 [50% of 15% on ₹ 1,60,000] in respect of asset purchased by the successor company on 1st January is fully allowable in the hands of the successor company.

Question 12

Honest Industry furnishes you the following details pertaining to the financial year 2016-17:

Description	*Plant & Machinery*	*Building*	*Intangible assets (patents)*
Rate of depreciation	*15%*	*10%*	*25%*
Opening balance as on 01-04-2016	*₹ 14,50,000*	*₹ 25,00,000*	*₹ 15,00,000*
Acquired before 30-09-2016	*₹ 12,00,000*	*Nil*	*₹ 5,00,000*
Acquired after 01-12-2016	*₹ 4,00,000*	*₹ 18,00,000*	*Nil*
Transferred in March 2017, one of the patents held for the past 2 years	-	-	*₹ 3,00,000*

A machinery acquired in July 2016 original cost ₹ 1,50,000 was destroyed by fire and the assessee received compensation of ₹ 50,000 from the insurance company.

Newly acquired building given above includes value of land of ₹ 3,00,000.

Calculate the eligible depreciation claim for the assessment year 2017-18.

Note : Ignore additional/accelerated depreciation.

Answer

Computation of depreciation allowable to Honest Industry for the A.Y. 2017-18

Particulars	**Plant & Machinery**	**Building**	**Intangible assets (patents)**	**Total (₹**
Rate of depreciation	15%	10%	25%	
Opening Balance as on 1.04.2016	14,50,000	25,00,000	15,00,000	
Add: Assets acquired during the year	16,00,000	15,00,000	5,00,000	

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	30,50,000	40,00,000	20,00,000	
Less: Moneys payable in respect of asset sold or destroyed	50,000	-	3,00,000	
W.D.V as on 31.03.2017	30,00,000	40,00,000	17,00,000	
Asset held for less than 180 days	**4,00,000**	**15,00,000**	-	
Depreciation@50% of applicable rate	30,000	75,000	-	1,05,000
Asset held for more than 180 days	**26,00,000**	**25,00,000**	**17,00,000**	
Depreciation at the applicable rates	3,90,000	2,50,000	4,25,000	10,65,000
Total Depreciation allowable				**11,70,000**

Note - *Land is not a depreciable asset. Therefore, ₹ 3 lacs, being the value of land, has been reduced from ₹ 18 lacs, being the value of building acquired during the year, for the purpose of computing depreciation.*

Question 13

Mr. Praveen Kumar has furnished the following particulars relating to payments made towards scientific research for the year ended 31.3.2017:

Sl. No.	***Particulars***	***₹ (in lacs)***
(i)	*Payments made to K Research Ltd.*	*20*
(ii)	*Payment made to LMN College*	*15*
(iii)	*Payment made to OPQ College*	*10*
(iv)	*Payment made to National Laboratory*	*8*
(v)	*Machinery purchased for in-house scientific research*	*25*
(vi)	*Salaries to research staff engaged in in-house scientific research*	*12*

Note: *K Research Ltd. and LMN College are approved research institutions and these payments are to be used for the purposes of scientific research.*

Compute the amount of deduction available under section 35 of the Income-tax Act, 1961 while arriving at the business income of the assessee.

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Answer

Computation of deduction allowable under section 35

Particulars	Amount (₹ in lacs)	Section	% of weighted deduction	Amount of deduction (₹ in lacs)
Payment for scientific research				
K Research Ltd. [See Note 3]	20	35(1)(ii)	175%	35.00
LMN College	15	35(1)(ii)	175%	26.25
OPQ College [See Note 1]	10	-	Nil	Nil
National Laboratory [See Note 4]	8	35(2AA)	200%	16.00
In-house research [See Note 2]				
Capital expenditure	25	35(1)(iv) r.w. 35(2)	100%	25.00
Revenue expenditure	12	35(1)(i)	100%	12.00
Deduction allowable under section 35				**114.25**

Notes:-

1. **Payment to OPQ College:** Since the note in the question below item (vi) clearly mentions that only K Research Ltd. and LMN College (mentioned in item (i) and (ii), respectively) are approved research institutions, it is a logical conclusion that OPQ College mentioned in item (iii) is not an approved research institution. Therefore, payment to OPQ College would not qualify for deduction under section 35.

2. **Deduction for in-house research and development:** Only company assessees are entitled to weighted deduction@200% under section 35(2AB) in respect of in-house research and development expenditure incurred. However, in this case, the assessee is an individual. Therefore, he would be entitled to deduction@100% of the revenue expenditure incurred under section 35(1)(i) and 100% of the capital expenditure incurred under section 35(1)(iv) read with section 35(2), assuming that such expenditure is laid out or expended on scientific research related to his business.

3. **Payment to K Research Ltd. (Alternative Answer):** Any sum paid to a company registered in India which has as its main object scientific research, as is approved by the prescribed authority, qualifies for a weighted deduction of 125% under section 35(1)(iia). Therefore, it is also possible to take a view that payment of ₹ 20 lakhs to K Research Ltd. qualifies for a weighted deduction of 125% under section 35(1)(iia) since K Research Ltd. is a company. The weighted deduction under section 35(1)(iia) would be ₹ 25 lacs (i.e., 125% of ₹ 20 lacs), in which case, the total deduction under section 35 would be ₹ 104.25 lacs.

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4. **Payment to National Laboratory:** The percentage of weighted deduction under section 35(2AA) in respect of amount paid to National Laboratory is 200%.

Question 14

Vivitha Bio-medicals Ltd. is engaged in the business of manufacture of bio-medical items. The following expenses were incurred in respect of activities connected with scientific research:

Year ended	*Item*	*Amount (₹)*
31.03.2014	*Land*	*10,00,000*
(Incurred after 1.9.2013)	*Building*	*25,00,000*
31.03.2015	*Plant and machinery*	*5,00,000*
31.03.2016	*Raw materials*	*2,20,000*
31.03.2017	*Raw materials and salaries*	*1,80,000*

The business was commenced on 01-09-2016.

In view of availability of better model of plant and machinery, the existing plant and machinery were sold for ₹ 8,00,000 on 1.03.2017.

Discuss the implications of the above for the assessment year 2017-18 along with brief computation of deduction permissible under section 35 assuming that necessary conditions have been fulfilled. You are informed that the assessee's line of business is eligible for claiming deduction under section 35 at 200% on eligible items.

Answer

1. As per section 35(2AB), where a company engaged in, *inter alia,* the business of biotechnology incurs any expenditure on scientific research during the current year, it is eligible for claiming weighted deduction of a sum equal to 200% of the eligible expenditure.

   Note : *The benefit of weighted deduction under this section would be available for expenditure incurred upto 31st March 2017 on in-house research and development facility.*

   The eligible expenditure and quantum of deduction will be:

   (a) Current year capital expenditure (except expenditure in the nature of cost of any land or building) or revenue expenditure incurred for scientific research (weighted deduction @ 200%) under section 35(2AB).

   (b) Any expenditure incurred during earlier 3 years immediately preceding the date of commencement of business on payment of salary or purchase of materials, or capital expenditure incurred other than expenditure on acquisition of land [actual expenditure qualifies for deduction under section 35(1)].

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The deduction available under section 35 for scientific research will, therefore, be:

	Particulars	₹
(a)	Land	Nil
(b)	Building	25,00,000
(c)	Revenue expenses of last 3 years	2,20,000
(d)	Capital expenditure of last 3 years: Plant and machinery	5,00,000
Expenditure allowable under section 35(1)		**32,20,000**
Current year revenue expenditure ₹ 1,80,000 [200% of ₹ 1,80,000 is allowable under section 35(2AB)]		3,60,000
Total deduction under section 35		**35,80,000**

2. Section 41(3) provides that where a capital asset used for scientific research is sold, without having been used for other purposes, the lower of sale proceeds or the total amount of deduction earlier allowed under section 35 will be considered as income from business of the previous year in which the sale took place.

   Therefore, the income chargeable to tax under section 41(3) would be lower of the following:

   (1) Sale proceeds i.e.,₹ 8,00,000

   (2) Total amount of deduction earlier allowed under section 35 i.e., ₹ 5,00,000

   ₹ 5,00,000 will be deemed to be the income chargeable to tax under section 41(3).

3. The difference between sale proceeds and business income under section 41(3) will be treated as short-term capital gain.

	₹
Sale proceeds of plant and machinery	8,00,000
Less: Business Income as per section 41(3)	5,00,000
Short-term capital gain	3,00,000

Question 15

Swadeshi Ltd., which follows mercantile system of accounting, obtained licence on 1.4.2015 from the Department of telecommunication for a period of 10 years. The total licence fee payable is ₹ 18,00,000. The relevant details are:

Year ended 31st March	*Licence fee payable for the year (₹)*	*Payments made*	
		Date	*Amount (₹)*
2016	*10,00,000*	*30.03.2016*	*3,70,000*
		15.05.2016	*6,30,000*
2017	*8,00,000*	*28.02.2017*	*5,40,000*

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Balance of ₹ 2,60,000 is pending as on 31.3.2017.

Compute the amount of deduction available to the assessee under section 35ABB for the assessment years 2016-17 and 2017-18. Can any deduction be claimed under section 32 also?

Answer

As per section 35ABB, any amount actually paid for obtaining licence to operate telecommunication services, shall be allowed as deduction in equal installments during the number of years for which the licence is in force. Therefore, the year of actual payment is relevant and not the previous year in which the liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee.

1. ₹ 3,70,000 paid on 30.03.2016 [P.Y.2015-16]

Unexpired period of licence 10 years

Hence ₹ 37,000 [i.e. ₹ 3,70,000/10] can be claimed under section 35ABB for period of 10 years commencing from A.Y.2016-17.

2. ₹ 11,70,000 paid during year ended 31.03.2017 [P.Y.2016-17]

Unexpired period of licence 9 years

Hence, ₹ 1,30,000 [i.e. ₹ 11,70,000/9] can be claimed under section 35ABB for a period of 9 years commencing from A.Y.2017-18.

3. Amount of deduction under section 35ABB

Assessment year	Amount (₹)
2016-17	37,000
2017-18	37,000 + 1,30,000 = 1,67,000

Where deduction under section 35ABB is claimed and allowed, deduction under section 32(1) cannot be allowed for the same previous year or any subsequent previous year.

Question 16

Win Limited commenced the business of operating a three star hotel in Tirupati on 1-4-2016.

It furnishes you the following information:

(i)	*Cost of land (acquired in June 2014)*	*₹ 60 lakhs*
(ii)	*Cost of construction of hotel building*	
	Financial year 2014-15	*₹ 30 lakhs*
	Financial year 2015-16	*₹ 150 lakhs*
(iii)	*Plant and Machineries (all new) acquired during financial year 2015-16*	*₹ 30 lakhs*
	[All the above expenditures were capitalized in the books of the company]	
	Net profit before depreciation for the financial year 2016-17	*₹ 80 lakhs*

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Determine the amount eligible for deduction under section 35AD of the Income-tax Act, 1961, for the assessment year 2017-18.

Answer

Under section 35AD, 100% of the capital expenditure incurred during the previous year, wholly and exclusively for the specified business, which includes the business of building and operating a hotel of two-star or above category anywhere in India which commences its operations on or after 1.4.2010, would be allowed as deduction from the business income. However, expenditure incurred on acquisition of any land, goodwill or financial instrument would not be eligible for deduction.

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

Accordingly, the deduction under section 35AD for the A.Y.2017-18 in the case of Win Ltd. would be calculated as follows, assuming that the expenditures were capitalised in the books of the company on 1.4.2016, being the date of commencement of operations-

Particulars	₹ (in lakhs)
Cost of land (not eligible for deduction under section 35AD)	Nil
Cost of construction of hotel building (₹ 30 lakhs + ₹ 150 lakhs)	180
Cost of plant and machinery	30
Deduction under section 35AD	**210**

Note:-

(1) For A.Y.2017-18, the loss from specified business of operating a three star hotel would be ₹ 130 lakhs (i.e. ₹ 210 lakhs – ₹ 80 lakhs). As per section 73A, any loss computed in respect of the specified business referred to in section 35AD shall be set off only against profits and gains, if any, of any other specified business. The unabsorbed loss, if any, will be carried forward for set off against profits and gains of any specified business in the following assessment year.

(2) Since the entire cost of plant and machinery and building qualifies for deduction under section 35AD, the same does not qualify for deduction under section 32.

Question 17

MNP Ltd. commenced operations of the business of a new four-star hotel in Chennai on 1.4.2016. The company incurred capital expenditure of ₹ 40 lakh during the period January, 2016 to March, 2016 exclusively for the above business, and capitalized the same in its books

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of account as on 1st April, 2016. Further, during the previous year 2016-17, it incurred capital expenditure of ₹ 2.5 crore (out of which ₹ 1 crore was for acquisition of land) exclusively for the above business. Compute the income under the head "Profits and gains of business or profession" for the assessment year 2017-18, assuming that MNP Ltd. has fulfilled all the conditions specified for claim of deduction under section 35AD and has not claimed any deduction under Chapter VI-A under the heading "C. – Deductions in respect of certain incomes". The profits from the business of running this hotel (before claiming deduction under section 35AD) for the assessment year 2017-18 is ₹ 80 lakhs. Assume that the company also has another existing business of running a four-star hotel in Kanpur, which commenced operations 5 years back, the profits from which was ₹ 130 lakhs for assessment year 2017-18.

Would MNP Ltd. be entitled to deduction under section 35AD if it transfers the operation of the hotel in Chennai to PQR Ltd, while continuing to own the said hotel?

Answer

Computation of income under the head "Profit and gains of business or profession" of MNP Ltd. for A.Y. 2017-18

Particulars	₹ (in lakh)	₹ (in lakh)
Profits from the specified business of new four-star hotel in Chennai (before providing deduction under section 35AD)		80
***Less**:* **Deduction under section 35AD**		
Capital expenditure incurred during the P.Y. 2016-17 (excluding the expenditure incurred on acquisition of land) = ₹ 250 lakh – ₹ 100 lakh ***(See Notes 1 & 2 below)***	150	
Capital expenditure incurred during January 2016 to March 2016 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2016 ***(See Note 3 below)***	40	
Total deduction under section 35AD for A.Y.2017-18		190
Income from the specified business of new hotel in Chennai		**(110)**
Profit from the existing business of running a four-star hotel in Kanpur ***(See Note 4 below)***		130
Net profit from business after set-off of loss of specified business against profits of another specified business under section 73A		**20**

Notes:

(1) According to the provisions of section 35AD, an assessee shall be allowed a deduction in respect of 100% of the capital expenditure incurred wholly and exclusively for the purpose of the specified business which, *inter alia,* includes the business in the nature of building and operating a new hotel of two-star or above category, anywhere in India. Therefore, the newly commenced four-star hotel business of MNP Ltd qualifies for

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deduction under section 35AD, since it has fulfilled all the conditions for claim of deduction under that section.

(2) The expenditure on acquisition of land, however, does not qualify for deduction under section 35AD.

(3) The capital expenditure incurred prior to commencement of specified business shall be allowed as deduction under section 35AD(1) in the year of commencement of specified business, if the same is capitalized in the books of accounts of the assessee on the date of commencement of its operations. Therefore, the expenditure of ₹ 40 lakh is allowable as deduction in A.Y. 2017-18, since it has been capitalized in the books of accounts of MNP Ltd. as on 1.4.2016.

(4) As per section 73A, the loss computed under section 35AD in respect of a specified business can be set off against the profit of another specified business. Building and operating a hotel of two-star and above category, anywhere in India, is a specified business, therefore, the loss from the business of new four-star hotel in Chennai can be set-off against the income of the existing four-star hotel in Kanpur.

(5) Section 35AD(6A) provides that where the assessee, MNP Ltd., builds a hotel of two-star or above category as classified by the Central Government and subsequently, while continuing to own the hotel, transfers the operation of the said hotel to another person, the assessee shall be deemed to be carrying on the specified business of building and operating a hotel. Therefore, in this case, MNP Ltd. would be eligible to claim investment linked deduction under section 35AD even if it transfers the operation of the Chennai hotel to PQR Ltd.

Question 18

Briefly discuss about the provisions relating to deductibility of interest on capital borrowed for the purpose of business or profession.

Answer

Under section 36(1)(iii), deduction is allowed in respect of interest on capital borrowed for the purposes of business or profession while computing income under the head “Profits and gains of business or profession”.

Further, *Explanation 8* to section 43(1) clarifies that interest relatable to a period after the asset is first put to use cannot be included in the actual cost of the asset.

The proviso to section 36(1)(iii) provides that no deduction shall be allowed in respect of any amount of interest paid, in respect of capital borrowed for acquisition of an asset (whether capitalized in the books of account or not) for any period beginning from the date on which the capital was borrowed for acquisition of the asset, till the date on which such asset was first put to use.

Thus, interest in respect of capital borrowed for any period from the date of borrowing to the date on which the asset was first put to use should be capitalized

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Question 19

Comment on the allowability of the following claim made by the assessee:

Mr. Achal, a hotelier, claimed expenditure on replacement of linen and carpets in his hotel as revenue expenditure.

Answer

The expenditure on replacement of linen and carpets in a hotel are in the nature of expenses incurred for the business and are allowable as revenue expenses under section 37(1).

Question 20

What are the conditions to be satisfied for the allowability of expenditure under section 37 of the Income-tax Act, 1961?

Answer

(1) The following conditions are to be fulfilled for the allowability of expenditure under section 37 -

- (i) The expenditure should not be of the nature described in section 30 to 36;
- (ii) It should not be in the nature of personal expenditure of the assessee;
- (iii) The expenditure should have been laid out or expended wholly or exclusively for the purposes of the business or profession;
- (iv) It should not be in the nature of a capital expenditure;
- (v) It should not have been incurred for any propose which is an offence or which is prohibited by law.

(2) No deduction is allowable for expenditure incurred by the assessee on advertisement in any souvenir, brochure, tract pamphlet or the like published by a political party [Section 37(2B)]

(3) As per *Explanation 2* to Section 37(1), any expenditure incurred by the assessee on the activities relating to Corporate Social Responsibilty referred to in Section 135 of the Companies Act, 2013 shall **not** be deemed to be an expenditure incurred for the purpose of business or profession. Hence, such expenditure shall be disallowed while computing total income.

Question 21

State with reasons, the allowability of the following expenses incurred by MN Limited, a wholesale dealer of commodities, under the Income-tax Act, 1961 while computing profit and gains from business or profession for the Assessment Year 2017-18.

(i) Construction of school building in compliance with CSR activities amounting to ₹ 5,60,000.

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(ii) Purchase of building for setting up a warehousing facility for storage of food grains amounting to ₹ 4,50,000.

(iii) Interest on loan paid to Mr. X (a resident) ₹ 50,000 on which tax has not been deducted.

(iv) Commodities transaction tax paid ₹ 20,000 on sale of bullion.

Answer

Allowability of the expenses incurred by MN Ltd., a wholesale dealer in commodities, while computing profits and gains from business or profession

(i) Construction of school building in compliance with CSR activities

Under section 37(1), only expenditure not being in the nature of capital expenditure or personal expense and not covered under sections 30 to 36, and incurred wholly and exclusively for the purposes of the business is allowed as a deduction while computing business income.

However, any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and hence, shall not be allowed as deduction under section 37.

Accordingly, the amount of ₹ 5,60,000 incurred by MN Ltd. towards construction of school building in compliance with CSR activities shall ***not*** be allowed as deduction under section 37.

Note: *The Explanatory Memorandum to the Finance (No.2) Bill, 2014, however, clarifies that CSR expenditure, which is of the nature described in sections 30 to 36, shall be allowed as deduction under these sections subject to fulfilment of conditions, if any, specified therein.*

Under section 35AC, 100% deduction is allowable in respect of the expenditure incurred on eligible projects/schemes specified under Rule 11K, which includes, inter alia, any project or scheme for construction of school buildings primarily for children belonging to the economically weaker sections of the society, as the Central Government may, by notification in the Official Gazette, specify in this behalf on the recommendation of the National Committee, being a committee constituted by the Central Government, from amongst persons of eminence in public life.

Therefore, if the expenditure of ₹ 5,60,000 on construction of school building is incurred for children belonging to the economically weaker sections of the society and the other conditions mentioned under section 35AC are fulfilled by MN Ltd., it can claim deduction of such expenditure under section 35AC.

(ii) Purchase of building for setting up a warehousing facility for storage of food grains

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MN Ltd. would be eligible for investment-linked tax deduction under section 35AD @150% in respect of amount of ₹ 4,50,000 invested in purchase of building for setting up a warehousing facility for storage of food grains which commences operation on or after 1st April, 2012 (P.Y.2016-17, in this case).

Therefore, the deduction under section 35AD while computing business income would be ₹ 6,75,000.

(iii) Interest on loan paid to Mr. X (a resident) ₹ 50,000 on which tax has not been deducted

₹ 15,000, being 30% of ₹ 50,000, would be disallowed under section 40(a)(ia) while computing the business income of MN Ltd. for non-deduction of tax at source under section 194A on interest of ₹ 50,000 paid by it to Mr. X.

The balance ₹ 35,000 would be allowed as deduction under section 36(1)(iii), assuming that the amount was borrowed for the purposes of business.

(iv) Commodities transaction tax of ₹ 20,000 paid on sale of bullion

Commodities transaction tax paid in respect of taxable commodities transactions entered into in the course of business during the previous year is allowable as deduction, provided the income arising from such taxable commodities transactions is included in the income computed under the head "Profits and gains of business or profession".

Taking that income from this commodities transaction is included while computing the business income of MN Ltd., the commodity transaction tax of ₹ 20,000 paid is allowable as deduction under section 36(1)(xvi).

Question 22

State with reasons, for the following sub-divisions, whether the following statements are true or false having regard to the provisions of the Income-tax Act, 1961:

(i) For a dealer in shares and securities, securities transaction tax paid in a recognized stock exchange is permissible business expenditure.

(ii) Where a person follows mercantile system of accounting, an expenditure of ₹ 25,000 has been allowed on accrual basis and in a later year, in respect of the said expenditure, assessee makes the payment of ₹ 25,000 through a cheque crossed as "& Co.", disallowance of ₹ 25,000 under section 40A(3) can be made in the year of payment.

(iii) It is mandatory to provide for depreciation under section 32 of the Income-tax Act, 1961, while computing income under the head "Profits and Gains from Business and Profession".

(iv) The mediclaim premium paid to GIC by Mr. Lomesh for his employees, by a draft, on 27.12.2016 is a deductible expenditure under section 36.

(v) Under section 35DDA, amortization of expenditure incurred under eligible Voluntary Retirement Scheme at the time of retirement alone, can be done.

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(vi) *An existing assessee engaged in trading activities, can claim additional depreciation under Section 32(1)(iia) in respect of new plant acquired and installed in the trading concern, where the increase in value of such plant as compared to the approved base year is more than 10%.*

Answer

(i) True : Section 36(1)(xv) allows a deduction of the amount of securities transaction tax paid by the assessee in respect of taxable securities transactions entered into in the course of business during the previous year as deduction from the business income of a dealer in shares and securities.

(ii) True : As per section 40A(3), in the case of an assessee following mercantile system of accounting, if an expenditure has been allowed as deduction in any previous year on due basis, and payment exceeding ₹ 20,000 has been made in the subsequent year otherwise than by an account payee cheque or an account payee bank draft, then the payment so made shall be deemed to be the income of the subsequent year in which such payment has been made.

(iii) True : According to the *Explanation 5* to section 32(1), allowance of depreciation is mandatory. Therefore, depreciation has to be provided mandatorily while calculating income from business / profession whether or not the assessee has claimed the same while computing his total income.

(iv) True : Section 36(1)(ib) provides deduction in respect of premium paid by an employer to keep in force an insurance on the health of his employees under a scheme framed in this behalf by GIC or any other insurer. The medical insurance premium can be paid by any mode other than cash, to be eligible for deduction under section 36(1)(ib).

(v) False : Expenditure incurred in making payment to the employee in connection with his voluntary retirement either in the year of retirement or in any subsequent year, will be entitled to deduction in 5 equal annual installments beginning from the year in which each payment is made to the employee.

(vi) False : Additional depreciation can be claimed only in respect of eligible plant and machinery acquired and installed by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation or generation and distribution of power. In this case, the assessee is engaged in trading activities and the new plant has been acquired and installed in a trading concern. Hence, the assessee will not be entitled to claim additional depreciation under section 32(1)(iia).

Question 23

State, with reasons, the allowability of the following expenses under the Income-tax Act, 1961 while computing income from business or profession for the Assessment Year 2017-18:

(i) *Provision made on the basis of actuarial valuation for payment of gratuity ₹ 5,00,000. However, no payment on account of gratuity was made before due date of*

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filing return.

(ii) Purchase of oil seeds of ₹ 50,000 in cash from a farmer on a banking day.

(iii) Tax on non-monetary perquisite provided to an employee ₹ 20,000.

(iv) Payment of ₹ 50,000 by using credit card for fire insurance.

(v) Salary payment of ₹ 2,00,000 outside India by a company without deduction of tax.

(vi) Sales tax deposited in cash ₹ 50,000 with State Bank of India.

(vii) Payment made in cash ₹ 30,000 to a transporter in a day for carriage of goods

Answer

(i) Not allowable as deduction: As per section 40A(7), no deduction is allowed in computing business income in respect of any provision made by the assessee in his books of account for the payment of gratuity to his employees except in the following two cases:

(1) where any provision is made for the purpose of payment of sum by way of contribution towards an approved gratuity fund or;

(2) where any provision is made for the purpose of making any payment on account of gratuity that has become payable during the previous year.

Therefore, in the present case, the provision made on the basis of actuarial valuation for payment of gratuity has to be disallowed under section 40A(7), since, no payment has been actually made on account of gratuity.

Note: It is assumed that such provision is not for the purpose of contribution towards an approved gratuity fund.

(ii) Allowable as deduction: As per Rule 6DD, in case the payment is made for purchase of agricultural produce directly to the cultivator, grower or producer of such agricultural produce, no disallowance under section 40A(3) is attracted even though the cash payment for the expense exceeds ₹ 20,000.

Therefore, in the given case, disallowance under section 40A(3) is not attracted since, cash payment for purchase of oil seeds is made directly to the farmer.

(iii) Not allowable as deduction: Income-tax of ₹ 20,000 paid by the employer in respect of non-monetary perquisites provided to its employees is exempt in the hands of the employee under section 10(10CC). As per section 40(a)(v), such income-tax paid by the employer is not deductible while computing business income.

(iv) Allowable as deduction: Payment for fire insurance is allowable as deduction under section 36(1). Since payment by credit card is covered under Rule 6DD, which contains the exceptions to section 40A(3), disallowance under section 40A(3) is not attracted in this case.

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(v) **Not allowable as deduction:** Disallowance under section 40(a)(iii) is attracted in respect of salary payment of ₹ 2,00,000 outside India by a company without deduction of tax at source.

(vi) **Allowable as deduction:** As per Rule 6DD, if the payment is made to the Government and, under the rules framed by it, such payment is required to be made in legal tender, no disallowance under section 40A(3) is attracted even though the cash payment for the expense exceeds ₹ 20,000.

Therefore, in the given case, no disallowance under section 40A(3) is attracted since payment of sales tax is covered by the above mentioned exception contained in Rule 6DD.

(vii) **Allowable as deduction:** The limit for attracting disallowance under section 40A(3) for payment otherwise than by way of account payee cheque or account payee bank draft is ₹ 35,000 in case of payment made for plying, hiring or leasing goods carriage. Therefore, in the present case, disallowance under section 40A(3) is not attracted for payment of ₹ 30,000 made in cash to a transporter for carriage of goods.

Question 24

Ramji Ltd., engaged in manufacture of medicines (pharmaceuticals), furnishes the following information for the year ended 31.03.2017:

(i) Municipal tax relating to office building ₹ 51,000 not paid till 30.09.2017.

(ii) Patent acquired for ₹ 20,00,000 on 01.09.2016 and used from the same month.

(iii) Capital expenditure on scientific research ₹ 10,00,000 which includes cost of land ₹ 2,00,000.

(iv) Amount due from customer X, outstanding for more than 3 years, written off as bad debt in the books ₹ 5,00,000.

(v) Income-tax paid ₹ 90,000 by the company in respect of non-monetary perquisites provided to its employees.

(vi) Provident fund contribution of employees ₹ 5,50,000 remitted in July ,2017.

(vii) Expenditure towards advertisement in souvenir of a political party ₹ 1,50,000.

(viii) Refund of sales tax ₹ 75,000 received during the year, which was claimed as expenditure in an earlier year.

State with reasons the taxability or deductibility of the items given above under the Income-tax Act, 1961.

Note: *Computation of total income is not required.*

Answer

(i) As per section 43B, municipal tax is not deductible for A.Y. 2017-18 since it is not paid on or before 30.09.2017, being the due date of filing the return for A.Y. 2017-18.

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Note – It is assumed that the company has not undertaken any international transaction or has not entered into a Specified Domestic transaction during the year, and therefore, does not have to file a transfer pricing report under section 92E. Therefore, the due date of filing of return of the company would be 30th September, 2017.

(ii) Patent is an intangible asset eligible for depreciation@25%, as per section 32(2)(ii). Since it has been acquired and put to use for more than 180 days during the previous year 2016-17, full depreciation of ₹ 5,00,000 (i.e. 25% of ₹ 20,00,000) is allowable as deduction.

(iii) Weighted deduction@200% is available under section 35(2AB) in respect of expenditure incurred by a company on scientific research on in-house research and development facility as approved by the prescribed authority. However, cost of land is not eligible for deduction.

Deduction under section 35(2AB) = 200% of ₹ 8 lakhs = ₹ 16,00,000.

Note: It is presumed that the in-house research and development facility is approved by the prescribed authority and is hence, eligible for weighted deducted @ 200% under section 35(2AB).

(iv) Bad debts i.e. ₹ 5,00,000 written off in the books of account as irrecoverable is deductible under section 36(1)(vii), provided the debt has been taken into account in computing the income of the company in the current previous year or any of the earlier previous years.

(v) As per section 40(a)(v), income-tax of ₹ 90,000 paid by the company in respect of non-monetary perquisites provided to its employees, exempt in the employee's hands under section 10(10CC), is not deductible while computing business income of the employer–company.

(vi) The employees' contribution to provident fund is taxable in the hands of the company since it is included in the definition of income under section 2(24)(x).

As per section 36(1)(va), provident fund contribution of employees is deductible only if such sum is credited to the employee's provident fund account on or before the due date under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952. In this case, since it is remitted after the due date under the said Act, it is not deductible. This conclusion is supported by the Hon'ble Gujarat High Court ruling in *CIT v. Gujarat State Road Transport Corporation [(2014) 223 Taxmann 398].*

Note: *The Delhi High Court, in CIT vs. Aimil Ltd.(2010) 321 ITR 508, has held that provident fund contribution of employees is deductible in the hands of the employer even if it is remitted after the due date under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952, provided the same is remitted before the due date of filing return of income.*

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(vii) Expenditure towards advertisement in souvenir of a political party is disallowed under section 37(2B) while computing business income.

However, the same is deductible under section 80GGB from gross total income provided the payment is made by any mode other than cash.

(viii) Refund of a trading liability is taxable under section 41(1), if a deduction was allowed in respect of the same to the taxpayer in an earlier year. Since sales tax was claimed as expenditure in an earlier year, refund of the same during the year would attract the provisions of section 41(1).

Question 25

Answer the following with reference to the provisions of the Income-tax Act, 1961:

(a) Bad debt claim disallowed in an earlier assessment year, recovered subsequently. Is the sum recovered chargeable to tax?

(b) Tax deducted at source on salary paid to employees not remitted till the 'due date' for filing the return prescribed in section 139. Is the expenditure to be disallowed under section 40(a)(ia)?

(c) X Co. Ltd. paid ₹ 120 lakhs as compensation as per approved Voluntary Retirement Scheme (VRS) during the financial year 2016-17. How much is deductible under section 35DDA for the assessment year 2017-18?

(d) Bad debt of ₹ 50,000 written off and allowed in the financial year 2014-15 recovered in the financial year 2016-17.

Answer

(a) Recovery of a bad debt claim disallowed in the earlier year cannot be brought to tax under section 41(4). Section 41(4) can be invoked only in a case where bad debts or part thereof has been allowed as deduction earlier under section 36(1)(vii).

(b) The scope of section 40(a)(ia) has been expanded w.e.f. A.Y. 2016-17 to cover all sums in respect of which tax is deductible under Chapter XVII-B. Section 192, which requires deduction of tax at source from salary income, forms part of Chapter XVII-B. Therefore, salary payment without deduction of tax at source would attract disallowance under section 40(a)(ia). However, only 30% of salary paid without deduction tax at source would be disallowed under section 40(a)(ia).

(c) It is deductible in 5 equal annual instalments commencing from the previous year of payment. ₹ 24 lakhs, being $1/5^{th}$ of ₹ 120 lakhs, is deductible under section 35DDA for the A.Y.2017-18.

(d) As per section 41(4), any amount recovered by the assessee against bad debt earlier allowed as deduction shall be taxed as income in the year in which it is received. Therefore, in this case, ₹ 50,000 would be taxable in the F.Y.2016-17 (A.Y.2017-18).

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Question 26

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

(a) Payment made in respect of a business expenditure incurred on 16th February, 2016 for ₹ 25,000 through a cheque duly crossed as "& Co." is hit by the provisions of section 40A(3).

(b) (i) It is a condition precedent to write off in the books of account, the amount due from debtor to claim deduction for bad debt.

(ii) Failure to deduct tax at source in accordance with the provisions of Chapter XVII-B, inter alia, from the amounts payable to a resident as rent or royalty, will result in disallowance while computing the business income where the resident payee has not paid the tax due on such income.

(c) Co-operative banks are not allowed to claim provision for bad and doubtful debts in respect of advances made by rural branches of such banks.

Answer

(a) True: In order to escape the disallowance specified in section 40A(3), payment in respect of the business expenditure ought to have been made through an account payee cheque. Payment through a cheque crossed as “& Co.” will attract disallowance under section 40A(3).

(b) (i) True: It is mandatory to write off the amount due from a debtor as not receivable in the books of account, in order to claim the same as bad debt under section 36(1)(vii). However, where the debt has been taken into account in computing the income of the assessee on the basis of ICDSs notified under section 145(2), without recording the same in the accounts, then, such debt shall be allowed in the previous year in which such debt becomes irrecoverable and it shall be deemed that such debt or part thereof has been written off as irrecoverable in the accounts for the said purpose.

(ii) True: Section 40(a)(ia) provides that failure to deduct tax at source from rent or royalty payable to a resident, in accordance with the provisions of Chapter XVII-B, will result in disallowance of 30% of such expenditure, where the resident payee has not paid the tax due on such income.

(c) False: Sub-clause (a) of section 36(1)(viia) allows the co-operative banks to claim deduction for provision for bad and doubtful debts in respect of advances made by rural branches of such banks. However, the deduction should not exceed 10% of the aggregate average advances made by the rural branches of such banks computed in the prescribed manner.

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Question 27

Write short notes on:

(i) Restrictions on deductions allowable to the partnership firm in respect of salary and interest to its partners under section 40(b) of the Income-tax Act, 1961.

(ii) Carry forward and set off of unabsorbed depreciation.

(iii) Additional depreciation.

Answer

(i) In the case of a partnership firm, the deduction on account of interest and salary paid to its partners are as subject to the following restrictions contained in section 40(b) -

(i) It should be authorised by and in accordance with the terms of the partnership deed.

(ii) It should not relate to a period before the date of such deed.

(iii) Remuneration should be paid to a working partner.

(iv) The amounts allowable are subject to the following limits -

(1) In the case of interest

Simple interest up to 12% p.a. is allowable. This restriction is not applicable if a person is a partner in his representative capacity in the firm and he receives interest from the firm in his individual capacity. Similarly, the restriction is also not applicable if a person who is a partner in his individual capacity receives interest for and on behalf of someone else from the firm in which he is a partner.

(2) In the case of salary, bonus, commission or remuneration paid by a firm to its working partners – It should not exceed the amount specified in the table below -

	For all firms	
(a)	On the first ₹ 3,00,000 of the book profit or in case of loss	₹ 1,50,000 or 90% of book profit, whichever is more
(b)	On the balance of the book profit	@ 60%

(ii) Section 32(2) provides for carry forward of unabsorbed depreciation.

Where, in any previous year, the profits or gains chargeable are not sufficient to give full effect to the depreciation allowance, such unabsorbed depreciation shall be added to the depreciation allowance for the following previous year and shall be deemed to be part of that allowance.

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If there is no depreciation allowance for that previous year, the unabsorbed depreciation of the earlier previous year shall become the depreciation allowance of that year. The effect of the provisions of section 32(2) is that unabsorbed depreciation brought forward shall be deemed as the current year depreciation. Consequently, such unabsorbed depreciation can be set-off not only against income under the head "Profits and gains of business or profession" but also against income under any other head. Further, the unabsorbed depreciation can be carried forward indefinitely till it is fully set off.

However, in the order of set-off losses under different heads of income, effect shall first be given to current year depreciation, then to brought forward business losses and finally to unabsorbed depreciation.

(iii) Section 32(1)(iia) provides that in the case of any new machinery or plant (other than ships and aircraft) acquired and installed after 31.3.2005 by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation or generation and distribution of power, a further sum equal to 20% of the actual cost of such machinery or plant shall be allowable as a deduction.

The additional depreciation is available to a new machinery or plant used in the manufacture or production of any article or thing or generation or generation and distribution of power. Additional depreciation will be taken into consideration for computing the WDV of the relevant block of assets.

Additional depreciation is not available in respect of the following assets:

(A) any machinery or plant

- (i) which has been used in India or outside India by any other person before its installation by the assessee; or
- (ii) installed in any office premises, residential accommodation including accommodation used in the nature of guest house ; or
- (iii) the whole of the actual cost of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income under the head "Profits and gains of business or profession" of any one previous year.

(B) any office appliances or road transport vehicles.

If the new plant and machinery is put to use for less than 180 days during the previous year, additional depreciation would be restricted to 10% (i.e., 50% of 20%). The balance additional depreciation can be claimed in the immediately succeeding previous year.

Question 28

Rao & Jain, a partnership firm consisting of two partners, reports a net profit of ₹ 7,00,000 before deduction of the following items:

(1) Salary of ₹ 20,000 each per month payable to two working partners of the firm (as authorized by the deed of partnership).

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(2) Depreciation on plant and machinery under section 32 (computed) ₹ 1,50,000.

(3) Interest on capital at 15% per annum (as per the deed of partnership). The amount of capital eligible for interest ₹ 5,00,000.

Compute:

(i) Book-profit of the firm under section 40(b) of the Income-tax Act, 1961.

(ii) Allowable working partner salary for the assessment year 2017-18 as per section 40(b).

Answer

(i) As per *Explanation 3* to section 40(b), "book profit" shall mean the net profit as per the profit and loss account for the relevant previous year computed in the manner laid down in Chapter IV-D as increased by the aggregate amount of the remuneration paid or payable to the partners of the firm if the same has been already deducted while computing the net profit.

In the present case, the net profit given is before deduction of depreciation on plant and machinery, interest on capital of partners and salary to the working partners. Therefore, the book profit shall be as follows:

Computation of Book Profit of the firm under section 40(b)

Particulars	₹	₹
Net Profit (before deduction of depreciation, salary and interest)		7,00,000
Less: Depreciation under section 32	1,50,000	
Interest @ 12% p.a. [being the maximum allowable as per section 40(b)] (5,00,000 × 12%)	60,000	2,10,000
Book Profit		**4,90,000**

(ii) Salary actually paid to working partners = ₹ 20,000 × 2 × 12 = ₹ 4,80,000.

As per the provisions of section 40(b)(v), the salary paid to the working partners is allowed subject to the following limits -

On the first ₹ 3,00,000 of book profit or in case of loss	₹ 1,50,000 or 90% of book profit, whichever is more
On the balance of book profit	60% of the balance book profit

Therefore, the maximum allowable working partners' salary for the A.Y. 2017-18 in this case would be:

Particulars	₹
On the first ₹ 3,00,000 of book profit [(₹ 1,50,000 or 90% of ₹ 3,00,000) whichever is more]	2,70,000

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On the balance of book profit [60% of (₹ 4,90,000 - ₹ 3,00,000)]	1,14,000
Maximum allowable partners' salary	3,84,000

Hence, allowable working partners' salary for the A.Y. 2017-18 as per the provisions of section 40(b)(v) is ₹ 3,84,000.

Question 29

During the financial year 2016-17, the following payments/expenditure were made/incurred by Mr. Yuvan Raja, a resident individual (whose turnover during the year ended 31.3.2016 was ₹ 99 lacs) :

(i) Interest of ₹ 12,000 was paid to Rehman & Co., a resident partnership firm, without deduction of tax at source;

(ii) Interest of ₹ 4,000 was paid as interest to Mr. R.D. Burman, a non-resident, without deduction of tax at source;

(iii) ₹ 3,00,000 was paid as salary to a resident individual without deduction of tax at source;

(iv) Commission of ₹ 15,000 was paid to Mr. Vidyasagar on 2.7.2016. without deduction of tax at source.

Briefly discuss whether any disallowance arises under the provisions of section 40(a)(i)/40(a)(ia) of the Income-tax Act, 1961.

Answer

Disallowance under section 40(a)(i)/40(a)(ia) of the Income-tax Act, 1961 is attracted where the assessee fails to deduct tax at source as is required under the Act, or having deducted tax at source, fails to remit the same to the credit of the Central Government within the stipulated time limit.

The assessee is a resident individual, who was not subjected to tax audit during the immediately preceding previous year i.e., P.Y.2015-16 (as his turnover was less than ₹ 100 lakh in that year) and the TDS obligations have to be considered bearing this in mind.

(i) The obligation to deduct tax at source from interest paid to a resident arises under section 194A in the case of an individual, only where he was subject to tax audit under section 44AB in the immediately preceding previous year, i.e., P.Y.2015-16. From the data given, it is clear that he was not subject to tax audit under section 44AB in the P.Y.2015-16. Hence, disallowance under section 40(a)(ia) is not attracted in this case.

(ii) In the case of interest paid to a non-resident, there is obligation to deduct tax at source under section 195, hence non-deduction of tax at source will attract disallowance under section 40(a)(i).

(iii) The scope of section 40(a)(ia) has been expanded w.e.f. A.Y. 2017-18 to cover all sums in respect of which tax is deductible under Chapter XVII-B. Section 192, which requires

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deduction of tax at source from salary paid, is covered under Chapter XVII-B. Therefore, disallowance under section 40(a)(ia) is attracted for failure to deduct tax at source under section 192 from salary payment. However, only 30% of the amount of salary paid without deduction of tax at source would be disallowed.

(iv) The obligation to deduct tax at source under section 194-H from commission paid in excess of ₹ 5,000 to a resident arises in the case of an individual, only where he was subject to tax audit under section 44AB in the immediately preceding previous year. From the data given, it is clear that he was not subject to tax audit under section 44AB in the P.Y.2015-16. Hence, there is no obligation to deduct tax at source under section 194H during the P.Y. 2016-17. Therefore, disallowance under section 40(a)(ia) is not attracted in this case.

Question 30

M/s. Arora Ltd., submits the following details of expenditure pertaining to the financial year 2016-17:

(i) Payment of professional fees to Mr. Mani ₹ 50,000. Tax was not deducted at source.

(ii) Interior works done by Mr. Hari for ₹ 2,00,000 on a contract basis. Payment made in the month of March 2017. Tax deducted in March 2016 was paid on 30.06.2017.

(iii) Factory Rent paid to Mr. Rao ₹ 15,00,000. Tax deducted at source and paid on 01.10.2017.

(iv) Interest paid on Fixed Deposits ₹ 2,00,000. Tax deducted on 31.12.2016 and paid on 28.09.2017.

Examine the above with reference to allowability of the same in the assessment year 2017-18 under the Income-tax Act, 1961. You answer must be with reference to section 40(a) read with relevant tax deduction at source provisions. Assume that the due date of filing the return of income is 30.09.2017.

Answer

Allowability of expenses of M/s. Arora Ltd. for the A.Y. 2017-18

(i) Payment of professional fees is subject to TDS under section 194J. Since no tax is deducted at source, ₹ 15,000, being 30% of the expenditure of ₹ 50,000 is disallowed under section 40(a)(ia).

(ii) Since the tax was deducted in March, 2017 and paid on or before the due date of filing the return (i.e., on or before September 30th, 2017), the expenditure on interior works will be allowed as deduction. Hence, disallowance under section 40(a)(ia) is not attracted.

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(iii) The maximum time allowable for deposit of tax deducted at source is upto the due date of filing of return i.e., 30th September, 2017. In this case, since tax deducted under section 194-I was paid after the due date of filing the return, ₹ 4,50,000 being 30% of ₹ 15,00,000 is disallowed under section 40(a)(ia) for the previous year 2016-17.

(iv) The tax deducted at source can be deposited on or before the due date of filing of return to avoid disallowance under section 40(a)(ia). In this case, disallowance would not be attracted since tax deducted during December 2016 was deposited before 30th September 2017 i.e. on 28.09.2017.

Question 31

Vinod is a person carrying on profession as film artist. His gross receipts from profession are as under:

	₹
Financial year 2014-15	*1,15,000*
Financial year 2015-16	*1,80,000*
Financial year 2016-17	*2,10,000*

What is his obligation regarding maintenance of books of accounts for each Assessment Year under section 44AA of Income-tax Act, 1961?

Answer

Section 44AA(1) requires every person carrying on any profession, notified by the Board in the Official Gazette (in addition to the professions already specified therein), to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act, 1961.

Thus, a person carrying on a notified profession shall be required to maintain specified books of accounts:

(i) if his gross receipts in all the three years immediately preceding the relevant previous year has exceeded ₹ 1,50,000; or

(ii) if it is a new profession which is setup in the relevant previous year, it is likely to exceed ₹ 1,50,000 in that previous year.

In the present case, Vinod is a person carrying on profession as film artist, which is a notified profession. Since his gross receipts have not exceeded ₹ 1,50,000 in financial year 2014-15, the requirement under section 44AA to compulsorily maintain the prescribed books of account is not applicable to him.

Question 32

Ramamurthy had 4 heavy goods vehicles as on 1.4.2016. He acquired 7 heavy goods vehicles on 27.6.2016. He sold 2 heavy goods vehicles on 31.5.2016.

He has brought forward business loss of ₹ 50,000 relating to assessment year 2013-14 of a discontinued business. Assuming that he opts for presumptive taxation of income as per section 44AE, compute his total income chargeable to tax for the assessment year 2017-18.

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Answer

Computation of total income of Mr. Ramamurthy for A.Y.2017-18

Particulars	₹
Presumptive business income under section 44AE	
4 heavy goods vehicles for 2 months (4 x ₹ 7,500 x 2)	60,000
Balance 2 heavy goods vehicles for 10 months (2 x ₹ 7,500 x 10)	1,50,000
7 heavy goods vehicles for 10 months (7 x ₹ 7,500 x10)	5,25,000
Business Income	7,35,000
Less: Brought forward business loss of discontinued business	50,000
Total Income	**6,85,000**

Note: *The assessee is eligible for computing the income from goods carriages applying the presumptive provisions of section 44AE, since he does not own more than 10 goods carriages at any time during the previous year.*

Question 33

Mr. Praveen engaged in retail trade, reports a turnover of ₹ 1,98,50,000 for the financial year 2016-17. His income from the said business as per books of account is computed at ₹ 13,20,000. Retail trade is the only source of income for Mr. Praveen.

(i) Is Mr. Praveen eligible to opt for presumptive determination of his income chargeable to tax for the assessment year 2017-18?

(ii) If so, determine his income from retail trade as per the applicable presumptive provision.

(iii) In case Mr. Praveen does not opt for presumptive taxation of income from retail trade, what are his obligations under the Income-tax Act, 1961?

(iv) What is the due date for filing his return of income under both the options?

Answer

(i) Yes. Since his total turnover for the F.Y.2016-17 is below ₹ 200 lakhs, he is eligible to opt for presumptive taxation scheme under section 44AD in respect of his retail trade business.

(ii) His income from retail trade, applying the presumptive tax provisions under section 44AD, would be ₹ 15,88,000, being 8% of ₹ 1,98,50,000.

(iii) Section 44AB makes it obligatory for every person carrying on business to get his accounts of any previous year audited if his total sales, turnover or gross receipts exceed ₹ 1 crore. However, if an eligible person opts for presumptive taxation scheme as per section 44AD(1), he shall not be required to get his accounts audited if the total turnover or gross receipts of the relevant previous year does not exceed ₹ 2 crore. The CBDT,

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has vide its Press Release dated 20th June, 2016, clarified that the higher threshold for non-audit of accounts has been given only to assessees opting for presumptive taxation scheme under section 44AD.

In this case, if Mr. Praveen does not opt for the presumptive taxation scheme under section 44AD, he has to get his books of accounts audited and furnish a report of such audit under section 44AB, since his turnover exceeds ₹ 1 crore during the P.Y.2016-17.

(iv) In case he opts for the presumptive taxation scheme under section 44AD, the due date would be 31st July, 2017.

In case he does not opt for the presumptive taxation scheme, he is required to get his books of account audited, in which case the due date for filing of return would be 30th September, 2017.

Question 34

Mr. Sukhvinder is engaged in the business of plying goods carriages. On 1st April, 2016, he owns 10 trucks (out of which 6 are heavy goods vehicles). On 2nd May, 2016, he sold one of the heavy goods vehicles and purchased a light goods vehicle on 6th May, 2016. This new vehicle could however be put to use only on 15th June, 2016.

Compute the total income of Mr. Sukhvinder for the assessment year 2017-18, taking note of the following data:

Particulars	**₹**	**₹**
Freight charges collected		*12,70,000*
Less : Operational expenses	*6,25,000*	
Depreciation as per section 32	*1,85,000*	
Other office expenses	*15,000*	*8,25,000*
Net Profit		*4,45,000*
Other business and non- business income		*70,000*

Answer

Section 44AE would apply in the case of Mr. Sukhvinder since he is engaged in the business of plying goods carriages and owns not more than ten goods carriages at any time during the previous year.

Section 44AE provides for computation of business income of such assessees on a presumptive basis. The income shall be deemed to be ₹ 7,500 from each goods carriage (whether it is heavy or light vehicle) - for every month or part the month during which such carriage vehicle is owned by the assessee in the previous year or such higher sum as declared by the assessee in his return of income.

Mr. Sukhvinder's business income calculated applying the provisions of section 44AE is ₹ 9,07,500 (See Notes 1 & 2 below) and his total income would be ₹ 9,77,500.

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However, as per section 44AE(7), Mr. Sukhvinder may claim lower profits and gains if he keeps and maintains proper books of account as per section 44AA and gets the same audited and furnishes a report of such audit as required under section 44AB. If he does so, then his income for tax purposes from goods carriages would be ₹ 4,45,000 instead of ₹ 9,07,500 and his total income would be ₹ 5,15,000.

Notes :

1. **Computation of total income of Mr. Sukhvinder for A.Y. 2017-18**

Particulars	Presumptive income	Where books are maintained
Income from business of plying goods carriages **[See Note 2 Below]**	9,07,500	4,45,000
Other business and non business income	70,000	70,000
Total Income	9,77,500	5,15,000

2. **Calculation of presumptive income as per section 44AE**

Type of carriage	No. of months	Rate per month	Amount
(1)	**(2)**	**(3)**	**(4)**
9 goods carriage – held throughout the year	12	7,500	8,10,000
1 goods carriage – held upto 2nd May	2	7,500	15,000
1 goods carriage – held from 6th May	11	7,500	82,500
		Total	9,07,500

Question 35

X Ltd. follows mercantile system of accounting. After negotiations with the bank, interest of ₹ 4 lakhs (including interest of ₹ 1.2 lakhs pertaining to year ended 31.03.2017 has been converted into loan. Can the interest of ₹ 1.2 lakhs so capitalized be claimed as business expenditure?

Answer

Under section 43B, interest on term loans and advances to scheduled banks shall be allowed only in the year of payment of such interest irrespective of the method of accounting followed by the assessee.

Explanation 3D to section 43B provides that if any interest payable by the assessee is converted into a loan, the interest so converted and not "actually paid" shall not be deemed as actual payment, and hence would not be allowed as deduction. Therefore, the interest of ₹ 1.2 lakhs converted into loan cannot be claimed as business expenditure.

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Question 36

Mr. B.A. Patel, a non-resident, operates an aircraft between London to Ahmedabad. For the Financial year ended on 31st March, 2017, he received the amounts as under:

(i) For carrying passengers from Ahmedabad ₹ 50 lacs.

(ii) For carrying passengers from London ₹ 75 lacs received in India.

(iii) For carrying of goods from Ahmedabad ₹ 25 lacs.

The total expenditure incurred by Mr. B.A. Patel for the purposes of the business for the financial year 2016-17 was ₹ 1.4 crores.

Compute the income of Mr. B.A. Patel under the head "Profits and Gains from business or profession" for the financial year ended on 31st March 2017 relevant to assessment year 2017-18.

Answer

Under section 44BBA, in case of an assessee, being a non-resident, engaged in the business of operation of aircraft, a sum equal to 5% of the aggregate of the following amounts shall be deemed to be his business income:

(a) the amount paid or payable, whether in or out of India, to the assessee on account of carriage of passengers, goods etc. from any place in India; and

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

Hence, the income of Mr. B.A. Patel chargeable to tax in India under the head "Profits and Gains of business or profession" is determined as under:

Particulars	₹
(i) For carrying passengers from Ahmedabad	50,00,000
(ii) For carrying passengers from London, amount received in India	75,00,000
(iii) For carrying goods from Ahmedabad	25,00,000
Total	**1,50,00,000**

Hence, income from business computed on presumptive basis as per section 44BBA is ₹ 7,50,000, being 5% of ₹ 1,50,00,000.

Note: *No deduction is allowable in respect of any expenditure incurred for the purpose of the business.*

Question 37

List items of expenses which otherwise are deductible shall be disallowed, unless payments are actually made within the due date for furnishing the return of income under Section 139(1). When can the deduction be claimed, if paid after the said date?

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Answer

Section 43B provides that the following expenses shall not be allowed as deduction unless the payments are actually made within the due date for furnishing the return of income under section 139(1):

(i) Any tax, duty, cess or fees under any law in force.

(ii) Any sum payable by the assessee as an employer by way of contribution to provident fund or superannuation fund or gratuity fund or any other fund for the welfare of the employees;

(iii) Any bonus or commission for services rendered payable to employees;

(iv) Any interest on any loan or borrowings from any public financial institution or State financial corporation or State industrial investment corporation;

(v) Interest on loans and advances from a scheduled bank;

(vi) Any sum paid as an employer in lieu of earned leave at the credit of his employee.

(vii) Any sum payable by the assessee to the Indian Railways for the use of railway assets.

In case the payment is made after the due date of filing of return of income, deduction can be claimed only in the year of actual payment.

Question 38

Mr. Asim, a 60 year old individual, engaged in the business of roasting and grounding of coffee, derives income of ₹ 10 lacs during the financial year 2016-17. Compute the tax payable by him assuming he has not earned any other income during the financial year 2016-17. What would be your answer if Mr. Asim is also engaged in the business of growing and curing coffee?

Answer

If Mr. Asim is engaged only in the business of roasting and grounding of coffee (and not growing and curing of coffee), his entire income of ₹ 10 lakhs would be treated as business income and his tax liability would be ₹ 1,23,600 (₹ 1,20,000+₹ 2,400+₹ 1,200).

If Mr. Asim is also engaged in the business of growing and curing of coffee, in addition to roasting and grounding of coffee, the provisions of Rule 7B of the Income-tax Rules, 1962 would apply. As per Rule 7B, where income is derived from the sale of coffee grown, cured, roasted and grounded by the seller in India, 40% of such income shall be treated as business income and the balance as agricultural income.

Therefore, in such a case, the business income would be 40% of ₹ 10,00,000 = ₹ 4,00,000

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Calculation of tax liability for A.Y 2017-18

Particulars	₹
Tax on ₹ 10,00,000 [being the aggregate of non-agricultural income (i.e. ₹ 4,00,000) and agricultural income (i.e. ₹ 6,00,000)]	1,20,000
Less: Tax on ₹ 9,00,000 [being aggregate of agricultural income (i.e. ₹ 6,00,000) and basic exemption limit (i.e. ₹ 3,00,000)]	
	1,00,000
	20,000
Less: Rebate u/s 87A	5,000
	15,000
Add: Education cess @ 2%	300
Secondary and higher education cess @ 1%	150
Total tax liability	**15,450**

Question 39

Mr. Tenzingh is engaged in composite business of growing and curing (further processing) coffee in Coorg, Karnataka. The whole of coffee grown in his plantation is cured. Relevant information pertaining to the year ended 31.3.2017 are given below:

Particulars	*₹*
WDV of car as on 1.4.2016	*3,00,000*
WDV of machinery as on 1.4.2016 (15% rate)	*15,00,000*
Expenses incurred for growing coffee	*3,10,000*
Expenditure for curing coffee	*3,00,000*
Sale value of cured coffee	*22,00,000*

Besides being used for agricultural operations, the car is also used for personal use; disallowance for personal use may be taken at 20%. The expenses incurred for car running and maintenance are ₹ 50,000. The machines were used in coffee curing business operations.

Compute the income arising from the above activities for the assessment year 2017-18. Show the WDV of the assets as on 1.4.2017.

Answer

Where an assessee is engaged in the composite business of growing and curing of coffee, the income will be segregated between agricultural income and business income, as per Rule 7B of the Income-tax Rules, 1962.

As per the above Rule, income derived from sale of coffee grown and cured by the seller in India shall be computed as if it were income derived from business, and 25% of such income

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shall be deemed to be income liable to tax. The balance 75% will be treated as agricultural income.

Particulars	₹	₹	₹
Sale value of cured coffee			22,00,000
Less: Expenses for growing coffee		3,10,000	
Car expenses (80% of ₹ 50,000)		40,000	
Depreciation on car (80% of 15% of ₹ 3,00,000) **[See Computation below]**		36,000	
Total cost of agricultural operations		3,86,000	
Expenditure for coffee curing operations	3,00,000		
Add: Depreciation on machinery (15% of 15,00,000) **[See Computation below]**	2,25,000		
Total cost of the curing operations		5,25,000	
Total cost of composite operations			9,11,000
Total profits from composite activities			**12,89,000**
Business income (25% of above)			3,22,250
Agricultural income (75% of above)			9,66,750

Computation of value of depreciable assets as on 31.3.2017

Particulars	₹	₹	₹
Car Opening value as on 1.4.2016		3,00,000	
Depreciation thereon at 15%	45,000		
Less: Disallowance @20% for personal use	9,000		
Depreciation actually allowed		36,000	
WDV as on 1.4.2017			2,64,000
Machinery Opening value as on 1.4.2016		15,00,000	
Less: Depreciation @ 15%		2,25,000	
WDV as on 1.4.2017			12,75,000

Explanation 7 to section 43(6) provides that in cases of 'composite income', for the purpose of computing written down value of assets acquired before the previous year, the total amount of depreciation shall be computed as if the entire composite income of the assessee (and not just 25%) is chargeable under the head "Profits and gains of business or profession". The depreciation so computed shall be deemed to have been "actually allowed" to the assessee.

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Question 40

Miss Vivitha, a resident and ordinarily resident in India, has derived the following income from various operations (relating to plantations and estates owned by her) during the year ended 31-3-2017:

S. No.	*Particulars*	₹
(i)	*Income from sale of centrifuged latex processed from rubber plants grown in Darjeeling.*	*3,00,000*
(ii)	*Income from sale of coffee grown and cured in Yercaud, Tamil Nadu.*	*1,00,000*
(iii)	*Income from sale of coffee grown, cured, roasted and grounded, in Colombo. Sale consideration was received at Chennai.*	*2,50,000*
(iv)	*Income from sale of tea grown and manufactured in Shimla.*	*4,00,000*
(v)	*Income from sapling and seedling grown in a nursery at Cochin. Basic operations were not carried out by her on land.*	*80,000*

You are required to compute the business income and agricultural income of Miss Vivitha for the assessment year 2017-18.

Answer

Computation of business income and agricultural income of Ms. Vivitha for the A.Y.2017-18

Sr. No.	Source of income	Gross (₹)	Business income		Agricultural income
			%	₹	₹
(i)	Sale of centrifuged latex from rubber plants grown in India.	3,00,000	35%	1,05,000	1,95,000
(ii)	Sale of coffee grown and cured in India.	1,00,000	25%	25,000	75,000
(iii)	Sale of coffee grown, cured, roasted and grounded outside India. **(See Note 1 below)**	2,50,000	100%	2,50,000	-
(iv)	Sale of tea grown and manufactured in India	4,00,000	40%	1,60,000	2,40,000
(v)	Saplings and seedlings grown in nursery in India **(See Note 2 below)**	80,000		Nil	80,000
	Total			**5,40,000**	**5,90,000**

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Notes:

1. Where income is derived from sale of coffee grown, cured, roasted and grounded by the seller in India, 40% of such income is taken as business income and the balance as agricultural income. However, in this question, these operations are done in Colombo, Sri lanka. Hence, there is no question of such apportionment and the whole income is taxable as business income. Receipt of sale proceeds in India does not make this agricultural income. In the case of an assessee, being a resident and ordinarily resident, the income arising outside India is also chargeable to tax.
2. *Explanation 3* to section 2(1A) provides that the income derived from saplings or seedlings grown in a nursery would be deemed to be agricultural income whether or not the basic operations were carried out on land.

Question 41

Mr. Tony has estates in Rubber, Tea and Coffee. He derives income from them. He has also a nursery wherein he grows and sells plants. For the previous year ending 31.3.2017, he furnishes the following particulars of his sources of income from estates and sale of plants. You are requested to compute the taxable income for the Assessment Year 2017-18:

Sl. No.	*Particulars*	*₹*
(i)	*Manufacture of Rubber*	*5,00,000*
(ii)	*Manufacture of Coffee grown and cured*	*3,50,000*
(iii)	*Manufacture of Tea*	*7,00,000*
(iv)	*Sale of plants from Nursery*	*1,00,000*

Answer

Computation of taxable income of Mr. Tony for A.Y.2017-18

	Particulars	**Business Income (₹)**	**Agricultural Income (₹)**
(a)	Income from manufacture of rubber (Rule 7A)		
	Business income is 35% of ₹ 5,00,000	1,75,000	
	Agricultural income is 65% of ₹ 5,00,000		3,25,000
(b)	Income from growing and curing of coffee (Rule 7B)		
	Business income is 25% of ₹ 3,50,000	87,500	
	Agricultural income is 75% of ₹ 3,50,000		2,62,500
(c)	Income from manufacture of tea (Rule 8)		
	Business income is 40% of ₹ 7,00,000	2,80,000	

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(d)	Agricultural income is 60% of ₹ 7,00,000		4,20,000
	Income from sale of plants in nursery is agricultural income [See Note below]	Nil	1,00,000
		5,42,500	**11,07,500**

Note: *Explanation 3* to Section 2(1A) provides that the income derived from saplings or seedlings grown in a nursery would be deemed to be agricultural income, whether or not the basic operations were carried out on land.

Question 42

Mr. Gupta is having a trading business and his Trading and Profit & Loss Account for the financial year 2016-17 is as under:

Particulars	***Amount (₹)***	***Particulars***	***Amount (₹)***
To Opening stock	*1,00,000*	*By Sales*	*2,70,00,000*
To Purchase	*2,49,00,000*	*By Closing stock*	*50,000*
To Gross profit	*20,50,000*		
Total	***2,70,50,000***	***Total***	***2,70,50,000***
Salary to employees (Including Contribution to PF)	*5,00,000*	*By Gross Profit b/d*	*20,50,000*
Donation to Prime Minister Relief Fund	*1,00,000*		
Provision for bad debts	*50,000*		
Bonus to employees	*50,000*		
Interest on bank loan	*50,000*		
Family planning expenditure incurred on employees	*20,000*		
Depreciation	*30,000*		
Income-tax	*1,00,000*		
To Net profit	*11,50,000*		
Total	***20,50,000***	***Total***	***20,50,000***

Other information:

(i) Depreciation allowable ₹ 40,000 as per Income-tax Rules, 1962.

(ii) No deduction of tax at source on payment of interest on bank loan has been made.

(iii) Out of salary, ₹ 25,000 pertains to his contributions to recognized provident fund which was deposited after the due date of filing return of income. Further, employees contribution of ₹ 25,000 was also deposited after the due date of filing return of income.

Calculate gross total income of Mr. Gupta for the Assessment Year 2017-18.

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Answer

Computation of Gross Total Income of Mr. Gupta for the A.Y. 2017-18

Particulars	₹	₹
Income from Business or profession		
Net profit as per Profit and Loss Account		11,50,000
Add **: Expenses not deductible**		
Donation to Prime Minister Relief Fund (Refer Note 1)	1,00,000	
Provision for bad debts (Refer Note 2)	50,000	
Family planning expenditure incurred on employees (Refer Note 3)	20,000	
Depreciation as per Profit and Loss Account	30,000	
Income-tax (Refer Note 4)	1,00,000	
Employer's contribution to recognized provident fund (Note 5)	25,000	3,25,000
		14,75,000
Less **: Expense allowed**		
Depreciation as per Income-tax Rules, 1962		40,000
		14,35,000
Add : Employee's contribution included in income as per Section 2(24)(x) (Refer Note 6)		25,000
Business Income / Gross Total Income		**14,60,000**

Notes:-

(1) Donation to Prime Minister Relief Fund is not allowed as deduction from the business income. It is allowed as deduction under section 80G from the gross total income.

(2) Provisions for bad debts is allowable as deduction under section 36(1)(viia) (subject to the limits specified therein) only in case of banks, public financial institutions, State Financial Corporation and State Industrial Investment Corporation. Therefore, it is not allowable as deduction in the case of Mr. Gupta.

(3) Expenditure on family planning is allowed as deduction under section 36(1)(ix) only to a company assessee. Therefore, such expenditure is not allowable as deduction in the hands of Mr. Gupta.

(4) Income-tax paid is not allowed as deduction as per the provisions of section 40(a)(ii).

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(5) Since, Mr. Gupta's contribution (by the employer) to recognized provident fund is deposited after the due date of filing return of income, the same is disallowed as per provisions of section 43B.

(6) Employee's contribution is includible in the income of the employer by virtue of Section 2(24)(x). The deduction for the same is not provided for as it was deposited after the due date.

(7) TDS provisions under section 194A are not attracted in respect of payment of interest on bank loan. Therefore, disallowance under section 40(a)(ia) is not attracted in this case.

Question 43

Mr. Raju, a manufacturer at Chennai, gives the following Manufacturing, Trading and Profit & Loss Account for the year ended 31.03.2017:

Manufacturing, Trading and Profit & Loss Account for the year ended 31.03.2017

Particulars	*₹*	*Particulars*	*₹*
To Opening Stock	*71,000*	*By Sales*	*2,32,00,000*
To Purchase of Raw Materials	*2,16,99,000*	*By Closing stock*	*2,00,000*
To Manufacturing Wages & Expenses	*5,70,000*		
To Gross Profit	*10,60,000*		
	2,34,00,000		*2,34,00,000*
To Administrative charges	*3,26,000*	*By Gross Profit*	*10,60,000*
To State VAT penalty	*5,000*	*By Dividend from domestic companies*	*15,000*
To State VAT paid	*1,10,000*	*By Income from agriculture (net)*	*1,80,000*
To General Expenses	*54,000*		
To Interest to Bank	*60,000*		
(On machinery term loan)			
To Depreciation	*2,00,000*		
To Net Profit	*5,00,000*		
	12,55,000		***12,55,000***

Following are the further information relating to the financial year 2016-17:

(i) *Administrative charges include ₹ 46,000 paid as commission to brother of the assessee. The commission amount at the market rate is ₹ 36,000.*

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(ii) *The assessee paid ₹ 33,000 in cash to a transport carrier on 29.12.2016. This amount is included in manufacturing expenses (Assume that the provisions relating to TDS are not applicable to this payment.)*

(iii) *A sum of ₹ 4,000 per month was paid as salary to a staff throughout the year and this has not been recorded in the books of account.*

(iv) *Bank term loan interest actually paid upto 31.03.2017 was ₹ 20,000 and the balance was paid in October 2017.*

(v) *Housing loan principal repaid during the year was ₹ 50,000 and it relates to residential property occupied by him. Interest on housing loan was ₹ 23,000. Housing loan was taken from Canara Bank. These amounts were not dealt with in the profit and loss account given above.*

(vi) *Depreciation allowable under the Act is to be computed on the basis of following information:*

Plant & Machinery (Depreciation rate @ 15%)	***₹***
Opening WDV (as on 01.04.2016)	*12,00,000*
Additions during the year (used for more than 180 days)	*2,00,000*
Total additions during the year	*4,00,000*
Note: Ignore additional depreciation under section 32(1)(iia)	

Compute the total income of Mr. Raju for the assessment year 2017-18.

Note: Ignore application of section 14A for disallowance of expenditures in respect of any exempt income.

Answer

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

Particulars		**₹**	**₹**
Profits and gains of business or profession			
Net profit as per profit and loss account			5,00,000
Add:	Excess commission paid to brother disallowed under section 40A(2)	10,000	
	Disallowance under section 40A(3) is not attracted since the limit for one time cash payment is ₹ 35,000 in respect of payment to transport operators. Therefore, amount of ₹ 33,000 paid in cash to a transport carrier is allowable as deduction.	Nil	
	Salary paid to staff not recorded in the books (Assuming that the expenditure is in the nature of unexplained expenditure	48,000	

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		₹	₹
	and hence, is deemed to be income as per section 69C and would be taxable @ 30% under section 115BBE – no deduction allowable in respect of such expenditure) **[See Note 1 below]**		
	Bank term loan interest paid after the due date of filing of return under section 139(1) – disallowed as per section 43B	40,000	
	State VAT penalty paid disallowed **[See Note 2 below]**	5,000	
	Depreciation debited to profit and loss account	2,00,000	3,03,000
			8,03,000
Less:	Dividend from domestic companies [Exempt under section 10(34)]	15,000	
	Income from agriculture [Exempt under section 10(1)]	1,80,000	
	Depreciation under the Income-tax Act, 1961 (As per working note)	2,25,000	4,20,000
			3,83,000
Income from house property			
Annual value of self-occupied property		Nil	
Less:	Deduction under section 24(b) – interest on housing loan	23,000	(23,000)
Gross Total Income			**3,60,000**
Less:	Deduction under section 80C in respect of Principal repayment of housing loan		50,000
Total Income			**3,10,000**

Working Note:

Computation of depreciation under the Income-tax Act, 1961

Particulars	₹
Depreciation@15% on ₹ 14 lakh (Opening WDV of ₹ 12 lakh plus assets purchased during the year and used for more than 180 days ₹ 2 lakh)	2,10,000
Depreciation @7.5% on ₹ 2 lakh (Cost of assets used for less than 180 days)	15,000
	2,25,000

Notes (Alternate views):

1. It is also possible to take a view that the salary not recorded in the books of account was an erroneous omission and that the assessee has offered satisfactory explanation for the same. In such a case, the same should not be added back as unexplained expenditure, but would be allowable as deduction while computing profits and gains of business and profession.

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2. Where the imposition of penalty is not for delay in payment of sales tax or VAT but for contravention of provisions of the Sales Tax Act (or VAT Act), the levy is not compensatory and therefore, not deductible. However, if the levy is compensatory in nature, it would be fully allowable. Where it is a composite levy, the portion which is compensatory is allowable and that portion which is penal is to be disallowed.

   Since the question only mentions "State VAT penalty paid" and the reason for levy of penalty is not given, it has been assumed that the levy is not compensatory and therefore, not deductible. It is, however, possible to assume that such levy is compensatory in nature and hence, allowable as deduction. In such a case, the total income would be ₹ 3,05,000.

Question 44

Mr. Sivam, a retail trader of Cochin gives the following Trading and Profit and Loss Account for the year ended 31st March, 2017:

Trading and Profit and Loss Account for the year ended 31.03.2017

Particulars	*₹*	*Particulars*	*₹*
To Opening stock	*90,000*	*By Sales*	*1,12,11,500*
To Purchases	*1,10,04,000*	*By Closing stock*	*1,86,100*
To Gross Profit	*3,03,600*		*-*
	1,13,97,600		*1,13,97,600*
To Salary	*60,000*	*By Gross profit b/d*	*3,03,600*
To Rent and rates	*36,000*	*By Income from UTI*	*2,400*
To Interest on loan	*15,000*		
To Depreciation	*1,05,000*		
To Printing & stationery	*23,200*		
To Postage & telegram	*1,640*		
To Loss on sale of shares (Short term)	*8,100*		
To Other general expenses	*7,060*		
To Net Profit	*50,000*		
	3,06,000		*3,06,000*

Additional Information:

(i) It was found that some stocks were omitted to be included in both the Opening and Closing Stock, the values of which were:

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Opening stock ₹ 9,000

Closing stock ₹ 18,000

(ii) Salary includes ₹ 10,000 paid to his brother, which is unreasonable to the extent of ₹ 2,000.

(iii) The whole amount of printing and stationery was paid in cash by way of one time payment.

(iv) The depreciation provided in the Profit and Loss Account ₹ 1,05,000 was based on the following information :

The written down value of plant and machinery is ₹ 4,20,000 as on 01.04.2016. A new plant falling under the same block of depreciation was bought on 1.7.2016 for ₹ 70,000. Two old plants were sold on 1.10.2016 for ₹ 50,000.

(v) Rent and rates includes sales tax liability of ₹ 3,400 paid on 7.4.2017.

(vi) Other general expenses include ₹ 2,000 paid as donation to a Public Charitable Trust.

You are required to advise Mr. Sivam whether he can opt for presumptive taxation under section 44AD and if so, whether it would be beneficial for him to declare income as per section 44AD. Assume that he has not opted for presumptive taxation scheme in any earlier previous year.

Answer

Computation of business income of Mr. Sivam for the A.Y. 2017-18

Particulars		₹	₹
Net Profit as per profit and loss account			50,000
Add:	Inadmissible expenses / losses		
	Under valuation of closing stock	18,000	
	Salary paid to brother – unreasonable [Section 40A(2)]	2,000	
	Printing and stationery paid in cash [Section 40A(3)]	23,200	
	Depreciation (considered separately)	1,05,000	
	Short term capital loss on shares	8,100	
	Donation to public charitable trust	2,000	1,58,300
			2,08,300
Less:	Deductions items:		
	Under valuation of opening stock	9,000	
	Income from UTI [Exempt under section 10(35)]	2,400	11,400
	Business income before depreciation		1,96,900
Less:	Depreciation (See Note 1)		66,000
			1,30,900

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Computation of business income as per section 44AD -

As per section 44AD, the business income would be 8% of turnover i.e., 1,12,11,500 x 8 /100 = ₹ 8,96,920

The business income under section 44AD is **₹ 8,96,920.**

In this case, Mr. Sivam is eligible to opt for presumptive taxation under section 44AD, since his turnover does not exceed ₹ 2 crore in the P.Y.2016-17. However, in his case, business income as per the normal provisions of the Act is lower than the presumptive income of ₹ 8,96,920 computed under section 44AD. Therefore, it is beneficial for him to compute business income as per the normal provisions of the Act. However, since his turnover exceeds ₹ 1 crore, he has to get his books of account audited under section 44AB, if he does not opt to declare his income as per the presumptive tax provisions of section 44AD.

Further, if he declares income as per presumptive tax provisions of section 44AD this year i.e., P.Y.2016-17, and he does not opt for presumptive taxation in any of the five succeeding previous years (i.e., from P.Y.2017-18 to P.Y.2021-22), say, for instance, in P.Y.2017-18, then he will not be eligible to opt for presumptive taxation for five assessment years succeeding the A.Y. 2018-19 relevant to the P.Y. 2017-18.

Notes:

1. **Calculation of depreciation**

Particulars	₹
WDV of the block of plant & machinery as on 1.4.2016	4,20,000
Add : Cost of new plant & machinery	70,000
	4,90,000
Less : Sale proceeds of assets sold	50,000
WDV of the block of plant & machinery as on 31.3.2017	4,40,000
Depreciation @ 15%	66,000
No additional depreciation is allowable as the assessee is not engaged in manufacture or production of any article.	

2. Since sales-tax liability has been paid before the due date of filing return of income under section 139(1), the same is deductible.

Question 45

Following is the profit and loss account of Mr. Q for the year ended 31-03-2017:

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Particulars	₹	Particulars	₹
To Repairs on Building	*1,81,000*	*By Gross Profit*	*6,01,000*
To Amount paid to IIT, Mumbai for an approved scientific research programme	*1,00,000*	*By I.T. Refund*	*8,100*
To Interest	*1,10,000*	*By Interest on Company Deposits*	*6,400*
To Travelling	*1,30,550*		
To Net Profit	*93,950*		
	6,15,500		***6,15,500***

Following additional information is furnished:

(1) Repairs on building includes ₹ 1,00,000 being cost of building a new room.

(2) Interest payments include ₹ 50,000 on which tax has not been deducted and penalty for contravention of Central Sales Tax Act of ₹ 24,000.

Compute the income chargeable under the head "Profits and gains of Business or Profession" of Mr. Q for the year ended 31-03-2017 ignoring depreciation.

Answer

Computation of income under the head "Profits and gains of business or profession" of Mr. Q for the A.Y. 2017-18

Particulars	₹	₹
Net profit as per profit and loss account		93,950
Add: Expenses not allowable		
(i) Expenses on building a new room – Capital expenditure, hence not allowable as per section 37(1).	1,00,000	
(ii) Interest payable on which tax has not been deducted at source [disallowed under section 40(a)] [See Note 1]	15,000	
(iii) Penalty for contravention of Central Sales Tax Act [Penalty paid for violation or infringement of any law is not allowable as deduction under section 37(1)]	24,000	
(iv) Payment to IIT, Mumbai for scientific research programme (to be treated separately)	1,00,000	2,39,000
		3,32,950
Less: Income not forming part of business income		
Interest from company deposits (chargeable under the head "Income from other sources")**(See Note 2 below)**	6,400	

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Income-tax refund (not an income chargeable to tax)	8,100	14,500
		3,18,450
Less: Weighted deduction@200% under section 35(2AA) for payment to IIT for an approved scientific research program.		2,00,000
Profit and gains of business or profession		**1,18,450**

***Note** –1. Section 40(a)(ia) provides for disallowance of 30% of any sum paid, on which tax is deductible under Chapter XVII-B, but the same has not been deducted. Hence, ₹ 15,000 being 30% of ₹ 50,000 has to be added back while computing business income.*

2. Interest on company deposits may also be treated as business income presuming that the interest has been earned by Mr. Q out of available temporary surplus funds which are not immediately required for his business purposes but nevertheless meant only for Mr. Q's business activities. In such a case, income under the head "Profit and gains of business or profession" would be ₹ 1,24,850.

Question 46

Following is the profit and loss account of Mr. A for the year ended 31.3.2017:

Particulars	*₹*	*Particulars*	*₹*
To Repairs on building	*1,30,000*	*By Gross profit*	*6,01,000*
To Advertisement	*51,000*	*By Income Tax Refund*	*4,500*
To Amount paid to Scientific Research Association approved u/s 35	*1,00,000*	*By Interest from company deposits*	*6,400*
To Interest	*1,10,000*	*By Dividends*	*3,600*
To Traveling	*1,30,000*		
To Net Profit	*94,500*		
	6,15,500		*6,15,500*

Following additional information is furnished:

(1) Repairs on building includes ₹ 95,000 being cost of raising a compound wall for the own business premises.

(2) Interest payments include interest of ₹ 12,000 payable outside India to a non-resident Indian on which tax has not been deducted and penalty of ₹ 24,000 for contravention of Central Sales Tax Act.

Compute the income chargeable under the head 'Profits and gains of business or profession' of Mr. A for the year ended 31.3.2017 ignoring depreciation.

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Answer

Profits and gains of business or profession of Mr. A for the year ended 31.3.2017

Particulars	₹	₹
Net profit as per profit and loss account		94,500
Add: Expenses not allowable		
(i) Expenses on raising compound wall – capital expenditure, hence disallowed	95,000	
(ii) Interest payable outside India to a non-resident, as tax has not been deducted at source [Section 40(a)(i)]	12,000	
(iii) Penalty for contravention of CST Act [Penalty paid for violation or infringement of any law is not allowable as deduction under section 37(1)]	24,000	
(iv) Contribution for scientific research (to be treated separately)	1,00,000	2,31,000
		3,25,500
Less: Income not forming part of business income		
Interest from company deposits	6,400	
Dividend	3,600	
Income-tax refund	4,500	14,500
		3,11,000
Less: Deduction under section 35 for scientific research [See Note below]		1,75,000
Profit and gains of business or profession		**1,36,000**

Note: Contribution to approved scientific research association qualifies for deduction @ 175% under section 35(1)(ii).

Question 47

Briefly explain the term "substantial interest". State three situations in which the same assumes importance.

Answer

As per *Explanation* to section 40A(2), a person shall be deemed to have a substantial interest in a business or profession, if, -

(1) in case where the business or profession is carried on by a company, such person who, at any time during the previous year, 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), carrying not less than 20% of the voting power.

(2) In any other case, such person who, at any time during the previous year, is beneficially entitled to not less than 20% of the profits of such business or profession.

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Following are the situations under which the substantial interest assumes importance -

(i) Taxability of deemed dividend under section 2(22)(e);

(ii) Disallowance of excessive or unreasonable expenditure under section 40A(2) to an individual who has a substantial interest in the business or profession of the assessee, and

(iii) Clubbing of salary income of spouse, under section 64(1)(ii) in respect of remuneration received by the spouse from a concern in which the individual has a substantial interest.

Question 48

Raghav Industries Ltd. furnishes you the following information for the year ended 31-03-2017:

(i) Scientific research expenditure related to its business ₹ 2,40,000 fully revenue in nature.

(ii) Building acquired for scientific research (including cost of land ₹ 5,00,000) in June 2016 for ₹ 12,00,000.

(iii) Amount paid to Indian Institute of Science, Bangalore for scientific research ₹ 50,000.

(iv) Demerger expenses incurred in financial year 2015-16 ₹ 5,00,000.

(v) Contribution to the account of employees as per pension scheme referred to in section 80CCD amounted to ₹ 30,00,000. Amount above 10% of the salary of employees is ₹ 7,00,000.

(vi) Amount recovered from employees towards provident fund contribution ₹ 12,00,000 of which amount remitted upto the end of the year was ₹ 7,00,000 and the balance was remitted before the 'due date' for filing the return prescribed in Section 139(1).

(vii) Tax on non-monetary perquisites provided to the employees, borne by the employer ₹ 4,50,000.

(viii) Gain due to change in the rate of exchange of foreign currency ₹ 1,00,000 related to import of machinery. The machinery was acquired two years ago and put to regular use since then.

Explain in brief how the above said items would be dealt with for the A.Y. 2017-18.

Note: Computation of total income not required.

Answer

(i) The entire revenue expenditure of ₹ 2,40,000 on scientific research related to the business of the company qualifies for deduction under section 35(1)(i).

Note – *If Raghav Industries Ltd. is a company engaged in the business of biotechnology or in any business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule, it would be entitled to a weighted deduction of ₹ 4,80,000 (200% of ₹ 2,40,000, being the revenue expenditure*

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on scientific research related to its business) under section 35(2AB), if the in-house research and development facility is approved by the prescribed authority and the company has entered into an agreement with the prescribed authority for cooperation in such research and development facility and for audit of accounts maintained for that facility.

(ii) 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, ₹ 7,00,000 (i.e. ₹ 12,00,000 – ₹ 5,00,000, being the cost of land) is allowable as deduction for the A.Y.2017-18. It is assumed that the scientific research is related to the business of Raghav Industries Ltd.

(iii) The amount of ₹ 50,000 paid to Indian Institute of Science, Bangalore, for scientific research qualifies for a weighted deduction@175% of the sum paid as per section 35(1)(ii). Therefore, Raghav Industries Ltd. would be entitled to a deduction of ₹ 87,500 (i.e., 175% of ₹ 50,000) for the A.Y.2017-18.

(iv) As per section 35DD, one-fifth of the expenditure incurred on demerger would be allowable as deduction for five successive previous years beginning from previous year 2015-16. Therefore, in the previous year 2016-17, ₹ 1,00,000, being one-fifth of ₹ 5,00,000 would be allowable as deduction.

(v) The employer's contribution to the account of an employee under a pension scheme referred to in section 80CCD, upto 10% of salary of the employee in the previous year, is allowable as deduction under section 36(1)(iva) while computing business income.

Disallowance under section 40A(9) would be attracted only in respect of the amount in excess of 10% of salary. Accordingly, ₹ 23 lakhs would be allowed as deduction and ₹ 7 lakhs would be disallowed.

(vi) As per section 2(24)(x), the amount of provident fund contribution recovered from employees i.e. ₹ 12 lakhs would be taxable as income of Raghav Industries Ltd. However, the company can claim deduction under section 36(1)(va) of amount credited to the account of the employee in the provident fund before the due date under the relevant Act.

If ₹ 7 lakhs has been remitted before the said due date, the same is allowable as deduction. If it has not been so remitted, then the same is not allowable as deduction. The deduction would be restricted to the amount remitted before the due date.

The balance ₹ 5 lakhs remitted after the due date under the said Act but before the due date of filing the return is not allowable as deduction.

(vii) The tax of ₹ 4,50,000 borne by the employer on non-monetary perquisites provided to the employees is disallowed under section 40(a)(v).

(viii) As per section 43A, the gain of ₹ 1,00,000, arising at the time of making payment in

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respect of an imported machinery, due to change in rate of exchange of foreign currency, has to be reduced from the actual cost of machinery, and depreciation would be computed on such reduced cost.

Question 49

Explain the tax treatment of Limited Liability Partnership under the Income-tax Act, 1961.

Answer

The taxation scheme of LLPs in the Income-tax Act, 1961 is on the same lines as applicable for general partnerships, i.e. tax liability would be attracted in the hands of the LLP and tax exemption would be available to the partners. Therefore, the same tax treatment would be applicable for both general partnerships and LLPs.

The rate of income-tax applicable to LLPs is the same as the rate applicable for firms i.e. 30% of total income.

The provisions of section 40(b) requiring payment of remuneration only to working partner in accordance with the terms of the partnership deed for a period commencing on or after the date of the partnership deed, would apply to LLPs as well. Further, disallowance of interest in excess of 12% per annum and salary exceeding the prescribed percentage of book profit would also be applicable in the case of LLPs.

However, whereas a partnership firm can opt for presumptive taxation scheme under section 44AD, an LLP cannot opt for such scheme.

Exercise

1. *An assessee uses plant and machinery for the purpose of carrying on his business. Under section 31, he shall be eligible for deduction on account of-*

   (a). both capital and revenue expenditure on repairs

   (b). current repairs

   (c). current repairs plus 1/5th of capital expenditure on repairs.

2. *An electricity company charging depreciation on straight line method on each asset separately, sells one of its machinery in April, 2016 at ₹ 1,20,000. The WDV of the machinery at the beginning of the year i.e. on 1st April, 2016 is ₹ 1,35,000. No new machinery was purchased during the year. The shortfall of ₹ 15,000 is treated as -*

   (a). Terminal depreciation

   (b). Short-term capital loss

   (c). Normal depreciation.

3. *X Ltd. acquires an asset which was previously used for scientific research for ₹ 2,75,000. The asset was brought into use for the business of X Ltd., after the research was completed. The actual cost of the asset to be included in the block of assets is -*

   (a). Nil

   (b). Market value of the asset on the date of transfer to business

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(c). ₹ 2,75,000 less notional depreciation under section 32 upto the date of transfer.

4. *A Ltd. has unabsorbed depreciation of ₹ 4,50,000 for the P.Y.2016-17. This can be carried forward -*
   (a). for a maximum period of 8 years and set-off against business income.
   (b). Indefinitely and set-off against business income.
   (c). Indefinitely and set-off against any head of income except salary.
5. *Deduction under section 33AB is allowed to an assessee provided the assessee deposits the profits with NABARD -*
   (a). before the end of the previous year
   (b). within 6 months from the end of the previous year
   (c). within 6 months from the end of the previous year or before the due date for filing the return of income, whichever is earlier.
6. *XYZ Ltd. incurred capital expenditure of ₹ 1,50,000 on 1.4.2016 for acquisition of patents and copyrights. Such expenditure is -*
   (a). Eligible for deduction in 14 years from A.Y.2017-18
   (b). Eligible for deduction in 5 years from A.Y.2017-18
   (c). Subject to depreciation under section 32
7. *Under section 44AE, presumptive taxation is applicable at a particular rate provided the assessee is the owner of a maximum of certain number of goods carriages. The rate per month or part of the month relevant for A.Y.2017-18 and the maximum number specified under the section are -*
   (a). ₹ 7,500 for each goods carriage in the case of an assessee owning not more than 10 goods carriages at any time during the year
   (b). ₹ 3,500 per carriage for an assessee owning not more than 10 goods carriages at the end of the previous year
   (c). ₹ 5,000 for a heavy goods carriage and ₹ 4,500 for other goods carriages for an assessee owning not more than 12 goods carriages at the end of the previous year
8. *In the case of a non-resident engaged in the business of operation of aircraft, the income is determined under section 44BBA at -*
   (a). 7.5% of turnover
   (b). 10% of turnover
   (c). 5% of turnover
9. *The W.D.V. of a block (Plant and Machinery, rate of depreciation 15%) as on 1.4.2016 is ₹ 3,20,000. A machinery costing ₹ 50,000 was acquired on 1.9.2016 but put to use on 1.11.2016. During Jan '2017, part of this block was sold for ₹ 2,00,000. The depreciation for A.Y.2017-18 would be -*
   (a). ₹ 21,750
   (b). ₹ 25,500
   (c). ₹ 21,125

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10. *Employer's contribution to provident fund/superannuation fund/gratuity fund is allowed as deduction in computing income under the head "Profits and gains of business or profession", provided it has been paid -*
    (a). before the end of the previous year
    (b). on or before the due date by which the employer is required to credit an employee's contribution to the employee's account in the relevant fund.
    (c). on or before the due date for filing the return of income under section 139(1).
11. *Is it compulsory for an assessee to claim depreciation under section 32 of the Income-tax Act, 1961?*
12. *Write short notes on -*
    (i) Enhanced depreciation
    (ii) Set-off and carry forward of unabsorbed depreciation.
13. *Discuss the provisions dealing with the computation of business income on a presumptive basis in case of resident assessees.*
14. *Discuss the concept of "block of assets" under the Income-tax Act, 1961.*
15. *Which are the deductions allowable only on actual payment under section 43B?*

Answers

1. b; **2.** a; **3.** a; **4.** c; **5.** c; **6.** c; **7.** a; **8.** c; **9.** a; **10.** c.

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4 Unit 4 : Capital Gains

Key Points		
Scope and year of chargeability [Section 45]		
Any profits or gains arising from the transfer of a capital asset effected in the previous year will be chargeable to tax under the head 'Capital Gains', and shall be deemed to be the income of the previous year in which the transfer took place [Section 45(1)]		
Section	**Deemed Income**	**Deemed Full Value of consideration for computation of capital gains under section 48**
45(1A)	Any profits or gains arising from money or other asset received under an insurance from an insurer on account of damage / destruction of any capital asset, as a result of, flood, hurricane, cyclone, riot or civil disturbance, accidental fire or explosion, action by an enemy or action taken in combating an enemy shall be deemed to be the income of the previous year in which such money or other asset is received.	The value of money or the fair market value of other asset received
45(2)	The profits or gains arising from the transfer by way of conversion by the owner of a capital asset into stock-in-trade of a business carried on by him shall be chargeable to income-tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him.	The fair market value of the capital asset on the date of such conversion
45(3)	The profits or gains arising from the transfer of a capital asset by a person to a firm or other association of persons (AOP) or body of individuals (BOI) in which he is or becomes a partner or member, by way of capital contribution or otherwise, shall be chargeable to tax as the income of the previous year in which such transfer takes place.	The amount recorded in the books of account of the firm, AOP or BOI as the value of the capital asset.

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45(4)	The profits or gains arising from the transfer of a capital asset by way of distribution of capital assets on the dissolution of a firm or other AOPs or BOIs or otherwise, shall be chargeable to tax as the income of the firm, AOP or BOI, of the previous year in which the said transfer takes place.	The fair market value of the capital asset on the date of such transfer.
45(5)	Capital gains arising from the transfer by way of compulsory acquisition under any law, or a transfer, the consideration for which was determined or approved by the Central Government or RBI will be chargeable as income of the previous year in which the consideration or part thereof is first received.	Compensation or consideration determined or approved in the first instance by the Central Government or RBI
	If the compensation or consideration is further enhanced by any court, Tribunal or other authority, the enhanced amount will be deemed to be the income chargeable of the previous year in which the amount was received by the assessee. However, any amount of compensation received in pursuance of an interim order of a court, Tribunal or other authority shall be deemed to be income chargeable under the head "Capital Gains" of the previous year in which the final order of such court, Tribunal or other authority is made.	Amount by which the compensation or consideration is enhanced or further enhanced. For this purpose cost of acquisition and cost of improvement shall be taken as 'Nil'.

Definitions [Section 2]

Section	Term	Definition
2(14)	Capital Asset	**Capital Asset** means – (a) property of any kind held by an assessee, whether or not connected with his business or profession; (b) any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the regulations made under the SEBI Act, 1992. **Exclusions from the definition of Capital Asset:** Stock in trade [other than securities referred to in (b) above], raw materials or consumables held for the purposes of business or profession;

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- Personal effects except jewellery, archeological collections, drawings, paintings, sculptures or any work of art;
- Rural agricultural land in India i.e. agricultural land not situated within specified urban limits.

The agricultural land described in (a) and (b) below, being land situated within the specified urban limits, would fall within the definition of "capital asset", and transfer of such land would attract capital gains tax -

(a) agricultural land situated in any area within the jurisdiction of a municipality or cantonment board having population of not less than ten thousand according to last preceding census, or

(b) agricultural land situated in any area within such distance, measured aerially, in relation to the range of population according to the last preceding census as shown hereunder -

	Shortest aerial distance from the local limits of a municipality or cantonment board referred to in item (a)	**Population according to the last preceding census of which the relevant figures have been published before the first day of the previous year.**
(i)	≤ 2 kilometers	> 10,000 ≤ 1,00,000
(ii)	≤ 6 kilometers	> 1,00,000 ≤ 10,00,000
(iii)	≤ 8 kilometers	> 10,00,000

- Gold Deposits Bonds issued under the Gold Deposit Scheme, 1999 notified by the Central Government;
- 6% Gold Bonds, 1977 or 7% Gold Bonds, 1980 or National Defence Gold Bonds, 1980, issued by the Central Government;
- Special Bearer Bonds, 1991 issued by the Central Government.

Note: *'Property' includes and shall be deemed to have always included any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever.*

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2(42A)	Short-term capital asset	Capital asset held by an assessee for not more than 36 months immediately preceding the date of its transfer is a **short-term capital asset**. However, a security (other than a unit) listed in a recognized stock exchange in India, a unit of UTI or a unit of an equity oriented fund or a zero coupon bond will be treated as short term capital asset if it is held for not more than 12 months immediately preceding the date of its transfer. Further, a share of a company (not being a share listed in a recognized stock exchange in India) would be treated as a short-term capital asset if it was held by the assessee for not more than 24 months immediately preceding the date of its transfer.
2(29A)	Long-term capital asset	Capital asset which is not a short-term capital asset is a **long-term capital asset**. The following assets are, therefore, long-term capital assets: ➢ a security (other than a unit) listed in a recognized stock exchange in India, a unit of UTI or a unit of an equity oriented fund or a zero coupon bond held for more than 12 months; and ➢ any other capital asset held for more than 36 months.

Transactions not regarded as transfer [Section 47]: Some Examples

- Any distribution of capital assets on the total or partial partition of a HUF
- Any transfer of capital asset under a gift or will or an irrevocable trust
- Any transfer of a capital asset by a holding company to its subsidiary or vice versa, if:
  - the parent company or its nominees hold whole of the share capital of subsidiary company, and
  - the transferee company is an Indian company
- Any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company if the amalgamated company is an Indian company
- Any transfer, in a demerger, of a capital asset by the demerged company to the resulting company, if the resulting company is an Indian company
- Any transfer by way of conversion of bonds, debentures, debenture stock, deposit certificates of a company, into shares or debentures of that company.
- Any transfer of a capital asset or intangible asset by a private company or

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unlisted public company to a LLP or any transfer of a share or shares held in a company by a shareholder on conversion of a company into a LLP in accordance with LLP Act, 2008 provided all conditions satisfied:

- total sales, turnover or gross receipts in the business of the company does not exceed ₹ 60 lakh in any of the three preceding previous years;
- the shareholders of a company become partners of the LLP and their capital contribution and profit sharing ratio in the LLP are in the same proportion as their shareholding in the company on the date of conversion;
- no consideration or benefit, directly or indirectly, other than share in profit and capital contribution in the LLP arises to the shareholders;
- the erstwhile shareholders of the company continue to be entitled to receive atleast 50% of the profit of the LLP for a period of 5 years from the date of conversion;
- all assets and liabilities of the company immediately before conversion become the assets and liabilities of the LLP;
- the total value of assets as appearing in the books of account of the company in any of the three previous years preceding the previous year in which the conversion takes place, should not exceed ₹ 5 crore.
- no amount is paid, either directly or indirectly, to any partner out of the 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.

➢ Any transfer of a capital asset or an intangible asset by a sole proprietary concern to a company in a scheme of succession provided:

- atleast 50% of the voting power in a company is held by sole proprietor and shareholding continues for a period of 5 years from the date of the succession;
- all assets and liabilities of the sole proprietary concern relating to the business immediately before succession become the assets and liabilities of the company;
- the sole proprietor does not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company.

➢ Any transfer of a capital asset in a scheme of reverse mortgage under a scheme made and notified by the Central Government.

➢ Any transfer by an individual of sovereign gold bonds issued by RBI by way of redemption

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Mode of computation of Capital Gains [Section 48]

Computation of long-term capital gains

Gross Sale consideration	xx
Less: Expenditure incurred wholly and exclusively in connection with such transfer (for example, brokerage on sale)	xx
Net Sale Consideration	xx
Less: Indexed cost of acquisition and indexed cost of improvement	xx
	xx
Less: Exemption under sections 54/54B/54EC/54F/54G etc.	xx
Long-term capital gains	**xx**

Notes:

(i) Deduction on account of securities transaction tax paid will not be allowed.

(ii) Indexed Cost of Acquisition =

$$\text{Cost of acquisition} \times \frac{\text{CII for the year in which the asset is transferred}}{\text{CII for the year in which the asset was first held by the assessee or 1981-82, whichever is later}}$$

(iii) Indexed Cost of Improvement =

$$\text{Cost of improvement} \times \frac{\text{CII for the year in which the asset is transferred}}{\text{CII for the year in which the improvement took place}}$$

(iv) Benefit of indexation will not apply to long term capital gains from transfer of bonds or debentures other than capital indexed bonds issued by the government and sovereign gold bonds issued by RBI.

Computation of short-term capital gains

Gross Sale consideration	xx
Less: Expenditure incurred wholly and exclusively in connection with such transfer (for example, brokerage on sale)	xx
Net Sale Consideration	xx
Less: Cost of acquisition and cost of improvement	xx
Less: Exemption under sections 54B/54D/54G	xx
Short-term capital gains	xx
	xx

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Capital Gains : Special Provisions

Section	Particulars
50	Any income from transfer of depreciable assets is deemed to be **capital gains arising from transfer of short-term capital assets**, irrespective of the period of holding (i.e., indexation benefit would not be available even if the period of holding of such assets is more than 36 months).
50B	**Capital Gains on Slump Sale** Any profits and gains arising from slump sale effected in the previous year shall be chargeable to income-tax as capital gains arising from the transfer of capital assets and shall be deemed to be the income of the previous year in which the transfer took place. Where the undertaking being transferred under slump sale is held for more than 36 months, the resultant gain is long-term; However, no indexation benefit would be available. If the undertaking is held for less than 36 months, the resultant gain is short-term. Net worth is deemed to be the cost of acquisition and the cost of improvement. 'Net worth' shall be aggregate value of total assets minus value of liabilities of such undertaking as per books of account. Capital gains = Sale consideration – Net Worth. Aggregate value of total assets would be the aggregate of the following : i) Written Down Value of depreciable assets; ii) Nil, in case of capital assets in respect of which the whole of the expenditure has been allowed or is allowable as deduction under section 35AD; and iii) Book value for other assets. Revaluation of assets shall be ignored for computing Net Worth.
50C	**Computation of capital gains on sale of land or building or both** Where consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted or assessed or assessable by the stamp valuation authority for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable, shall, for the purpose of section 48, be deemed to be the full value of consideration received or accruing as a result of such transfer. However, where the date of the agreement fixing the amount of consideration for the transfer of immovable property and the date of registration are not the same, the stamp duty value on the date of the agreement may be taken for the purposes of computing the full value of consideration.

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<table>
<tr><td></td><td>
However, the stamp duty value on the date of agreement can be adopted only in a case where the amount of consideration, or part thereof, has been paid by way of an account payee cheque or account payee bank draft or use of electronic clearing system through a bank account, on or before the date of the agreement for the transfer of such immovable property.
Where the assessee claims before any Assessing Officer that the value adopted or assessed or assessable by the stamp valuation authority exceeds the fair market value of the property on the date of transfer, the Assessing Officer may refer the valuation of the capital asset to the Valuation Officer, provided the value so adopted or assessed or assessable has not been disputed in any appeal or revision.
<table>
<tr><th>Sl. No.</th><th>Condition</th><th>Deemed Sale Consideration</th></tr>
<tr><td>1.</td><td>Actual Consideration < Stamp Duty Value</td><td>Stamp Duty Value</td></tr>
<tr><td>2.</td><td>Actual Consideration > Stamp Duty Value</td><td>Actual Sale Consideration</td></tr>
<tr><td>3.</td><td>Value ascertained by Valuation Officer > Stamp Duty Value</td><td>Stamp Duty Value</td></tr>
<tr><td>4.</td><td>Value ascertained by Valuation Officer < Stamp Duty Value</td><td>Value ascertained by Valuation Officer</td></tr>
</table>
</td></tr>
<tr><td>50D</td><td>
Fair Market Value deemed to be full value of consideration in certain cases
Where, on transfer of a capital asset, consideration received is not ascertainable or cannot be determined then, fair market value of the asset as on the date of transfer shall be deemed as the full value of consideration received or accruing as a result of such transfer.
</td></tr>
<tr><td>51</td><td>
Advance money received and forfeited upto 31.3.2014
Where the assessee has received advance money on an earlier occasion for transfer of capital asset, but the transfer could not be effected due to failure of negotiations, then, the advance money forfeited by the assessee has to be reduced from the cost of acquisition (and indexation would be calculated on the cost so reduced) while computing capital gains, when the capital asset is transferred or sold.
However, such advance money received on or after 1.4.2014 would be taxable under section 56(2) under the head "Income from other sources". Therefore, advance money received and forfeited on or after 1.4.2014 should not be deducted from the cost for determining the indexed cost of acquisition while computing capital gains arising on transfer of the asset.
</td></tr>
</table>

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111A	**Tax on short-term capital gains on sale of equity shares and units of equity oriented fund on which STT is chargeable** ➢ Any short-term capital gains on transfer of equity shares or units of an equity oriented fund shall be liable to tax @15%, if securities transaction tax has been paid on such sale. ➢ In case of resident individuals and HUF, the short term capital gain shall be reduced by the unexhausted basic exemption limit and the balance shall be taxed at 15%. ➢ No deduction under Chapter VI-A can be claimed in respect of such short term capital gain. ➢ Short-term capital gains arising from transaction undertaken in foreign currency on a recognized stock exchange located in an International Financial Services Centre (IFSC) would be taxable at a concessional rate of 15% even when STT is not paid in respect of such transaction.
112	**Tax on long term capital gains** ➢ Any long term capital gains, other than long term capital gains exempt under section 10(38), shall be liable to tax@20%. ➢ In case of resident individuals and HUFs, the long term capital gain shall be reduced by the unexhausted basic exemption limit, and the balance shall be subject to tax at 20%. ➢ Capital gains on transfer of listed securities (other than units) or zero coupon bonds shall be chargeable to tax @10% computed without the benefit of indexation or @20% availing the benefit of indexation, whichever is more beneficial to the assessee. ➢ The assessee is not entitled to claim any deduction under Chapter VI-A in respect of long term capital gains.

Sl. No.	Nature of asset	Cost of acquisition
1	Goodwill of business, trademark, brand name etc., - - Self generated - Acquired from previous owner The cost of improvement of such assets would be Nil.	 Nil Purchase price
2	Where capital assets became the property of the assessee by way of distribution of assets on total or partial partition of HUF, under a gift or will, by succession, inheritance, distribution of assets on liquidation of a	Cost to the previous owner.

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	company, etc.	
3	**Bonus Shares** If bonus shares are allotted before 1.4.1981 If bonus shares are allotted on or after 1.4.1981	Fair Market Value on 1.4.1981 Nil
4.	**Rights Shares** Where by virtue of holding a capital asset, being a share or any other security, the assessee becomes entitled to subscribe to additional shares or is allotted addition shares without any payment, then, the period for treating such shares and securities as a short-term capital asset or otherwise shall be calculated from the date of allotment of such shares and securities.	
	Original shares (which forms the basis of entitlement of rights shares)	Amount actually paid for acquiring the original shares
	Rights entitlement (which is renounced by the assessee in favour of a person)	Nil
	Rights shares acquired by the assessee	Amount actually paid for acquiring the rights shares
	Rights shares which are purchased by the person in whose favour the assessee has renounced the rights entitlement	Purchase price paid to the renouncer of rights entitlement as well as the amount paid to the company which has allotted the rights shares.

Capital Gains : Exemptions under section 10

Section	Particulars
10(33)	Any income arising from the transfer of a capital asset being a unit of Unit Scheme 1964 of UTI

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10(37)	Where any individual or HUF owns urban agricultural land which has been used for agricultural purposes for a period of two years immediately preceding the date of transfer by such individual or a parent of his or by such HUF and the same is compulsorily acquired under any law or the consideration for such transfer is determined or approved by the Central Government or the RBI, resultant capital gain will be exempt provided the compensation or consideration for such transfer is received on or after 1.4.2004.
10(38)	Any income arising from the transfer of a long term capital asset being an equity share in a company or a unit of an equity oriented fund shall be exempt, if such transaction is chargeable to securities transaction tax. However, long-term capital gains arising from transaction undertaken in foreign currency on a recognized stock exchange located in an International Financial Services Centre (IFSC) would be exempt even if STT is not paid in respect of such transaction.

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Exemption of Capital Gains [Sections 54 to 54GB]

S. No.	Particulars	Section 54	Section 54B	Section 54EC	Section 54EE	Section 54D	Section 54G	Section 54GA	Section 54F	Section 54GB
1	**Eligible Assessee**	Individual / HUF's	Individual / HUF's	Any assessee	Any assessee	Any assessee	Any assessee	Any assessee	Individual / HUF's	Individual / HUF's
2	**Asset transferred**	Residential House	Urban Agricultural Land	Any Asset	Any asset	Land & building forming part of an industrial undertaking	Land, Building, Machinery or Plant or any right in land or building used for business of Industrial Undertaking.	Land, Building, Machinery, Plant or any right in land or building used for business of an industrial undertaking situated in an urban area.	Any asset other than Residential House.	Residential property (house or plot of land)
3	**Period of holding of the asset transferred**	Long-term capital asset	At least 2 years immediately preceding the date of transfer	Long-term capital asset	Long-term capital asset	At least 2 years immediately preceding the date of transfer.	Long-term/ Short-term capital asset	Long-term/ Short term capital asset	Long-term capital asset	Long-term capital asset
4	**Other Conditions**	Income from such house should be chargeable under the head "Income from house property"	Land should be used for agricultural purposes by assessee or his parents or a HUF for two years	-		The transfer should be by way of compulsory Acquisition of the industrial undertaking	Shifting the Industrial Undertaking from Urban Area to Rural Area	Shifting to Special Economic Zone	Assessee should not own more than one residential house on the date of transfer	

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S. No.	Particulars	Section 54	Section 54B	Section 54EC	Section 54EE	Section 54D	Section 54G	Section 54GA	Section 54F	Section 54GB
5	**Qualifying asset i.e., asset in which capital gains has to be invested**	One Residential House situated in India	Agricultural Land (Urban/ Rural)	Long Term Specified Asset – Bonds of NHAI or RECL (Redeemable after 3 years)	Long term Specified Asset - Unit issued before the 1st April, 2019 of Specified Fund as notified by the Central Government	Land or Building	Land, Building, New Plant & Machinery and expenses on shifting the Industrial Undertaking	Land, Building, new plant and machinery and expenses on shifting the industrial undertaking to the SEZ.	One Residential House situated in India	Equity shares of an eligible company, being newly incorporated SME engaged in manufacturing of an article or thing or an ***eligible start-up engaged in an eligible business.***
6	**Time limit for purchase/ construction**	Purchase within 1 year before or 2 years after the date of transfer or construct within 3 years after the date of transfer	Purchase within 2 years from the date of transfer	Purchase within 6 months from the date of transfer	Purchase within 6 months after the date of such transfer	Purchase/ construct within 3 years after transfer, for shifting or re-establishing the existing undertaking or setting up a new industrial undertaking.	Purchase/ construct within 1 year before or 3 years after the transfer.	Purchase/ construct within 1 year before or 3 years after the transfer.	Purchase within 1 year before or 2 years after the date of transfer or Construct within 3 years after the date of transfer	Equity Shares to be subscribed before the due date of filing the return. Thereafter, within one year from the date of subscription, new plant and machinery should be purchased by the company.

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S. No.	Particulars	Section 54	Section 54B	Section 54EC	*Section 54EE*	Section 54D	Section 54G	Section 54GA	Section 54F	Section 54GB
7	**Amount of Exemption**	Cost of new Residential House or Capital Gain, whichever is lower, is exempt	Cost of new Agricultural Land or Capital Gain, whichever is lower, is exempt	Capital Gain or amount invested in specified bonds, whichever is lower. Maximum permissible investment in such bonds out of capital gains arising in any financial year is ₹ 50 lakhs, whether such investment is made in the current FY or subsequent FY.	Capital Gain or amount invested in notified units of specified fund, whichever is lower. Maximum permissible investment in such units out of capital gains arising in any FY is ₹ 50 lakhs, whether such investment is made in the current FY or subsequent FY.	Cost of new asset or Capital Gain, whichever is lower.	Cost of new assets plus expenses incurred or Capital Gains, whichever is lower, is exempt.	Cost of new assets plus expenses incurred for shifting or Capital Gain, whichever is lower, is exempt.	Cost of new Residential House ≥ Net sale consideration of original asset, entire Capital gain is exempt. Cost of new Residential House < Net sale consideration of original asset, proportionate capital gain is exempt.	Cost of new plant & machinery ≥ Net sale consideration of residential house, entire Capital gain is exempt. Cost of new Residential House < Net sale consideration of Residential House, proportionate capital gain is exempt.

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Question 1

Mr. Dinesh received a vacant site as gift from his friend in November 2002. The site was acquired by his friend for ₹ 3,00,000 in April 1990. Dinesh constructed a residential building during the year 2004-05 in the said site for ₹ 15,00,000. He carried out some further extension of the construction in the year 2007-08 for ₹ 5,00,000.

Dinesh sold the residential building for ₹ 55,00,000 in January 2017 but the State stamp valuation authority adopted ₹ 65,00,000 as value for the purpose of stamp duty.

Compute his long term capital gain, for the assessment year 2017-18 based on the above information. The cost inflation indices are as follows:

Financial Year	*Cost inflation index*
1990-91	*182*
2002-03	*447*
2004-05	*480*
2007-08	*551*
2016-17	*1125*

Answer

Computation of long term capital gain of Mr. Dinesh for the A.Y. 2017-18

Particulars	**₹**	**₹**
Full value of consideration **(Note 1)**		65,00,000
Less: Indexed cost of acquisition-land (₹ 3,00,000 × 1125/447) **(Note 2 & 3)**	7,55,036	
Indexed Cost of acquisition-building (₹ 15,00,000 × 1125/480) **(Note 3)**	35,15,625	
Indexed Cost of improvement-building (₹ 5,00,000 x 1125/551)	10,20,871	52,91,532
Long-term capital gain		**12,08,468**

Notes:

1. As per section 50C, where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted by the Stamp Valuation Authority, such value adopted by the Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of such transfer. Accordingly, full value of consideration will be ₹ 65 lakhs in this case.
2. Since Dinesh has acquired the asset by way of gift, therefore, as per section 49(1), cost of the asset to Dinesh shall be deemed to be cost for which the previous owner acquired the asset i.e., ₹ 3,00,000, in this case.

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3. Indexation benefit is available since both land and building are long-term capital assets. However, as per the definition of indexed cost of acquisition under clause (iii) of *Explanation* below section 48, indexation benefit for land will be available only from the previous year in which Mr. Dinesh first held the land i.e., P.Y. 2002-03.

Alternative view: *In the case of CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.), the Bombay High court held that indexation cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.*

As per this view, the indexation cost of acquisition of land would be ₹ 18,54,396 and long term capital gain would be ₹ 1,09,108.

Question 2

Mr. Abhishek a senior citizen, pledged his residential house with a bank, under a notified reverse mortgage scheme. He was getting loan from bank in monthly installments. Mr. Abhishek did not repay the loan on maturity and hence gave possession of the house to the bank, to discharge his loan. How will the treatment of long-term capital gain be on such reverse mortgage transaction?

Answer

Section 47(xvi) provides that any transfer of a capital asset in a transaction of reverse mortgage under a scheme made and notified by the Central Government shall not be considered as a transfer for the purpose of capital gain.

Accordingly, the pledging of residential house with bank by Mr. Abhishek will not be regarded as a transfer. Therefore, no capital gain will be charged on such transaction.

Further, section 10(43) provides that the amount received by the senior citizen as a loan, either in lump sum or in installment, in a transaction of reverse mortgage would be exempt from income-tax. Therefore, the monthly installment amounts received by Mr. Abhishek would not be taxable.

However, capital gains tax liability would be attracted at the stage of alienation of the mortgaged property by the bank for the purposes of recovering the loan.

Question 3

Ms. Anshu transferred land and building on 02-01-2017 and furnishes the following information:

	Particulars	***(₹)***
(i)	*Net consideration received*	*23,00,000*
(ii)	*Value adopted by Stamp Valuation Authority*	*25,00,000*
(iii)	*Value ascertained by Valuation Officer on reference by the Assessing Officer*	*27,00,000*
(iv)	*This land was acquired by Anshu on 1-04-1981. Fair Market Value of the land as on 01-04-1981 was*	*1,10,000*

(v) Anshu constructed a residential building on the land at a cost of ₹ 3,20,000 (construction completed on 01-12-2002 during the financial year 2002-03) *Brought forward short term capital loss incurred on sale of shares during financial year 2011-12 ₹ 1,50,000,*	

Anshu seeks your advice regarding the amount to be invested in NHAI bonds so as to be exempt from capital gain tax under the Income-tax Act, 1961.

Cost inflation index for FY 1981-82 : 100

Cost inflation index for FY 2002-03 : 447

Cost inflation index for FY 2016-17 : 1125

Answer

Computation of Capital Gains of Ms. Anshu for the A.Y. 2017-18

Particulars	₹	₹
Full value of consideration **[See Notes (i) & (ii) below]**		25,00,000
***Less*: Indexed Cost of acquisition [See Note (iii) below]**		
Indexed cost of land (₹ 1,10,000 × 1125/100)	12,37,500	
Indexed cost of building (₹ 3,20,000 × 1125/447)	8,05,369	20,42,869
Long-term capital gain		**4,57,131**
Less: Brought forward short-term capital loss set off **[See Note (iv) below]**		1,50,000
Taxable capital gains (Amount to be invested in NHAI bonds to get full exemption from tax on capital gains) [See Note (v) below]		**3,07,131**

Notes :

(i) As per section 50C(1), where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted by the Stamp Valuation Authority for the purpose of payment of stamp duty, such value adopted by the Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of such transfer. Accordingly, full value of consideration would be ₹ 25 lacs in this case.

(ii) As per section 50C(3), where the valuation is referred by the Assessing Officer to Valuation Officer and the value ascertained by such Valuation Officer exceeds the value adopted by the Stamp Valuation Authority for the purpose of payment of stamp duty, the value adopted by the Stamp Valuation Authority shall be taken as the full value of the consideration received or accruing as a result of the transfer. Since the value ascertained by the Valuation Officer (i.e. ₹ 27 lakhs), is higher than the value adopted by the Stamp

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Valuation Authority (i.e. ₹ 25 lakhs), the full value of consideration in this case would be ₹ 25 lakhs.

(iii) Since the cost of land acquired by Anshu on 1.4.1981 is not given in the question, the fair market value as on 1.4.1981 is taken as the cost of acquisition. Indexation benefit is available since land and building are both long-term capital assets, as they are held by Anshu for more than 36 months.

(iv) As per section 74, brought forward unabsorbed short term capital loss can be set off against any capital gains, short term or long term, for 8 assessment years immediately succeeding the assessment year for which the loss was first computed. Therefore, short-term capital loss on sale of shares during the F.Y.2011-12 can be set-off against the current year long-term capital gains on sale of land and building.

(v) As per section 54EC, an assessee can avail exemption in respect of long-term capital gains, if such capital gains are invested in the bonds issued by the NHAI redeemable after 3 years. Such investment is required to be made within a period of 6 months from the date of transfer of the asset. The exemption shall be the amount of capital gains or the amount of such investment made, whichever is less. Therefore, in this case, if Anshu invests the entire capital gains in bonds of NHAI, she can get full exemption from tax on capital gains.

Question 4

Mr. Mithun purchased 100 shares of M/s Goodmoney Co. Ltd. on 01-04-2005 at rate of ₹ 1,000 per share in public issue of the company.

Company allotted bonus shares in the ratio of 1:1 on 01.12.2015. He has also received dividend of ₹ 10 per share on 01.05.2016.

He has sold all the shares on 01.10.2016 at the rate of ₹ 4,000 per share through a recognized stock exchange and paid brokerage of 1% and securities transaction tax of 0.02% to celebrate his 75th birthday. The cost inflation Index are as follows:

Financial Year	***Cost Inflation Index***
2005-06	*497*
2016-17	*1125*

Compute his total income and tax liability for Assessment Year 2017-18, assuming that he is having no income other than given above.

Answer

Computation of total income and tax liability of Mr. Mithun for A.Y. 2017-18

Particulars	**₹**
Short term capital gains on sale of bonus shares	
Gross sale consideration (100 x ₹ 4,000)	4,00,000
Less : Brokerage @ 1%	4,000
Net sale consideration	3,96,000

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Less: Cost of acquisition of bonus shares	NIL
Total Income (Short term Capital Gains)	**3,96,000**
Tax Liability	
15% of (₹ 3,96,000-₹ 3,00,000)	14,400
Less: Rebate U/s 87A	5,000
	9,400
Add : Education cess @ 2%	188
Secondary and higher education cess @ 1%	94
Tax payable	**9,682**
Tax payable (Rounded Off)	**9,680**

Notes:

(1) Long-term capital gains on sale of original shares through a recognized stock exchange (STT paid) is exempt under section 10(38).

(2) Since bonus shares are held for less than 12 months before sale, the gain arising there from is a short term capital gain chargeable to tax@15% as per section 111A after adjusting the unexhausted basic exemption limit. Since Mr. Mithun is over 60 years of age, he is entitled for a higher basic exemption limit of ₹ 3,00,000 for A.Y. 2017-18.

(3) Dividend income is exempt under section 10(34).

(4) Brokerage paid is allowable since it is an expenditure incurred wholly and exclusively in connection with the transfer. Hence, it qualifies for deduction under section 48(i).

(5) Cost of bonus shares will be Nil as such shares are allotted after 1.04.1981.

(6) Securities transaction tax is not allowable as deduction.

Question 5

Mr. Selvan, acquired a residential house in January, 2000 for ₹ 10,00,000 and made some improvements by way of additional construction to the house, incurring expenditure of ₹ 2,00,000 in October, 2004. He sold the house property in October, 2016 for ₹ 75,00,000. The value of property was adopted as ₹ 80,00,000 by the State stamp valuation authority for registration purpose. He acquired a residential house in January, 2016 for ₹ 25,00,000. He deposited ₹ 20,00,000 in capital gains bonds issued by National Highways Authority of India (NHAI) in June, 2017.

Compute the capital gain chargeable to tax for the assessment year 2017-18.

What would be the tax consequence and in which assessment year it would be taxable, if the house property acquired in January, 2016 is sold for ₹ 40,00,000 in March, 2018?

Cost inflation index: F.Y.1999-00 : 389

F.Y. 2004-05 : 480

F.Y. 2016-17 : 1125

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Answer

(I) Computation of Capital Gains Chargeable to tax for A.Y. 2017-18

Particulars	₹	₹
Sale consideration (i.e. Stamp Duty Value) (Note 1)		80,00,000
Less: Indexed Cost of Acquisition		
₹ 10,00,000 × 1125/389	28,92,031	
Indexed Cost of Improvement		
₹ 2,00,000 × 1125/480	4,68,750	33,60,781
		46,39,219
Less: Exemption under section 54 (Note 2)		25,00,000
Taxable Capital Gains		**21,39,219**

Notes:

1. As per the provisions of section 50C, in case the stamp duty value adopted by the stamp valuation authority is higher than the actual sale consideration, the stamp duty value shall be deemed as the full value of consideration.
2. Exemption under section 54 is available if a new residential house is purchased within one year before or two years after the date of transfer. Since the cost of new residential house is less than the capital gain, capital gain to the extent of cost of new asset is exempt under section 54.
3. Exemption under section 54EC is available in respect of investment in bonds of National Highways Authority of India only if the investment is made within a period of six months after the date of such transfer. In this case, since the investment is made after six months, exemption under section 54EC would not be available.

(II) If the new asset purchased by the assessee on the basis of which exemption under section 54 is claimed, is transferred within 3 years from the date of its acquisition, then for computing the taxable short-term capital gain on such transfer, the cost of acquisition of such asset shall be taken as Nil.

Particulars (A.Y.2018-19)	₹
Sale consideration	40,00,000
Less: Cost of acquisition	Nil
Short-term capital gains	40,00,000

Question 6

Mr. Rakesh purchased a house property on 14th April, 1979 for ₹ 1,05,000. He entered into an agreement with Mr. Bobby for the sale of house on 15th September, 1982 and received an

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advance of ₹ 25,000. However, since Mr. Bobby did not remit the balance amount, Mr. Rakesh forfeited the advance.

Later on, he gifted the house property to his friend Mr. Aakash on 15th June, 1986.

Following renovations were carried out by Mr. Rakesh and Mr. Aakash to the house property:

	₹
By Mr. Rakesh during F.Y. 1979-80	*10,000*
By Mr. Rakesh during F.Y. 1983-84	*50,000*
By Mr. Aakash during F.Y. 1993-94	*1,90,000*

The fair market value of the property as on 1.4.1981 is ₹ 1,50,000.

Mr. Aakash entered into an agreement with Mr. Chintu for sale of the house on 1st June, 1995 and received an advance of ₹ 80,000. The said amount was forfeited by Mr. Aakash, since Mr. Chintu could not fulfil the terms of the agreement.

Finally, the house was sold by Mr. Aakash to Mr. Sanjay on 2nd January, 2017 for a consideration of ₹ 12,00,000.

Compute the capital gains chargeable to tax in the hands of Mr. Aakash for the assessment year 2017-18. Cost inflation indices are as under:

Financial Year	*Cost inflation index*
1981-82	*100*
1983-84	*116*
1986-87	*140*
1993-94	*244*
2016-17	*1125*

Answer

Computation of taxable capital gains of Mr. Aakash for the A.Y. 2017-18

Particulars	₹
Sale consideration	12,00,000
Less: Indexed cost of acquisition (Working Note: 1)	5,62,500
	6,37,500
Less: Indexed cost of improvement (Working Note: 2)	13,60,939
Long term capital loss	**(7,23,439)**

Working Note: 1

Indexed cost of acquisition is determined as under:

Cost to the previous owner i.e., Mr. Rakesh is ₹ 1,05,000

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Fair Market Value on 1st April, 1981 is ₹ 1,50,000	
Cost to the previous owner or FMV on 1st April, 1981, whichever is more, is to be taken as cost of acquisition of Mr. Aakash	₹ 1,50,000
Less: Advance money forfeited by Mr. Aakash (as per section 51) (Note: Advance forfeited by Mr. Rakesh, the previous owner, should, however, not be deducted)	₹ 80,000
Cost of acquisition	₹ 70,000
Indexed cost of acquisition (₹ 70,000 × 1125/140)	**₹ 5,62,500**

140 is the CII for F.Y. 1986-87, being the first year in which property is held by Mr. Aakash and 1125 is the CII for F.Y. 2016-17, being the year in which the property is sold.

Alternative view: *In the case of CIT v. Manjula J. Shah 16 Taxmann 42, the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset. As per this view, the indexed cost of acquisition of house would be ₹ 7,87,500, taking CII of 100 for the F.Y. 1980-81 since F.M.V. as on 1st April, 1981 is taken as cost of acquisition of Mr. Aakash.*

Note: *Clause (ix) of Section 56(2), provides that the advance which is forfeited in the previous year 2014-15 relevant to A.Y. 2015-16 would be chargeable to tax under the head "Income from Other sources" and hence, such forfeited amount shall not be reduced from the cost of acquisition of the transferred capital asset. In the present case, the advance was forfeited in a previous year prior to P.Y. 2014-15. Therefore, such amount would be deductible from the cost of acquisition while determining the Capital gains on transfer of such asset.*

Working Note: 2

Indexed cost of Improvement is determined as under:

Expenditure incurred before 1st April, 1981 should not be considered		NIL
Expenditure incurred on or after 1st April, 1981		
- During 1983-84: Indexed cost of Improvement	[₹ 50,000 × 1125/116]	₹ 4,84,914
- During 1993-94: Indexed cost of Improvement	[₹ 1,90,000 × 1125/244]	₹ 8,76,025
Total indexed cost of improvement		**₹13,60,939**

Question 7

X Co. (P) Ltd., converted into a Limited Liability Partnership (LLP) by name All Trade LLP, with effect from 01.04.2016.

The following details are given to you:

Asst. year 2009-10 : Business loss brought forward	*₹ 2,00,000*
Asst. year 2016-17 : Business loss brought forward	*₹ 5,00,000*

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(These are related to erstwhile X Co. (P) Ltd.)

Total income of All Trade LLP, for the financial year 2016-17 is ₹ 6,00,000 (Before set off of brought forward business losses of erstwhile company i.e. X Co. (P) Ltd.)

Assume that all the conditions prescribed in section 47(xiiib) were satisfied by X Co. (P) Ltd. at the time of conversion to LLP.

(i) Explain whether All Trade LLP can set off and carry forward the business loss of its predecessor i.e. X Co. (P) Ltd.?

(ii) State whether the change in the profit sharing ratio of the shareholders of the company in the LLP at later date would have any tax consequence.

Answer

(i) Section 72A(6A), provides that where a private company is succeeded by a LLP fulfilling the conditions laid down in the proviso to section 47(xiiib), then, notwithstanding anything contained in any other provision of the Income-tax Act, 1961, the accumulated loss and unabsorbed depreciation of the predecessor company shall be deemed to be the loss or allowance for depreciation of the successor LLP for the purpose of the previous year in which the business reorganisation was effected and other provisions of the Act relating to set-off and carry forward of losses and depreciation allowance shall apply accordingly.

Therefore, All Trade LLP can carry forward and set-off the business loss of ₹ 6 lakh of erstwhile X Co (P) Ltd. against its business income for the F.Y.2016-17. The unabsorbed business loss of ₹ 1 lakh, relating to A.Y. 2016-17, will be carried forward to the next year.

(ii) Section 47(xiiib) requires that the shareholders of the company become partners of the LLP in the same proportion as their shareholding in the company. Further, the aggregate of the profit sharing ratio of the shareholders of the company in the LLP should be not less than 50% at any time during the period of 5 years from the date of conversion. If the entity fails to fulfill this condition, the benefit of set-off of business loss availed by the LLP would be deemed to be the profits and gains of the LLP chargeable to tax in the previous year in which the LLP fails to fulfill the condition.

Question 8

Ms. Chhaya transferred a vacant site to Ms. Dayama for ₹ 4,25,000. The stamp valuation authority fixed the value of vacant site for stamp duty purpose at ₹ 6,00,000. The total income of Chhaya and Dayama before considering the transfer of vacant site are ₹ 50,000 and ₹ 2,05,000, respectively. The indexed cost of acquisition for Ms. Chhaya in respect of vacant site is ₹ 4,00,000 (computed).

Determine the total income of both Ms. Chhaya and Ms. Dayama taking into account the above said transaction.

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Answer

Section 56(2)(vii) would get attracted in case of transfer of immovable property for inadequate consideration, since the difference between the stamp duty value and sale consideration is more than ₹ 50,000 and therefore ₹ 1,75,000 (i.e. ₹ 6,00,000 - ₹ 4,25,000) will be taxed under the head "Income from other sources" in the hands of transferee, i.e., Ms. Dayama. Further, for the transferor, Ms. Chhaya, the value adopted for stamp duty purpose will be taken as the deemed sale consideration under section 50C for computation of capital gains.

Particulars	Chhaya (Transferor) ₹	Dayama (Transferee) ₹
Capital gains		
Deemed sale consideration under section 50C	6,00,000	
Less: Indexed cost of acquisition	4,00,000	
	2,00,000	
Income from other sources		
Difference between stamp duty value and sale consideration of immovable property, taxable under section 56(2)(vii)		1,75,000
Other income (computed)	50,000	2,05,000
Total income	**2,50,000**	**3,80,000**

Question 9

Mr. Chandru transferred a vacant site on 28.10.2016 for ₹ 100 lakhs. The site was acquired for ₹ 9,99,300 on 30.6.2000. He invested ₹ 50 lakhs in eligible bonds issued by Rural Electrification Corporation Ltd. (RECL) on 20.3.2017.

Again, he invested ₹ 20 lakhs in eligible bonds issued by National Highways Authority of India (NHAI) on 16.4.2017.

Compute the chargeable capital gain in the hands of Mr. Chandru for the A.Y. 2017-18.

Financial year	*Cost Inflation Index*
2000-01	*406*
2016-17	*1125*

Answer

Computation of chargeable capital gain of Mr. Chandru for the A.Y.2017-18

Particulars	₹
Sale consideration	1,00,00,000
Less: Indexed cost of acquisition (₹ 9,99,300 × 1125/406)	27,68,996
	72,31,004

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Less: Deduction under section 54EC (See Note 3 below)	50,00,000
Long term capital gain	**22,31,004**

Note:

(1) Since the site was held for more than 36 months prior to the date of transfer, it is a long-term capital asset and the capital gain arising upon its transfer is long-term capital gain.

(2) In order to claim exemption under section 54EC, Mr. Chandru has to invest in specified bonds of RECL or NHAI within a period of 6 months from the date of transfer of the asset.

(3) As per second proviso to section 54EC(1), out of capital gains arising from transfer of one or more capital assets in a financial year, the investment eligible for exemption, cannot exceed ₹ 50 lakhs, whether such investment is made in the same financial year or in the subsequent financial year or in both the years.

In this case, Mr. Chandru has invested ₹ 50 lakhs in RECL bonds in the F.Y.2016-17 and ₹ 20 lakhs in NHAI bonds in the F.Y.2017-18, both within six months from the date of transfer. However, he would be eligible for exemption of only ₹ 50 lakhs for investment made in such bonds.

Question 10

How will you calculate the period of holding in case of the following assets?

(1) Shares held in a company in liquidation

(2) Bonus shares

(3) Flat in a co-operative society

(4) Transfer of a security by a depository (i.e., demat account)

Answer

(1) Shares held in a company in liquidation - The period after the date on which the company goes into liquidation shall be excluded while calculating the period of holding. Therefore, the period of holding shall commence from the date of acquisition and end with the date on which the company goes into liquidation.

(2) Bonus shares - The period of holding shall be reckoned from the date of allotment of bonus shares and will end with the date of transfer.

(3) Flat in a co-operative society - The period of holding shall be reckoned from the date of allotment of shares in the society and will end with the date of transfer.

Note – Any transaction whether by way of becoming a member of, or acquiring shares in, a co-operative society or by way of any agreement or any arrangement or in any other manner whatsoever which has the effect of transferring, or enabling enjoyment of, any immovable property is a transfer as per section 2(47)(vi). Hence, it is possible to take a view that any date from which such right is obtained may be taken as the date of acquisition.

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(4) Transfer of security by a depository - The period of holding shall be computed from the date on which the securities were credited to the demat account and will end with the date of transfer (sale). The first-in-first-out (FIFO) method will be adopted for determining the period of holding.

Question 11

Mr. A is a proprietor of Akash Enterprises having 2 units. He transferred on 1.4.2016 his Unit 1 by way of slump sale for a total consideration of ₹ 25 lacs. Unit 1 was started in the year 2004-05. The expenses incurred for this transfer were ₹ 28,000. His Balance Sheet as on 31.3.2016 is as under:

Liabilities	*Total (₹)*	*Assets*	*Unit 1 (₹)*	*Unit 2 (₹)*	*Total (₹)*
Own Capital	*15,00,000*	*Building*	*12,00,000*	*2,00,000*	*14,00,000*
Revaluation Reserve (for building of unit 1)	*3,00,000*	*Machinery*	*3,00,000*	*1,00,000*	*4,00,000*
Bank loan (70% for unit 1)	*2,00,000*	*Debtors*	*1,00,000*	*40,000*	*1,40,000*
Trade creditors (25% for unit 1)	*1,50,000*	*Other assets*	*1,50,000*	*60,000*	*2,10,000*
Total	***21,50,000***	***Total***	***17,50,000***	***4,00,000***	***21,50,000***

Other information:

(i) Revaluation reserve is created by revising upward the value of the building of Unit 1.

(ii) No individual value of any asset is considered in the transfer deed.

(iii) Other assets of Unit 1 include patents acquired on 1.7.2014 for ₹ 50,000 on which no depreciation has been charged.

Compute the capital gain for the assessment year 2017-18.

Answer

Computation of capital gains on slump sale of Unit 1

Particulars	₹
Sale value	25,00,000
Less: Expenses on sale	28,000
Net sale consideration	24,72,000
Less: Net worth (See Note 1 below)	12,50,625
Long-term capital gain	**12,21,375**

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Notes:

1. Computation of net worth of Unit 1 of Akash Enterprises

Particulars	₹	₹
Building (excluding ₹ 3 lakhs on account of revaluation)		9,00,000
Machinery		3,00,000
Debtors		1,00,000
Patents (See Note 2 below)		28,125
Other assets (₹ 1,50,000 – ₹ 50,000)		1,00,000
Total assets		14,28,125
Less: Creditors	37,500	
Bank Loan	1,40,000	1,77,500
Net worth		**12,50,625**

2. Written down value of patents as on 1.4.2016

Value of patents:	₹
Cost as on 1.7.2014	50,000
Less: Depreciation @ 25% for Financial Year 2014-15	12,500
WDV as on 1.4.2015	37,500
Less: Depreciation for Financial Year 2015-16	9,375
WDV as on 1.4.2016	28,125

For the purposes of computation of net worth, the written down value determined as per section 43(6) has to be considered in the case of depreciable assets. The problem has been solved assuming that the Balance Sheet values of ₹ 3 lakh and ₹ 9 lakh (₹ 12 lakh – ₹ 3 lakh) represent the written down value of machinery and building, respectively, of Unit 1.

3. Since the Unit is held for more than 36 months, capital gain arising would be long term capital gain. However, indexation benefit is not available in case of slump sale.

Question 12

Sachin received ₹ 15,00,000 on 23.01.2017 on transfer of his residential building in a transaction of reverse mortgage under a scheme notified by the Central Government. The building was acquired in March 1991 for ₹ 8,00,000.

Is the amount received on reverse mortgage chargeable to tax in the hands of Sachin under the head 'Capital gains'?

Cost inflation index for the F.Y. 1990-91 – 182; F.Y. 2016-17 - 1125

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Answer

As per section 47(xvi), any transfer of a capital asset in a transaction of Reverse Mortgage under a scheme made and notified by the Central Government will not be regarded as a transfer. Therefore, capital gains tax liability is not attracted.

Section 10(43) provides that the amount received by a senior citizen as a loan, either in lump sum or in installments, in a transaction of Reverse Mortgage would be exempt from income-tax. Therefore, the amount received by Sachin in a transaction of Reverse Mortgage of his residential building is exempt under section 10(43).

Question 13

Mr. Roy, aged 55 years owned a Residential House in Ghaziabad. It was acquired by Mr. Roy on 10-10-1986 for ₹ 6,00,000. He sold it for ₹ 65,00,000 on 4-11-2016. The stamp valuation authority of the State fixed value of the property at ₹ 72,00,000. The assessee paid 2% of the sale consideration as brokerage on the sale of the said property.

Mr. Roy acquired a residential house property at Kolkata on 10-12-2016 for ₹ 7,00,000 and deposited ₹ 3,00,000 on 10-4-2017 and ₹ 5,00,000 on 15-6-2017 in the capital gains bonds of Rural Electrification Corporation Ltd. He deposited ₹ 4,00,000 on 6-7-2017 and ₹ 9,00,000 on 1-11-2017 in the capital gain deposit scheme in a Nationalized Bank for construction of an additional floor on the residential house property in Kolkata.

Compute the Capital Gain chargeable to tax for the Assessment Year 2017-18 and income-tax chargeable thereon assuming Mr. Roy has no other income.

Cost Inflation Index for Financial Year 1986-87: 140 and Financial Year 2016-17: 1125

Answer

Computation of Capital Gains chargeable to tax in the hands of Mr. Roy for the A.Y. 2017-18

Particulars	₹	₹
Gross Sale Consideration on transfer of residential house		72,00,000
[As per section 50C, in case the actual sale consideration is lower than the stamp duty value fixed by the stamp valuation authority, the stamp duty value shall be deemed as the full value of consideration]		
Less: Brokerage@2% of actual sale consideration of ₹ 65,00,000		1,30,000
Net Sale Consideration		70,70,000
Less: Indexed cost of acquisition [₹ 6,00,000 x 1125/140]		48,21,429
Long-term capital gain		22,48,571

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***Less:* Exemption under section 54**		
- Acquisition of residential house property at Kolkata on 10.12.2016 (i.e., within the prescribed time of two years from 4.11.2016, being the date of transfer of residential house at Ghaziabad).	7,00,000	
- Amount deposited in Capital Gains Accounts Scheme on or before the due date of filing return of income for construction of additional floor on the residential house property at Kolkata. Since Mr. Roy has no other source of income, his due date for filing return of income is 31st July, 2017 [Therefore, ₹ 4,00,000 deposited on 6.7.2017 will be eligible for exemption whereas ₹ 9,00,000 deposited on 1.11.2017 will not be eligible for exemption under section 54]	4,00,000	11,00,000
Exemption under section 54EC Amount deposited in capital gains bonds of RECL within six months from the date of transfer (i.e., on or before 3.5.2017) would qualify for exemption. [Therefore, in this case, ₹ 3,00,000 deposited in capital gains bonds of RECL on 10.4.2017 would be eligible for exemption under section 54EC, whereas ₹ 5,00,000 deposited on 15.6.2017 would not qualify for exemption]		3,00,000
Long-term capital gain		**8,48,571**

Computation of tax liability of Mr. Roy for A.Y. 2017-18

Particulars	₹
Tax on ₹ 5,98,571 (i.e Long term capital gain ₹ 8,48,571 less basic exemption limit of ₹ 2,50,000) is charged @ 20% [Section 112] (Since long-term capital gains is the only source of income, the entire basic exemption limit can be exhausted against this income)	1,19,714
Add: Education cess@2% and Secondary & higher education cess @ 1%	3,591
Total tax liability	**1,23,306**
Total tax liability (rounded off)	**1,23,310**

Note: *As per the decision of Gauhati High Court in CIT vs Rajesh Kumar Jalan 286 ITR 274 and Haryana High Court in CIT vs Jagriti Agarwal 245 CTR 629, exemption under section 54*

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is allowable even if the amount of capital gain is deposited in Capital Gains Accounts Scheme within the period specified for filing a belated return under section 139(4) [i.e., on or before 31.3.2018].

If we apply the above interpretation in this case, Mr. Roy would be eligible for exemption under section 54 in respect of ₹ 9,00,000 deposited in Capital Gains Accounts Scheme on 01.11.2017 also, since the said date falls within the time specified under section 139(4). On the basis of this interpretation, the long term capital gain chargeable to tax in the hands of Mr. Roy would be Nil and the consequent tax liability would also be Nil.

Question 14

Mr. Raj Kumar sold a house to his friend Mr. Dhuruv on 1st November, 2016 for a consideration of ₹ 25,00,000. The Sub-Registrar refused to register the document for the said value, as according to him, stamp duty had to be paid on ₹ 45,00,000, which was the Government guideline value. Mr. Raj Kumar preferred an appeal to the Revenue Divisional Officer, who fixed the value of the house as ₹ 32,00,000 (₹ 22,00,000 for land and the balance for building portion). The differential stamp duty was paid, accepting the said value determined. What are the tax implications in the hands of Mr. Raj Kumar and Mr. Dhuruv for the assessment year 2017-18? Mr. Raj Kumar had purchased the land on 1st June, 2010 for ₹ 5,19,000 and completed the construction of house on 1st October, 2014 for ₹ 14,00,000.

Cost inflation indices may be taken as 711 for the financial year 2010-11, 1024 for the financial year 2014-15 and 1125 for the financial year 2016-17.

Answer

In the hands of the seller, Mr. Raj Kumar

As per section 50C(1), where the consideration received or accruing as a result of transfer of land or building or both, is less than the value adopted or assessed or assessable by the stamp valuation authority, the value adopted or assessed or assessable by the stamp valuation authority shall be deemed to be the full value of consideration received or accruing as a result of transfer.

Where the assessee appeals against the stamp valuation and the value is reduced in appeal by the appellate authority (Revenue Divisional Officer, in this case), such value will be regarded as the consideration received or accruing as a result of transfer.

In the given problem, land has been held for a period exceeding 36 months and building for a period less than 36 months immediately preceding the date of transfer. So land is a long-term capital asset, while building is a short-term capital asset.

Particulars	₹
Long term capital gain on sale of land	
Consideration received or accruing as a result of transfer of land	22,00,000
Less: Indexed cost of acquisition ₹ 5,19,000 x 1125/711	8,21,203

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Long-term capital gain (A)	**13,78,797**
Short-term capital loss on sale of building	
Consideration received or accruing from transfer of building	10,00,000
Less: Cost of acquisition	14,00,000
Short term capital loss (B)	**4,00,000**

As per section 70, short-term capital loss can be set-off against long-term capital gains. Therefore, the net taxable long-term capital gains would be ₹ 9,78,797 (i.e., ₹ 13,78,797 – ₹ 4,00,000).

In the hands of the buyer Mr. Dhuruv

As per section 56(2)(vii), where an individual or HUF receives from a non-relative, any immovable property for a consideration which is less than the stamp value (or the value reduced by the appellate authority, as in this case) by an amount exceeding ₹ 50,000, then the difference between such value and actual consideration of such property is chargeable to tax as income from other sources. Therefore, ₹ 7,00,000 (i.e. ₹ 32,00,000 - ₹ 25,00,000) would be charged to tax as income from other sources under section 56(2)(vii) in the hands of Mr. Dhuruv.

Question 15

Compute the net taxable capital gains of Smt. Megha on the basis of the following information-

A house was purchased on 1.5.1997 for ₹ 4,50,000 and was used as a residence by the owner. The owner had contracted to sell this property in June, 2008 for ₹ 10 lacs and had received an advance of ₹ 70,000 towards sale. The intending purchaser did not proceed with the transaction and the advance was forfeited by the owner. The property was sold in April, 2016 for ₹ 16,00,000. The owner, from out of sale proceeds, invested ₹ 3 lacs in a new residential house in January, 2017.

Cost inflation index :- F.Y. 1997-98 – 331; F.Y. 2016-17 - 1125

Answer

Computation of net taxable capital gains of Smt. Megha for the A.Y.2017-18

Particulars	₹
Sale consideration	16,00,000
Less: Indexed cost of acquisition (See Working note below)	12,91,541
Long term capital gain	3,08,459
Less: Exemption under section 54 (See Note 1 below)	3,00,000
Taxable long term capital gain	**8,459**

Working Note:

Indexed cost of acquisition	**₹**
Purchase price	4,50,000
Less: Amount forfeited (See Note 2 below)	70,000
Cost of acquisition	3,80,000
Indexed cost of acquisition ₹ 3,80,000 × 1125/331	12,91,541

Notes:

(1) Exemption under section 54 is available if one new residential house is purchased within two years from the date of transfer of existing residential house, which is a long-term capital asset. Since the cost of new residential house is less than the long-term capital gains, capital gains to the extent of cost of new house, i.e., ₹ 3 lakh, is exempt under section 54.

(2) As per section 51, any advance received and retained by the assessee, as a result of earlier negotiations for sale of the asset, shall be deducted from the purchase price for computing the cost of acquisition of the asset.

Question 16

State, with reasons, whether the following statements are True or False.

(i) Alienation of a residential house in a transaction of reverse mortgage under a scheme made and notified by the Central Government is treated as "transfer" for the purpose of capital gains.

(ii) Zero coupon bonds of eligible corporation, held for more than 12 months, will be long-term capital assets.

(iii) In the case of a dealer in shares, income by way of dividend is taxable under the head "Profits and gains of business or profession".

(iv) Where an urban agricultural land owned by an individual, continuously used by him for agricultural purposes for a period of two years prior to the date of transfer, is compulsorily acquired under law and the compensation is fixed by the State Government, resultant capital gain is exempt.

(v) Zero Coupon Bond means a bond on which no payment and benefits are received or receivable before maturity or redemption.

(vi) Income from growing and manufacturing tea in India is treated as agricultural income wholly.

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Answer

(i) False : As per section 47(xvi), such alienation in a transaction of reverse mortgage under a scheme made and notified by the Central Government is not regarded as "transfer" for the purpose of capital gains.

(ii) True : Section 2(42A) defines the term 'short-term capital asset'. Under the proviso to section 2(42A), zero coupon bond held for not more than 12 months will be treated as a short-term capital asset. Consequently, such bond held for more than 12 months will be a long-term capital asset.

(iii) False : In view of the provisions of section 56(2)(i), dividend income is taxable under the head "Income from other sources" in the case of all assessees.

(iv) False: As per section 10(37), where an individual owns urban agricultural land which has been used for agricultural purposes for a period of two years immediately preceding the date of transfer, and the same is compulsorily acquired under any law and the compensation is determined or approved by the Central Government or the Reserve Bank of India, resultant capital gain will be exempt.

In this case, the compensation has been fixed by the State Government and hence the exemption will not be available.

(v) True: As per section 2(48), 'Zero Coupon Bond' means a bond issued by any infrastructure capital company or infrastructure capital fund or a public sector company, or Scheduled Bank on or after 1st June 2005, in respect of which no payment and benefit is received or receivable before maturity or redemption from such issuing entity and which the Central Government may notify in this behalf.

(vi) False : Only 60% of the income derived from the sale of tea grown and manufactured by the seller in India is treated as agricultural income and the balance 40% of the income shall be non-agricultural income chargeable to tax [Rule 8 of Income-tax Rules, 1962].

Question 17

Singhania & Co. own six machines, put in use for business in March, 2016. The depreciation on these machines is charged @ 15%. The written down value of these machines as on 1st April, 2016 was ₹ 8,50,000. Three of the old machines were sold on 10th June, 2016 for ₹ 11,00,000.

A new plant was bought for ₹ 8,50,000 on 30th November, 2016.

You are required to:

(i) determine the claim of depreciation for Assessment Year 2017-18.

(ii) compute the capital gains liable to tax for Assessment Year 2017-18.

(iii) If Singhania & Co. had sold the three machines in June, 2016 for ₹ 21,00,000, will there be any difference in your above workings? Explain.

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Answer

(i) **Computation of depreciation for A.Y.2017-18**

Particulars	₹
W.D.V. of the block as on 1.4.2016	8,50,000
Add: Purchase of new plant during the year	8,50,000
	17,00,000
Less: Sale consideration of old machinery during the year	11,00,000
W.D.V of the block as on 31.03.2017	6,00,000

Since the value of the block as on 31.3.2017 comprises of a new asset which has been put to use for less than 180 days, depreciation is restricted to 50% of the prescribed percentage of 15% i.e. depreciation is restricted to 7½%. Therefore, the depreciation allowable for the year is ₹ 45,000, being 7½% of ₹ 6,00,000.

Note: It is assumed that the firm is not eligible for additional depreciation under section 32(1)(iia).

(ii) The provisions under section 50 for computation of capital gains in the case of depreciable assets can be invoked only under the following circumstances:

(a) When one or some of the assets in the block are sold for consideration more than the value of the block.

(b) When all the assets are transferred for a consideration more than the value of the block.

(c) When all the assets are transferred for a consideration less than the value of the block.

Since in the first two cases, the sale consideration is more than the written down value of the block, the computation would result in short term capital gains.

In the third case, since the written down value exceeds the sale consideration, the resultant figure would be a short term capital loss.

In the given case, capital gains will not arise as the block of asset continues to exist, and some of the assets are sold for a price which is lesser than the written down value of the block.

(iii) If the three machines are sold in June, 2016 for ₹ 21,00,000, then short term capital gains would arise, since the sale consideration is more than the aggregate of the written down value of the block at the beginning of the year and the additions made during the year.

Particulars	₹	₹
Sale consideration		21,00,000
Less: W.D.V. of the machines as on 1.4.2016	8,50,000	
Purchase of new plant during the year	8,50,000	17,00,000
Short term capital gains		**4,00,000**

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Question 18

Ms. Paulomi has transferred 1,000 shares of Hetal Ltd., (which she acquired at a cost of ₹ 10,000 in the financial year 2002-03) to Dhaval, her brother, at a consideration of ₹ 3,12,934 on 15.5.2016 privately.

During the financial year 2016-17, she has paid through e-banking ₹ 15,000 towards medical premium, ₹ 50,000 towards life insurance premium and ₹ 25,000 towards PPF.

Assuming she has no other source of income, compute her total income and tax payable for the Assessment Year 2017-18.

Cost Inflation Index: for F.Y.2002- 03: 447; F.Y.2016-17 : 1125

Answer

Computation of total income and tax liability of Ms. Paulomi for A.Y. 2017-18

Particulars	₹
Sale consideration	3,12,934
Less: Indexed cost of acquisition (₹ 10,000 × 1125/447)	25,168
Long term capital gain	2,87,766
Total income	**2,87,770**
Tax liability	
Income-tax @ 20% on ₹ 37,770 (₹ 2,88,750 – ₹ 2,50,000)	7,554
Less: Rebate under section 87A	5,000
	2,554
Add: Education cess and secondary and higher education cess @ 3%	77
Total tax payable	**2,631**
Tax payable (rounded off)	**2,630**

Notes :

1. As per section 112, deductions under Chapter VI-A are not allowable against long term capital gain. Therefore, Paulomi is not entitled to deduction under section 80C in respect of payment of life insurance premium and contribution to PPF. She is also not entitled to deduction under section 80D in respect of medical insurance premium paid by her.
2. Since Paulomi has not transferred her shares through the Stock Exchange and, therefore, has not paid securities transaction tax, she is not entitled to claim exemption under section 10(38) in respect of long term capital gain.
3. She is, however, entitled to reduce the long-term capital gain by the unexhausted basic exemption limit and pay tax on the balance @20% as per section 112. In this case, since she has no other source of income, the entire basic exemption limit of ₹ 2,50,000 to the extent of long-term capital gain can be reduced from the long-term capital gain.

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Question 19

Aarav converts his plot of land purchased in July, 2002 for ₹ 80,000 into stock-in-trade on 31st March, 2016. The fair market value as on 31.3.2016 was ₹ 2,00,000. The stock-in-trade was sold for ₹ 2,25,000 in the month of January, 2017.

Find out the taxable income, if any, and if so under which 'head of income' and for which Assessment Year?

Cost Inflation Index: F.Y. 2002-03: 447; F.Y. 2015-16: 1081; F.Y. 2016-17: 1125.

Answer

Conversion of a capital asset into stock-in-trade is a transfer within the meaning of section 2(47) in the previous year in which the asset is so converted. However, the capital gains will be charged to tax only in the year in which the stock-in-trade is sold.

The cost inflation index of the financial year in which the conversion took place should be considered for computing indexed cost of acquisition. Further, the fair market value on the date of conversion would be deemed to be the full value of consideration for transfer of the asset as per section 45(2). The sale price less the fair market value on the date of conversion would be treated as the business income of the year in which the stock-in-trade is sold.

Therefore, in this problem, both capital gains and business income would be charged to tax in the A.Y. 2017-18.

Particulars	₹
Capital Gains	
Sale consideration (Fair market value on the date of conversion)	2,00,000
Less: Indexed cost of acquisition (₹ 80,000 × 1081/447)	1,93,468
Long-term capital gain	**6,532**
Profits & Gains of Business or Profession	
Sale price of stock-in-trade	2,25,000
Less: Fair market value on the date of conversion	2,00,000
	25,000
Computation of taxable income of Mr. Aarav for A.Y.2017-18	
Particulars	**₹**
Profits and gains from business or profession	25,000
Long term capital gains	6,532
	31,532

Question 20

Discuss the tax implications arising consequent to conversion of a capital asset into stock-in-trade of business and its subsequent sale.

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Answer

The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade. However, as per section 45(2), the profits or gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold. For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset. Indexation benefit is available upto the year of conversion of capital asset in stock-in-trade.

On subsequent sale of such stock-in-trade, business profits would arise. The business income chargeable to tax would be the difference between the price at which the stock-in-trade is sold and the fair market value on the date of conversion of the capital asset into stock-in-trade.

Question 21

What is the cost of acquisition of self-generated assets, for the purpose of computation of capital gains?

Answer

1. **Cost of acquisition of a capital asset, being goodwill of a business or a trade mark or brand name associated with a business or a right to manufacture, produce or process any article or thing, or right to carry on any business, tenancy rights, stage carriage permits and loom hours [Section 55(2)(a)]**

   (i) If the above capital assets have been purchased by the assessee, the cost of acquisition is the amount of the purchase price. For example, if Mr. A purchases a stage carriage permit from Mr. B for ₹ 2 lacs, that will be the cost of acquisition for Mr. A.

   (ii) If the above capital assets are self-generated, the cost of acquisition shall be taken as nil.

   (iii) In case the capital asset is acquired by any mode given under clauses (i) to (iv) of section 49(1), the cost of acquisition will be the cost to the previous owner if the previous owner paid for it. However, if it was self-generated by the previous owner, the cost of acquisition will be taken as nil.

2. **Cost of acquisition of other self-generated assets not covered under section 55(2)(a):**

   In respect of self-generated goodwill of a profession and other self-generated assets not specifically covered under section 55(2)(a), the decision of the Supreme Court in *CIT v. B.C. Srinivasa Setty [1981] 128 ITR 294* will apply. In that case, the Supreme Court held that if the cost of acquisition of a self-generated asset is incapable of determination, then transfer of such asset is not taxable and consequently the gains thereon cannot be brought to charge.

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Question 22

Mr. Malik owns a factory building on which he had been claiming depreciation for the past few years. It is the only asset in the block. The factory building and land appurtenant thereto were sold during the year. The following details are available:

Particulars	***₹***
Building completed in September, 2009 for	*10,00,000*
Land appurtenant thereto purchased in April, 2002 for	*12,00,000*
Advance received from a prospective buyer for land in May, 2003, forfeited in favour of assessee, as negotiations failed	*50,000*
WDV of the building block as on 1.4.2016	*8,74,800*
Sale value of factory building in November, 2016	*8,00,000*
Sale value of appurtenant land in November, 2016	*40,00,000*

The assessee is ready to invest in long-term specified assets under section 54EC, within specified time.

Compute the amount of taxable capital gain for the assessment year 2017-18 and the amount to be invested under section 54EC for availing the maximum exemption.

Cost inflation indices are as under :

Financial Year	*Cost inflation index*
2002-03	*447*
2003-04	*463*
2016-17	*1125*

Answer

Computation of taxable capital gain of Mr. Malik for A.Y.2017-18

Particulars	**₹**	**₹**
Factory building		
Sale price of building	8,00,000	
Less: WDV as on 1.4.2016	8,74,800	
Short-term capital loss on sale of building		(-) 74,800
Land appurtenant to the above building		
Sale value of land	40,00,000	
Less: Indexed cost of acquisition (₹ 11,50,000 × 1125/447)	28,94,295	
Long-term capital gains on sale of land		11,05,705
Chargeable long term capital gain		**10,30,905**

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Investment under section 54EC

In this case, both land and building have been held for more than 36 months and hence, are long-term capital assets. Exemption under section 54EC is available if the capital gains arising from transfer of a long-term capital asset are invested in long-term specified assets like bonds of National Highways Authority of India and Rural Electrification Corporation Ltd., within 6 months from the date of transfer. As per section 54EC, the amount to be invested for availing the maximum exemption is the net amount of capital gain arising from transfer of long-term capital asset, which is ₹ 10,30,905 (rounded off to ₹ 10,30,910) in this case.

Notes :

1. Where advance money has been received by the assessee, and retained by him, as a result of failure of the negotiations, section 51 will apply. The advance retained by the assessee will go to reduce the cost of acquisition. Indexation is to be done on the cost of acquisition so arrived at after reducing the advance money forfeited i.e. ₹ 12,00,000 – ₹ 50,000 = ₹ 11,50,000. It may be noted that in cases where the advance money is forfeited during the previous year 2015-16 or thereafter, the amount forfeited would be taxable under the head "Income from Other Sources" and such amount will not be deducted from the cost of acquisition of such asset while calculating capital gains.
2. Factory building on which depreciation has been claimed, is a depreciable asset. Profit / loss arising on sale is deemed to be short-term capital gain/loss as per section 50, and no indexation benefit is available.
3. Land is not a depreciable asset, hence section 50 will not apply. Being a long-term capital asset (held for more than 36 months), indexation benefit is available.
4. As per section 74, short term capital loss can be set-off against any income under the head "Capital gains", long-term or short-term. Therefore, in this case, short-term capital loss of ₹ 74,800 can be set-off against long-term capital gain of ₹ 11,05,705.

Question 23

Mr. A is an individual carrying on business. His stock and machinery were damaged and destroyed in a fire accident.

The value of stock lost (total damaged) was ₹ 6,50,000. Certain portion of the machinery could be salvaged. The opening WDV of the block as on 1-4-2016 was ₹ 10,80,000.

During the process of safeguarding machinery and in the fire fighting operations, Mr. A lost his gold chain and a diamond ring, which he had purchased in April, 2004 for ₹ 1,20,000. The market value of these two items as on the date of fire accident was ₹ 1,80,000.

Mr. A received the following amounts from the insurance company:

(i)	*Towards loss of stock*	*₹ 4,80,000*
(ii)	*Towards damage of machinery*	*₹ 6,00,000*
(iii)	*Towards gold chain and diamond ring*	*₹ 1,80,000*

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You are requested to briefly comment on the tax treatment of the above three items under the provisions of the Income-tax Act, 1961.

Answer

(i) Compensation towards loss of stock: Any compensation received from the insurance company towards loss/damage to stock in trade is to be construed as a trading receipt. Hence, ₹ 4,80,000 received as insurance claim for loss of stock has to be assessed under the head "Profit and gains of business or profession".

Note - The assessee can claim the value of stock destroyed by fire as revenue loss, eligible for deduction while computing income under the head "Profits and gains of business or profession".

(ii) Compensation towards damage to machinery: The question does not mention whether the salvaged machinery is taken over by the Insurance company or whether there was any replacement of machinery during the year. Assuming that the salvaged machinery is taken over by the Insurance company, and there was no fresh addition of machinery during the year, the block of machinery will cease to exist. Therefore, ₹ 4,80,000 being the excess of written down value (i.e ₹ 10,80,000) over the insurance compensation (i.e. ₹ 6,00,000) will be assessable as a short-term capital loss.

Note – If new machinery is purchased in the next year, it will constitute the new block of machinery, on which depreciation can be claimed for that year.

(iii) Compensation towards loss of gold chain and diamond ring: Gold chain and diamond ring are capital assets as envisaged by section 2(14). They are not "personal effects", which alone are to be excluded. As per section 45(1A), if any profit or gain arises in a previous year owing to receipt of insurance claim, the same shall be chargeable to tax as capital gains. The capital gains has to be computed by reducing the indexed cost of acquisition of jewellery from the insurance compensation of ₹ 1,80,000.

Question 24

Mr. A who transfers land and building on 02.01.2017, furnishes the following information:

(i) Net consideration received ₹ 18 lakhs.

(ii) Value adopted by stamp valuation authority, which was not contested by Mr. A ₹ 22 lakhs.

(iii) Value ascertained by Valuation Officer on reference by the Assessing Officer ₹ 25 lakhs.

(iv) This land was distributed to Mr. A on the partial partition of his HUF on 1.4.1981. Fair market value of the land as on 1.4.81 was ₹ 1,10,000.

(v) A residential building was constructed on the above land by Mr. A at a cost of ₹ 3,20,000 (construction completed on 1.12.2003) during the financial year 2003-04.

(vi) Brought forward unabsorbed short-term capital loss (incurred on sale of shares during the financial year 2012-13) ₹ 75,000.

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Mr. A seeks your advice as to the amount to be invested in NHAI/RECL bonds so as to be exempt from clutches of capital gain tax. Cost inflation indices for the financial years 1981-82, 2003-04 & 2016-17 are 100, 463 and 1125, respectively.

Answer

Computation of Capital Gains of Mr. A for the Assessment Year 2017-18

Particulars	₹	₹
Full value of consideration (deemed) (See Note-1&2)		22,00,000
(Indexation benefit is available since land and buildings are long-term capital assets)		
Less: Indexed cost of land (₹ 1,10,000 × 1125/100)	12,37,500	
Indexed cost of building (₹ 3,20,000 × 1125/ 463)	7,77,538	20,15,038
Long-term capital gain		**1,84,962**
Less: Brought forward short-term capital loss set off(See Note-4)		75,000
Amount to be invested in NHAI / RECL bonds		**1,09,962**

Notes :

(1) Where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted or assessed by any authority of a State Government (Stamp Valuation Authority) for the purpose of payment of stamp duty in respect of such asset and the same is not contested by the assessee, such value adopted or assessed shall be deemed to be the full value of the consideration received or accruing as a result of such transfer [Section 50C(1)]. Accordingly, the full value of consideration will be ₹ 22 lakhs in this case.

(2) It is further provided in section 50C(3) that where the valuation is referred by the Assessing Officer to Valuation Officer and the value ascertained by such Valuation Officer exceeds the value adopted or assessed by the Stamp Valuation Authority, the value adopted or assessed by the Stamp Valuation Authority shall be taken as the full value of the consideration received or accruing as a result of the transfer. Since the value ascertained by the valuation officer (i.e. ₹ 25 lakhs) is higher than the value adopted by the stamp valuation authority (i.e. ₹ 22 lakhs), the full value of consideration in this case is ₹ 22 lakhs.

(3) Cost of land which is acquired on partition of HUF is the cost to the previous owner. Since date and cost of acquisition to the previous owner are not given, fair market value as on 1.4.1981 is taken as the cost and indexed.

(4) Brought forward unabsorbed short term capital loss can be set off against any capital gains, short term or long term, for 8 assessment years immediately succeeding the assessment year for which the loss was first computed.

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(5) As per section 54EC, an assessee can avail exemption in respect of long-term capital gains, if such capital gains are invested in the bonds issued by the NHAI / RECL redeemable after 3 years. Such investment is required to be made within a period of 6 months from the date of transfer of the asset. The exemption shall be the amount of capital gain or the amount of such investment made, whichever is less.

Question 25

Mr. X is in possession of agricultural land situated within urban limits, which is used for agricultural purposes during the preceeding 3 years by his father. On 4.4.2016, this land is compulsorily acquired by the Central Government of India on a compensation fixed and paid by it for ₹ 10 lakhs. Advise X as to the tax consequences, assuming that the entire amount is invested in purchase of shares.

Answer

Section 10(37) exempts the capital gains arising to an individual or a Hindu Undivided Family from transfer of agricultural land by way of compulsory acquisition, or a transfer, the consideration for which is determined or approved by the RBI or the Central Government.

Such exemption is available where the compensation or the enhanced compensation or consideration, as the case may be, is received on or after 1st April, 2004 and the land has been used for agricultural purposes during the preceding two years by such individual or a parent of his or by such Hindu undivided family.

Since all the above conditions are fulfilled in this case, X is entitled to exemption under section 10(37) of the entire capital gains arising on sale of agricultural land.

Question 26

Mr. Sagar, a resident individual acquired a plot of land at a cost of ₹ 75,000 in June, 1999. He constructed a house for his residence on that land at a cost of ₹ 1,25,000 in the financial year 2001-02.

He transferred the house for ₹ 15,00,000 in May, 2016 and acquired another residential house in June, 2016 for ₹ 8,00,000.

He furnishes other particulars as under

Insurance agency commission earned	*45,000*
(Net of TDS of ₹ 5,000)	
Investment in NSC VIII issue	*20,000*
(i.e. on 20-3-2017)	

Cost inflation index details are given below:

Financial Year	***Cost Inflation Index***
1999 – 2000	*389*

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2001 – 2002	*426*
2016 – 2017	*1125*

Compute the total income of Mr. Sagar for the assessment year 2017-18.

Answer

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

Particulars	₹	₹
Capital Gains		
Sale consideration		15,00,000
Less: Indexed cost of land (₹75,000 x 1125/389)	2,16,902	
Indexed cost of building (₹ 1,25,000 x 1125/426)	3,30,106	5,47,008
		9,52,992
Less: Exemption under section 54 **(See Note 2 below)**		8,00,000
Long-term capital gain		**1,52,992**
Profit and gains from business or profession/Income from other sources		
Insurance agency commission earned (Gross) (₹ 45,000 + ₹ 5,000)		50,000
Gross Total Income		**2,02,992**
Less: **Deduction under Chapter VI-A**		
Section 80C - Investment in NSC VIII		20,000
Total Income		**1,82,992**
Total Income (Rounded off)		**1,82,990**

Notes:

(1) Since the building and the land are held for more than 36 months, the same are long-term capital assets and the capital gain arising on sale of such assets is a long-term capital gain.

(2) As per the provisions of section 54, the capital gain arising on transfer of a long-term residential property shall not be chargeable to tax to the extent such capital gain is invested in the purchase of a residential house property one year before or two years after the date of transfer of original asset or constructed a residential house property within three years after such date. Since Mr. Sagar has purchased another residential house in June, 2016 for ₹ 8,00,000, the capital gain arising on transfer of residential house property in May, 2016 is exempt under section 54 to that extent.

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Question 27

Mr. Y submits the following information pertaining to the year ended 31st March, 2017:

(i) On 30.11.2016, when he attained the age of 60, his friends in India gave a flat at Surat as a gift, each contributing a sum of ₹ 20,000 in cash. The cost of the flat purchased using the various gifts was ₹ 3.40 lacs.

(ii) His close friend abroad sent him a cash gift of ₹ 75,000 through his relative for the above occasion.

(iii) Mr. Y sold the above flat on 30.1.2017 for ₹ 3.6 lacs. The Registrar's valuation for stamp duty purposes was ₹ 3.7 lacs. Neither Mr. Y nor the buyer, questioned the value fixed by the Registrar.

(iv) He had purchased some unlisted equity shares in X Pvt. Ltd., on 5.2.2007 for ₹ 3.5 lacs. These shares were sold on 15.3.2017 for ₹ 2.8 lacs.

You are requested to calculate the total income of Mr. Y for the assessment year 2017-18.

[Cost Inflation Index for F.Y. 2006-07: 519, 2016-17: 1125]

Answer

Computation of total income of Mr. Y for A.Y. 2017-18

Particulars	₹	₹	₹
Capital Gains			
Short term capital gains (on sale of flat)			
(i) Sale consideration	3,60,000		
(ii) Stamp duty valuation	3,70,000		
Consideration for the purpose of capital gains as per section 50C (stamp duty value, since it is higher than sale consideration)		3,70,000	
Less: Cost of acquisition [As per section 49(4), cost to be taken into consideration for 56(2)(vii) will be the cost of acquisition]		3,40,000	30,000
Long term capital loss on sale of equity shares of X Pvt. Ltd			
Sale consideration		2,80,000	
Less: Indexed cost of acquisition (₹ 3,50,000 × 1125/519)		7,58,671	
Long term capital loss to be carried forward		**4,78,671**	
(See Note 1 below)			
Income from other sources:			
Gift from friends by way of immovable property on			3,40,000

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30.11.2016 **[See Note 3 below]**.			
Gift received from a close friend (unrelated person) **[See Note 2 below]**			75,000
Total income			**4,45,000**

Notes:

1. In the given problem, unlisted shares of X Pvt. Ltd. have been held for more than **24 months** and hence, constitute a long term capital asset. The loss arising from sale of such shares is, therefore, a long-term capital loss. As per section 70(3), long term capital loss can be set-off only against long-term capital gains. Therefore, long-term capital loss cannot be set-off against short-term capital gains. However, such long-term capital loss can be carried forward to the next year for set-off against long-term capital gains arising in that year.
2. Any sum received from an unrelated person will be deemed as income and taxed as income from other sources if the aggregate sum received exceeds ₹ 50,000 in a year [Section 56(2)(vii)].
3. Receipt of immovable property without consideration would attract the provisions of section 56(2)(vii).

Question 28

Mr. Bala sold his vacant site on 21.09.2016 for ₹ 7,00,000. It was acquired by him on 01.10.1995 for ₹ 1,50,000.

The State stamp valuation authority fixed the value of the site at the time of transfer @ ₹ 13,00,000.

Compute capital gains in the hands of Bala and give your reasons for computation.

Cost inflation index : F.Y.1995-96: 281 and F.Y. 2016-17 : 1125.

Answer

Computation of capital gains of Bala for the A.Y.2017-18

Particulars	₹
Deemed sale consideration as per section 50C	13,00,000
Less : Indexed cost of acquisition (₹ 1,50,000 × 1125 /281)	6,00,534
Taxable long term capital gain	**6,99,466**

Note: According to section 50C(1), where the consideration received or accruing as a result of the transfer of land or building or both is less than the value adopted or assessed or assessable by the State Stamp Valuation Authority for the purpose of payment of stamp duty in respect of such transfer, then the value so adopted or assessed or assessable by the State Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of the transfer.

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In this case, since the consideration of ₹ 7,00,000 received on transfer of land is less than the value of ₹ 13,00,000 fixed by the State Stamp Valuation Authority, the value adopted by the State Stamp Valuation Authority is deemed to be the full value of consideration and capital gains is calculated accordingly.

Question 29

Mr. 'X' furnishes the following data for the previous year ending 31.3.2017:

(a) Unlisted Equity Shares of AB Ltd., 10,000 in number were sold on 31.5.2016, at ₹ 500 for each share.

(b) The above shares of 10,000 were acquired by 'X' in the following manner:

(i) Received as gift from his father on 1.6.1980 (5,000 shares) the fair market value on 1.4.1981 ₹ 50 per share.

(ii) Bonus shares received from AB Ltd. on 21.7.1985 (2,000 shares).

(iii) Purchased on 1.2.1994 at the price of ₹ 125 per share (3,000 shares).

(c) Purchased one residential house at ₹ 25 lakhs, on 1.5.2017 from the sale proceeds of shares.

(d) 'X' is already owning a residential house, even before the purchase of above house.

You are required to compute the taxable capital gain. He has no other source of income chargeable to tax.

(Cost Inflation Index – Financial year 1985-86: 133; 1993-94: 244; Financial year 2016-17: 1125)

Answer

Computation of taxable capital gain of Mr. 'X' for A.Y. 2017-18

	Particulars	₹	₹
Sale consideration received on sale of 10,000 shares @ ₹ 500 each			50,00,000
Less: Indexed cost of acquisition			
(a)	5,000 shares received as gift from father on 1.6.1980 Indexed cost 5,000 x ₹ 50 x 1125/100	28,12,500	
(b)	2,000 bonus shares received from AB Ltd	Nil	
	Bonus shares are acquired on 21.7.1985 i.e. after 01.04.1981. Hence, the cost is Nil.		
(c)	3000 shares purchased on 1.2.1994 @ ₹ 125 per share. The indexed cost is 3000 x 125 x 1125/244	17,28,996	45,41,496
Long term capital gain			**4,58,504**
Less : Exemption under section 54F (See Note below)			

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₹ 4,58,504 x ₹ 25,00,000 / ₹ 50,00,000		2,29,252
Taxable long term capital gain		**2,29,252**

Note: *Exemption under section 54F can be availed by the assessee subject to fulfillment of the following conditions:*

(a) The assessee should not own more than one residential house on the date of transfer of the long-term capital asset;

(b) The assessee should purchase a residential house within a period of 1 year before or 2 years after the date of transfer or construct a residential house within a period of 3 years from the date of transfer of the long-term capital asset.

In this case, the assessee has fulfilled the two conditions mentioned above. Therefore, he is entitled to exemption under section 54F.

Question 30

Ms. Vimla sold a residential building at Jodhpur for ₹ 15,00,000 on 01-07-2016.

The building was acquired for ₹ 1,50,000 on 01-06-1997.

She paid brokerage @ 2% at the time of sale of the building. She invested ₹ 7 lakhs in purchase of a residential building in December 2016 and deposited ₹ 2 lakhs in NHAI Capital Gains Bond in March, 2017. Compute her taxable capital gain.

Cost inflation index of F.Y.1997-98: 331; F.Y. 2016-17: 1125

Answer

Computation of taxable capital gain of Ms. Vimla for A.Y.2017-18

Particulars	₹	₹
Sale price of residential building	15,00,000	
Less : Brokerage @ 2%	30,000	
Net consideration		14,70,000
Less : Indexed cost of acquisition		
₹ 1,50,000 x 1125/331		5,09,819
		9,60,181
Less: Deduction under section 54 for purchase of new residential house in December 2016		7,00,000
Taxable long term capital gain		**2,60,181**

Note: One of the conditions for claiming exemption under section 54EC for the investment in RECL/NHAI Capital Gains bonds is that the deposit should be made within 6 months from the

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date of transfer. In this case, the transfer took place on 1.7.2016 and the 6 months period within which the deposit should be made for the purpose of section 54EC would expire by 31.12.2016. The investment in REC/NHAI Capital Gains bonds was made only in March 2017. Therefore, the assessee is not eligible for exemption under section 54EC.

Question 31

Mrs. Malini Hari shifted her industrial undertaking located in corporation limits of Faridabad, to a Special Economic Zone (SEZ) on 1.12.2016.

The following particulars are available:

	Particulars	₹
(a)	*Land: Purchased on 20.01.2003*	*4,26,000*
	Sold for	*22,00,000*
(b)	*Building [Construction completed on 14.03.2006]*	
	WDV of building as on 01.04.2016	*8,20,000*
	Sold for	*11,39,000*
(c)	*WDV of cars as on 01.04.2016*	*7,40,000*
	Sold for	*6,00,000*
(d)	*Expenses on shifting the undertaking*	*1,15,000*
(e)	*Assets acquired for the undertaking in the SEZ (on or before 25.06.2017):*	
	(i) Land	*3,00,000*
	(ii) Building	*5,00,000*
	(iii) Computers	*1,00,000*
	(iv) Car	*4,20,000*
	(v) Machinery (Second hand)	*2,00,000*
	(vi) Furniture	*50,000*

There is no intention of investing in any other asset in this undertaking.

Compute the exemption available under section 54GA for the assessment year 2017-18.

Cost inflation indices for F.Y.2002-03 – 447; F.Y.2016-17: 1125.

Answer

Where an assessee shifts an existing undertaking from an urban area to a SEZ and incurs expenses for shifting and acquires new assets for the undertaking in the SEZ, exemption under section 54GA would be available in such a case.

The capital gain, short-term or long-term, arising from transfer of land, building, plant and machinery in the existing undertaking would be exempt under section 54GA if the assessee, within a period of one year before or three years after the date on which the transfer took place,

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(i) acquires plant and machinery for use in the undertaking in the SEZ;

(ii) acquires land or building or constructs building for the business of the undertaking in the SEZ;

(iii) incurs expenses on shifting of the undertaking.

Computation of capital gain :

(a) *Land:*

Sale price	22,00,000
Less: Indexed cost of acquisition 4,26,000 x 1125/447	10,72,148
Long-term capital gain	11,27,852

(b) *Building:*

Sale value	11,39,000
Less: Opening WDV	8,20,000
Short-term capital gain under section 50	3,19,000

(c) *Plant:*

Car

Sale value	6,00,000
Less: Opening WDV	7,40,000
Short term capital loss under section 50	(-)1,40,000
Net short term capital gain (₹ 3,19,000 – ₹ 1,40,000)	1,79,000

Total capital gain (LTCG+STCG) i.e. ₹ 11,27,852+ ₹ 1,79,000 = ₹ 13,06,852

Exemption under section 54GA is available in respect of the following assets acquired and expenses incurred:

Particulars	₹
Land	3,00,000
Building	5,00,000
Plant:	
Computers	1,00,000
Car	4,20,000
Machinery	2,00,000
Expenses of shifting	1,15,000
Total Exemption	**16,35,000**

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Note:

1. The total exemption available under section 54GA is the lower of capital gains of ₹ 13,06,852 or the amount of investment which is ₹ 16,35,000. Hence, the amount of exemption available under section 54GA is ₹ 13,06,852. The taxable capital gains would be Nil.
2. Furniture purchased is not eligible for exemption under section 54GA.
3. There is no restriction regarding purchase of second hand machinery.
4. Computers and car would constitute Plant.

Question 32

Mr. Thomas inherited a house in Jaipur under will of his father in May, 2003. The house was purchased by his father in January, 1980 for ₹ 2,50,000. He invested an amount of ₹ 7,00,000 in construction of one more floor in this house in June, 2005. The house was sold by him in November, 2016 for ₹ 37,50,000. The valuation adopted by the registration authorities for charge of stamp duty was ₹ 47,25,000 which was not contested by the buyer, but as per assessee's request, the Assessing Officer made a reference to Valuation officer. The value determined by the Valuation officer was ₹ 47,50,000. Brokerage @ 1% of sale consideration was paid by Mr. Thomas to Mr. Sunil. The fair market value of house as on 01.04.1981 was ₹ 2,70,000.

You are required to compute the amount of capital gain chargeable to tax for A.Y. 2017-18 with the help of given information and by taking CII for the F.Y. 2003-04 : 463, F.Y. 2005-06: 497 and for F.Y. 2016-17:1125.

Answer

Computation of Long term Capital Gain for A.Y. 2017-18

Particulars	₹	₹
Sale consideration as per section 50C (Note-1)		47,25,000
Less: Expenses incurred on transfer being brokerage @ 1% of sale consideration of ₹ 37.50 lacs		37,500
		46,87,500
Less: Indexed cost of acquisition (Note-2) (₹ 2,70,000 × 1125/463)	6,56,048	
Indexed cost of improvement (₹ 7,00,000 × 1125/497)	15,84,507	22,40,555
Long term capital gain		**24,46,945**

Notes:

1. As per section 50C, where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the valuation by the stamp valuation authority, such value adopted or assessed by the stamp valuation authority

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shall be deemed to be the full value of consideration. Where a reference is made to the valuation officer, and the value ascertained by the valuation officer exceeds the value adopted by the stamp valuation authority, the value adopted by the stamp valuation authority shall be taken as the full value of consideration.

Sale consideration	₹ 37,50,000
Valuation made by registration authority for stamp duty	₹ 47,25,000
Valuation made by the valuation officer on a reference	₹ 47,50,000

Applying the provisions of section 50C to the present case, ₹ 47,25,000, being, the value adopted by the registration authority for stamp duty, shall be taken as the sale consideration for the purpose of charge of capital gain.

2. The house was inherited by Mr. Thomas under the will of his father and therefore, the cost incurred by the previous owner shall be taken as the cost. Fair market value as on 01.04.81, accordingly, shall be adopted as the cost of acquisition of the house property. However, indexation benefit will be given from the year in which Mr. Thomas first held the asset i.e. P.Y.2003-04.

   Alternative view: *In the case of CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.), the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.*

   As per this view, the indexed cost of acquisition of house would be ₹ 30,37,500 and long term capital gain would be ₹ 65,493.

Question 33

Ms. Vasudha contends that sale of a work of art held by her is not exigible to capital gains tax. Is she correct?

Answer

As per section 2(14)(ii), the term “personal effects” excludes any work of art. As a result, any work of art will be considered as a capital asset and sale of the same will attract capital gains tax. Thus, the contention of Ms. Vasudha is not correct.

Question 34

Ms. Vasumathi purchased 10,000 equity shares of ABC Co. Pvt. Ltd. on 28.2.2005 for ₹ 1,20,000. The company was wound up on 31.7.2016. The following is the summarized financial position of the company as on 31.7.2016:

Liabilities	₹	*Assets*	₹
60,000 Equity shares	*6,00,000*	*Agricultural lands*	*42,00,000*
General reserve	*40,00,000*	*Cash at bank*	*6,50,000*
Provision for taxation	*2,50,000*		
	48,50,000		***48,50,000***

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The tax liability was ascertained at ₹ 3,00,000. The remaining assets were distributed to the shareholders in the proportion of their shareholding. The market value of 6 acres of agricultural land (in an urban area) as on 31.7.2016 is ₹ 10,00,000 per acre.

The agricultural land received above was sold by Ms. Vasumathi on 28.2.2017 for ₹ 15,00,000.

Discuss the tax consequences in the hands of the company and Ms. Vasumathi.

The cost inflation indices are: F.Y.2004-05: 480; F.Y.2016-17 : 1125

Answer

In the hands of the company

As per section 46(1), distribution of capital assets amongst the shareholders on liquidation of the company is not regarded as "transfer" in the hands of the company. Consequently, there will be no capital gains in the hands of the company.

In the hands of Ms. Vasumathi (shareholder)

Section 46(2) provides that such capital gains would be chargeable in the hands of the shareholder.

Particulars	₹
Ms. Vasumathi holds 1/6th of the shareholding of the company	
Market value of agricultural land received (1 acre @ ₹ 10 Lakhs)	10,00,000
Cash at bank [1/6th of (₹ 6,50,000 – ₹ 3,00,000)]	58,333
	10,58,333
Less: Deemed dividend under section 2(22)(c) - 1/6th of (₹ 40,00,000- ₹ 50,000)	6,58,333
Consideration for computing Capital Gain	4,00,000
Less: Indexed cost of acquisition of Shares (₹ 1,20,000 x 1125/ 480)	2,81,250
Long term capital gains	**1,18,750**

Notes:

1. Where the capital asset became the property of the assessee on the distribution of the capital assets of a company on its liquidation and the assessee has been assessed to capital gains in respect of that asset under section 46, the cost of acquisition means the fair market value of the asset on the date of distribution. Hence, the short-term capital gains in the hands of Ms. Vasumathi (shareholder) at the time of sale of urban agricultural land should be computed as follows:

Particulars	₹
Sale consideration	15,00,000
Less: Fair market value of the agricultural land on the date of distribution	10,00,000
Short term capital gain	**5,00,000**

2. Dividend under section 2(22)(c) amounting to ₹ 6,58,333 will be exempt under section 10(34).
3. The tax liability ascertained at ₹ 3,00,000 has to be reduced from bank balance while computing full value of consideration under section 46(2). ₹ 50,000, being the difference between ₹ 3,00,000 and ₹ 2,50,000, has to be reduced from General Reserve for calculating deemed dividend under section 2(22)(c).

Question 35

State with reasons whether the following statements are true or false having regard to the provisions of the Income-tax Act, 1961:

(a) Capital gain of ₹ 75 lakh arising from transfer of long term capital assets on 1.5.2016 will be exempt from tax if such capital gain is invested in the bonds redeemable after three years, issued by NHAI under section 54EC.

(b) As per section 49(2A), read with section 47(xa) of the Income-tax Act, 1961, no capital gains would arise on conversion of foreign currency exchangeable bonds into shares or debentures, for facilitating the issue of FCEBs by companies.

Answer

(a) False : The exemption under section 54EC has been restricted, by limiting the maximum investment in long term specified assets (i.e. bonds of NHAI or RECL, redeemable after 3 years) to ₹ 50 lakh, whether such investment is made during the relevant previous year or the subsequent previous year, or both. Therefore, in this case, the exemption under section 54EC can be availed only to the extent of ₹ 50 lakh, provided the investment is made before 1.11.2016 (i.e., within six months from the date of transfer).

(b) True : As per section 47(xa), any transfer by way of conversion of bonds referred to in section 115AC into shares and debentures of any company is not regarded as transfer. Therefore, there will be no capital gains on conversion of foreign currency exchangeable bonds into shares or debentures.

Question 36

Mrs. X, an individual resident woman, wanted to know whether income-tax is attracted on sale of gold and jewellery gifted to her by her parents on the occasion of her marriage in the year 1979 which was purchased at a total cost of ₹ 2,00,000?

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Answer

The definition of capital asset under section 2(14) includes jewellery. Therefore, capital gains is attracted on sale of jewellery, since jewellery is excluded from personal effects. The cost to the previous owner or the fair market value as on 1.4.1981, whichever is more beneficial to the assessee, would be treated as the cost of acquisition. Accordingly, in this case, long term capital gain @ 20% will be attracted in the year in which the gold and jewellery is sold by Mrs. X.

Question 37

Mr. Kumar, aged 50 years, is the owner of a residential house which was purchased in September, 1993 for ₹ 5,00,000. He sold the said house on 5th August, 2016 for ₹ 24,00,000. Valuation as per stamp valuation authority of the said residential house was ₹ 43,00,000. He invested ₹ 5,00,000 in NHAI Bonds on 12th January, 2017. He purchased a residential house on 5th July, 2017 for ₹ 10,00,000. He gives other particulars as follows:

Interest on Bank Fixed Deposit	*₹ 32,000*
Investment in public provident fund	*₹ 50,000*

You are requested to calculate the taxable income for the assessment year 2017-18 and the tax liability, if any.

Cost inflation index for F.Y. 1993-94 and 2016-17 are 244 and 1125, respectively.

Answer

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

Particulars	₹	₹
Capital Gains:		
Sale price of the residential house	24,00,000	
Valuation as per Stamp Valuation authority	43,00,000	
(Value to be taken is the higher of actual sale price or valuation adopted for stamp duty purpose as per section 50C)		
Therefore, Consideration for the purpose of Capital Gains	43,00,000	
Less: Indexed Cost of Acquisition		
₹ 5,00,000 x 1125/244	23,05,328	
	19,94,672	
Less: Exemption under section 54 ₹ 10,00,000		
Exemption under section 54EC ₹ 5,00,000	15,00,000	

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Long-term capital gains		4,94,672
Income from other sources:		
Interest on bank deposits		32,000
Gross Total Income		**5,26,672**
Less: Deduction under Chapter VI-A		
Section 80C – Deposit in PPF (restricted to ₹ 32,000)		
		32,000
Total Income		**4,94,672**

Computation of Tax liability of Mr. Kumar for A.Y. 2017-18

Particulars	₹
Tax on ₹ 2,44,672 @ 20% [i.e. long term capital gain less basic exemption limit (₹ 4,94,672- ₹ 2,50,000)]	48,934
Less: Rebate u/s 87A	5,000
	43,934
Add: Education Cess@2% & SHEC @ 1%	1,318
Tax Payable	**45,252**
Tax Payable (Rounded off)	**45,250**

Notes:

1. The basic exemption limit of ₹ 2,50,000 can be adjusted against long term capital gains.
2. Deduction under section 80C should be restricted to gross total income excluding long term capital gain.

Question 38

Mr. Pranav, a resident individual aged 55 years, had purchased a plot of land at a cost of ₹ 75,000 in June, 1999. He constructed a house for his residence on that land at a cost of ₹ 1,25,000 in August, 2001. He sold that house in May, 2016 at ₹ 16,00,000 and purchased another residential house in June, 2016 for ₹ 8,00,000. He furnishes other income and investment as follows :

Particulars	₹
Interest on fixed deposit with a bank (Net of TDS ₹ 5,000)	*45,000*
Investment in PPF	*20,000*

CII for financial year 1999-2000, 2001-02 and 2016-17 are 389, 426 and 1125 respectively.

You are required to compute taxable income and tax payable by Mr. Pranav for the

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assessment year 2017-18.

Answer

Computation of taxable income and tax payable by Mr. Pranav for the A.Y. 2017-18

	Particulars	₹	₹
1.	**Income from Capital Gains**		
	Full value of consideration		16,00,000
	Less : Indexed cost of acquisition of land (₹ 75,000 × 1125/389)		2,16,902
	Less: Indexed cost of construction of house (₹ 1,25,000 × 1125/426)		3,30,106
			10,52,992
	Less : Deduction under section 54 Cost of new residential house		8,00,000
	Long term capital gains		**2,52,992**
2.	**Income from other sources**		
	Interest on Bank deposit (Net)	45,000	
	Add : Tax deducted at source	5,000	50,000
	Gross total income		**3,02,992**
	Less: Deduction under section 80C : Investment in PPF		20,000
	Taxable income		**2,82,992**
	Components of Total income		
	Special income		
	Long-term Capital gains	2,52,992	
	Normal Income (₹ 50,000 – ₹ 20,000)	30,000	
		2,82,992	
	Tax on normal income of ₹ 30,000		Nil
	Tax on LTCG		
	[LTCG (Maximum amount not chargeable to tax - Normal Income) @ 20%] under section112 = {₹ 2,52,992 – (₹ 2,50,000 – ₹ 30,000)} x 20%		6,598
	Less: Rebate under section 87A		5,000
			1,598

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	Add : Education cess @ 2%	32
	Secondary and higher education cess @ 1%	16
	Tax payable	**1,646**
	Less: Tax deducted at source	5,000
		3,354
	Tax Refundable (rounded off)	**3,350**

Question 39

Mr. C inherited from his father 8 plots of land in 1980. His father had purchased the plots in 1960 for ₹ 5 lakhs. The fair market value of the plots as on 1-4-1981 was ₹ 8 lakhs. (₹ 1 lakh for each plot)

On 1st June 2001, C started a business of dealer in plots and converted the 8 plots as stock-in-trade of his business. He recorded the plots in his books at ₹ 45 lakhs being the fair market value on that date. In June 2005, C sold the 8 plots for ₹ 50 lakhs.

In the same year, he acquired a residential house property for ₹ 35 lakhs. He invested an amount of ₹ 5 lakhs in construction of one more floor in his house in June 2006. The house was sold by him in June 2016 for ₹ 75,00,000.

The valuation adopted by the registration authorities for charge of stamp duty was ₹ 98,00,000. As per the assessee's request, the Assessing Officer made a reference to a Valuation Officer. The value determined by the Valuation Officer was ₹ 1,05,00,000. Brokerage of 1 % of sale consideration was paid by C.

The relevant Cost Inflation Indices are:

F.Y. 1981-82	*100*
F.Y. 2001-02	*426*
F.Y. 2005-06	*497*
F.Y. 2006-07	*519*
F.Y. 2016-17	*1125*

Give the tax computation for the Assessment Year 2017-18.

Answer

Computation of total income and tax liability of Mr. C for A.Y. 2017-18

Particulars	₹	₹
Capital Gains on sale of residential house property Value declared by Mr. C ₹ 75,00,000 Value adopted by Stamp Valuation Authority ₹ 98,00,000		

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Valuation as per Valuation Officer ₹ 1,05,00,000		
Gross Sale consideration (See Note 1)		98,00,000
Less: Brokerage@1% of sale consideration		75,000
Net Sale consideration		97,25,000
Less: Indexed cost of acquisition (₹ 35,00,000 × 1125/497)	79,22,535	
Indexed cost of improvement (₹ 5,00,000 × 1125/519)	10,83,815	90,06,350
Long-term capital gains (Total Income)		7,18,650
Tax on total income (See Note 2)		
Long-term capital gain taxable@20% (₹ 7,18,650 – ₹ 2,50,000)		93,730
Add: Education cess @ 2%		1,875
Secondary and higher education cess @ 1%		977
Total tax liability		**96,542**
Tax liability (rounded off)		96,540

Notes:

1. As per section 50C, in case the value of sale consideration declared by the assessee is less than the value adopted by the Stamp Valuation Authority for the purpose of charging stamp duty, then, the value adopted by the Stamp Valuation Authority shall be taken to be the full value of consideration. In case the valuation is referred to the Valuation Officer and the value determined is more than the value adopted by the Stamp Valuation Authority, the value determined by the Valuation Officer shall be ignored. Therefore, in the present case, the sale consideration would be the stamp valuation of ₹ 98,00,000, since the same is more than the sale value declared by Mr. C and less than the value determined by the Valuation Officer.
2. As per section 112, the unexhausted basic exemption limit can be exhausted against the long-term capital gains. Since Mr. C does not have any other income in the current year, the whole of the basic exemption limit of ₹ 2,50,000 is exhausted against the long-term capital gains of ₹ 7,18,650 and the balance long-term capital gains shall be taxable@20%. It is assumed that Mr. C is a resident individual below the age of 60 years.

Question 40

Ms. Mohini transferred a house to her friend Ms. Ragini for ₹ 35,00,000 on 01-10-2016. The Sub Registrar valued the land at ₹ 48,00,000. Ms. Mohini contested the valuation and the matter was referred to Divisional Revenue Officer, who valued the house at ₹ 41,00,000. Accepting the said value, differential stamp duty was also paid and the transfer was completed.

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The total income of Mohini and Ragini for the assessment year 2017-18, before considering the transfer of said house are ₹ 2,80,000 and ₹ 3,45,000, respectively. Ms. Mohini had purchased the house on 15th May 2011 for ₹ 25,00,000 and registration expenses were ₹ 1,50,000.

You are required to explain provisions of Income-tax Act, 1961 applicable to present case and also determine the total income of both Ms. Mohini and Ms. Ragini taking into account the above said transactions. Cost inflation indices for:

(i) Financial Year 2011-12 :785 and

(ii) Financial Year 2016-17 : 1125

Answer

Computation of total income of Ms. Mohini for A.Y. 2017-18

Particulars	₹	₹
Long-term capital gain		
Full value of consideration	41,00,000	
(As per section 50C read with section 155(15), in case the actual sale consideration is less than the stamp duty value fixed by the stamp valuation authority (Sub-registrar, in this case), the stamp duty value shall be deemed as the full value of consideration.		
Where the assessee contests the stamp valuation, and the value is reduced by the Divisional Revenue Officer, such reduced value will be regarded as the full value of consideration accruing as a result of transfer.		
Hence, in this case, ₹ 41,00,000, being the valuation by Divisional Revenue Officer on which stamp duty is paid, would be deemed as full value of consideration, since the same is lower than the valuation by the Sub-registrar)		
Less: Indexed cost of acquisition [₹ 26,50,000 x $\frac{1125}{785}$]	37,97,771	3,02,229
Other Income		2,80,000
Total Income		**5,82,229**
Note: *Cost of acquisition includes purchase price plus registration expenses i.e., ₹ 25,00,000 + ₹ 1,50,000*		**or 5,82,230**

Computation of total income of Ms. Ragini for A.Y. 2017-18

Particulars	₹
Income from other sources	
Immovable property received for inadequate consideration	6,00,000

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As per section 56(2)(vii), where an individual receives from a non-relative, any immovable property for a consideration which is less than the stamp duty value (or the value reduced by the Divisional Revenue Officer, as in this case) by an amount exceeding ₹ 50,000, then, the difference between such value and actual consideration of such property would be chargeable to tax as income from other sources. Therefore, ₹ 6,00,000 (i.e., ₹ 41,00,000 – ₹ 35,00,000) would be chargeable to tax as income from other sources.	
Other Income	3,45,000
Total Income	**9,45,000**

Question 40

Mr. Martin, a resident individual sold his residential house property on 08-06-2016 for ` 70 lakhs which was purchased by him for ` 20 lakhs on 05-05-2005.

He paid ₹ 1 lakh as brokerage for the sale of said property. The stamp duty valuation assessed by sub registrar was ₹ 80 lakhs.

He bought another house property on 25-12-2016 for ₹ 15 lakhs.

He deposited ₹ 10 lakhs on 10-11-2016 in the capital gain bond of National Highway Authority of India (NHAI).

He deposited another ₹ 5 lakhs on 10-07-2017 in the capital gain deposit scheme with SBI for construction of additional floor of house property.

Compute income under the head "Capital Gains" for A.Y.2017-18 as per Income-tax Act, 1961 and also income-tax payable on the assumption that he has no other income chargeable to tax.

Cost inflation index for Financial Year 2005-06: 497 and 2016-17: 1125.

Answer

Computation of income under the head "Capital Gains" of Mr. Martin for A.Y. 2017-18

Particulars	₹	₹
Long-term capital gain		
Full value of consideration	80,00,000	
[As per section 50C, in case the actual sale consideration (i.e., ₹ 70 lakhs, in this case) is less than the stamp duty value (i.e., ₹ 80 lakhs, in this case) assessed by the stamp valuation authority (Sub-registrar, in this case), the stamp		

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duty value shall be deemed as the full value of consideration]		
Less: Expenses in connection with transfer (brokerage paid for sale of property)	1,00,000	
	79,00 ,000	
Less: Indexed cost of acquisition [20,00,000 x 1125 / 497]	45,27,163	38,72,837
***Less*: Exemption under section 54:**		
- Purchase of new residential house property within two years from the date of sale of residential house	15,00,000	
- Deposit in Capital Gains Accounts Scheme on or before the due date of filing of return of income u/s 139(1) for construction of additional floor on such house property.	10,00,000	
	25,00,000	
Exemption under section 54EC:		
- Investment in capital gains bond of NHAI within 6 months from the date of transfer (i.e., before 8.12.2016)	5,00,000	30,00,000
Taxable Capital Gains/Total Income		**3,72,837**
Total Income (rounded off)		3,72,840

Computation of tax liability of Mr. Martin for A.Y. 2017-18

Particulars	₹
Tax on ₹ 1,22,840 @ 20% [i.e., long term capital gain less basic exemption limit (3,72,840–2,50,000)]	24,568
Less: Rebate under section 87A	5,000
	19,568
Add: Education cess@2% & SHEC@ 1%	587
Tax Payable	**20,155**
Tax Payable (rounded off)	20,160

Notes:

(1) Since Mr. Martin is a resident individual, the basic exemption limit of ₹ 2,50,000 has been adjusted against long term capital gains and the balance long-term capital gains is chargeable to tax @ 20% under section 112. Further, since his total income is less than ₹ 5 lakh, he is eligible for rebate under section 87A.

(2) Exemption under section 54 is available in respect of reinvestment of capital gains on sale of residential house in one residential house in India. In this case, exemption would be available for amount invested in purchase of new residential

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house and amount deposited for construction of additional floor in the same house, since they together constitute one residential house.

Exercise

1. *Distribution of assets at the time of liquidation of a company -*
   - *(a) is not a transfer in the hands of the company or the shareholders*
   - *(b) is not a transfer in the hands of the company but capital gains is chargeable to tax on such distribution in the hands of the shareholders*
   - *(c) is not a transfer in the hands of the shareholders but capital gains is chargeable to tax on such distribution in the hands of the company.*
2. *For an assessee, who is a salaried employee who invests in shares, what is the benefit available in respect of securities transaction tax paid by him on sale of 100 listed shares of X Ltd. which has been held by him for 14 months before sale?*
   - *(a) Rebate under section 88E is allowable in respect of securities transaction tax paid*
   - *(b) Securities transaction tax paid is treated as expenses of transfer and deducted from sale consideration.*
   - *(c) Long term capital gains is completely exempt under section 10(38)*
3. *Under section 50C, the guideline value for stamp duty is taken as the full value of consideration only if -*
   - *(a) the asset transferred is building and the actual consideration is less than the guideline value*
   - *(b) the asset transferred is either land or building or both and the actual consideration is less than the guideline value*
   - *(c) the asset transferred is building, irrespective of the actual consideration.*
4. *When there is a reduction of capital by a company and amounts are distributed to shareholders,*
   - *(a) the entire distribution is subject to capital gains tax.*
   - *(b) the entire distribution is subject to tax under the head "Income from other sources".*
   - *(c) The distribution attributable to accumulated profits is chargeable as deemed dividend and distribution attributable to capital is subject to capital gains tax.*
5. *Where there is a transfer of a capital asset by a partner to the firm by way of capital contribution or otherwise, the consideration would be taken as -*
   - *(a) The market value of the capital asset on the date of transfer*
   - *(b) The cost less notional depreciation of the capital asset*
   - *(c) The value of the asset recorded in the books of the firm.*

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6. *Under section 54EC, capital gains are exempted if invested in the bonds issued by NHAI & RECL-*

    (a) *within a period of 6 months from the date of transfer of the asset*

    (b) *within a period of 6 months from the end of the previous year*

    (c) *within a period of 6 months from the end of the previous year or the due date for filing the return of income under section 139(1), whichever is earlier*

7. *Any payment made by a company on purchase of its own listed shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956-*

    (a) *shall be regarded as dividend*

    (b) *shall not be regarded as dividend but capital gains tax liability is attracted in the hands of the shareholder*

    (c) *shall neither be regarded as dividend nor will it attract capital gains tax in the hands of the shareholder.*

8. *Discuss the conditions to be satisfied for claiming exemption of tax in respect of -*

    (a) *Capital gains on compulsory acquisition of agricultural land situated within specified urban limits*

    (b) *Capital gains on sale of listed equity shares/units of an equity oriented fund.*

9. *Write short notes on -*

    (i) *Capital gains in the case of slump sale under section 50B*

    (ii) *Reference to Valuation Officer under section 55A*

10. *What is the tax treatment, under the Income-tax Act, 1961, of capital gains arising on transfer of assets in case of shifting of industrial undertaking from an urban area to any special economic zone? Discuss.*

11. *List ten transactions which are not regarded as transfer for the purpose of capital gains. Discuss the provisions relating to the same.*

12. *Explain the computation of capital gain in case of depreciable asset under section 50.*

13. *What are the transactions not regarded as transfer as per section 47 of the Income-tax Act, 1961?*

Answers

1. b; **2.** c; **3.** b; **4.** c; **5**. c; **6.** a; **7.** b

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4 Unit 5 : Income From Other Sources

Key Points
Where any income, profits or gains includible in the total income of an assessee, cannot be included under any of the other heads, it would be chargeable under the head 'Income from other sources'. Hence, this head is the residuary head of income [Section 56(1)]

Specific Incomes Chargeable under this head [Section 56(2)]

(1) Dividend Income

(2) Casual income (winnings from lotteries, cross word puzzles, races including horse races, card games and other games, gambling, betting etc.). Such winnings are chargeable to tax at a flat rate of 30% under section 115BB and no expenditure or deduction under Chapter VIA can be allowed from such income. No loss can be set-off against such income and even the unexhausted basic exemption limit cannot be exhausted against such income.

(3) **Sum of money or property received by an Individual or a Hindu undivided family [Section 56(2)(vii)]**

	Nature of asset	Particulars	Taxable value
1	Money	Without consideration	The whole amount, if the same exceeds ₹ 50,000.
2	Movable property	Without consideration	The aggregate fair market value of the property, if it exceeds ₹ 50,000.
3	Movable property	Inadequate consideration	The difference between the aggregate fair market value and the consideration, if such difference exceeds ₹ 50,000.
4	Immovable property	Without consideration	The stamp value of the property, if it exceeds ₹ 50,000.
5	Immovable property	Inadequate consideration	The difference between the stamp duty value and the consideration, if such difference exceeds ₹ 50,000.

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Receipts exempted from the applicability of section 56(2)(vii)

Any sum of money or value of property received -

(a) from any relative; or

(b) on the occasion of the marriage of the individual; or

(c) under a will or by way of inheritance; or

(d) in contemplation of death of the payer or donor, as the case may be; or

(e) from any local authority as defined in the *Explanation* to section 10(20); or

(f) from any fund or university or other educational institution or hospital or other medical institution or any trust or institution referred to in section 10(23C); or

(g) from any trust or institution registered under section 12AA

Also, any shares received by an individual or HUF as a consequence of demerger or amalgamation of a company or a business re-organisation of a co-operative bank shall not be subject to tax by virtue of the provisions of section 56(2)(vii).

Meaning of "relative" for the purpose of section 56(2)(vii)

(a) in case of an individual –

(i) spouse of the individual;

(ii) brother or sister of the individual;

(iii) brother or sister of the spouse of the individual;

(iv) brother or sister of either of the parents of the individual;

(v) any lineal ascendant or descendant of the individual;

(vi) any lineal ascendant or descendant of the spouse of the individual;

(vii) spouse of any of the persons referred to above.

(b) In case of Hindu Undivided Family, any member thereof.

(4) **Other receipts chargeable under this head**

Section	Provision
56(2)(viia)	(i) Transfer of shares of a company without consideration or for inadequate consideration would attract the provisions of section 56(2), if the recipient is a firm or a company. (ii) If such shares are received without consideration, the aggregate FMV on the date of transfer would be taxed as the income of the recipient firm or company, if it exceeds ₹ 50,000. (iii) If such shares are received for inadequate consideration, the difference between the aggregate FMV and the consideration would be taxed as the income of the recipient firm or company, if such difference exceeds ₹ 50,000.

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	(iv) However, the provisions of section 56(2)(viia) would not apply in the case of transfer of shares - (1) of a company in which the public are substantially interested; or (2) to a company in which the public are substantially interested.
56(2)(viib)	Consideration received in excess of FMV of shares issued by a closely held company to any person, being a resident, to be treated as income of such company, where shares are issued at a premium
56(2)(viii)	Interest received on compensation/enhanced compensation deemed to be income in the year of receipt and taxable under the head "Income from Other Sources".
56(2)(ix)	Any sum of money received as an advance or otherwise in the course of negotiations for transfer of a capital asset, if such sum is forfeited and the negotiations do not result in transfer of such asset.

Deductions allowable [Section 57]

S.No.	Particulars	Deduction
1.	In case of dividends (other than dividends u/s 115-O) or interest on securities	Any reasonable sum paid by way of commission or remuneration to a banker or any other person.
2.	Family Pension	Sum equal to - 33 1/3% of such income or - ₹ 15,000, whichever is less
3.	Interest on compensation/enhanced compensation received	50% of such interest income

Deductions not allowable [Section 58]

S. No.	Deductions not allowable
1.	Any personal expense of the assessee
2.	Any interest chargeable to tax under the Act which is payable outside India on which tax has not been paid or deducted at source.
3.	Any payment taxable in India as salaries, if it is payable outside India unless tax has been paid thereon or deducted at source.
4.	Any payment to a relative or associate concern otherwise than by account payee cheque or draft, if the aggregate of such payments exceed ₹ 20,000 during a day
5.	Income-tax and wealth-tax paid.
6.	Any expenditure or allowance in connection with income by way of earnings from lotteries, cross word puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature

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Question 1

State whether the following are chargeable to tax and the amount liable to tax :

(i) A sum of ₹ 1,20,000 was received as gift from non-relatives by Raj on the occasion of the marriage of his son Pravin.

(ii) Interest on enhanced compensation of ₹ 50,000 was received as per court decree in December 2016 by Mr. Yogesh. Out of the said amount, a sum of ₹ 35,000, relates to preceding financial years.

(iii) Interest on enhanced compensation of ₹ 96,000 received on 12-3-2017 for acquisition of urban land, of which 40% relates to the earlier year.

Answer

S.No.	Taxable/Not Taxable	Amount liable to tax (₹)	Reason
(i)	Taxable	1,20,000	The exemption from applicability of section 56(2)(vii) would be available if, *inter alia,* gift is received from a relative or gift is received on the occasion of marriage of the individual himself. In this case, since gift is received by Mr. Raj from a non-relative on the occasion of marriage of his son, it would be taxable in his hands under section 56(2)(vii).
(ii)	Taxable	25,000	As per section 56(2)(viii), interest on enhanced compensation is taxable in the year in which it is received. Deduction of 50% in respect of the said income is allowed under section 57(iv). Therefore, ₹ 25,000 (i.e., ₹ 50,000 – ₹ 25,000) is taxable in the hands of Mr. Yogesh in the F.Y.2016-17.
(iii)	Taxable	48,000	As per section 145A, interest received by the assessee on enhanced compensation shall be deemed to be the income of the year in which it is received, irrespective of the method of accounting followed by the assessee. Interest of ₹ 96,000 on enhanced compensation is chargeable to tax in the year of receipt i.e. P.Y. 2016-17 under section 56(2)(viii) after providing deduction of 50% under section 57(iv). Therefore, ₹ 48,000 is chargeable to tax under the head “Income from other sources”.

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Question 2

On 10.10.2016, Mr. Govind (a bank employee) received ₹ 5,00,000 towards interest on enhanced compensation from State Government in respect of compulsory acquisition of his land effected during the financial year 2011-12.

Out of this interest, ₹ 1,50,000 relates to the financial year 2013-14; ₹ 1,65,000 to the financial year 2014-15; and ₹ 1,85,000 to the financial year 2015-16. He incurred ₹ 50,000 by way of legal expenses to receive the interest on such enhanced compensation.

How much of interest on enhanced compensation would be chargeable to tax for the assessment year 2017-18?

Answer

Section 145A provides that interest received by the assessee on enhanced compensation shall be deemed to be the income of the assessee of the year in which it is received, irrespective of the method of accounting followed by the assessee and irrespective of the financial year to which it relates.

Section 56(2)(viii) states that such income shall be taxable as 'Income from other sources'.

50% of such income shall be allowed as deduction by virtue of section 57(iv) and no other deduction shall be permissible from such Income.

Therefore, legal expenses incurred to receive the interest on enhanced compensation would not be allowed as deduction from such income.

Computation of interest on enhanced compensation taxable as "Income from other sources" for the A.Y 2017-18:

Particulars	₹
Interest on enhanced compensation taxable under section 56(2)(viii)	5,00,000
Less: Deduction under section 57(iv) (50% x ₹ 5,00,000)	2,50,000
Taxable interest on enhanced compensation	2,50,000

Question 3

The following details have been furnished by Mrs. Hemali pertaining to the year ended 31.3.2017 :

(i) Cash gift of ₹ 51,000 received from her friend on the occasion of her "Shastiaptha Poorthi", a wedding function celebrated on her husband completing 60 years of age. This was also her 25th wedding anniversary.

(ii) On the above occasion, a diamond necklace worth ₹ 2 lacs was presented by her sister living in Dubai.

(iii) When she celebrated her daughter's wedding on 21.2.2017, her friend assigned in Mrs. Hemali's favour, a fixed deposit held by the said friend in a scheduled bank; the value of

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the fixed deposit and the accrued interest on the said date was ₹ 51,000.

Compute the income, if any, assessable as income from other sources.

Answer

(i) Any sum of money received by an individual on the occasion of the marriage of the individual is exempt. This provision is, however, not applicable to a cash gift received during a wedding function celebrated on completion of 60 years of age.

The gift of ₹ 51,000 received from a non-relative is, therefore, chargeable to tax under section 56(2)(vii) in the hands of Mrs. Hemali.

(ii) The provisions of section 56(2)(vii) are not attracted in respect of any sum of money or property received from a relative. Thus, the gift of diamond necklace received from her sister is not taxable under section 56(2)(vii), even though jewellery falls within the definition of "property".

(iii) To be exempt from applicability of section 56(2)(vii), the property should be received on the occasion of the marriage of the individual, not that of the individual's son or daughter. Therefore, this exemption provision is not attracted in this case.

Any sum of money received without consideration by an individual is chargeable to tax under section 56(2)(vii), if the aggregate value exceeds ₹ 50,000 in a year. "Sum of money" has, however, not been defined under section 56(2)(vii).

Therefore, there are two possible views in respect of the value of fixed deposit assigned in favour of Mrs. Hemali –

(1) The first view is that fixed deposit does not fall within the meaning of "sum of money" and therefore, the provisions of section 56(2)(vii) are not attracted. It may be noted that fixed deposit is also not included in the definition of "property".

(2) However, another possible view is that fixed deposit assigned in favour of Mrs. Hemali falls within the meaning of "sum of money" received.

Income assessable as "Income from other sources"

If the first view is taken, the total amount chargeable to tax as "Income from other sources" would be ₹ 51,000, being cash gift received from a friend on her Shastiaptha Poorthi.

As per the second view, the provisions of section 56(2)(vii) would also be attracted in respect of the fixed deposit assigned and the "Income from other sources" of Mrs. Hemali would be ₹ 1,02,000 (₹ 51,000 + ₹ 51,000).

Question 4

Decide the following transactions in the context of Income-tax Act, 1961:

(i) Mr. B transferred 500 shares of Reliance Industries Ltd. to M/s. B Co. (P) Ltd. on 10.10.2016 for ₹ 3,00,000 when the market price was ₹ 5,00,000. The indexed cost of acquisition of shares for Mr. B was computed at ₹ 4,45,000. The transfer was not

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subjected to securities transaction tax.

Determine the income chargeable to tax in the hands of Mr. B and M/s. B Co. (P) Ltd. because of the above said transaction.

(ii) *Mr. Chezian is employed in a company with taxable salary income of ₹ 5,00,000. He received a cash gift of ₹ 1,00,000 from Atma Charitable Trust (registered under section 12AA) in December 2016 for meeting his medical expenses.*

Is the cash gift so received from the trust chargeable to tax in the hands of Mr. Chezian?

Answer

(i) Transfer of shares without consideration or for inadequate consideration would attract the provisions of section 56(2)(viia), if the recipient is a firm or a company. The purpose of this provision is to prevent the practice of transferring unlisted shares at prices much below the fair market value.

The provisions of section 56(2)(viia) would, however, not be attracted in the case of, *inter alia*, transfer of shares of a company in which public are substantially interested. In this case, the shares of Reliance Industries Ltd. are transferred. Since Reliance Industries Ltd. is a company in which public are substantially interested, the provisions of section 56(2)(viia) would not be attracted in the hands of M/s. B Co. (P) Ltd.

The indexed cost of acquisition (₹ 4,45,000) less the actual sale consideration (₹ 3,00,000) would result in a long term capital loss of ₹ 1,45,000 in the hands of Mr. B, which is eligible for set off against any other long term capital gain.

(ii) The provisions of section 56(2)(vii) would not apply to any sum of money or any property received from any trust or institution registered under section 12AA. Therefore, the cash gift of ₹ 1 lakh received from Atma Charitable Trust, being a trust registered under section 12AA, for meeting medical expenses would not be chargeable to tax under section 56(2)(vii) in the hands of Mr. Chezian.

Question 5

Check the taxability of the following gifts received by Mrs. Rashmi during the previous year 2016-17 and compute the taxable income from gifts for Assessment Year 2017-18:

(i) *On the occasion of her marriage on 14.8.2016, she has received ₹ 90,000 as gift out of which ₹ 70,000 are from relatives and balance from friends.*

(ii) *On 12.9.2016, she has received gift of ₹ 18,000 from cousin of her mother.*

(iii) *A cell phone worth ₹ 21,000 is gifted by her friend on 15.8.2016.*

(iv) *She gets a cash gift of ₹ 25,000 from the elder brother of her husband's grandfather on 25.10.2016.*

(v) *She has received a cash gift of ₹ 12,000 from her friend on 14.4.2016.*

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Answer

Computation of taxable income of Mrs. Rashmi from gifts for A.Y.2017-18

Sl. No.	Particulars	Taxable amount (₹)	Reason for taxability or otherwise of each gift
1.	Relatives and friends	Nil	Gifts received on the occasion of marriage are not taxable.
2.	Cousin of Mrs. Rashmi's mother	18,000	Cousin of Mrs. Rashmi's mother is not a relative. Hence, the cash gift is taxable.
3.	Friend	Nil	Cell phone is not included in the definition of property as per *Explanation* to section 56(2)(vii). Hence, it is not taxable.
4.	Elder brother of husband's grandfather	25,000	Brother of husband's grandfather is not a relative. Hence, the cash gift is taxable.
5.	Friend	12,000	Cash gift from friend is taxable.
Aggregate value of gifts		**55,000**	

Since the sum of money received by Mrs. Rashmi without consideration during the previous year 2016-17 exceeds ₹ 50,000, the whole of the amount is chargeable to tax under section 56(2)(vii) of the Income-tax Act, 1961.

Question 6

Smt. Laxmi reports the following transactions to you:

(i) Received cash gifts on the occasion of her marriage on 18-7-2016 of ₹ 1,20,000. It includes gift of ₹ 20,000 received from non-relatives.

(ii) On 1-8-2016, being her birthday, she received a gift by means of cheque from her mother's maternal uncle, the amount being ₹ 40,000.

(iii) On 1-12-2016 she acquired a vacant site from her friend for ₹ 1,05,000. The State stamp valuation authority fixed the value of site at ₹ 1,80,000 for stamp duty purpose.

(iv) She bought 100 equity shares of a listed company from another friend for ₹ 60,000. The value of share in the stock exchange on the date of purchase was ₹ 1,15,000.

Determine the amounts chargeable to tax in the hands of Smt. Laxmi for the A.Y. 2017-18.

Your answer should be supported by reasons.

Answer

Computation of amount chargeable to tax in hands of Smt. Laxmi for A.Y. 2017-18

	Particulars	₹
(i)	Cash gift of ₹ 1,20,000 received on the occasion of her marriage is not	Nil

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	taxable since gifts received by an individual on the occasion of marriage is excluded under section 56(2)(vii), even if the same are from non-relatives.	
(ii)	Even though mother's maternal uncle does not fall within the definition of "relative" under section 56(2)(vii), gift of ₹ 40,000 received from him by cheque is not chargeable to tax since the aggregate sum of money received by Smt. Laxmi without consideration from non-relatives(other than on the occasion of marriage) during the previous year 2016-17 does not exceed ₹ 50,000.	Nil
(iii)	Purchase of land for inadequate consideration on 1.12.2016 would attract the provisions of section 56(2)(vii). Where any immovable property is received for a consideration which is less than the stamp duty value of the property by an amount exceeding ₹ 50,000, the difference between the stamp duty value and consideration is chargeable to tax in the hands of Individual. Therefore, in the given case ₹ 75,000 is taxable in the hands of Smt. Laxmi.	75,000
(iv)	Since shares are included in the definition of "property" and difference between the purchase value and fair market value of shares is ₹ 55,000 (₹ 1,15,000 - ₹ 60,000) i.e. it exceeds ₹ 50,000, the difference would be taxable under section 56(2)(vii).	55,000
Amount chargeable to tax		**1,30,000**

Question 7

Discuss the taxability or otherwise in the hands of the recipients, as per the provisions of the Income-tax Act, 1961:

(i) ABC Private Limited, a closely held company, issued 10,000 shares at ₹ 130 per share. (The face value of the share is ₹ 100 per share and the fair market value of the share is ₹ 120 per share).

(ii) Mr. A received an advance of ₹ 50,000 on 1-09-2016 against the sale of his house. However, due to non-payment of instalment in time, the contract has cancelled and the amount of ₹ 50,000 was forfeited.

(iii) Mr. N, a member of his father's HUF, transferred a house property to the HUF without consideration. The value of the house is ₹ 10 lacs as per the Registrar of stamp duty.

(iv) Mr. Kumar gifted a car to his sister's son (Sunil) for achieving good marks in CA Final exam. The fair market value of the car is ₹ 5,00,000.

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Answer

S. No.	Taxable/Not Taxable	Reason
(i)	Taxable	Since ABC Private Limited, a closely held company, issued 10,000 shares at a premium (i.e., issue price exceeds the face value of shares), the excess of the issue price of the shares over the fair market value would be taxable under section 56(2)(viib) in its hands under the head "Income from other sources". Therefore, ₹ 1,00,000 [10,000 × ₹ 10 (₹ 130 – ₹ 120)] shall be taxable as income in the hands of ABC Private Limited under the head "Income from other sources".
(ii)	Taxable	Any sum of money received as an advance or otherwise in the course of negotiations for transfer of a capital asset would be chargeable to tax under the head "Income from other sources", if such amount is forfeited and the negotiations do not result in transfer of such capital asset [Section 56(2)(ix)]. Therefore, the amount of ₹ 50,000 received as advance would be chargeable to tax in the hands of Mr. A under the head "Income from other sources", since it is forfeited on account of cancellation of contract for transfer of house, being a capital asset, due to non-payment of installment in time.
(iii)	Not Taxable	As per section 56(2)(vii), immovable property received without consideration by a HUF from its relative is not taxable. In the present case, since Mr. N is a member of his father's HUF, he is a relative of the HUF. Hence, ₹ 10 lakhs, being the stamp duty value of house property received by HUF, without consideration, would not be chargeable to tax in the hands of the HUF.[1]
(iv)	Not Taxable	Car is not included in the definition of "property", for the purpose of taxability under section 56(2)(vii), in the hands of the recipient under the head "Income from other sources". Further, the same has been received by Sunil from his mother's brother, who falls within the definition of "relative". Hence, ₹ 5,00,000, being the fair market value of car received without consideration from a relative is not taxable in the hands of Sunil, even though its value exceeds ₹ 50,000.

[1] However, income from such asset would be included in the hands of Mr. N under section 64(2)

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Question 8

State with proper reasons whether the following statements are True/False with regard to provisions of Income-tax Act, 1961:

(i) "A" receives ₹ 2 lakh from his friends on the occasion of his marriage on 22.04.2016 and ₹ 1 lakh from the brother of his father-in-law on 31.12.2016. A's income includible under "other sources" for the previous year 2016-17 would be ₹ 3 lakh.

(ii) Dividend received (on which no Dividend Distribution Tax has been paid) by a dealer in shares or one engaged in buying/selling of shares, is chargeable under the head "Income from other sources".

Answer

(i) False : As per section 56(2)(vii), where any sum of money is received without consideration by an individual or a Hindu undivided family from any person or persons and the aggregate value of all such sums received during the previous year exceeds ₹ 50,000, the whole of the aggregate value of such sum shall be included in the total income of such individual or Hindu Undivided Family under the head "Income from other sources".

However, in order to avoid hardship in genuine cases, certain sums of money received have been exempted, which includes, *inter-alia,* any sum received on the occasion of the marriage of the individual and any sum received from any relative. As such, ₹ 2 lakh received from friends on the occasion of marriage is exempt.

However, brother of father-in-law is not included in the definition of relative. Hence, ₹ 1 lakh is taxable under the head "Income from other sources".

The statement that ₹ 3 lakh is includible in A's income is, therefore, false.

(ii) True: By virtue of section 56(2)(i), dividend received [other than dividend in respect of which dividend distribution tax is paid by the company and hence, is exempt in the hands of recipients u/s 10(34)] is always taxable under the head "Income from other sources". Even if such dividend is received by a dealer in shares or one engaged in buying/selling of shares, the same would be taxable under the head "Income from other sources".

Note*: In this content, it may be noted that section 115BBA brings to tax any income by way of aggregate dividend in excess of Rs. 10 lakhs in the hands of an individual, HUF or a firm, resident in India @ 10%.*

Question 9

From the following particulars of Pankaj for the previous year ended 31st March, 2017, compute the income chargeable under the head "Income from other sources":

Sl. No.	*Particulars*	*₹*
(i)	*Directors fee from a company*	*10,000*

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(ii)	*Interest on bank deposits*	*3,000*
(iii)	*Income from undisclosed source*	*12,000*
(iv)	*Winnings from lotteries (Net)*	*35,000*
(v)	*Royalty on a book written by him*	*9,000*
(vi)	*Lectures in seminars*	*5,000*
(vii)	*Interest on loan given to a relative*	*7,000*
(viii)	*Interest on debentures of a company (listed in a recognised stock exchange) net of taxes*	*3,600*
(ix)	*Interest on Post Office Savings Bank Account*	*500*
(x)	*Interest on Government Securities*	*2,200*
(xi)	*Interest on Monthly Income Scheme of Post Office*	*33,000*

He paid ₹ 1,000 for typing the manuscript of book written by him.

Answer

Computation of income of Pankaj chargeable under the head "Income from other sources" for the A.Y. 2017-18

	Particulars	₹	₹
1.	Directors' fees		10,000
2.	Interest on bank deposit		3,000
3.	Income from undisclosed source (taxable @ 30% u/s 115BBE)		12,000
4.	Royalty on books written **(See Note below)**	9,000	
	Less: expenses	1,000	8,000
5.	Lectures in seminars		5,000
6.	Interest on loan given to a relative		7,000
7.	Interest on listed debentures		
	Net Received	3,600	
	Add: T.D.S. @ 10%		
	$\frac{3600 \times 10}{100 - 10}$	400	4,000
8.	Interest on Post Office Savings Bank [exempt under section 10(15)]		-
9.	Interest on Government securities		2,200
10.	Interest on Post Office Monthly Income Scheme		33,000
11.	Winnings from lotteries (taxable @ 30% u/s 115BB)		

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Net	35,000	
Add: T.D.S. @ 30% $\left(\frac{35,000 \times 30}{100-30}\right)$	15,000	50,000
Income from Other Sources		**1,34,200**

Note : *Royalty income would be chargeable to tax under the head "Income from Other Sources", only if it is not chargeable to tax under the head "Profits and gains of business or profession". This problem has been solved assuming that the same is not taxable under the head "Profits and gains of business or profession" and hence, is chargeable to tax under the head "Income from other sources".*

Question 10

Rahul holding 28% of equity shares in a company, took a loan of ₹ 5,00,000 from the same company. On the date of granting the loan, the company had accumulated profit of ₹ 4,00,000. The company is engaged in some manufacturing activity.

(i) Is the amount of loan taxable as deemed dividend in the hands of Rahul, if the company is a company in which the public are substantially interested?

(ii) What would be your answer, if the lending company is a private limited company (i.e. a company in which the public are not substantially interested)?

Answer

Any payment by a company, other than a company in which the public are substantially interested, of any sum by way of advance or loan to an equity shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting power, is deemed as dividend under section 2(22)(e), to the extent the company possesses accumulated profits.

(i) The provisions of section 2(22)(e), however, will not apply where the loan is given by a company in which public are substantially interested. In such a case, the loan would not be taxable as deemed dividend in the hands of Rahul.

(ii) However, if the loan is taken from a private company (i.e. a company in which the public are not substantially interested), which is a manufacturing company and not a company where lending of money is a substantial part of the business of the company, then, the provisions of section 2(22)(e) would be attracted, since Rahul holds more than 10% of the equity shares in the company.

The amount chargeable as deemed dividend cannot, however, exceed the accumulated profits held by the company on the date of giving the loan. Therefore, the amount taxable as deemed dividend in the hands of Rahul would be limited to the accumulated profit i.e., ₹ 4,00,000 and not the amount of loan which is ₹ 5,00,000.

Question 11

When would the dividend income be taxed in the hands of a shareholder?

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Answer

The provisions relating to the year of taxability of dividend are contained in section 8 of the Income-tax Act, 1961.

(a) Any dividend declared by a company or distributed or paid by it within the meaning of section 2(22) shall be deemed to be the income of the previous year in which it is so declared, distributed or paid, as the case may be.

(b) Any interim dividend shall be deemed to be the income of the previous year in which the amount of such dividend is unconditionally made available by the company to the member who is entitled to it.

Students may note that any dividend which is liable for dividend distribution tax covered by section 115-O (being a dividend declared by a domestic company) is exempt under section 10(34) and hence would not be chargeable to tax. However, dividend referred to in Section 2(22)(e) is not subject to dividend distribution tax in the hands of the domestic company under section 115-O, but would be chargeable to tax in the hands of the shareholder.

Question 12

How is "dividend stripping" enforced by section 94(7) of the Income-tax Act, 1961?

Answer

According to section 94(7),where :

(a) any person buys or acquires any securities or units within a period of three months prior to the record date ; and

(b) such person sells or transfers such securities within a period of three months after such record date or transfers such units within a period of nine months after such record date ; and

(c) the dividend or income on such securities or units received or receivable by such person is exempt from tax,

then, the loss, if any, arising to him on account of such purchase and sale of securities or units, to the extent such loss does not exceed the amount of dividend or income received or receivable on such securities or units, has to be ignored for the purposes of computing his income chargeable to tax.

Exercise

1. *Income from letting of machinery, plant and furniture is -*

   (a). always chargeable to tax under the head "Profits and gains of business and profession"

   (b). always chargeable to tax under the head "Income from other sources"

   (c). chargeable under the head "Income from other sources" only if not chargeable under the head "Profits and gains of business and profession".

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2. *In respect of winnings from lottery, crossword puzzle or race including horse race or card game etc.*

   (a). no deduction under Chapter VI-A is allowed and basic exemption limit cannot be exhausted.

   (b). no deduction under Chapter VI-A but unexhausted basic exemption can be exhausted.

   (c). Both deduction under Chapter VI-A and basic exemption are allowed.

3. *The deduction allowable in respect of family pension taxable under "Income from other sources" is*

   (a). 33-1/3% of the pension

   (b). 30% of the pension or ₹ 15,000, whichever is less

   (c). 33-1/3% of the pension or ₹ 15,000, whichever is less

4. *Deemed dividend under section 2(22)(e) is chargeable to tax -*

   (a). On the basis of method of accounting regularly employed by the assessee

   (b). On the basis of mercantile system of accounting only

   (c) On payment basis as prescribed under section 8 of the Income-tax Act, 1961.

5. *Ganesh received ₹ 60,000 from his friend on the occasion of his birthday.*

   (a) The entire amount of ₹ 60,000 is taxable.

   (b) ₹ 25,000 is taxable.

   (c) The entire amount is exempt.

6. *Write short notes on -*

   (a) Bond washing transactions

   (b) Dividend stripping

7. *State the incomes which are chargeable only under the head "Income from other sources".*

8. *Which are incomes chargeable under the head "Income from other sources" only if they are not chargeable under the head "Profits and gains of business or profession"?*

9. *What are the deductions allowable from the following income -*

   (a) Dividend

   (b) Income from letting on hire machinery, plant or furniture.

10. *What are the inadmissible deductions while computing income under the head "Income from other sources".*

11. *Karan's bank account shows the following deposits during the financial year 2016-17. Compute his total income for the A.Y. 2017-18, assuming that his income from house property (computed) is ₹ 62,000.*

    (i) Gift from his sister in Amsterdam ₹ 2,30,000

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(ii) Gift from his friend on his birthday ₹ 10,000

(iii) Dividend from shares of various Indian companies ₹ 12,600

(iv) Gift from his mother's friend on his engagement ₹ 25,000

(v) Gift from his fianceé ₹ 75,000

(vi) Interest on bank deposits (Fixed Deposit) ₹ 25,000

12. *What are the deductions allowable under section 57 of the Income-tax Act, 1961 in respect of "Income from other sources"?*

Answers

1. c; **2.** a; **3.** c; **4.** c; **5.** a; **11.** ₹ 1,97,000

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5 Income of Other Persons Included in Assessee's Total Income

Key Points		
Section	**Income to be clubbed**	**Provision**
60	Income transferred without transfer of asset	When a person transfers the income accruing to an asset without the transfer of the asset itself, such income is to be included in the total income of the transferor, whether the transfer is revocable or irrevocable.
61	Income arising from revocable transfer of assets	Such income is to be included in the hands of the transferor. A transfer is deemed to be revocable if it – (i) contains any provision for re-transfer of the whole or any part of the income or assets to the transferor; or (ii) gives right to re-assume power over the whole or any part of the income or the asset.
64(1)(ii)	Income arising to spouse by way of remuneration from a concern in which the individual has substantial interest	Such income arising to spouse is to be included in the total income of the individual. However, if remuneration received is attributable to the application of technical or professional knowledge and experience of spouse, then, such income is not to be clubbed.
64(1)(iv)	Income arising to spouse from assets transferred without adequate consideration	Income arising from an asset (other than house property) transferred otherwise than for adequate consideration or in connection with an agreement to live apart, from one spouse to another shall be included in the total income of the transferor.

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		However, this provision will not apply in the case of transfer of house property, since the transferor-spouse would be the deemed owner as per section 27.
64(1)(vi)	Income arising to son's wife from an asset transferred without adequate consideration	Income arising from an asset transferred otherwise than for adequate consideration, by an individual to his or her son's wife shall be included in the total income of the transferor.
64(1)(vii)/ 64(1)(viii)	Income arising from transfer of assets for the benefit of spouse or son's wife	All income arising to any person or association of persons from assets transferred without adequate consideration is includible in the income of the transferor, to the extent such income is used by the transferee for the immediate or deferred benefit of the transferor's spouse or son's wife.
64(1A)	Income of minor child	All income arising or accruing to a minor child (including a minor married daughter) shall be included in the total income of his or her parent. The income of the minor child shall be included with the income of that parent, whose total income, before including minor's income, is higher. The parent, in whose total income, the income of the minor child or children are included, shall be entitled to exemption of such income subject to a maximum of ₹ 1,500 per child. The following income of a minor child shall, however, not be clubbed in the hands of his or her parent - (a) Income from manual work done by him or activity involving application of minor's skill, talent or specialized knowledge and experience; and (b) Income of a minor child suffering from any disability specified in section 80U.
Note: *As per Explanation 2 to section 64 'income' includes 'loss'. Therefore, clubbing provisions would be attracted in all the above cases, even if there is a loss and not income.*		

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Question 1

Mr. Sharma has four children consisting 2 daughters and 2 sons. The annual income of 2 daughters were ₹ 9,000 and ₹ 4,500 and of sons were ₹ 6,200 and ₹ 4,300, respectively. The daughter who has income of ₹ 4,500 was suffering from a disability specified under section 80U.

Compute the amount of income earned by minor children to be clubbed in hands of Mr. Sharma.

Answer

As per section 64(1A), in computing the total income of an individual, all such income accruing or arising to a minor child shall be included. However, income of a minor child suffering from disability specified under section 80U would not be included in the income of the parent but would be taxable in the hands of the minor child. Therefore, in this case, the income of daughter suffering from disability specified under section 80U should not be clubbed with the income of Mr. Sharma.

Under section 10(32), income of each minor child includible in the hands of the parent under section 64(1A) would be exempt to the extent of the actual income or ₹ 1,500, whichever is lower. The remaining income would be included in the hands of the parent.

Computation of income earned by minor children to be clubbed with the income of Mr. Sharma:

	Particulars	₹
(i)	Income of one daughter	9,000
	Less: Income exempt under section 10(32)	1,500
	Total (A)	7,500
(ii)	Income of two sons (₹ 6,200 + ₹ 4,300)	10,500
	Less: Income exempt under section 10(32) (₹ 1,500 + ₹ 1,500)	3,000
	Total (B)	7,500
	Total Income to be clubbed as per section 64(1A) (A+B)	**15,000**

Note: It has been assumed that:

(1) All the four children are minor children;

(2) The income does not accrue or arise to the minor children on account of any manual work done by them or activity involving application of their skill, talent or specialized knowledge and experience;

(3) The income of Mr. Sharma, before including the minor children's income, is greater than the income of Mrs. Sharma, due to which the income of the minor children would be included in his hands; and

(4) This is the first year in which clubbing provisions are attracted.

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Question 2

During the previous year 2016-17, the following transactions occurred in respect of Mr. A.

(a) Mr. A had a fixed deposit of ₹ 5,00,000 in Bank of India. He instructed the bank to credit the interest on the deposit @ 9% from 1-4-2016 to 31-3-2017 to the savings bank account of Mr. B, son of his brother, to help him in his education.

(b) Mr. A holds 75% share in a partnership firm. Mrs. A received a commission of ₹ 25,000 from the firm for promoting the sales of the firm. Mrs. A possesses no technical or professional qualification.

(c) Mr. A gifted a flat to Mrs. A on April 1, 2016. During the previous year 2016-17, Mrs. A's "Income from house property" (computed) was ₹ 52,000.

(d) Mr. A gifted ₹ 2,00,000 to his minor son who invested the same in a business and he derived income of ₹ 20,000 from the investment.

(e) Mr. A's minor son derived an income of ₹ 20,000 through a business activity involving application of his skill and talent.

During the year, Mr. A got a monthly pension of ₹ 10,000. He had no other income. Mrs. A received salary of ₹ 20,000 per month from a part time job.

Discuss the tax implications of each transaction and compute the total income of Mr. A, Mrs. A and their minor child.

Answer

Computation of total income of Mr. A, Mrs. A and their minor son for the A.Y. 2017-18

Particulars	Mr. A (₹)		Mrs. A (₹)	Minor Son (₹)
Salary income (of Mrs. A)		-	2,40,000	-
Pension income (of Mr. A) (₹ 10,000×12)		1,20,000		
Income from House Property ***[See Note (3) below)***		52,000	-	-
Income from other sources				
Interest on Mr. A's fixed deposit with Bank of India (₹ 5,00,000×9%) ***[See Note (1) below]***	45,000		-	-
Commission received by Mrs. A from a partnership firm, in which Mr. A has substantial interest ***[See Note (2) below]***	25,000	70,000	-	-
Income before including income of minor son under section 64(1A)		**2,42,000**	**2,40,000**	**-**
Income of the minor son from the investment made in the business out of the amount		18,500	-	-

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gifted by Mr. A ***[See Note (4) below]***				
Income of the minor son through a business activity involving application of his skill and talent ***[See Note (5) below]***		-	-	20,000
Total Income		**2,60,500**	**2,40,000**	**20,000**

Notes:

(1) As per section 60, in case there is a transfer of income without transfer of asset from which such income is derived, such income shall be treated as income of the transferor. Therefore, the fixed deposit interest of ₹ 45,000 transferred by Mr. A to Mr. B shall be included in the total income of Mr. A.

(2) As per section 64(1)(ii), in case the spouse of the individual receives any amount by way of income from any concern in which the individual has substantial interest (i.e. holding shares carrying at least 20% voting power or entitled to at least 20% of the profits of the concern), then, such income shall be included in the total income of the individual. The only exception is in a case where the spouse possesses any technical or professional qualifications and the income earned is solely attributable to the application of her technical or professional knowledge and experience, in which case, the clubbing provisions would not apply.

In this case, the commission income of ₹ 25,000 received by Mrs. A from the partnership firm has to be included in the total income of Mr. A, as Mrs. A does not possess any technical or professional qualification for earning such commission and Mr. A has substantial interest in the partnership firm as he holds 75% share in the firm.

(3) According to section 27(i), an individual who transfers any house property to his or her spouse otherwise than for adequate consideration or in connection with an agreement to live apart, shall be deemed to be the owner of the house property so transferred. Hence, Mr. A shall be deemed to be the owner of the flat gifted to Mrs. A and hence, the income arising from the same shall be computed in the hands of Mr. A.

Note: *The provisions of section 56(2)(vii) would not be attracted in the hands of Mrs. A, since she has received immovable property without consideration from a relative i.e., her husband.*

(4) As per section 64(1A), the income of the minor child is to be included in the total income of the parent whose total income (excluding the income of minor child to be so clubbed) is greater. Further, as per section 10(32), income of a minor child which is includible in the income of the parent shall be exempt to the extent of ₹ 1,500 per child.

Therefore, the income of ₹ 20,000 received by minor son from the investment made out of the sum gifted by Mr. A shall, after providing for exemption of ₹ 1,500 under section 10(32), be included in the income of Mr. A, since Mr. A's income of ₹ 2,42,000 (before including the income of the minor child) is greater than Mrs. A's income of ₹ 2,40,000. Therefore, ₹ 18,500 (i.e., ₹ 20,000 – ₹ 1,500) shall be included in Mr. A's income. It is assumed that this is the first year in which clubbing provisions are attracted.

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Note *– The provisions of section 56(2)(vii) would not be attracted in the hands of the minor son, since he has received a sum of money exceeding ₹ 50,000 without consideration from a relative i.e., his father.*

(5) In case the income earned by the minor child is on account of any activity involving application of any skill or talent, then, such income of the minor child shall not be included in the income of the parent, but shall be taxable in the hands of the minor child.

Therefore, the income of ₹ 20,000 derived by Mr. A's minor son through a business activity involving application of his skill and talent shall not be clubbed in the hands of the parent. Such income shall be taxable in the hands of the minor son.

Question 3

Mr. Vaibhav started a proprietary business on 01.04.2015 with a capital of ₹ 5,00,000. He incurred a loss of ₹ 2,00,000 during the year 2015-16. To overcome the financial position, his wife Mrs. Vaishaly, a software Engineer, gave a gift of ₹ 5,00,000 on 01.04.2016, which was immediately invested in the business by Mr. Vaibhav. He earned a profit of ₹ 4,00,000 during the year 2016-17. Compute the amount to be clubbed in the hands of Mrs. Vaishaly for the Assessment Year 2017-18. If Mrs. Vaishaly gave the said amount as loan, what would be the amount to be clubbed?

Answer

Section 64(1)(iv) of the Income-tax Act, 1961 provides for the clubbing of income in the hands of the individual, if the income earned is from the assets (other than house property) transferred directly or indirectly to the spouse of the individual, otherwise than for adequate consideration or in connection with an agreement to live apart.

In this case, Mr. Vaibhav received a gift of ₹ 5,00,000 on 1.4.2016 from his wife Mrs. Vaishaly, which he invested in his business immediately. The income to be clubbed in the hands of Mrs. Vaishaly for the A.Y. 2017-18 is computed as under:

Particulars	Mr. Vaibhav's capital contribution (₹)	Capital contribution out of gift from Mrs. Vaishaly (₹)	Total (₹)
Capital as on 1.4.2016	3,00,000 (5,00,000 – 2,00,000)	5,00,000	8,00,000
Profit for P.Y.2016-17 to be apportioned on the basis of capital employed on the first day of the previous year i.e. as on 1.4.2016 (3:5)	1,50,000 $\left(4,00,000 \times \frac{3}{8}\right)$	2,50,000 $\left(4,00,000 \times \frac{5}{8}\right)$	4,00,000

Therefore, the income to be clubbed in the hands of Mrs. Vaishaly for the A.Y.2017-18 is ₹ 2,50,000.

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In case Mrs. Vaishaly gave the said amount of ₹ 5,00,000 as a *bona fide* loan, then, clubbing provisions would not be attracted.

Question 4

State True or False, with reasons:

Mr. Y, who is a physically handicapped minor (suffering from a disability of the nature specified in section 80U), earns bank interest of ₹ 50,000 and ₹ 60,000 from marking bags manually by himself. The total income of Mr. Y shall be computed in his hands separately.

Answer

True. The clubbing provisions of section 64(1A) are not applicable in a case where the minor child is suffering from any disability of the nature specified in section 80U. The income of such minor child will not be clubbed in the hands of either of the parents. Consequently, the total income of Mr. Y will be assessed in his hands.

Question 5

Mrs. Kasturi transferred her immovable property to ABC Co. Ltd. subject to a condition that out of the rental income, a sum of ₹ 36,000 per annum shall be utilized for the benefit of her son's wife.

Mrs. Kasturi claims that the amount of ₹ 36,000 (utilized by her son's wife) should not be included in her total income as she no longer owned the property.

State with reasons whether the contention of Mrs. Kasturi is valid in law.

Answer

The clubbing provisions under section 64(1)(viii) are attracted in case of transfer of any asset, directly or indirectly, otherwise than for adequate consideration, to any person to the extent to which the income from such asset is for the immediate or deferred benefit of son's wife. Such income shall be included in computing the total income of the transferor-individual.

Therefore, income of ₹ 36,000 meant for the benefit of daughter-in-law is chargeable to tax in the hands of transferor i.e., Mrs. Kasturi in this case.

The contention of Mrs. Kasturi is, hence, not valid in law.

Note - *In order to attract the clubbing provisions under section 64(1)(viii), the transfer should be otherwise than for adequate consideration. In this case, it is presumed that the transfer is otherwise than for adequate consideration and therefore, the clubbing provisions are attracted.*

If it is presumed that the transfer was for adequate consideration, the provisions of section 64(1)(viii) would not be attracted.

Question 6

Discuss the tax implications of income arising from revocable transfer of assets. When will the clubbing provisions not apply at present, even where there is revocable transfer of assets?

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Answer

Income arising from revocable transfer of assets [Sections 61 & 63]

(i) All income arising to any person by virtue of a revocable transfer of assets is to be included in the total income of the transferor.

(ii) A transfer is deemed to be revocable if:

(a) it contains any provision for the re-transfer, directly or indirectly, of the whole or any part of the income or assets to the transferor, or

(b) it gives, in any way, the transferor, a right to re-assume power, directly or indirectly, over the whole or any part of the income or the assets.

Transfer not revocable during the life time of the beneficiary or the transferee [Section 62]

If there is a transfer of asset which is not revocable during the life time of the beneficiary or transferee, the income from the transferred asset is not includible in the total income of the transferor provided the transferor derives no direct or indirect benefit from such income.

If the transferor receives direct or indirect benefit from such income, such income is to be included in his total income even though the transfer may not be revocable during the life time of the beneficiary or transferee.

Question 7

Explain the provisions of the Income-tax Act, 1961, with regard to clubbing of income of spouse under section 64.

Answer

As per section 64(1)(ii), any income arising directly or indirectly to the spouse of an individual by way of salary, commission, fees or any other form of remuneration, whether in cash or in kind, from a concern in which such individual has a substantial interest, would be clubbed. However, such rule does not apply where the spouse possesses technical or professional qualification and the income of the spouse is solely attributable to the application of his or her technical or professional knowledge and experience.

Where both husband and wife have substantial interest in a concern and both are in receipt of salary etc. from the said concern, such income will be clubbed with the income of the spouse whose total income, excluding such income, is greater.

An individual shall be deemed to have substantial interest in a concern under the following circumstances:

(a) If the concern is a company, equity shares carrying not less than 20% of the voting power are, at any time during the previous year, owned beneficially by such person or partly by such person and partly by one or more of his relatives.

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(b) In any other case, if such person is entitled, or such person and one or more of his relatives are entitled in the aggregate, at any time during the previous year, to not less than 20% of the profits of such concern.

As per section 64(1)(iv), where there is a transfer of an asset other than house property, directly or indirectly from one spouse to another, otherwise than for adequate consideration or in connection with an agreement to live apart, any income that arises either directly or indirectly to the transferee from the transfer of the asset shall be included in the total income of the transferor.

However, any income from the accretion of transferred asset is not liable to be clubbed. It may be noted that natural love and affection will not constitute adequate consideration for the purpose of section 64(1).

Question 8

Compute the gross total income of Mr. & Mrs. A from the following information:

	Particulars	***₹***
(a)	*Salary income (computed) of Mrs.A*	*2,30,000*
(b)	*Income from profession of Mr.A*	*3,90,000*
(c)	*Income of minor son B from company deposit*	*15,000*
(d)	*Income of minor daughter C from special talent*	*32,000*
(e)	*Interest from bank received by C on deposit made out of her special talent*	*3,000*
(f)	*Gift received by C on 30.09.2016 from friend of Mrs. A*	*2,500*

Brief working is sufficient. Detailed computation under various heads of income is NOT required.

Answer

As per the provisions of section 64(1A) of the Income-tax Act, 1961, all the income of a minor child has to be clubbed in the hands of that parent whose total income (excluding the income of the minor) is greater. The income of Mr. A is ₹ 3,90,000 and income of Mrs. A is ₹ 2,30,000. Since the income of Mr. A is greater than that of Mrs. A, the income of the minor children have to be clubbed in the hands of Mr. A. It is assumed that this is the first year when clubbing provisions are attracted.

Income derived by a minor child from any activity involving application of his/her skill, talent, specialised knowledge and experience is not to be clubbed. Hence, the income of minor child C from exercise of special talent will not be clubbed.

However, interest from bank deposit has to be clubbed even when deposit is made out of income arising from application of special talent.

The Gross Total Income of Mrs. A is ₹ 2,30,000. The total income of Mr. A giving effect to the provisions of section 64(1A) is as follows:

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

Particulars	₹	₹
Income from profession		3,90,000
Income of minor son B from company deposit	15,000	
Less: Exemption under section 10(32)	1,500	13,500
Income of minor daughter C		
From special talent – not to be clubbed	-	
Interest from bank	3,000	
Gift of ₹ 2,500 received from a non-relative is not taxable under section 56(2)(vii) being less than the aggregate limit of ₹ 50,000	Nil	
	3,000	
Less : Exemption under section 10(32)	1,500	1,500
Gross Total Income		**4,05,000**

Question 9

A proprietary business was started by Smt. Rani in the year 2014. As on 1.4.2015 her capital in business was ₹ 3,00,000.

Her husband gifted ₹ 2,00,000 on 10.4.2015, which amount Smt. Rani invested in her business on the same date. Smt. Rani earned profits from her proprietory business for the Financial year 2015-16, ₹ 1,50,000 and Financial year 2016-17 ₹ 3,90,000. Compute the income, to be clubbed in the hands of Rani's husband for the Assessment year 2017-18 with reasons.

Answer

Section 64(1) of the Income-tax Act, 1961 provides for the clubbing of income in the hands of the individual, if the income earned is from the assets transferred directly or indirectly to the spouse of the individual, otherwise than for adequate consideration. In this case Smt. Rani received a gift of ₹ 2,00,000 from her husband which she invested in her business. The income to be clubbed in the hands of Smt. Rani's husband for A.Y.2017-18 is computed as under:

Particulars	Smt. Rani's Capital Contribution	Capital Contribution Out of gift from husband	Total
	₹	₹	₹
Capital as at 1.4.2015	3,00,000	--	3,00,000
Investment on 10.04.2015 out of gift received from her husband		2,00,000	2,00,000
	3,00,000	2,00,000	5,00,000

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Profit for F.Y. 2015-16 to be apportioned on the basis of capital employed on the first day of the previous year i.e., on 1.4.2015	1,50,000		1,50,000
Capital employed as at 1.4.2016	**4,50,000**	**2,00,000**	**6,50,000**
Profit for F.Y.2016-17 to be apportioned on the basis of capital employed as at 1.4.2016 (i.e., 45 : 20)	2,70,000	1,20,000	3,90,000

Therefore, the income to be clubbed in the hands of Smt. Rani's husband for A.Y.2017-18 is ₹ 1,20,000.

Question 10

Write short notes on "Clubbing of income of minor children in the hands of parent".

Answer

Income earned by a minor child would be clubbed in the hands of the parent. If both parents are having income, then income of minor child would be clubbed in the hands of that parent whose income is higher before clubbing the income of minor child.
Under the following situations the income of the minor child would not be clubbed in the hands of parent :-

(a) Income earned by minor child through manual work done by him.

(b) Income from activity involving application of his skill, talent or specialised knowledge and experience.

If the relationship of husband and wife does not subsist between the parents, the income of the minor child would be clubbed in the hands of the parent who maintains the child during the previous year. The parent is entitled to claim an exemption under section 10(32) upto ₹ 1,500 per minor child if the income of the minor child is included in his total income.

Where any such income is once included in the total income of either parent, any such income arising in any succeeding previous year shall not be included in the total income of the other parent, unless the Assessing Officer is satisfied after giving that parent an opportunity of being heard, that it is necessary to do so.

Question 11

Mr. Vatsan has transferred, through a duly registered document, the income arising from a godown to his son, without transferring the godown. In whose hands will the rental income from godown be charged?

Answer

Section 60 expressly states that where there is transfer of income from an asset without transfer of the asset itself, such income shall be included in the total income of the transferor. Hence, the rental income derived from the godown shall be clubbed in the hands of Mr. Vatsan.

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Question 12

Mr. Dhaval and his wife Mrs. Hetal furnish the following information:

Sl. No.	*Particulars*	*₹*
(i)	*Salary income (computed) of Mrs. Hetal*	*4,60,000*
(ii)	*Income of minor son 'B' who suffers from disability specified in Section 80U*	*1,08,000*
(iii)	*Income of minor daughter 'C' from singing*	*86,000*
(iv)	*Income from profession of Mr. Dhaval (computed)*	*7,50,000*
(v)	*Cash gift received by 'C' on 2.10.2016 from friend of Mrs. Hetal on winning of singing competition*	*48,000*
(vi)	*Income of minor married daughter 'A' from company deposit*	*30,000*

Compute the total income of Mr. Dhaval and Mrs. Hetal for the Assessment Year 2017-18.

Answer

Computation of Total Income of Mr. Dhaval and Mrs. Hetal for the A.Y. 2017-18

Particulars		**Mr. Dhaval (₹)**	**Mrs. Hetal (₹)**
Salaries			4,60,000
Profits and gains of business or profession		7,50,000	
Income from other sources:			
Income by way of interest from company deposit earned by minor daughter A [See Note (d)]	30,000		
Less : Exemption under section 10(32)	1,500	28,500	
Total Income		**7,78,500**	**4,60,000**

Notes:

(a) The income of a minor child suffering from any disability of the nature specified in section 80U shall not be included in the hands of the parents. Hence, ₹ 1,08,000, being the income of minor son 'B' who suffers from disability specified under section 80U, shall not be included in the hands of either of his parents.

(b) The income derived by the minor from manual work or from any activity involving exercise of his skill, talent or specialised knowledge or experience will not be included in the income of his parent. Hence, in the given case, ₹ 86,000 being the income of the minor daughter 'C' shall not be clubbed in the hands of the parents.

(c) Under section 56(2)(vii), cash gifts received from any person/persons exceeding ₹ 50,000 during the year in aggregate is taxable. Since the cash gift in this case does not exceed ₹ 50,000, the same is not taxable.

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(d) The clubbing provisions are attracted even in respect of income of minor married daughter. The income of the minor will be included in the income of that parent whose total income is greater. Hence, income of minor married daughter 'A' from company deposit shall be clubbed in the hands of the Mr. Dhaval and exemption under section 10(32) of ₹ 1,500 per child shall be allowed in respect of such income.

Question 13

Mr. Dhaval has an income from salary of ₹ 3,50,000 and his minor children's income are as under:

Particulars	***₹***
Minor daughter has earned the following income:	
From a TV show	*50,000*
From interest on FD with a bank (deposited by Mr. Dhaval from his income)	*5,000*
Minor son has earned the following income:	
From the sale of a own painting	*10,000*
From interest on FD with a bank (deposited by Mr. Dhaval from his income)	*1,000*

Compute the gross total income of Mr. Dhaval.

Answer

Computation of Gross Total Income of Mr. Dhaval

Particulars	**₹**	**₹**
Income from Salary		3,50,000
Income from other sources:		
Minor Daughter's income		
Income from T.V. show (See Note below)		Nil
Interest income from FD with a Bank	5,000	
Less : Exempt under section 10(32)	1,500	3,500
Minor son's income		
Income from sale of self made painting (See Note below)		Nil
Interest income from FD with a Bank	1,000	
Less : Exempt under section 10(32)	1,000	Nil
Gross Total Income		**3,53,500**

Note: *The income derived by the minor from manual work or from any activity involving exercise of his skill, talent or specialised knowledge or experience will not be included in the income of his parent. Hence, in the given case ₹ 50,000 being the income of the minor*

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daughter from TV show and ₹ 10,000 being the income of minor son from sale of own painting, shall not be clubbed in the hands of Mr. Dhaval.

Question 14

Mr. Mittal has four minor children consisting of three daughters and one son. The annual income of all the children for the Assessment Year 2017-18 were as follows:

	₹
First daughter (Including Scholarship received ₹ 5,000)	*10,000*
Second Daughter	*8,500*
Third Daughter (Suffering from disability specified U/s 80U)	*4,500*
Son	*40,000*

Mr. Mittal gifted ₹ 2,00,000 to his minor son who invested the same in the business and derived income of ₹ 20,000 which is included above.

Compute the amount of Income earned by minor children to be clubbed in the hands of Mr. Mittal.

Answer

Computation of income earned by minor children to be clubbed with the income of Mr. Mittal

	Particulars	₹
(i)	Income of first daughter ***[See Notes 1 & 2]***	5,000
	Less: Income exempt under section 10(32) ***[See Note 4]***	1,500
	Income to be clubbed	3,500
(ii)	Income of second daughter ***[See Note 1]***	8,500
	Less: Income exempt under section 10(32) ***[See Note 4]***	1,500
	Income to be clubbed	7,000
(iii)	Income of son ***[See Note 5]***	40,000
	Less: Income exempt under section 10(32) ***[See Note 4]***	1,500
	Income to be clubbed	38,500
	Total Income to be clubbed as per section 64(1A) [(i)+(ii)+(iii)]	**49,000**

Notes:

(1) As per section 64(1A), in computing the total income of an individual, all such income accruing or arising to his minor child shall be included.

(2) The income accruing or arising to a minor child on account of activity involving application of their skill, talent or specialized knowledge and experience is not includible

in the total income of the parent. Therefore, scholarship received by the first daughter is not includible in the hands of Mr. Mittal, assuming that the same is received on account of skill, talent or specialized knowledge of the minor daughter. The balance income of ₹ 5,000 (₹ 10,000 – ₹ 5,000) is includible in the hands of Mr. Mittal after providing deduction of ₹ 1,500 under section 10(32).

(3) Further, as per the provisions of section 64(1A), income of a minor child suffering from any disability of the nature specified in section 80U would not be included in the total income of the parent. Therefore, in this case, the income of third daughter suffering from disability specified under section 80U is not includible in the total income of Mr. Mittal.

(4) Under section 10(32), income of each minor child includible in the hands of the parent under section 64(1A) would be exempt to the extent of the actual income or ₹1,500, whichever is lower.

(5) The specific provision under *Explanation 3* to section 64 for inclusion of income from business where the assets transferred directly or indirectly by an individual are invested by the transferee in business are applicable in cases of transfer to spouse or son's wife only. In case of minor, all income accruing or arising to him or her is, in any case, includible in the hands of the parent.

Question 15

Mr. Ramesh gifted a sum of ₹ 5 lacs to his brother's minor son on 16-4-2016. On 18-4-2016, his brother gifted debentures worth ₹ 6 lacs to Mrs. Ramesh. Son of Mr. Ramesh's brother invested the amount in fixed deposit with Bank of India @ 9% p.a. interest and Mrs. Ramesh received interest of ₹ 45,000 on debentures received by her.

Discuss the implications under the provisions of the Income-tax Act, 1961.

Answer

In the given case, Mr. Ramesh gifted a sum of ₹ 5 lacs to his brother's minor son on 16.4.2016 and simultaneously, his brother gifted debentures worth ₹ 6 lacs to Mr. Ramesh's wife on 18.4.2016. Mr. Ramesh's brother's minor son invested the gifted amount of ₹ 5 lacs in fixed deposit with Bank of India.

These transfers are in the nature of cross transfers. Accordingly, the income from the assets transferred would be assessed in the hands of the deemed transferor because the transfers are so intimately connected to form part of a single transaction and each transfer constitutes consideration for the other by being mutual or otherwise.

If two transactions are inter-connected and are part of the same transaction in such a way that it can be said that the circuitous method was adopted as a device to evade tax, the implication of clubbing provisions would be attracted[1].

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[1] It was so held by the Apex Court in *CIT vs. Keshavji Morarji (1967) 66 ITR 142.*

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As per section 64(1A), all income of a minor child is includible in the hands of the parent, whose total income, before including minor's income is higher. Accordingly, the interest income arising to Mr. Ramesh's brother's son from fixed deposits would be included in the total income of Mr. Ramesh's brother, assuming that Mr. Ramesh's brother's total income is higher than his wife's total income, before including minor's income. Mr. Ramesh's brother can claim exemption of ₹ 1,500 under section 10(32).

Interest on debentures arising in the hands of Mrs. Ramesh would be taxable in the hands of Mr. Ramesh as per section 64(1)(iv).

This is because both Mr. Ramesh and his brother are the indirect transferors of the income to their spouse and minor son, respectively, with an intention to reduce their burden of taxation.

In the hands of Mr. Ramesh, interest received by his spouse on debentures of ₹ 5 lacs alone would be included and not the entire interest income on the debentures of ₹ 6 lacs, since the cross transfer is only to the extent of ₹ 5 lacs.

Hence, only proportional interest (i.e., $5/6^{th}$ of interest on debentures received) ₹ 37,500 would be includible in the hands of Mr. Ramesh.

The provisions of section 56(2)(vii) are not attracted in respect of sum of money transferred or value of debentures transferred, since in both the cases, the transfer is from a relative.

Question 16

Mr. B is the Karta of a HUF, whose members derive income as given below:

	Particulars	***₹***
(i)	*Income from B' s profession*	*45,000*
(ii)	*Mrs. B' s salary as fashion designer*	*76,000*
(iii)	*Minor son D (interest on fixed deposits with a bank which were gifted to him by his uncle)*	*10,000*
(iv)	*Minor daughter P's earnings from sports*	*95,000*
(v)	*D's winnings from lottery (gross)*	*1,95,000*

Discuss the tax implications in the hands of Mr. and Mrs. B.

Answer

Clubbing of income and other tax implications

As per the provisions of section 64(1A), in case the marriage of the parents subsist, the income of a minor child shall be clubbed in the hands of the parent whose total income, excluding the income of the minor child to be clubbed, is greater. In this problem, it has been assumed that the marriage of Mr. B and Mrs. B subsists.

Further, in case the income arises to the minor child on account of any manual work done by the child or as a result of any activity involving application of skill, talent, specialized

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knowledge or experience of the child, then, the same shall not be clubbed in the hands of the parent.

Tax implications

(i) Income of ₹ 45,000 from Mr. B's profession shall be taxable in the hands of Mr. B under the head "Profits and gains of business or profession".

(ii) Salary of ₹ 76,000 received by Mrs. B as a fashion designer shall be taxable as "Salaries" in the hands of Mrs. B.

(iii) Income from fixed deposit of ₹ 10,000 arising to the minor son D, shall be clubbed in the hands of the mother, Mrs. B as "Income from other sources", since her income is greater than income of Mr. B before including the income of the minor child.

As per section 10(32), income of a minor child which is includible in the income of the parent shall be exempt to the extent of ₹ 1,500 per child. The balance income would be clubbed in the hands of the parent as "Income from other sources".

(iv) Income of ₹ 95,000 arising to the minor daughter P from sports shall not be included in the hands of the parent, since such income has arisen to the minor daughter on account of an activity involving application of her skill.

(v) Income of ₹ 1,95,000 arising to minor son D from lottery shall be included in the hands of Mrs. B as "Income from other sources", since her income is greater than the income of Mr. B before including the income of minor child.

Note – Mrs. B can reduce the tax deducted at source from such lottery income while computing her net tax liability.

Exercise

1. *Income of a minor child suffering from any disability of the nature specified in section 80U is -*

   (a) *to be assessed in the hands of the minor child*

   (b) *to be clubbed with the income of that parent whose total income, before including minor's income, is higher*

   (c) *completely exempt from tax*

2. *Income arising to a minor married daughter is -*

   (a) *to be assessed in the hands of the minor married daughter*

   (b) *to be clubbed with the income of that parent whose total income, before including minor's income, is higher*

   (c) *completely exempt from tax*

3. *Where a member of a HUF has converted or transferred his self-acquired property for inadequate consideration into joint family property, income arising therefrom is taxable -*

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(a) *as the income of the transferor-member*

(b) *in the hands of the HUF*

(c) *in the hands of the karta of the HUF*

4. *If such converted property is subsequently partitioned among the members of the family, the income derived from such converted property as is received by the spouse of the transferor will be taxable -*

   (a) *as the income of the transferor-member*

   (b) *as the income of the spouse of the transferor*

   (c) *as the income of the HUF.*

5. *Exemption of a certain amount (not exceeding the income clubbed) is available under section 10(32), where a minor's income is clubbed with the income of the parent. The maximum exemption available is -*

   (a) *upto ₹ 1,200 in respect of each minor child*

   (b) *upto ₹ 1,500 in respect of each minor child*

   (c) *upto ₹ 2,000 in respect of each minor child*

6. *Mr. A gifts cash of ₹ 1,00,000 to his brother's wife Mrs. B. Mr. B gifts cash of ₹ 1,00,000 to Mrs. A. From the cash gifted to her, Mrs. B invests in a fixed deposit, income therefrom is ₹ 10,000. Aforesaid ₹ 10,000 will be included in the total income of ....*

   (a) *Mr. A*

   (b) *Mr. B*

   (c) *Mrs. B*

7. *Write short notes on the following in the context of clubbing of income -*

   (a) *Substantial interest*

   (b) *Transfer and revocable transfer.*

8. *Under what circumstances can an income arising to the spouse of an individual be included in the income of the individual? Discuss.*

9. *State when the income arising to the son's wife can be included in the hands of the individual.*

10. *When can income arising to a minor child be clubbed in the hands of the father or mother? Discuss.*

11. *Discuss the tax consequences arising on conversion of self-acquired property into joint family property.*

Answers

1. a; **2.** b; **3.** a; **4.** a; **5.** b; **6.** b.

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6 Set Off and Carry Forward of Losses

Key Points			
Inter-source and Inter-head Set-off [Sections 70 & 71]			
Section	**Provision**	**Exceptions**	
70	**Inter-source set-off under the same head of income** Any loss in respect of one source shall be set-off against income from any other source under the same head of income.	(i)	Loss from speculative business
		(ii)	Loss from specified business under section 35AD
		(iii)	Long term capital loss and
		(iv)	Loss from the activity of owning and maintaining race horses
71	**Inter head adjustment** Loss under one head of income can be set-off against income assessable under any other head of income.	(i)	Loss under the head "Profits and gains of business or profession" cannot be set off against income under the head "Salaries"
		(ii)	Loss under the head "Capital gains" cannot be set-off against income under any other head.
		(iii)	Speculation loss and loss from the activity of owning and maintaining race horses cannot be set-off against income under any other head.

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Carry forward and Set-off of brought forward losses

Section	Nature of loss to be carried forward	Income against which the brought forward loss can be set-off	Maximum permissible period [from the end of the relevant assessment year] for carry forward of losses
71B	Unabsorbed loss from house property	Income from house property	8 assessment years
72	Unabsorbed business loss	Profits and gains from business or profession	8 assessment years
73	Loss from speculation business	Income from speculation business	4 assessment years
73A	Loss from specified business under section 35AD	Profit from any specified business	Indefinite period
74	Long-term capital loss	Long-term capital gains	8 assessment years
	Short-term capital loss	Short-term/Long-term capital gains	8 assessment years
74A	Loss from the activity of owning and maintaining race horses	Income from the activity of owning and maintaining race horses.	4 assessment years

Order of set-off of losses

1.	Current year depreciation / Current year capital expenditure on scientific research and current year expenditure on family planning, to the extent allowed.
2.	Brought forward loss from business/profession [Section 72(1)]
3.	Unabsorbed depreciation [Section 32(2)]
4.	Unabsorbed capital expenditure on scientific research [Section 35(4)].
5.	Unabsorbed expenditure on family planning [Section 36(1)(ix)]

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Question 1

Mr. Garg, a resident individual, furnishes the following particulars of his income and other details for the previous year 2016-17.

		₹
(1)	*Income from Salary*	*15,000*
(2)	*Income from business*	*66,000*
(3)	*Long term capital gain on sale of land*	*10,800*
(4)	*Loss on maintenance of race horses*	*15,000*
(5)	*Loss from gambling*	*9,100*

The other details of unabsorbed depreciation and brought forward losses pertaining to Assessment Year 2016-17 are as follows:

		₹
(1)	*Unabsorbed depreciation*	*11,000*
(2)	*Loss from Speculative business*	*22,000*
(3)	*Short term capital loss*	*9,800*

Compute the Gross total income of Mr. Garg for the Assessment Year 2017-18 and the amount of loss, if any that can be carried forward or not.

Answer

Computation of Gross Total Income of Mr. Garg for the A.Y. 2017-18

Particulars	₹	₹
(i) Income from salary		15,000
(ii) **Profits and gains of business or profession**	66,000	
Less : Unabsorbed depreciation brought forward from A.Y.2016-17	11,000	55,000
(Unabsorbed depreciation can be set-off against any head of income)		
(iii) **Capital gains**		
Long term capital gain on sale of land	10,800	
Less : Brought forward short term capital loss		
[Short-term capital loss can be set-off against both short-term capital gains and long-term capital gains as per section 74(1)]	9,800	1,000
Gross total income		**71,000**

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Amount of loss to be carried forward to A.Y.2018-19

		₹
(1)	**Loss from speculative business [to be carried forward as per section 73]** [Loss from a speculative business can be set off only against income from another speculative business. Since there is no income from speculative business in the current year, the entire loss of ₹ 22,000 brought forward from A.Y.2016-17 has to be carried forward to A.Y. 2018-19 for set-off against speculative business income of that year. It may be noted that speculative business loss can be carried forward for a maximum of four years as per section 73(4), i.e., upto A.Y.2020-21]	22,000
(2)	**Loss on maintenance of race horses [to be carried forward as per section 74A]** [As per section 74A(3), the loss incurred in the activity of owning and maintaining race horses in any assessment year cannot be set-off against income from any other source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum of four assessment years i.e., upto A.Y.2021-22]	15,000
(3)	**Loss from gambling can neither be set-off nor be carried forward**	

Question 2

Mr. Batra furnishes the following details for year ended 31.03.2017:

Particulars	***₹***
Short term capital gain	*1,40,000*
Loss from speculative business	*60,000*
Long term capital gain on sale of land	*30,000*
Long term capital loss on sale of shares (securities transaction tax not paid)	*1,00,000*
Income from business of textile (after allowing current year depreciation)	*50,000*
Income from activity of owning and maintaining race horses	*15,000*
Income from salary	*1,00,000*
Loss from house property	*40,000*

Following are the brought forward losses:

(i) Losses from activity of owning and maintaining race horses-pertaining to A.Y.2014-15 ₹ 25,000.

(ii) Brought forward loss from business of textile ₹ 60,000 - Loss pertains to A.Y. 2009-10.

Compute gross total income of Mr. Batra for the Assessment Year 2017-18. Also state the eligible carry forward losses for the Assessment Year 2018-19.

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Answer

Computation of Gross Total Income of Mr. Batra for the A.Y. 2017-18

Particulars	₹	₹
Salaries	1,00,000	
Less: Current year loss from house property	(40,000)	60,000
Profit and gains of business or profession		
Income from textile business	50,000	
Less: Loss from textile business brought forward from A.Y. 2009-10	60,000	
Balance business loss of A.Y. 2009-10 **[See Note 1]**	(10,000)	NIL
Income from the activity of owning and maintaining race horses	15,000	
Less: Loss from activity of owning and maintaining race horses brought forward from A.Y. 2014-15	25,000	
Loss to be carried forward to A.Y. 2018-19 **[See Note 2]**	(10,000)	NIL
Capital Gain		
Short term capital gain		1,40,000
Long term capital gain on sale of land	30,000	
Less: Long term capital loss on sale of shares	1,00,000	
Loss to be carried forward to A.Y. 2018-19 **[See Note 3]**	(70,000)	NIL
Gross Total Income		**2,00,000**

Losses to be carried forward to A.Y. 2018-19

Particulars	₹
Current year loss from speculative business [See Note-4]	60,000
Current year long term capital loss on sale of shares	70,000
Loss from activity of owning and maintaining of race horse pertaining to A.Y.2014-15	10,000

Notes:-

(1) As per section 72(3), business loss can be carried forward for a maximum of eight assessment years immediately succeeding the assessment year for which the loss was first computed. Since the eight year period for carry forward of business loss of A.Y. 2009-10 expired with the A.Y. 2017-18, the balance unabsorbed business loss of ₹ 10,000 cannot be carried forward to A.Y. 2018-19.

(2) As per section 74A(3), the loss incurred on maintenance of race horses cannot be set-off against income from any source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum period of 4 assessment years.

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(3) Long term capital gains on sale of shares on which securities transaction tax is not paid is not exempt under section 10(38). Therefore, long-term capital loss on sale of such shares can be set-off against long-term capital gain on sale of land. The balance loss of ₹ 70,000 cannot be set-off against short term capital gain or against any other head of income. The same has to be carried forward for set-off against long-term capital gain of the subsequent assessment year. Such long-term capital loss can be carried forward for a maximum of eight assessment years.

(4) Loss from speculation business cannot be set-off against any income other than profit and gains of another speculation business. Such loss can, however, be carried forward for a maximum of four years as per section 73(4) to be set-off against income from speculation business.

Question 3

The following are the details relating to Mr. Srivatsan, a resident Indian, aged 57, relating to the year ended 31.3.2017:

Particulars	*₹*
Income from salaries	*2,20,000*
Loss from house property	*1,90,000*
Loss from cloth business	*2,40,000*
Income from speculation business	*30,000*
Loss from specified business covered by section 35AD	*20,000*
Long-term capital gains from sale of urban land	*2,50,000*
Long-term capital loss from sale of listed shares in recognized stock exchange (STT paid)	*1,10,000*
Loss from card games	*32,000*
Income from betting (Gross)	*45,000*
Life Insurance Premium paid	*1,20,000*

Compute the total income and show the items eligible for carry forward.

Answer

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

Particulars	₹	₹
Salaries		
Income from salaries	2,20,000	
Less: Loss from house property	1,90,000	30,000
Profits and gains of business or profession		
Income from speculation business	30,000	

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Less: Loss from cloth business set off	30,000	Nil
Capital gains		
Long-term capital gains from sale of urban land	2,50,000	
Less: Loss from cloth business set off	2,10,000	40,000
Income from other sources		
Income from betting		45,000
Gross total income		**1,15,000**
Less: Deduction under section 80C (life insurance premium paid)		30,000
Total income		**85,000**

Losses to be carried forward:

Particulars	₹
(1) Loss from cloth business **(₹ 2,40,000 - ₹ 30,000 - ₹2,10,000)**	Nil
(2) Loss from specified business covered by section 35AD	20,000

Notes:

(i) Long-term capital gains from sale of listed shares in a recognized stock exchange is exempt under section 10(38). Loss from an exempt source cannot be set off against profits from a taxable source. Therefore, long-term capital loss on sale of listed shares cannot be set-off against long-term capital gains from sale of urban land.

(ii) Loss from specified business covered by section 35AD can be set-off only against profits and gains of any other specified business. Therefore, such loss cannot be set off against any other income. The unabsorbed loss has to be carried forward for set-off against profits and gains of any specified business in the following year.

(iii) Business loss cannot be set off against salary income. However, the balance business loss of ₹ 2,10,000 (₹ 2,40,000 – ₹ 30,000 set-off against income from speculation business) can be set-off against long-term capital gains of ₹ 2,50,000 from sale of urban land. Consequently, the taxable long-term capital gains would be ₹ 40,000.

(iv) Loss from card games can neither be set off against any other income, nor can it be carried forward.

(v) For providing deduction under Chapter VI-A, gross total income has to be reduced by the amount of long-term capital gains and casual income. Therefore, the deduction under section 80C in respect of life insurance premium paid has to be restricted to ₹ 30,000 [i.e., Gross Total Income of ₹ 1,15,000 – ₹ 40,000 (LTCG) – ₹ 45,000 (Casual income)].

(vi) Income from betting is chargeable at a flat rate of 30% under section 115BB and no expenditure or allowance can be allowed as deduction from such income, nor can any loss be set-off against such income.

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Question 4

Mr. Soohan submits the following details of his income for the assessment year 2017-18:

Particulars	*₹*
Income from salary	*3,00,000.00*
Loss from let out house property	*40,000.00*
Income from sugar business	*50,000.00*
Loss from iron ore business b/f (discontinued in P.Y. 2011-12)	*1,20,000.00*
Short term capital loss	*60,000.00*
Long term capital gain	*40,000.00*
Dividend	*5,000.00*
Income received from lottery winning (Gross)	*50,000.00*
Winnings from card games	*6,000.00*
Agricultural income	*20,000.00*
Long term capital gain from shares (STT paid)	*10,000.00*
Short term capital loss under section 111A	*10,000.00*
Bank interest	*5,000.00*

Calculate gross total income and losses to be carried forward.

Answer

Computation of gross total income of Mr. Soohan for the A.Y.2017-18

Particulars	₹	₹
Salaries		
Income from salary	3,00,000	
Less: Loss from house property set-off against salary income as per section 71	(40,000)	2,60,000
Profits and gains of business or profession		
Income from sugar business	50,000	
Less: Brought forward loss from iron-ore business set-off as per section 72(1)	(50,000)	Nil
Balance business loss of ₹ 70,000 of P.Y.2011-12 carried forward to A.Y.2018-19		
Capital gains		
Long term capital gain	40,000	

Less: Short term capital loss set-off	(40,000)	Nil
Balance short-term capital loss of ₹ 20,000 to be carried forward		
Short-term capital loss of ₹ 10,000 under section 111A also to be carried forward		
Income from other sources		
Winnings from lottery	50,000	
Winnings from card games	6,000	
Bank interest	5,000	61,000
Gross Total Income		**3,21,000**
Losses to be carried forward to A.Y.2018-19		
Loss of iron-ore business	70,000	
Short term capital loss (₹ 20,000 + ₹ 10,000)	30,000	

Notes:

1. The following income are exempt under section 10 –
   (i) Dividend income [Exempt under section 10(34)], assuming that dividend is received from a domestic company.
   (ii) Agricultural income [Exempt under section 10(1)].
   (iii) Long-term capital gains on which STT is paid [Exempt under section 10(38)].
2. It is presumed that loss from iron-ore business relates to P.Y.2011-12, the year in which the business was discontinued.

Question 5

Mr. Rajat submits the following information for the financial year ending 31st March, 2017. He desires that you should:

(a) Compute the total income and

(b) Ascertain the amount of losses that can be carried forward.

			Particulars	***₹***
(i)	*He has two houses :*			
	(a)	*House No. I – Income after all statutory deductions*		*72,000*
	(b)	*House No. II – Current year loss*		*(30,000)*
(ii)	*He has three proprietary businesses :*			
	(a)	*Textile Business :*		
		(i)	*Discontinued from 31st October, 2016 – Current year loss*	*40,000*

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		(ii) Brought forward business loss of A.Y.2013-14	*95,000*
	(b)	*Chemical Business :*	
		(i) Discontinued from 1st March, 2015 – hence no profit/loss	*Nil*
		(ii) Bad debts allowed in earlier years recovered during this year	*35,000*
		(iii) Brought forward business loss of A.Y. 2015-16	*50,000*
	(c)	*Leather Business : Profit for the current year*	*1,00,000*
	(d)	*Share of profit in a firm in which he is partner since 2004*	*16,550*
(iii)	*(a)*	*Short-term capital gain*	*60,000*
	(b)	*Long-term capital loss*	*35,000*
(iv)	*Contribution to LIC towards premium*		*10,000*

Answer

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

Particulars	₹	₹
1. Income from house property		
House No.1	72,000	
House No.2	(-) 30,000	42,000
2. Profits and gains of business or profession		
Profit from leather business	1,00,000	
Bad debts recovered taxable under section 41(4)	35,000	
	1,35,000	
Less: Current year loss of textile business	(-) 40,000	
	95,000	
Less: Brought forward business loss of textile business for A.Y.2013-14 set off against the business income of current year	95,000	Nil
3. Capital Gains		
Short-term capital gain		60,000
Gross Total Income		**1,02,000**
Less: Deduction under Chapter VI-A		
Under section 80C – LIC premium paid		10,000
Total Income		**92,000**

Statement of losses to be carried forward to A.Y. 2018-19

Particulars	₹
Business loss of A.Y. 2015-16 to be carried forward under section 72	50,000
Long term capital loss of A.Y. 2017-18 to be carried forward under section 74	35,000

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Notes:

(1) Share of profit from firm of ₹ 16,550 is exempt under section 10(2A).

(2) Long-term capital loss cannot be set-off against short-term capital gains. Therefore, it has to be carried forward to the next year to be set-off against long-term capital gains of that year.

Question 6

Mr. A furnishes you the following information for the year ended 31.03.2017:

		(₹)
(i)	*Income from plying of vehicles (computed as per books)* *(He owned 5 heavy goods vehicle throughout the year)*	*3,20,000*
(ii)	*Income from retail trade of garments* *(Computed as per books) (Sales turnover ₹ 1,21,70,000)*	*7,50,000*
(iii)	*He has brought forward depreciation relating to A.Y. 2016-17*	*1,00,000*
(iv)	*He deposited ₹ 1,50,000 into his PPF account on 6.1.2017*	

Compute taxable income of Mr. A and his tax liability for the assessment year 2017-18 with reasons for your computation.

Answer

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

Particulars	₹
Income from retail trade – as per books (See Note 1 below)	7,50,000
Income from plying of vehicles – as per books (See Note 2 below)	3,20,000
	10,70,000
Less : Set off of brought forward depreciation relating to A.Y. 2016-17	1,00,000
Gross total income	**9,70,000**
Less: Deduction under section 80C – Contribution to PPF	1,50,000
Taxable income	**8,20,000**
Tax liability	89,000
Add: Education cess and SHEC@3%	2,670
Tax Payable	**91,670**

Note :

1. **Income from retail trade:** Presumptive business income under section 44AD is ₹ 9,73,600 i.e., 8% of turnover of ₹ 1,21,70,000. However, the income computed as per books is ₹ 7,50,000 which is to be further reduced by the amount of unabsorbed depreciation of ₹ 1,00,000. Since the income computed as per books is lower than the income deemed under section 44AD, the assessee can adopt the income as per books.

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However, if he does not opt for presumptive taxation under section 44AD, he has to get his books of accounts audited under section 44AB, since his turnover exceeds Rs.1 crore.

2. **Income from plying of vehicles:** Income calculated under section 44AE(1) would be ₹ 7,500 x 12 x 5 which is equal to ₹ 4,50,000. However, the income from plying of vehicles as per books is ₹ 3,20,000, which is lower than the presumptive income of ₹ 4,50,000 calculated as per section 44AE(1). Hence, the assessee can adopt the income as per books i.e. ₹ 3,20,000, provided he maintains books of account as per section 44AA and gets his accounts audited and furnishes an audit report as required under section 44AB.

It is to be further noted that in both the above cases, had presumptive income provisions been opted, all deductions under sections 30 to 38, including depreciation would have been deemed to have been given full effect to and no further deduction under those sections would be allowable.

If the assessee opted for income to be assessed on presumptive basis, his total income would be as under:

Particulars	₹
Income from retail trade under section 44AD [₹ 1,21,70,000 @ 8%]	9,73,600
Income from plying of vehicles under section 44AE [₹ 7,500 x 12 x 5]	4,50,000
	14,23,600
Less: Set off of brought forward depreciation – not possible as it is deemed that it has been allowed and set off	Nil
Gross total income	**14,23,600**
Less: Deduction under section 80C - Contribution to PPF	1,50,000
Taxable income	**12,73,600**
Tax thereon	2,07,080
Add : Education cess and SHEC@3%	6,212
Total tax liability	**2,13,292**
Total tax liability (rounded off)	**2,13,290**

Question 7

Compute the total income of Mr. Krishna for the assessment year 2017-18 from the following particulars:

Particulars	Amount (₹)
Income from business before adjusting the following items:	*1,75,000*
(a) Business loss brought forward from assessment year 2014-15	*70,000*
(b) Current depreciation	*40,000*
(c) Unabsorbed depreciation of earlier year	*1,55,000*

Income from house property (Gross Annual Value)	*4,32,000*
Municipal taxes paid	*32,000*
Mr. Krishna sold a plot at Noida on 12th September, 2016 for a consideration of ₹ 6,40,000, which had been purchased by him on 20th December, 2013 at a cost of ₹ 4,10,000	
Long-term capital loss on sale of shares sold through recognized stock exchange (STT paid)	*75,000*
Long-term capital gain on sale of debentures	*60,000*
Dividend on shares held as stock in trade	*22,000*
Dividend from a company carrying on agri business	*10,000*

During the previous year 2016-17, Mr. Krishna has repaid ₹ 1,67,000 towards housing loan from a scheduled bank. Out of ₹ 1,67,000, ₹ 97,000 was towards payment of interest and rest towards principal payments.

Cost inflation indices: F.Y. 2012-13: 852 & F.Y.2016-17: 1125.

Answer

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

	Particulars	₹	₹
I.	**Income from house property**		
	Gross Annual Value	4,32,000	
	Less: Municipal taxes paid	32,000	
	Net Annual Value (NAV)	4,00,000	
	Less: Deductions under section 24		
	(a) 30% of NAV	1,20,000	
	(b) Interest on housing loan	97,000	1,83,000
II.	**Income from business**		
	Income from business	1,75,000	
	Less : Current year depreciation under section 32(1)	40,000	
		1,35,000	
	Less: Set-off of brought forward business loss of A.Y. 2014-15 under section 72	70,000	
		65,000	
	Less: Unabsorbed depreciation set-off ***[See Note 3]***	65,000	Nil

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III.	**Capital gains**		
	Long term capital gain on sale of debentures	60,000	
	Less: Unabsorbed depreciation set-off ***[See Note 3]***	60,000	Nil
	Short term capital gain on sale of land ***[See Note 2]***	2,30,000	
	Less: Unabsorbed depreciation set-off ***[See Note 3]***	30,000	2,00,000
IV.	**Income from other sources**		
	Dividend on shares (**whether held as stock-in-trade or from a company carrying on agricultural operations)** – exempt under section 10(34)	-	Nil
Gross total income			**3,83,000**
Less : Chapter VI-A deduction			
Section 80C [Principal repayment of housing loan]			70,000
Total income			**3,13,000**

Notes:

(1) Loss from an exempt source cannot be set-off against gains from a taxable source. Since long-term capital gains on sale of listed equity shares through a recognized stock exchange is eligible for exemption under section 10(38), consequently, long-term capital loss on sale of listed equity shares, being loss from an exempt source, cannot be set-off against long-term capital gains on sale of debentures.

(2) Since land is held for a period of less than 36 months, the gain of ₹ 2,30,000 arising from sale of such land is a short-term capital gain.

(3) Brought forward unabsorbed depreciation can be adjusted against any head of income. However, it is most beneficial to set-off unabsorbed depreciation first against long-term capital gains, since it is taxable at a higher rate of 20% (the other income of the assessee falling in the 10% slab rate). Therefore, unabsorbed depreciation is first set-off against long-term capital gains to the extent of ₹ 60,000. The remaining unabsorbed depreciation is adjusted against business income to the extent of ₹ 65,000 and the balance of ₹ 30,000 is adjusted against short-term capital gains.

In the alternative, the balance of ₹ 30,000 may also be set-off against income from house property, in which case, the net income from house property would be ₹ 1,53,000 and short-term capital gains would be ₹ 2,30,000. The gross total income and total income would, however, remain unchanged.

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Question 8

Simran, engaged in various types of activities, gives the following particulars of her income for the year ended 31.3.2017:

	Particulars	₹
(a)	*Profit of business of consumer and house-hold products*	*50,000*
(b)	*Loss of business of readymade garments*	*10,000*
(c)	*Brought forward loss of catering business which was closed in A.Y. 2016-17*	*15,000*
(d)	*Short-term loss on sale of securities and shares*	*15,000*
(e)	*Profit of speculative transactions entered into during the year*	*12,500*
(f)	*Loss of speculative transactions of A.Y. 2012-13 not set off till A.Y. 2016-17*	*15,000*

Compute the total income of Simran for the A.Y. 2017-18.

Answer

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

Particulars	₹	₹
Profit of business of consumer and house-hold products	50,000	
Less: Loss of business of readymade garments for the year adjusted under section 70(1)	10,000	
	40,000	
Less: Brought forward loss of catering business closed in A.Y. 2016-17 set off against business income for the current year as per section 72(1)	15,000	25,000
Profit of speculative transaction		12,500
Total Income		**37,500**

Notes :

1. Loss of speculative transaction of A.Y. 2012-13 is not allowed to be set off against the profit of speculative transaction of the A.Y.2017-18, since, as per the provisions of section 73(4), such loss can be carried forward for set-off for a maximum period of 4 years only i.e. up to A.Y.2016-17.
2. Short term capital loss of ₹ 15,000 on sale of securities and shares has to be carried forward as per section 74 since there is no income under the head Capital Gains for the A.Y.2017-18. The loss is to be carried forward for set off in future years against income chargeable under the head Capital Gains. Such loss can be carried forward for a maximum period of 8 assessment years.

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Question 9

M/s. Vivitha & Co., a partnership firm, with four partners A, B, C and D having equal shares, furnishes the following details, summarized from the valid returns of income filed by it:

Assessment year	***Item eligible for carry forward and set off***
2015-16	*Unabsorbed business loss ₹ 1,20,000*
2016-17	*Unabsorbed business loss ₹ 1,90,000*
2016-17	*Unabsorbed depreciation ₹ 1,20,000*
2016-17	*Unabsorbed long-term capital losses:*
	-from shares ₹ 1,10,000; -from building ₹ 1,90,000

C who was a partner during the last three years, retired from the firm with effect from 1.4.2016.

The summarized results of the firm for the assessment year 2017-18 are as under:

Particulars	***₹***
Income from house property	*70,000*
Income from business:	
Speculation	*2,20,000*
Non-speculation	*(-) 50,000*
Capital gains	
Short-term (from sale of shares)	*40,000*
Long-term (from sale of building)	*2,10,000*
Income from other sources	*60,000*

Briefly discuss how the items brought forward from earlier years can be set off in the hands of the firm for the assessment year 2017-18, in the manner most beneficial to the assessee. Also show the items to be carried forward.

Answer

According to section 78(1), where there is a change in the constitution of the firm, the loss relatable to outgoing partner (whether by way of retirement or death) has to be excluded for the purposes of carry forward. However, this provision does not apply in the case of unabsorbed depreciation.

Accordingly, M/s. Vivitha & Co. is entitled to carry forward the losses to the extent given below:

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Item	Loss (₹)	Relatable to C (₹)	Balance eligible for carry forward (₹)
Business loss of A.Y.2015-16	1,20,000	30,000	90,000
Business loss of A.Y.2016-17	1,90,000	47,500	1,42,500
Long term capital loss of A.Y.2016-17	3,00,000	75,000	2,25,000

Set off of items in the hands of M/s. Vivitha & Co. for the A.Y. 2017-18

	Particulars	₹	₹
1.	**Income from house property**		
	Current year income	70,000	
	Less: Brought forward unabsorbed depreciation (See Note 1)	70,000	NIL
2.	**Profits and gains of business or profession**		
	Current year speculative business profits	2,20,000	
	Less: Current year Non-speculation loss set off (See Note 2)	50,000	
		1,70,000	
	Less: Brought forward business losses of earlier year (2015-16 ₹ 90,000 and 2016-17 ₹ 80,000) (See Note 3)	1,70,000	NIL
3.	**Capital gain**		
	Short term (from sale of shares)		40,000
	Long-term (from sale of building)	2,10,000	
	Less: Brought forward long term capital loss of A.Y.2016-17 (See Note 4)	2,10,000	NIL
4.	**Income from other sources**		
	Current year income (before set off)	60,000	
	Less: Brought forward depreciation (See Note 1)	50,000	10,000
	Total Income		**50,000**
	Losses to be carried forward to A.Y. 2018-19		
	Business loss (₹ 1,42,500 - ₹ 80,000)		62,500
	Long term capital loss (₹ 2,25,000 – ₹ 2,10,000)		15,000
	Both these losses relate to A.Y. 2016-17		

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Notes:

(1) Unabsorbed depreciation can be set off against income from any head. Hence, it will be advantageous to set off unabsorbed depreciation against income from house property and income from other sources.

(2) In the current year, non-speculation business loss can be set off against speculation business income.

(3) Brought forward non-speculation business loss can also be set off against speculation business income of current year.

(4) According to section 74, brought forward long-term capital losses shall be set off only against long-term capital gains of current year.

(5) The set-off and carry forward of losses should be most beneficial to the assessee. If brought forward depreciation is set off against current year's business income first, then the quantum of brought forward business loss which can set off against current year's business income will be lower. This will not be beneficial to the assessee.

Question 10

Mr. P, a resident individual, furnishes the following particulars of his income and other details for the previous year 2016-17:

Sl. No.	*Particulars*	*₹*
(i)	*Income from salary*	*18,000*
(ii)	*Net annual value of house property*	*70,000*
(iii)	*Income from business*	*80,000*
(iv)	*Income from speculative business*	*12,000*
(v)	*Long term capital gain on sale of land*	*15,800*
(vi)	*Loss on maintenance of race horse*	*9,000*
(vii)	*Loss on gambling*	*8,000*

Depreciation allowable under the Income-tax Act, 1961, comes to ₹ 8,000, for which no treatment is given above.

The other details of unabsorbed depreciation and brought forward losses (pertaining to A.Y. 2016-17) are:

Sl. No.	*Particulars*	*₹*
(i)	*Unabsorbed depreciation*	*9,000*
(ii)	*Loss from speculative business*	*16,000*
(iii)	*Short term capital loss*	*7,800*

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Compute the gross total income of Mr. P for the Assessment year 2017-18, and the amount of loss that can or cannot be carried forward.

Answer

Computation of Gross Total Income of Mr. P for the A.Y. 2017-18

Particulars	₹	₹
(i) Income from salary		18,000
(ii) Income from House Property		
Net Annual Value	70,000	
Less : Deduction under section 24 (30% of ₹ 70,000)	21,000	49,000
(iii) Income from business and profession		
(a) Income from business	80,000	
Less : Current year depreciation	8,000	
	72,000	
Less : Unabsorbed depreciation	9,000	63,000
(b) Income from speculative business	12,000	
Less : Brought forward loss from speculative business	12,000	Nil
(Balance loss of ₹ 4,000 (i.e. ₹ 16,000 – ₹ 12,000) can be carried forward to the next year)		
(iv) Income from capital gain		
Long term capital gain on sale of land	15,800	
Less : Brought forward short term capital loss	7,800	8,000
Gross total income		**1,38,000**

Amount of loss to be carried forward to the next year

Particulars	₹
Loss from speculative business (to be carried forward as per section 73)	4,000
Loss on maintenance of race horses (to be carried forward as per section 74A)	9,000

Notes :

(i) Loss on gambling can neither be set-off nor be carried forward.

(ii) As per section 74A(3), the loss incurred on maintenance of race horses cannot be set-off against income from any other source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum period of 4 assessment years.

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(iii) Speculative business loss can set off only against income from speculative business of the current year and the balance loss can be carried forward to A.Y. 2018-19. It may be noted that speculative business loss can be carried forward for a maximum of four years as per section 73(4).

Question 11

Ms. Geeta, a resident individual, provides the following details of her income / losses for the year ended 31.3.2017:

(i) Salary received as a partner from a partnership firm ₹ 7,50,000. The same was allowed to the firm.

(ii) Loss on sale of shares listed in BSE ₹ 3,00,000. Shares were held for 15 months and STT paid on sale.

(iii) Long-term capital gain on sale of land ₹ 5,00,000.

(iv) ₹ 51,000 received in cash from friends in party.

(v) ₹ 55,000, received towards dividend on listed equity shares of domestic companies.

(vi) Brought forward business loss of assessment year 2016-17 ₹ 12,50,000.

The return for assessment year 2016-17 was filed in time.

Compute gross total income of Ms. Geeta for the Assessment Year 2017-18 and ascertain the amount of loss that can be carried forward.

Answer

Computation of Gross Total Income of Ms. Geeta for the Assessment Year 2017-18

Particulars		₹
Profits and gains of business and profession		
Salary received as a partner from a partnership firm is taxable under the head "Profits and gains of business and profession"		7,50,000
Less: Brought forward business loss of Assessment Year 2016-17 to be set-off against business income		7,50,000
		Nil
Capital Gains		
Long term capital gain on sale of land (See Note 2)		5,00,000
Income from other sources		
Cash gift received from friends - since the value of cash gift exceeds ₹ 50,000, the entire sum is taxable	51,000	
Dividend received from a domestic company is exempt under section 10(34)	Nil	51,000
Gross Total Income		**5,51,000**

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Notes :

1. Balance brought forward business loss of assessment year 2016-17 of ₹ 5,00,000 has to be carried forward to the next year.
2. Long-term capital loss on sale of shares cannot be set-off against long-term capital gain on sale of land since loss from an exempt source cannot be set-off against profit from a taxable source. Since long-term capital gain on sale of listed shares on which STT is paid is exempt under section 10(38), loss on sale of listed shares is a loss from an exempt source. So, it cannot be set-off against long-term capital gain on sale of land, which is a profit from a taxable source.

Question 12

Mr. Aditya furnishes the following details for the year ended 31-03-2017:

Particulars	Amount (₹)
Loss from speculative business A	*25,000*
Income from speculative business B	*5,000*
Loss from specified business covered under section 35AD	*20,000*
Income from salary	*2,50,000*
Loss from house property	*1,50,000*
Income from trading business	*45,000*
Long-term capital gain from sale of urban land	*2,00,000*
Long-term capital loss on sale of shares (STT not paid)	*75,000*
Long-term capital loss on sale of listed shares in recognized stock exchange (STT paid)	*82,000*

Following are the brought forward losses:

(1) Losses from owning and maintaining of race horses pertaining to A.Y. 2016-17 ₹ 2,000.

(2) Brought forward loss from trading business ₹ 5,000 relating to A.Y.2013-14.

Compute the total income of Mr. Aditya and show the items eligible for carry forward.

Answer

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

Particulars	₹	₹
Salaries		
Income from Salary	2,50,000	
Less: Loss from house property set-off against salary income as per section 71(1)	1,50,000	1,00,000

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Profits and gains of business or profession		
Income from trading business	45,000	
Less: Brought forward loss from trading business of A.Y. 2013-14 can be set off against current year income from trading business as per section 72(1), since the eight year time limit as specified under section 72(3), within which set-off is permitted, has not expired.	5,000	40,000
Income from speculative business B	5,000	
Less: Loss from speculative business A set-off as per section 73(1)	25,000	
Loss from speculative business A to be carried forward to A.Y.2018-19 as per section 73(2)	20,000	
Loss from specified business covered under section 35AD to be carried forward for set-off against income from specified business as per section 73A.	20,000	
Capital Gains		
Long term capital gain on sale of urban land	2,00,000	
Less: Long term capital loss on sale of shares (STT not paid) set-off as per section 74(1)]	75,000	1,25,000
Long-term capital loss of ₹ 82,000 on sale of listed shares on which STT is paid cannot be set-off against long-term capital gain on sale of urban land since loss from an exempt source cannot be set-off against profit from a taxable source.		
Total Income		**2,65,000**

Items eligible for carried forward to A.Y.2018-19

Particulars	₹
Loss from speculative business A Loss from speculative business can be set-off only against profits from any other speculation business. As per section 73(2), balance loss not set-off can be carried forward to the next year for set-off against speculative business income of that year. Such loss can be carried forward for a maximum of four assessment years i.e., upto A.Y.2021-22, in this case, as specified under section 73(4).	20,000
Loss from specified business Loss from specified business under section 35AD can be set-off only against profits of any other specified business. If loss cannot be so set-off, the same has to be carried forward to the subsequent year for set off against income from specified business, if any, in that year. As per section 73A(2), such loss can be	20,000

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carried forward indefinitely for set-off against profits of any specified business .	
Loss from the activity of owning and maintaining race horses Losses from the activity of owning and maintaining race horses (current year or brought forward) can be set-off only against income from the activity of owning and maintaining race horses. If it cannot be so set-off, it has to be carried forward to the next year for set-off against income from the activity of owning and maintaining race horses, if any, in that year. It can be carried forward for a maximum of four assessment years, i.e., upto A.Y.2020-21, in this case as specified under section 74A(3).	2,000

Exercise

1. *In a case where the business is succeeded by inheritance, and the legal heirs constitute themselves as a partnership firm, then -*
   a) *the partnership firm can carry forward and set-off the loss of the predecessor.*
   b) *the partnership firm cannot carry forward and set-off the loss of the predecessor.*
   c) *the loss of the predecessor can be carried forward and set-off only by the individual partners in proportion to the share of profits of the firm.*
2. *According to section 80, no loss which has not been determined in pursuance of a return filed in accordance with the provisions of section 139(3), shall be carried forward. The exceptions to this are -*
   (a) Loss from specified business under section 73A
   (b) *Loss under the head "Capital Gains" and unabsorbed depreciation carried forward under section 32(2)*
   (c) *Loss from house property and unabsorbed depreciation carried forward under section 32(2)*
3. *Section 70 enables set off of losses under one source of income against income from any other source under the same head. The exceptions to this section are -*
   (a) Loss under the head "Capital Gains", Loss from speculative business and loss from the activity of owning and maintaining race horses
   (b) Long-term capital loss, Loss from speculative business and loss from the activity of owning and maintaining race horses
   (c) Short-term capital loss and loss from speculative business
4. *The maximum period for which speculation loss can be carried forward is -*
   (a) 4 years
   (b) 8 years
   (c) indefinitely
5. *Mr. A incurred short-term capital loss of ₹ 10,000 on sale of shares through the National Stock Exchange. Such loss can be set-off -*
   (a) only against short-term capital gains

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   (b) against both short-term capital gains and long-term capital gains

   (c) against any head of income.

6. *Explain the provisions of carry forward and set off of business losses under section 72 of the Income-tax Act, 1961.*

7. *Write short notes on:*

   (a) Loss can be carried forward only by the person who has incurred the loss.

   (b) Carry forward and set off of losses by closely held companies.

8. *Write short notes on -*

   (a) Inter-head adjustment

   (b) Inter-source adjustment.

9. *Discuss the correctness of the following statements -*

   (i) Long term capital loss can be set-off against short-term capital gains arising in that year.

   (ii) Business loss can be set-off against salary income arising in that year.

10. *Discuss briefly on -*

    (a) Carry forward and set-off of losses by closely held companies

    (b) Set-off and carry forward of speculation business loss.

Answers

1. a; **2.** c; **3.** b; **4.** a; **5.** b.

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7 Deductions from Gross Total Income

Key Points			
Deductions in respect of payments			
Section	**Eligible Assessee**	**Eligible Payments**	**Permissible Deduction**
80C	Individual or HUF	**Contribution to PPF, Payment of LIC premium, etc.** Sums paid or deposited in the previous year - Life insurance premium paid - Contribution to PPF, SPF, RPF and superannuation fund - Repayment of housing loan	**₹ 1,50,000**
80CCC	Individual	**Contribution to certain pension funds** Any amount paid or deposited to keep in force a contract for any annuity plan of LIC of India or any other insurer for receiving pension from the fund.	**₹ 1,50,000** Section 80CCE. Maximum permissible deduction under section 80C, 80CCC & 80CCD(1) is ₹1,50,000
80CCD	Individuals employed by the Central Government or any other employer as well as self-employed individuals.	**Contribution to Pension Scheme of Central Government** An individual employed by the Central Government on or after 1.1.2004 or any other employer or any other assessee, being an individual, who has paid or deposited any amount in his account under a notified pension scheme.	In case of a salaried individual, deduction of own contribution under section 80CCD(1) is restricted to 10% of his salary. In any other case, deduction under section 80CCD(1) is restricted to 10% of gross total income.

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			Further, additional deduction of upto ₹ 50,000 is available under section 80CCD(1B). The entire employer's contribution would be included in the salary of the employee. The deduction of employer's contribution under section 80CCD(2) would be restricted to 10% of salary. **However, the limit ₹ 1.50 lakh under section 80CCE does not apply to deduction under section 80CCD(2) and 80CCD(1B).**
80CCG	Resident Individual, being a new retail investor	**Investment made under notified equity savings scheme** Payment made for acquisition of listed equity shares or **listed units of equity oriented fund** by new retail investor in accordance with the scheme notified by the Central Government. For availing this deduction, gross total income of the individual ≤ **₹ 12 lacs**. Minimum lock in period is three years from acquisition date. The fixed lock-in period as per the Rajiv Gandhi Equity Savings Scheme, 2013 is from the date of purchase of eligible securities upto 31st March of the year immediately following the relevant financial year.	50% of the amount invested in such listed equity shares or listed units **(or)** ₹ 25,000, whichever is **lower**. The deduction is available for three consecutive assessment years beginning with the assessment year in which equity shares or units were first acquired.

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<table>
<tr><td>80DD</td><td>Resident Individual or HUF</td><td>Maintenance including medical treatment of a dependent disabled
Any amount incurred for the medical treatment, training and rehabilitation of a dependent disabled
and / or
Any amount paid or deposited under the scheme framed in this behalf by the LIC or any other insurer or Administrator or Specified Company.</td><td>Flat deduction of ₹ 75,000.

In case of severe disability (i.e. person with 80% or more disability) the flat deduction shall be ₹ 1,25,000.</td></tr>
<tr><td>80D</td><td>Individual and HUF</td><td>Medical Insurance Premium
(1) Any premium paid, otherwise than by way of cash, to keep in force an insurance on the health of –
<table><tr><td>in case of an individual</td><td>self, spouse and dependent children</td></tr><tr><td>in case of HUF</td><td>family member</td></tr></table>(2) Contribution to CGHS of such other scheme as notified by Central Government.
(3) Payment, including cash payment, for preventive health check up of himself, spouse, dependent children.
(4) Any premium paid, otherwise than by way of cash, to keep in force an insurance on the health of parents, whether or not dependent on the individual.
(5) Payment, including cash payment, for preventive health check up of parents.</td><td>[(1), (2)] Maximum ₹25,000 (₹ 30,000, in case the individual or his or her spouse is a senior citizen)

plus [(3), (4)/(5)] Maximum ₹ 5,000, in aggregate (subject to the overall individual limits of ₹ 25,000/ ₹ 30,000, as the case may be)

[(4), (5)] Maximum ₹25,000 (₹ 30,000, in case either or both of the parents are senior citizen)</td></tr>
</table>

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<table>
<tr>
<td>80DDB</td>
<td>Resident Individual or HUF</td>
<td>Deduction for medical treatment of specified diseases or ailments
Amount paid for specified diseases or ailment
<table>
<tr><td>In case the assessee is an individual</td><td>For himself or his dependent spouse, children, parents, brothers or sisters</td></tr>
<tr><td>In case the assessee is a HUF</td><td>For any member of his family</td></tr>
</table>
</td>
<td>Actual sum paid or ₹ 40,000 (₹ 60,000, if the payment is for medical treatment of a senior citizen and ₹ 80,000, if the payment is for medical treatment of a very senior citizen), whichever is less,
minus
the amount reimbursed from the insurance company or the employer.</td>
</tr>
<tr>
<td>80E</td>
<td>Individual</td>
<td>Interest on loan taken for higher education
Interest on loan should be taken from any financial institution or approved charitable institution.
Such loan is taken for pursuing his higher education or higher education of his or her relative i.e., spouse or children of the individual.</td>
<td>The deduction is available for interest payment in the initial assessment year (year of commencement of interest payment) and seven assessment years immediately succeeding the initial assessment year
or
until the interest is paid in full by the assessee,
whichever is earlier.</td>
</tr>
<tr>
<td>80EE</td>
<td>Individuals</td>
<td>Additional deduction for interest on loan borrowed for acquisition of self-occupied house property by an individual (over and above the deduction of ₹ 2 lakhs under section 24)</td>
<td>Additional deduction of upto ₹ 50,000 would be allowed in respect of interest on loan taken from a financial institution.
<u>Conditions</u>:
(1) Loan should be sanctioned during P.Y.2016-17
(2) Loan sanctioned ≤ ₹ 35 lakhs
(3) Value of house ≤ ₹ 50 lakhs
(4) The assessee should not own any residential house on the date of sanction of loan.</td>
</tr>
</table>

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<table>
<tr>
<td>80G</td>
<td>All assessees</td>
<td>Donations to certain funds, charitable institutions etc.
Prime Minister’s National Relief Fund,
Prime Minister’s Drought Relief Fund,
National Children’s Fund,
Rajiv Gandhi Foundation,
Government or any approved local authority, institution for promotion of family planning
Certain funds/institutions etc.

Qualifying amount is calculated as follows:
Step 1: Compute adjusted total income, i.e., the gross total income as reduced by the following:
1. Deductions under Chapter VI-A, except under section 80G
2. Short term capital gains taxable under section 111A
3. Long term capital gains taxable under section 112
Step 2: Calculate 10% of adjusted total income.
Step 3: Calculate the actual donation, which is subject to qualifying limit
Step 4: Lower of Step 2 or Step 3 is the maximum permissible deduction.
Step 5: The said deduction is given first for donations qualifying for 100% deduction and thereafter, the balance for donations qualifying for 50% deduction.</td>
<td>There are four categories of deductions –
(1) 100% deduction of amount donated, without any qualifying limit
(2) 50% deduction of amount donated, without any qualifying limit
(3) 100% deduction of amount donated, subject to qualifying limit
(4) 50% deduction of amount donated, subject to qualifying limit.
No deduction shall be allowed for donation in excess of ₹ 10,000, if paid in cash.</td>
</tr>
</table>

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80GG	Individual **not** in receipt of house rent allowance	**Rent paid** Least of the following is allowable as deduction: (1) 25% of total income; (2) Rent paid – 10% of total income (3) ₹ 5,000 p.m.	No deduction if any residential accommodation is owned by the assessee or his spouse or his minor child or his HUF at the place where he ordinarily resides or performs the duties of his office or employment or carries on his business or profession.
80GGB	Indian company	**Contributions to political parties** Any sum contributed by it to a political party or an electoral trust.	Actual contribution (otherwise than by way of **cash**)
80GGC	Any person, other than local authority and an artificial juridical person funded by the Government.	**Contributions to political parties** Amount contributed to a political party or an electoral trust.	Actual contribution (otherwise than by way of **cash**)
Deductions in respect of Certain Incomes			
Section	**Eligible Assessee**	**Eligible Income**	**Permissible Deduction**
80QQB	Resident individual	**Royalty income, etc., of authors of certain books other than text books** Lump sum consideration for assignment or grant of any of his interests in the copyright of any book, being a work of literary, artistic or scientific nature or of royalty or copyright fees	Amount received or receivable or ₹ 3,00,000, whichever is less.
		Royalty or copyright fee received otherwise than by way of lump sum	Maximum 15% of value of books sold

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80RRB	Resident individual, being a patentee	**Royalty on patents** Any income by way of royalty on patents	Whole of such income or ₹ 3,00,000, whichever is less.
80TTA	Individual or a HUF	**Interest on deposits in savings account** Any income by way of interest on deposits in a savings account with a bank, a co-operative society or a post office (not being time deposits, which are repayable on expiry of fixed periods)	Actual interest subject to a maximum of ₹ 10,000.
Other Deductions			
Section	**Eligible Assessee**	**Condition for deduction**	**Permissible Deduction**
80U	Resident Individual	**Deduction in case of a person with disability** Any person, who is certified by the medical authority to be a person with disability.	₹ 75,000, in case of a person with disability. ₹ 1,25,000, in case of a person with severe disability (80% or more disability).

Question 1

Explain how contributions to political parties are deductible in the hands of corporate and non-corporate assessees under the income-tax law.

Answer

Section 80GGB provides for deduction of any sum contributed in the previous year by an Indian company to a political party.

Section 80GGC provides for deduction of any sum contributed by any other person to a political party. However, this deduction will not be available in respect of sum contributed by a local authority and every artificial juridical person, wholly or partly funded by the Government.

It may be noted that cash donations to political parties would not qualify for deduction under section 80GGB and section 80GGC.

Deduction under sections 80GGB and 80GGC would be available in respect of contributions made to a political party registered under section 29A of the Representation of the People Act, 1951.

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Note: For the purpose of section 80GGB, the word "contribute" shall have the same meaning assigned to it under section 293A of the Companies Act, 1956, which provides that –

(a) a donation or subscription or payment given by a company to a person for carrying on any activity which is likely to effect public support for a political party shall also be deemed to be contribution for a political purpose;

(b) the expenditure incurred, directly or indirectly, by a company on advertisement in any publication (being a publication in the nature of a souvenir, brochure, tract, pamphlet or the like) by or on behalf of a political party or for its advantage shall also be deemed to be a contribution to such political party or a contribution for a political purpose to the person publishing it.

However, it may be noted that as per section 37(2B), no allowance shall be allowed in respect of expenses incurred by him on advertisement in any souvenir, brochure, tract or the like published by any political party. It is only after computation of gross total income, contribution to a registered political party is allowed as deduction under section 80GGB to an Indian company.

Question 2

The gross total income of Mr. Nepal for the Assessment Year 2017-18, was ₹ 12,00,000. He has made the following investment/payments during the previous year 2016-17-

	Particulars	*₹*
1.	*L.I.C. premium paid (Policy value ₹ 1,00,000) (taken on 1.03.2012)*	*25,000*
2.	*Contribution to Public Provident Fund (PPF)*	*70,000*
3.	*Repayment of housing loan to Indian Bank*	*50,000*
4.	*Payment made to L.I.C. pension fund*	*20,000*
5.	*Medical insurance premium for self, wife and dependent children.*	*28,000*
6.	*Mediclaim premium for parents (aged over 80 years)*	*32,000*

Compute eligible deduction under Chapter VI-A for the Assessment Year 2017-18.

Answer

Computation of eligible deduction under Chapter - VI A of Mr. Nepal for A.Y. 2017-18

Particulars	₹	₹
Deduction under Section 80C		
LIC premium paid ₹ 25,000	20,000	
[Limited to 20% of policy value, since policy has been taken before 1.04.2012 (20% x ₹ 1,00,000)]		
Contribution to P.P.F.	70,000	
Repayment of housing loan to Indian Bank	50,000	
	1,40,000	

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Deduction under Section 80CCC		
Payment to LIC Pension Fund	20,000	
	1,60,000	
Deduction limited to ₹ 1,50,000 as per section 80CCE		1,50,000
Deduction under Section 80D		
Payment of medical insurance premium ₹ 28,000 for self, wife and dependent children. Deduction limited to ₹ 25,000.	25,000	
Medical insurance premium paid for parents ₹ 32,000 (limited to ₹ 30,000, being the limit applicable for senior citizens)	30,000	55,000
Eligible deduction under Chapter VI A		**2,05,000**

Question 3

Ria, Roma and Raj, three new retail investors, have made the following investments in equity shares/units of equity oriented fund of Rajiv Gandhi equity savings scheme for the previous year 2016-17 as below:

	Ria (₹)	*Roma (₹)*	*Raj (₹)*
Investment in listed equity shares	*50,000*	*23,000*	*-*
Investment in equity oriented funds	*10,000*	*12,000*	*55,000*
Gross total income	*10,80,000*	*11,50,000*	*12,60,000*

Calculate the amount of deduction allowable under section 80CCG in all the three cases for the Assessment Year 2017-18.

What would be the tax treatment in the hands of Raj, if he sells his investments in the Financial Year 2017-18?

Answer

Deduction under section 80CCG is available to:

(i) a new retail investor who complies with the conditions of the Rajiv Gandhi Equity Savings Scheme; and

(ii) whose gross total income for the financial year in which investment is made under the scheme is less than or equal to ₹ 12 lakh.

The question specifies that Ms. Ria, Ms. Roma & Mr. Raj are new retail investors. The gross total income of Ms. Ria and Ms. Roma does not exceed ₹ 12 lakh. Therefore, Ms. Ria and Ms. Roma would be eligible for deduction under section 80CCG. **However, since gross total income of Mr. Raj for the A.Y. 2017-18 exceeds ₹ 12 lakh, he is not eligible for deduction under section 80CCG for that year, even though he is a new retail investor.**

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Computation of deduction under section 80CCG for A. Y. 2017-18

Particulars	Ms. Ria	Ms. Roma
Investment in listed equity shares	50,000	23,000
Investment in units of equity-oriented fund	10,000	12,000
Total Investment in eligible securities	**60,000**	**35,000**
Maximum amount of investment eligible for deduction under section 80CCG [Actual Investment or ₹ 50,000, whichever is lower]	50,000	35,000
Deduction under section 80CCG for A.Y. 2017-18 (50% of above)	25,000	17,500

Tax treatment on sale of investment by Mr. Raj in the Financial Year 2017-18

In the case of Mr. Raj, since no deduction under section 80CCG was allowed to him in the A.Y. 2017-18 on account of his gross total income exceeding ₹ 12 lakh, no amount invested in that year can be subject to tax in A.Y. 2018-19 on account of sale of investments before the expiry of the prescribed time limit.

Question 4

Mr. Chaturvedi having gross total income of ₹ 6,35,000 for the financial year 2016-17 furnishes you the following information:

(i) Deposited ₹ 50,000 in tax saver deposit in the name of major son in a nationalized bank.

(ii) Paid ₹ 25,000 towards premium on life insurance policy of his married daughter (Sum Assured ₹ 2,50,000). The policy was taken on 01.05.2012.

(iii) Contributed ₹ 10,000 to Prime Minister's National Relief Fund.

(iv) Donated ₹ 20,000 to a Government recognized institution for scientific research by a cheque.

Note: *Assume that the gross total income of Mr. Chaturvedi comprises of only income under the head 'Salaries' and 'Income from house property'.*

Compute the total income of Mr. Chaturvedi for the assessment year 2017-18.

Answer

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

Particulars	₹	₹
Gross total income		6,35,000
Less: **Deductions under Chapter VI-A**		
(i) Deposit of ₹ 50,000 in tax saver deposit in the name of major son in a nationalized bank – Fixed deposit in the name of son	-	

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	does not qualify for deduction under section 80C		
(ii)	Premium on life insurance policy of his married daughter – Full amount is eligible for deduction under section 80C (since premium paid does not exceed 10% of sum assured)	25,000	
(iii)	Contribution of ₹ 10,000 to PM's National Relief Fund, eligible for 100% deduction under section 80G	10,000	
(iv)	Payment of ₹ 20,000 to a Government recognized institution for scientific research - Eligible for deduction under section 80GGA since the payment is made by way of cheque	20,000	55,000
Total Income			**5,80,000**

Question 5

State with proper reasons whether the following statements are True/False with regard to the provisions of the Income-tax Act, 1961:

(i) During the financial year 2016-17, Mr. Amit paid interest on loan availed by him for his son's higher education. His son is already employed in a firm. Mr. Amit will get the deduction under section 80E.

(ii) Subscription to notified bonds of NABARD would qualify for deduction under section 80C.

(iii) In order to be eligible to claim deduction under section 80C, investment/contribution/ subscription etc. in eligible or approved modes, should be made from out of income chargeable to tax.

(iv) Where an individual repays a sum of ₹ 30,000 towards principal and ₹ 14,000 as interest in respect of loan taken from a bank for pursuing eligible higher studies, the deduction allowable under section 80E is ₹ 44,000.

(v) Mrs. Sheela, widow of Mr. Satish (who was an employee of M/s. XYZ Ltd.), received ₹ 7 lakhs on 1.5.2016, being amount standing to the credit of Mr. Satish in his NPS Account, in respect of which deduction has been allowed under section 80CCD to Mr. Satish in the earlier previous years. Such amount received by her as a nominee on closure of the account is deemed to be her income for A.Y.2017-18.

Answer

(i) True : The deduction under section 80E available to an individual in respect of interest on loan taken for his higher education or for the higher education of his relative. For this purpose, relative means, *inter alia,* spouse and children of the individual. Therefore, Mr. Amit will get the deduction under section 80E. It is immaterial that his son is already employed in a firm. This would not affect Mr. Amit's eligibility for deduction under section 80E.

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(ii) True : Under section 80C(2) subscription to such bonds issued by NABARD (as the Central Government may notify in the Official Gazette) would qualify for deduction under section 80C.

(iii) False : There is no stipulation under section 80C that the investment, subscription, etc. should be made from out of income chargeable to tax.

(iv) False : Deduction under section 80E is in respect of interest paid on education loan. Hence, the deduction will be limited to ₹ 14,000.

(v) False : A proviso has been inserted in section 80CCD(3) to provide that the amount received by the nominee, on closure of NPS account on the death of the assessee, shall not be deemed to be the income of the nominee.

Question 6

Discuss the allowability of the following:

(i) Rajan has to pay to a hospital for treatment ₹ 62,000 and spent nothing for life insurance or for maintenance of handicapped dependent.

(ii) Raja, a resident Indian, has spent nothing for treatment in the previous year and deposited ₹ 25,000 with LIC for maintenance of handicapped dependant.

(iii) Rajan has incurred ₹ 20,000 for treatment and ₹ 25,000 was deposited with LIC for maintenance of handicapped dependant.

(iv) Payment of ₹ 50,000 by cheque to an electoral trust by an Indian company.

Answer

(i) The deduction of ₹ 75,000 under section 80DD is allowed in full, irrespective of the amount of expenditure incurred or paid by the assessee. If the expenditure is incurred in respect of a dependant with severe disability, the deduction allowable is ₹ 1,25,000.

(ii) The assessee Rajan has deposited ₹ 25,000 for maintenance of handicapped dependent. The assessee is, however, eligible to claim ₹ 75,000 since the deduction of ₹ 75,000 is allowed in full, irrespective of the amount deposited with LIC. In the case of dependant with severe disability, the deduction allowable is ₹ 1,25,000.

(iii) Section 80DD allows a deduction of ₹ 75,000 irrespective of the actual amount spent on maintenance of handicapped dependent and/or actual amount deposited with LIC. Therefore, the deduction will be ₹ 75,000 even though the total amount incurred/deposited is ₹ 45,000. If the dependant is a person with severe disability the quantum of deduction is ₹ 1,25,000.

(iv) Amount paid by an Indian Company to an electoral trust is eligible for deduction under section 80GGB from gross total income, since such payment is made otherwise than by way of cash.

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Question 7

For the Assessment year 2017-18, the Gross Total Income of Mr. Chaturvedi, a resident in India, was ₹ 8,18,240 which includes long-term capital gain of ₹ 2,45,000 and Short-term capital gain of ₹ 58,000. The Gross Total Income also includes interest income of ₹ 12,000 from savings bank deposits with banks. Mr. Chaturvedi has invested in PPF ₹ 1,40,000 and also paid a medical insurance premium ₹ 31,000. Mr. Chaturvedi also contributed ₹ 50,000 to Public Charitable Trust eligible for deduction under section 80G by way of an account payee cheque. Compute the total income and tax thereon of Mr. Chaturvedi, who is 70 years old as on 31.3.2017.

Answer

Computation of total income and tax payable by Mr. Chaturvedi for the A.Y. 2017-18

Particulars	₹	₹
Gross total income including long term capital gain		8,18,240
Less : Long term capital gain		2,45,000
		5,73,240
Less : Deductions under Chapter VI-A:		
Under section 80C in respect of PPF deposit	1,40,000	
Under section 80D (it is assumed that premium of ₹ 31,000 is paid by otherwise than by cash. The deduction would be restricted to ₹ 30,000, since Mr. Chaturvedi is a senior citizen)	30,000	
Under section 80G (See Notes 1 & 2 below)	19,662	
Under section 80TTA (See Note 3 below)	10,000	1,99,662
Total income (excluding long term capital gains)		**3,73,578**
Total income (including long term capital gains)		**6,18,578**
Total income (rounded off)		**6,18,580**
Tax on total income (including long-term capital gains of ₹ 2,45,000)		
LTCG ₹ 2,45,000 x 20%		49,000
Balance total income ₹ 3,73,580		7,358
		56,358
Add: Education cess @2% and Secondary and higher education cess @1%		1,691
Total tax liability		**58,049**
Total tax liability (rounded off)		**58,050**

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Notes :

1. **Computation of deduction under section 80G:**

Particulars	₹
Gross total income (excluding long term capital gains)	5,73,240
Less : Deduction under section 80C, 80D & 80TTA	1,80,000
	3,93,240
10% of the above	39,324
Contribution made	50,000
Lower of the two eligible for deduction under section 80G	39,324
Deduction under section 80G – 50% of ₹ 39,324	**19,662**

2. Deduction under section 80G is allowed only if amount is paid by any mode other than cash, in case of amount exceeding ₹ 10,000. Therefore the contribution made to public charitable trust is eligible for deduction since it is made by way of an account payee cheque.

3. Deduction of upto ₹ 10,000 under section 80TTA is allowed, *inter alia,* to an individual assessee if gross total income includes interest income from deposits in a saving account with bank.

Question 8

Mr. Rajmohan whose gross total income was ₹ 6,40,000 for the financial year 2016-17 furnishes you the following information:

(i) Stamp duty paid on acquisition of residential house (self-occupied) ₹ 50,000.

(ii) Five year time deposit in an account under Post Office Time Deposit Rules, 1981 ₹ 20,000.

(iii) Donation to a recognized charitable trust ₹ 25,000 which is eligible for deduction under section 80G at the applicable rate.

(iv) Interest on loan taken for higher education of spouse paid during the year ₹ 10,000.

Compute the total income of Mr. Rajmohan for the Assessment year 2017-18.

Answer

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

Particulars	₹	₹
Gross Total Income		6,40,000
Less: **Deduction under Chapter VI-A**		
Under section 80C		
Stamp duty paid on acquisition of residential house	50,000	

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Five year time deposit with Post Office	20,000	
	70,000	
Under section 80E		
Interest on loan taken for higher education of spouse, being a relative.	10,000	
Under section 80G (See Note below)		
Donation to recognized charitable trust (50% of ₹ 25,000)	12,500	92,500
Total Income		**5,47,500**

Note: *In case of deduction under section 80G in respect of donation to a charitable trust, the net qualifying amount has to be restricted to 10% of adjusted total income, i.e., gross total income less deductions under Chapter VI-A except 80G. The adjusted total income is, therefore, ₹ 5,60,000 (i.e. 6,40,000 – ₹ 80,000), 10% of which is ₹ 56,000, which is higher than the actual donation of ₹ 25,000. Therefore, the deduction under section 80G would be ₹ 12,500, being 50% of the actual donation of ₹ 25,000.*

Question 9

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

(a) For grant of deduction under section 80-IB, filing of audit report in prescribed form is must for a corporate assessee; filing of return within the due date laid down in section 139(1) is not required.

(b) Filing of belated return under section 139(4) of the Income-tax Act, 1961 will debar an assessee from claiming deduction under section 80-IE.

Answer

(a) False : Section 80AC stipulates compulsory filing of return of income on or before the due date specified under section 139(1), as a pre-condition for availing the benefit of deduction, *inter alia*, under section 80-IB.

(b) True : As per section 80AC, the assessee has to furnish his return of income on or before the due date specified under section 139(1), to be eligible to claim deduction under, *inter alia,* section 80-IE.

Question 10

Can a Primary Co-operative Agricultural and Rural Development Bank claim deduction under section 80P in respect of income derived from the business of banking?

Answer

Sub-section (4) to section 80P provides that the provisions of section 80P shall not apply to any co-operative bank, other than, *inter alia,* a primary co-operative agricultural and rural

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development bank (PCARB). Thus, a PCARB is entitled to claim deduction under section 80P in respect of income derived from the business of banking.

Question 11

Deduction under section 80CCD is available only to individuals employed by the Central Government. Discuss the correctness of this statement.

Answer

The deduction under section 80CCD is available to the individuals employed by the Central Government or any other employer. The deduction is also available to self-employed individuals. Therefore, the statement is incorrect.

Question 12

Mr. Abhik, an individual, made payment of health insurance premium to GIC in an approved scheme. Premium paid on his health is ₹ 20,000 and his spouse's health is ₹ 15,000 during the year 2016-17. He also paid health insurance premium of ₹ 35,000 on his father's health who is a senior citizen and not dependent on him. The payments have not been made by cash. Compute the amount of deduction under section 80D available to Mr. Abhik from his gross total income for the assessment year 2017-18.

Answer

Mr. Abhik will be eligible to claim deduction under section 80D on payment of health insurance premium to GIC in a medical insurance scheme approved by the Central Government. The premium is paid otherwise than by way of cash and hence qualifies for deduction under section 80D. Therefore, the amount of deduction under section 80D would be –

Particulars	₹
On health insurance premium paid on the health of himself and his spouse (₹ 20,000 + ₹ 15,000 = ₹ 35,000, but restricted to ₹ 25,000)	25,000
On health insurance premium paid on the health of his father, ₹ 35,000 but restricted to ₹ 30,000 in the case of a parent, who is a senior citizen (whether dependent or not)	30,000
Total deduction under section 80D	**55,000**

Question 13

Compute the eligible deduction under Chapter VI-A for the Assessment year 2017-18 of Ms. Roma, who has a gross total income of ₹ 15,00,000 for the assessment year 2017-18 and provides the following information about her investments/payments during the year 2016-17:

Sl. No.	*Particulars*	*Amount (₹)*
1.	*Life Insurance premium paid (Policy taken on 01-01-2012 and sum assured is ₹ 1,50,000)*	*35,000*

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2.	*Public Provident Fund contribution*	*1,50,000*
3.	*Repayment of housing loan to Bhartiya Mahila Bank, Bangalore*	*20,000*
4.	*Payment to L.I.C. Pension Fund*	*1,40,000*
5.	*Mediclaim Policy taken for self, wife and dependent children, premium paid*	*30,000*
6.	*Medical Insurance premium paid by cheque for parents (Senior Citizen)*	*32,000*

Answer

Computation of eligible deduction under Chapter VI-A of Ms. Roma for Assessment Year 2017-18

Particulars	₹	₹
Deduction under section 80C		
- Life insurance premium paid ₹ 35,000 (deduction restricted to 20% of the sum assured since the policy was taken before 1.4.2012) ₹ 1,50,000 x 20%	30,000	
- Public Provident Fund	1,50,000	
- Repayment of housing loan to Bhartiya Mahila Bank, Bangalore	20,000	
	2,00,000	
Restricted to a maximum of ₹ 1,50,000	1,50,000	
Deduction under section 80CCC for payment towards LIC pension fund	1,40,000	
	2,90,000	
As per section 80CCE, aggregate deduction under, *inter alia,* section 80C and 80CCC, is restricted to		1,50,000
Deduction under section 80D		
- Payment of medical insurance premium of ₹ 30,000 towards medical policy taken for self, wife and dependent children restricted to	25,000	
- Medical insurance premium paid ₹ 32,000 for parents, being senior citizen, restricted to	30,000	5,000
Eligible deduction under Chapter VI-A		**2,05,000**

Exercise

1. *Mr. Srivastav, aged 72 years, paid medical insurance premium of ₹ 32,000 by cheque and ₹ 4,000 by cash during May, 2016 under a Medical Insurance Scheme of the General Insurance Corporation. The above sum was paid for insurance of his own health. He would be entitled to a deduction under section 80D of a sum of -*

   (a). ₹ 25,000

   (b). ₹ 30,000

   (c). ₹ 20,000

2. *Mr. Ramesh pays a rent of ₹ 5,000 per month. His total income is ₹ 2,80,000 (i.e. Gross Total Income as reduced by deductions under Chapter VI-A except section 80GG). He is also in receipt of HRA. He would be eligible for a deduction under section 80GG of an amount of -*

   (a). ₹ 60,000

   (b). ₹ 32,000

   (c). ₹ 70,000

   (d). Nil

3. *The deduction allowable under section 80LA in respect of eligible income of Offshore Banking Units and International Financial Services Centre is -*

   (a). 50% of such income for 5 consecutive assessment years

   (b). 100% of such income for 10 consecutive assessment years

   (c). 100% of such income for 5 consecutive assessment years and 50% of such income for 5 consecutive assessment years thereafter

4. *The deduction under section 80QQB in respect of royalty income of authors of certain books is subject to a maximum limit of -*

   (a). ₹ 1,00,000

   (b). ₹ 3,00,000

   (c). ₹ 5,00,000

5. *Under section 80GGB, deduction is allowable in respect of contribution to political parties by -*

   (a). any person other than local authority and every artificial juridical person wholly or partly funded by the Government

   (b). Local authority and every artificial juridical person wholly or partly funded by the Government

   (c). An Indian company

6. *₹ 1.5 lakh is the maximum qualifying limit for deduction under -*

   (a). Section 80CCC alone.

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(b). Sections 80C and 80CCC

(c) Sections 80C, 80CCC and 80CCD(1)

7. *Write short notes on -*

   (i) Deduction in respect of royalty income on patents

   (ii) Deduction in respect of royalty income of authors of certain books.

   (iii) Deduction in respect of royalty income on patents.

   (iv) Deduction from Gross Total Income under section 80GG.

8. *What is the deduction available from the gross total income of a company in respect of any contribution given to a political party?*

9. *Who are the assessees eligible to claim deduction under section 80LA? What is the quantum of deduction available under this section? What are the conditions to be fulfilled for claiming such deduction?*

10. *Write briefly about the provisions regarding deductions from gross total income in respect of medical treatment of dependent disabled under section 80DD of the Income-tax Act, 1961 and in respect of medical treatment of assessee himself/dependent under section 80DDB of the Income-tax Act, 1961.*

Answers

1. b; **2.** d; **3.** c; **4.** b; **5.** c; **6.** c

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8 Computation of Total Income and Tax Payable

Steps in computation of total income & tax liability		
Income-tax is a tax levied on the total income of the previous year of every person. The levy of income-tax is, therefore, on the total income of the assessee. The total income has to be computed as per the provisions of the Income-tax Act, 1961 in the following manner -		
(1)	**Ascertain residential status**	• In case of an individual, the number of days of his stay in India during the relevant previous year and/or the earlier previous years would determine his residential status. • An individual/HUF can be either a - ▪ Resident and ordinarily resident ▪ Resident but not ordinarily resident ▪ Non-resident • Persons, other than an individual and HUF, can be either resident or non-resident. An Indian company is resident in India. The determining factor for every other assessee is the place where the control and management of its affairs are situated during that year i.e., whether in India or outside India. • The residential status of a person determines the scope of his taxable income. For example, income which accrues outside India and is received outside India is taxable in the hands of a resident and ordinarily resident but is not taxable in the case of a non-resident.
(2)	**Exclude income which do not form part of total income**	• Exclude income which do not form part of total income, like, agricultural income, dividend income from domestic companies, etc. These income are wholly exempt from tax Certain income are excluded from total income subject to limits, like house rent allowance, leave encashment etc.

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		In such cases, the exempt portion has to be excluded and the remaining amount has to be included under the respective head of income. • Section 10 of the Income-tax Act, 1961 provides for the exclusions from total income.
(3)	**Identify & Group income under the respective head**	• There are five heads of income, namely, - ▪ Salaries, ▪ Income from house property, ▪ Profits and gains of business or profession ▪ Capital Gains ▪ Income from other sources • The income of a person should be identified and grouped under the respective head of income. • Each head of income has a charging section (for example, section 15 for salaries, section 22 for income from house property). • Deeming provisions are also contained under certain heads, by which specific items are sought to be taxed under those heads. For example, if bad debts allowed as deduction in an earlier year is recovered in a subsequent year, then the amount recovered would be deemed as business income of the person in the year of recovery. • The charging section and the deeming provisions would help you to determine the scope of income chargeable under a particular head.
(4)	**Compute the income under each head**	• Assess the income under each head by - ▪ applying the charging and deeming provisions, ▪ excluding the specific exemptions provided for in section 10 relating to that head, subject to the limits specified therein, ▪ allowing the permissible deductions under that head, and ▪ disallowing the non-permissible deductions. • For example, while computing net consideration for capital gains, brokerage is a permissible deduction from gross sale consideration but securities transaction tax paid is not permissible.

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(5)	**Apply clubbing provisions**	• An individual in a higher tax bracket may have a tendency to divert his income to another person who is not subject to tax or who is in a lower tax bracket. For example, an individual may make a fixed deposit in the name of his minor son, so that income from such deposit would accrue to his son, who does not have any other income. • In order to prevent evasion of income-tax by such means, there are specific provisions under the Income-tax Act, 1961 to include the income of one person in the hands of another person, in certain cases. • For example, income of a minor child (say, interest income) is includible in the hands of the parent whose total income is higher before including minor's income. Such interest income will be included in the hands of the parent under the head "Income from other sources" after providing for deduction of up to ₹ 1,500 under section 10(32). • However, if a minor child earns income on account of his or her special skills or talent, like music or dance, then such income is not includible in the hands of the parent.
(6)	**Give effect to the provisions for set-off and carry forward and set-off of losses**	• **Inter-source set-off of losses** ▪ A person may have income from one source and loss from another source under the same head of income. For instance, a person may have profit from wholesale trade of merchandise and loss from the business of plying vehicles. The loss of one business can be set-off against the profits of another business to arrive at the net income under the head "Profits and gains of business or profession". ▪ Set-off of loss from one source against income from another source within the same head of income is permissible, subject to certain exceptions, like long-term capital loss cannot be set-off against short-term capital gains though short-term capital loss can be set-off against long-term capital gains. • **Inter-head set-off of losses** ▪ Likewise, set-off of loss from one head (say, loss from house property) against income from another head (say, Salaries) is also permissible, subject to certain exceptions, like business loss cannot be set-off against salary income.

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- **Carry forward and set-off of losses**
  - Unabsorbed losses of the current year can be carried forward to the next year for set-off only against the respective head of income.
  - Here again, if there are any restrictions relating to inter-source set-off, the same will apply, like long-term capital loss which is carried forward can be set-off only against long-term capital gains and not short-term capital gains of a later year.
  - The maximum number of years up to which any particular loss can be carried forward is also provided under the Act.
- For example, business loss can be carried forward for a maximum of 8 assessment years to be set-off against business income.

</td></tr>
<tr><td>(7)</td><td>Determine the gross total income (GTI)</td><td>

- The income computed under each head, after giving effect to the clubbing provisions and provisions for set-off and carry forward and set-off of losses, have to be aggregated to arrive at the gross total income.
- The process of computing GTI is depicted hereunder -

Add income computed under each head – Apply clubbing provisions – Apply the provisions for set-off and carry forward of losses

</td></tr>
<tr><td>(8)</td><td>Allow deductions permissible from gross total income</td><td>

Certain deductions are allowable from gross total income to arrive at the total income. These deductions contained in Chapter VI-A can be classified as –

- **Deduction in respect of certain payments, for example,**

Section	Nature of Payment/Deposit
80C	Payment of life insurance premium, tuition fees of children, deposit in public provident fund, repayment of housing loan etc.
80D	Medical insurance premium paid by an individual/HUF for the specified persons/ contribution to CGHS etc.
80E	Payment of interest on educational loan taken for self or relative

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• Deduction in respect of certain income, for example,
<table>
<tr><th>Section</th><th>Nature of Income</th></tr>
<tr><td>80QQB</td><td>Royalty income of authors of certain books other than text books</td></tr>
<tr><td>80RRB</td><td>Royalty on patents.</td></tr>
<tr><td>80TTA</td><td>Interest on savings account with a bank, co-op-society and post office.</td></tr>
</table>
• Other Deductions – Deduction under section 80U in case of a person with disability
There are limits in respect of deduction under certain sections. The payment/income are allowable as deduction subject to such limits. For example, the maximum deduction under section 80RRB is ₹ 3 lakhs.
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<td>(9)</td>
<td>Find out the total income</td>
<td>
• The gross total income as reduced by the above deductions under Chapter VI-A is the total income.
Total income = GTI – Deductions under Chapter VI-A
• Tax is calculated on the total income of the assessee.
</td>
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<tr>
<td>(10)</td>
<td>Calculate the tax liability
(apply the rates of tax on the total income)</td>
<td>
• The rates of tax are specified in the Finance Act.
▪ For individuals and HUF, there is a basic exemption limit and slab rate of tax.
▪ Companies and firms are subject to a flat rate of tax, without any basic exemption limit.
▪ The rates of tax have to be applied on the total income to compute the tax liability.
• Rates of tax in respect of certain income are provided under the Income-tax Act, 1961 itself.
For instance, casual income, like lottery income, is chargeable to tax at a flat rate of 30% as per section 115BB and long-term capital gains is chargeable to tax at a flat rate of 20% as per section 112. These are also to be considered while calculating the tax liability.
• Rebate of upto ₹ 5,000 from income-tax is available under section 87A, for resident individuals having total income upto ₹ 5 lakh.
• Surcharge@15% is attracted, if total income exceeds ₹ 1 crore
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- Education cess (EC) @2% of tax liability and Secondary and higher education cess (SHEC)@1% have to be added to arrive at the total tax liability.

Total Tax Liability	=	Tax on total income at applicable rates	+	Surcharge, if total income >₹ 1 crore	+	EC @2%	+	SHEC @1%
			-	Rebate u/s 87A, if total income ≤ ₹ 5 lakh				

</td></tr>
<tr><td>(11)</td><td>Reduce tax deducted at source (TDS) and advance tax to arrive at the net tax liability</td><td>

- Tax is deductible at source at the time of payment of salary, rent, interest, fees for professional services, royalty etc.
- The payer has to deduct tax at source at the rates specified in the respective section, say, tax is deductible@10% in respect of royalty and fees for professional services.
- Such tax deducted at source has to be reduced by the payee to determine his net tax liability.
- The Income-tax Act, 1961 also requires payment of advance tax in instalments during the previous year itself on the basis of estimated income, if the tax payable, after reducing TDS, is ₹ 10,000 or more.
- Both Corporate and non-corporate assessees are required to pay advance tax in four instalments, on or before 15th June, 15th September, 15th December and 15th March of the financial year.
- The advance tax so paid should also be deducted to arrive at the net tax liability.

Net Tax Liability	=	Total tax liability	-	TDS	-	Advance tax paid

</td></tr>
<tr><td>(12)</td><td>Return of Income</td><td>

- Return of income is the form in which an assessee has to fill the particulars relating to his total income and tax liability.
- The net tax liability arrived at after deducting TDS and advance tax, has to be paid on or before the due date of filing of return of income by way of self-assessment tax.

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		• An individual/HUF is required to file a return of income, if his/its total income, before giving effect to the provisions of section 10(38) or Chapter VIA deductions, exceed the basic exemption limit. • A firm or company has to file its return of income, irrespective of whether it earns a profit or incurs loss.

Question 1

Ms. Vaishali, employed in a private sector company, furnishes following information for the year ended 31.03.2017.

Particulars	*₹*
Income from salary (computed)	*3,45,000*
Bank interest (Fixed Deposit)	*15,000*
Tax on non-monetary perquisite paid by employer	*20,000*
Amount contributed by her during the year are given below:	
Contribution to recognized provident fund	*60,000*
Health insurance premium-on self (paid by crossed cheque)	*7,000*
Medical expenditure for dependent sister with disability	*20,000*

Compute the total income of Ms. Vaishali for the assessment year 2017-18.

Answer

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

Particulars	₹	₹
Income from salary (computed)		3,45,000
Income from other sources		
Bank Interest (Fixed Deposit)		15,000
Gross Total Income		**3,60,000**
***Less:* Deductions under Chapter VI-A**		
Section 80C		
Contribution to recognized provident fund	60,000	
Section 80D		
Medical insurance premium (Note -2)	7,000	
Section 80DD		
Medical expenditure for dependent sister with disability (flat deduction irrespective of expenditure incurred)	75,000	1,42,000
Total income		**2,18,000**

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Note:

1. Tax on non-monetary perquisite paid by employer is exempt in the hands of employee under section 10(10CC).
2. Medical insurance premium paid by cheque for self is allowed as deduction under section 80D.

Question 2

Dr. Gurumoorthy, a resident individual at Madurai, aged 50 years is running a clinic. His Income and Expenditure Account for the year ending March 31st 2017 is as under :

	Expenditure	₹		Income	₹
To	Medicine consumed	38,40,000	By	Consultation and Medicalcharges	51,00,000
To	Staff salary	4,25,000			
To	Clinic consumables	1,55,000	By	Income-tax refund (principal ₹ 15,000, interest ₹ 1,500)	16,500
To	Rent paid	1,20,000			
To	Administrative expenses	3,00,000			
To	Donation to IIT Delhi for Research approved under section 35(2AA)	1,00,000	By	Dividend from Indian companies	27,000
			By	Winning from lottery	
To	Net Profit	2,92,500		Net of TDS	35,000
			By	Rent	54,000
		52,32,500			**52,32,500**

(i) Rent paid includes ₹ 36,000 paid by cheque towards rent for his residence.

(ii) Clinic equipments are:

01.04.2016 Opening WDV ₹ 4,50,000

07.02.2017 Acquired (cost) ₹ 1,00,000

(iii) Rent received relates to property let out at Madurai. Gross Annual Value ₹ 54,000. The municipal tax of ₹ 9,000, paid in January 2017 has been included in "administrative expenses".

(iv) Dr. Gurumoorthy availed a loan of ₹ 5,50,000 from a bank for higher education of his daughter. He repaid principal of ₹ 50,000, and interest thereon ₹ 65,000 during the year 2016-17.

(v) He paid ₹ 60,000 as tuition fee to the university for full time education of his son.

From the above, compute the total income of Dr. Gurumoorthy for the A.Y.2017-18.

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Answer

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

	Particulars	₹	₹	₹
I	**Income from house property**			
	Gross Annual Value		54,000	
	Less: Municipal taxes paid		9,000	
	Net Annual Value		**45,000**	
	Less: Deduction under section 24 @30%		13,500	31,500
II	**Income from profession**			
	Net profit as per Income and Expenditure account		2,92,500	
	Less: Items of income to be treated separately			
	(i) Income tax refund (including interest)	16,500		
	(ii) Dividend from Indian companies	27,000		
	(iii) Winning from lottery (net of TDS)	35,000		
	(iv) Rent received	54,000	1,32,500	
			1,60,000	
	Add: **Expenditure debited but not allowable**			
	(i) Rent for his residence	36,000		
	(ii) Municipal tax paid relating to residential house at Madurai included in administrative expenses	9,000	45,000	
			2,05,000	
	Less**: Expenditure allowable but not debited**			
	Depreciation on Clinic equipments u/s 32			
	- on ₹ 4,50,000 @ 15%	67,500		
	- on ₹ 1,00,000 @7.5% (i.e.50% of 15%)	7,500		
		75,000		
	Additional deduction of 100% in respect of amount paid to IIT [since weighted deduction of 200% is available in respect of such payment under section 35(2AA)]	1,00,000	1,75,000	30,000
III	**Income from other sources**			
	Interest on Income-tax refund		1,500	
	Dividend from Indian companies	27,000		
	Less: Exempt under section 10(34)	27,000	Nil	
	Winnings from lottery **(See Note 1)**		50,000	51,500

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	Gross Total Income		**1,13,000**
	Less: Deductions under Chapter VI A:		
	- **Under section 80C**		
	Tuition fee paid to university for full time education of his son	60,000	
	- **Under section 80E**		
	Interest on loan taken for higher education of daughter	65,000	
		1,25,000	
	but restricted to **(See Note 2)**		63,000
	Total income		**50,000**

Notes:

1. Winnings from lottery should be grossed up for the chargeability under the head "Income from other sources". The applicable rate of TDS is 30%. Gross income from lottery, would, therefore, be ₹ 35,000/70% = ₹ 50,000

2. Deduction under Chapter VI-A cannot exceed Gross Total Income. Further, no deduction is allowable from income by way of winning from lottery. Therefore, the maximum deduction allowable would be₹ 63,000.

	₹
Gross Total Income	1,13,000
Less: Winnings from lottery	50,000
Maximum deduction under Chapter VI-A	**63,000**

The total income of ₹ 50,000 would, therefore, represent winnings from lottery taxable at a flat rate of 30%, without any basic exemption limit.

3. Dr. Gurumoorthy is staying in a rented premises in Madurai itself. Hence, he would not be eligible for deduction under section 80GG, since he owns a house in Madurai which he has let out.

Question 3

Ms. Purvi, aged 55 years, is a Chartered Accountant in practice. She maintains her accounts on cash basis. Her Income and Expenditure account for the year ended March 31, 2017reads as follows:

Expenditure	***(₹)***	***Income***	***(₹)***	***(₹)***
Salary to staff	*15,50,000*	*Fees earned:*		
Stipend to articled		*Audit*	*27,88,000*	
assistants	*1,37,000*	*Taxation services*	*15,40,300*	
Incentive to articled		*Consultancy*	*12,70,000*	*55,98,300*

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assistants	*13,000*	*Dividend on shares of Indian companies(Gross)*		*10,524*
Office rent	*12,24,000*			
Printing and stationery	*12,22,000*	*Income from UTI*		*7,600*
Meeting, seminar and Conference	*31,600*	*Honorarium received from various institutions for valuation of answer papers*		*15,800*
Purchase of car	*80,000*			
Repair, maintenance and petrol of car	*4,000*	*Rent received from residential flat let out*		*85,600*
Travelling expenses	*5,25,000*			
Municipal tax paid in respect of house property	*3,000*			
Net Profit	*9,28,224*			
	57,17,824			***57,17,824***

Other Information:

(i) Allowable rate of depreciation on motor car is 15%.

(ii) Value of benefits received from clients during the course of profession is ₹ 10,500.

(iii) Incentives to articled assistants represent amount paid to two articled assistants for passing IPCC Examination at first attempt.

(iv) Repairs and maintenance of car include ₹ 2,000 for the period from 1-10-2016 to 30-09-2017.

(v) Salary include ₹30,000 to a computer specialist in cash for assisting Ms. Purvi in one professional assignment.

(vi) The travelling expenses include expenditure incurred on foreign tour of ₹ 32,000 which was within the RBI norms.

(vii) Medical Insurance Premium on the health of dependent brother and major son dependent on her amounts to ₹5,000 and ₹ 10,000, respectively, paid in cash.

(viii) She invested an amount of ₹ 10,000 in National Saving Certificate.

Compute the total income and tax payable of Ms. Purvi for the assessment year 2017-18.

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Answer

Computation of total income and tax liability of Ms. Purvi for the A.Y. 2017-18

Particulars	₹	₹
Income from house property **(See Working Note 1)**		57,820
Profit and gains of business or profession **(See Working Note 2)**		9,20,200
Income from other sources **(See Working Note 3)**		15,800
Gross Total Income		**9,93,820**
Less: Deductions under Chapter VI-A **(See Working Note 4)**		10,000
Total Income		**9,83,820**
Tax on total income		
Upto ₹ 2,50,000	Nil	
₹ 2,50,001 – ₹ 5,00,000 @10%	25,000	
₹ 5,00,001 - ₹ 9,83,820 @20%	96,764	1,21,764
Add: Education cess @ 2%		2,435
Secondary and higher education cess @ 1%		1,218
Total tax liability		**1,25,417**

Working Notes:

(1) Income from House Property

Particulars	₹	₹
Gross Annual Value under section 23(1)	85,600	
Less: Municipal taxes paid	3,000	
Net Annual Value (NAV)	82,600	
Less: Deduction under section 24 @ 30% of NAV	24,780	57,820

Note - Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent.

(2) Income under the head "Profits & Gains of Business or Profession"

Particulars	₹	₹
Net profit as per Income and Expenditure account		9,28,224
Add: Expenses debited but not allowable		
(i) Salary paid to computer specialist in cash disallowed under section 40A(3), since such cash payment exceeds ₹ 20,000	30,000	

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(ii) Amount paid for purchase of car is not allowable under section 37(1) since it is a capital expenditure	80,000	
(ii) Municipal Taxes paid in respect of residential flat let out	3,000	1,13,000
		10,41,224
Add: Value of benefit received from clients during the course of profession [taxable as business income under section 28(iv)]		10,500
		10,51,724
Less: Income credited but not taxable under this head:		
(i) Dividend on shares of Indian companies	10,524	
(ii) Income from UTI	7,600	
(iii) Honorarium for valuation of answer papers	15,800	
(iv) Rent received from letting out of residential flat	85,600	1,19,524
		9,32,200
Less: Depreciation on motor car @15% (See Note (i) below)		12,000
		9,20,200

Notes :

(i) It has been assumed that the motor car was put to use for more than 180 days during the previous year and hence, full depreciation @ 15% has been provided for under section 32(1)(ii).

***Note**: Alternatively, the question can be solved by assuming that motor car has been put to use for less than 180 days and accordingly, only 50% of depreciation would be allowable as per the second proviso below section 32(1)(ii).*

(ii) Incentive to articled assistants for passing IPCC examination in their first attempt is deductible under section 37(1).

(iii) Repairs and maintenance paid in advance for the period 1.4.2017 to 30.9.2017 i.e. for 6 months amounting to ₹1,000 is allowable since Ms. Purvi is following the cash system of accounting.

(iv) ₹ 32,000 expended on foreign tour is allowable as deduction assuming that it was incurred in connection with her professional work. Since it has already been debited to income and expenditure account, no further adjustment is required.

(3) Income from other sources

Particulars	₹	₹
Dividend on shares of Indian companies	10,524	

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Less: Exempt under section 10(34)	10,524	Nil
Income from UTI	7,600	
Less: Exempt under section 10(35)	7,600	Nil
Honorarium for valuation of answer papers		15,800
		15,800

(4) Deduction under Chapter VI-A :

Particulars	₹
Deduction under section 80C (Investment in NSC)	10,000
Deduction under section 80D (See Notes (i) & (ii) below)	Nil
Total deduction under Chapter VI-A	**10,000**

Notes:

(i) Premium paid to insure the health of brother is not eligible for deduction under section 80D, even though he is a dependent, since brother is not included in the definition of "family" under section 80D.

(ii) Premium paid to insure the health of major son is not eligible for deduction, even though he is a dependent, since payment is made in cash.

Question 4

Calculate the income-tax liability for the assessment year 2017-18 in the following cases:

	Mr. A (age 45)	***Mrs. B (age 62)***	***Mr. C (age 81)***	***Mr. D (age 82)***
Status	*Resident*	*Non-resident*	*Resident*	*Non-resident*
Total income other than long-term capital gain	*2,40,000*	*2,80,000*	*5,90,000*	*4,80,000*
Long-term capital gain	*15,000*	*10,000*	*60,000*	*Nil*
	from sale of vacant site	*from sale of listed shares (STT paid)*	*from sale of agricultural land in rural area*	

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Answer

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

Particulars	**Mr. A (age 45)**	**Mrs. B (age 62)**	**Mr. C (age 81)**	**Mr. D (age 82)**
Residential Status	Resident	Non-resident	Resident	Non-resident
Applicable basic exemption limit	₹ 2,50,000	₹ 2,50,000	₹ 5,00,000	₹ 2,50,000
Asset sold	Vacant site	Listed shares (STT paid)	Rural agricultural land	-
Long-term capital gain (on sale of above asset)	₹ 15,000 [Taxable@20% u/s 112]	₹ 10,000 [exempt u/s 10(38)]	₹ 60,000 (Exempt – not a capital asset)	-
Other income	₹ 2,40,000	₹ 2,80,000	₹ 5,90,000	₹ 4,80,000
Tax liability				
On LTCG (after adjusting Basic Exemption limit)	₹ 1,000	-	-	-
On Other income	₹ Nil	₹ 3,000	₹ 18,000	₹ 23,000
	₹ 1,000	₹ 3,000	₹ 18,000	₹ 23,000
Less: Rebate u/s 87A	₹ 1,000			
	₹ Nil			
Add: Education cess @2% & SHEC @1%	Nil	90	540	690
Total tax liability	**₹ Nil**	**₹ 3,090**	**₹ 18,540**	**₹ 23,690**

Notes:

1. *Since Mrs. B and Mr. D are non-residents, they cannot avail the higher basic exemption limit of ₹ 3,00,000 and ₹ 5,00,000 for persons over the age of 60 years and 80 years, respectively.*
2. *Since Mr. A is a resident whose total income does not exceed ₹ 5 lakhs, he is eligible for rebate of ₹ 5,000 or the actual tax payable, whichever is lower, under section 87A*

Question 5

Mr. Y carries on his own business. An analysis of his trading and profit & loss for the year ended 31-3-2017 revealed the following information :

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(1) The net profit was ₹ 11,20,000.

(2) The following incomes were credited in the profit and loss account:

(a) Dividend from UTI ₹ 22,000.

(b) Interest on debentures ₹ 17,500.

(c) Winnings from races ₹ 15,000.

(3) It was found that some stocks were omitted to be included in both the opening and closing stocks, the value of which were:

Opening stock ₹ 8,000.

Closing stock ₹ 12,000.

(4) ₹ 1,00,000 was debited in the profit and loss account, being contribution to a University approved and notified under section 35(1)(ii).

(5) Salary includes ₹ 20,000 paid to his brother which is unreasonable to the extent of ₹ 2,500.

(6) Advertisement expenses include 15 gift packets of dry fruits costing ₹ 1,000 per packet presented to important customers.

(7) Total expenses on car was ₹ 78,000. The car was used both for business and personal purposes. ¾th is for business purposes.

(8) Miscellaneous expenses included ₹ 30,000 paid to A &Co., a goods transport operator in cash on 31-1-2017for distribution of the company's product to the warehouses.

(9) Depreciation debited in the books was ₹ 55,000. Depreciation allowed as per Income-tax Rules, 1962 was ₹ 50,000.

(10) Drawings ₹ 10,000.

(11) Investment in NSC ₹ 15,000.

Compute the total income of Mr. Y for the assessment year 2017-18.

Answer

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

Particulars	₹
Profits and gains of business or profession ***(See Working Note 1 below)***	10,46,500
Income from other sources ***(See Working Note 2 below)***	32,500
Gross Total Income	**10,79,000**
Less: Deduction under section 80C (Investment in NSC)	15,000
Total Income	**10,64,000**

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Working Notes :

1. Computation of profits and gains of business or profession

Particulars		₹	₹
Net profit as per profit and loss account			11,20,000
Add:	**Expenses debited to profit and loss account but not allowable as deduction**		
	Salary paid to brother disallowed to the extent considered unreasonable [Section 40A(2)]	2,500	
	Motor car expenses attributable to personal use not allowable (₹ 78,000 × ¼)	19,500	
	Depreciation debited in the books of account	55,000	
	Drawings (not allowable since it is personal in nature) **[See Note (iii)]**	10,000	
	Investment in NSC **[See Note (iii)]**	15,000	1,02,000
			12,22,000
Add:	Under statement of closing stock		12,000
			12,34,000
Less:	Under statement of opening stock		8,000
			12,26,000
Less:	Contribution to a University approved and notified under section 35(1)(ii) is eligible for weighted deduction@175%. Since only the actual contribution (100%) has been debited to profit and loss account, the additional 75% has to be deducted.		75,000
			11,51,000
Less:	**Incomes credited to profit and loss account but not taxable as business income**		
	Income from UTI [Exempt under section 10(35)]	22,000	
	Interest on debentures (taxable under the head "Income from other sources")	17,500	
	Winnings from races (taxable under the head "Income from other sources")	15,000	54,500
			10,96,500
Less:	Depreciation allowable under the Income-tax Rules, 1962		50,000
			10,46,500

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Notes :

(i) Advertisement expenses of revenue nature, namely, gift of dry fruits to important customers, is incurred wholly and exclusively for business purposes. Hence, the same is allowable as deduction under section 37.

(ii) Disallowance under section 40A(3) is not attracted in respect of cash payment of ₹ 30,000 to A & Co., a goods transport operator, since, in case of payment made for plying, hiring or leasing goods carriages, an increased limit of ₹ 35,000 is applicable (i.e. payment of upto ₹ 35,000 can be made in cash without attracting disallowance under section 40A(3))

(iii) Since drawings and investment in NSC have been given effect to in the profit and loss account, the same have to be added back to arrive at the business income.

2. Computation of "Income from other sources"

Particulars	₹
Interest on debentures	17,500
Winnings from races	15,000
	32,500

Note:

The following assumptions have been made in the above solution:

1. *The figures of interest on debentures and winnings from races represent the gross income (i.e., amount received plus tax deducted at source).*
2. *In point no. 9 of the question, it has been given that depreciation as per Income-tax Rules, 1962 is ₹ 50,000. It has been assumed that, in the said figure of ₹ 50,000, only the proportional depreciation (i.e., 75% for business purposes) has been included in respect of motor car.*

Question 6

Dr. Shashank is a noted child specialist of Mumbai. His Income and Expenditure account for the financial year ended 31-03-2017 is given below:

Expenditure	***Amount (₹)***	***Income***	***Amount (₹)***
To Staff salary	*12,78,000*	*By Fee receipts*	*56,76,000*
To Administrative expenses	*11,64,000*	*By Winning at TV game*	
To Medicine consumed	*23,95,800*	*show (Net of TDS)*	*35,000*
To Consumables	*57,500*	*By LIC policy matured*	*1,15,000*
To Depreciation	*1,25,000*	*By Honorarium for giving*	
To Rent of clinic	*1,20,000*	*lectures at seminars*	*24,000*

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To Donation to National Children's Fund	*51,000*		
To Excess of income over expenditure	*6,58,700*		
Total	*58,50,000*	*Total*	*58,50,000*

(1) Depreciation computed as per Income-tax Rules, 1962 has been ascertained at ₹ 75,000.

(2) Medicines consumed include cost of medicine for self and family of ₹ 18,000 and for treating poor patients of ₹ 24,000 from whom he did not charge any fee either.

(3) Salary includes ₹ 30,000 paid in cash to a computer specialist who computerized his patient's data on 29th September, 2016 at 3 p.m.

(4) Donation to National Children's Fund has been made by way of account payee cheque.

(5) He has paid a sum of ₹ 25,000 for a Life Insurance Policy (Sum assured ₹ 2,00,000) of himself, which was taken on 1-07-2012.

(6) He also contributed ₹ 1,20,000 towards Public Provident Fund.

(7) Dr. Shashank also paid interest of ₹ 10,000 on loan taken for higher education of his daughter.

(8) Dr. Shashank made investments in equity shares listed in a recognized stock exchange of ₹ 30,000 and units of equity oriented fund of Rajiv Gandhi Equity Savings Scheme of ₹ 40,000.

(9) Dr. Shashank also made donation of ₹ 1,00,000 to a charitable trust registered & eligible for deduction under Income-tax Act, 1961.

You are required to compute the total income and tax payable by Dr. Shashank for the Assessment Year 2017-18.

Answer

Computation of Total income of Dr. Shashank for the Assessment Year 2017-18

Particulars	₹
Profits and gains of business or profession **(Working Note 1)**	6,33,700
Income from other sources **(Working Note 2)**	74,000
Gross Total Income	**7,07,700**
Less: Deduction under Chapter VI-A **(Working Note 3)**	2,52,635
Total Income	**4,55,065**
Total Income (rounded off)	**4,55,070**

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Computation of tax liability of Dr. Shashank for the Assessment Year 2017-18

Particulars	₹
Tax on winnings from TV game show [₹50,000 @ 30%]	15,000
Tax on balance income of ₹ 4,05,070 (₹4,55,070 – ₹ 50,000)	
10% of ₹ 1,55,070 [i.e., ₹ 4,05,070 – ₹ 2,50,000[1] (basic exemption limit)]	15,507
	30,507
Less: Rebate under section 87A (since total income does not exceed ₹ 5,00,000)	5,000
	25,507
Add: Education cess@2% and secondary and higher education cess@1%	765
Total tax liability	26,272
Less: Tax deducted at source	15,000
Net tax liability	**11,272**
Net tax liability (rounded off)	**11,270**

Working Notes:

1. Computation of income under the head "Profits and gains of business or profession"

Particulars	₹	₹
Surplus as per Income and Expenditure Account		6,58,700
Add: **Expenses disallowed**		
Depreciation (₹1,25,000 – ₹75,000)	50,000	
Medicine consumed for self and family (disallowed under section 37, being expenditure of personal nature)	18,000	
Medicine consumed for treating poor patients from whom fees was not charged is an allowable expense, since the same is incurred in the course of carrying on medical profession.	-	
Cash payment of salary disallowed under section 40A(3), since the same is in excess of ₹ 20,000	30,000	
Donation to National Children's Fund (not allowable as deduction while computing income from profession)	51,000	1,49,000
		8,07,700

[1]Assuming that Dr. Shashank is less than 60 years of age as on 31.3.2017

Less: **Income credited to Income and Expenditure Account but not chargeable to income-tax or not chargeable under this head**		
Maturity proceeds of LIC policy [Exempt under section 10(10D)] ***[See Note 2]***	1,15,000	
Winning from TV game show (taxable under the head "Income from other sources")	35,000	
Honorarium for giving lectures at seminars (taxable under the head "Income from other sources")	24,000	1,74,000
Chargeable income from profession		**6,33,700**

2. Computation of income under the head "Income from other sources"

Particulars	₹	₹
Honorarium for giving lectures at seminars		24,000
Winning from TV Game Show (Gross)		50,000
Income from other sources		**74,000**

3. Computation of deduction under Chapter VI-A

Section	Particulars		₹
80C	Life Insurance Premium [₹ 25,000 restricted to 10% of ₹2,00,000 (i.e. sum assured) since the policy is issued on or after 1.4.2012]		20,000
	Contribution to Public Provident Fund		1,20,000
			1,40,000
80CCG	Listed equity shares	₹ 30,000	
	Units of equity oriented fund	₹ 40,000	
	Total investment under Rajiv Gandhi Equity Savings Scheme [See Note 3]	₹ 70,000	
	Maximum deduction – 50% of ₹ 70,000 or ₹ 25,000, whichever is lower		25,000
80E	Interest on loan taken for higher education of daughter		10,000
80G	Donation to National Children's Fund [100% deduction allowable, since it is made by a mode other than cash]	₹ 51,000	

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	Donation to a registered charitable trust [50% of actual contribution of ₹ 1,00,000 or 10% of adjusted total income, whichever is lower] **[See Working Note 4 below]**	₹ 26,635	77,635
Total deduction under Chapter VI-A			**2,52,635**

4. **Deduction under section 80G in respect of donation to charitable trust**

Particulars	₹	₹
Adjusted Total Income		
Gross Total income	7,07,700	
Less: Deductions under Chapter VI-A except under section 80G	1,75,000	
	5,32,700	
10% of Adjusted Total Income (A)		53,270
Actual contribution to charitable trust (B)		1,00,000
Lower of A & B	53,270	
Deduction under section 80G in respect of donation to registered charitable trust [**See Note 1]**		
50% of ₹ 53,270		**26,635**

Notes:

(1) It is assumed that the donation of ₹ 100,000 to the charitable trust is made by any mode other than cash.

(2) The maturity proceeds received under a life insurance policy are wholly exempt from tax under section 10(10D), assuming that the conditions given thereunder are satisfied (i.e., the annual premium does not exceed the specified percentage of actual capital sum assured)

(3) Dr. Sashank is eligible for deduction under section 80CCG since his gross total income does not exceed ₹12 lakh. It is assumed that he is a new retail investor.

Question 7

Mrs. Deepali (aged 40 years), working with M/s Good Company Ltd., a manufacturer of tyres based at Mumbai, has received the following payments during the financial year 2016-17from her employer:

Basic salary *₹ 60,000 per month.*

Dearness allowance *40% of basic salary.*

Her employer has taken on rent her own house on a monthly rent of ₹ 15,000 and the same has been provided for residence of Mrs. Deepali. Company is recovering ₹ 2,000 per month as

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rent of house.

Mrs. Deepali has further furnished the following details:

(i) She has paid professional tax of ₹ 6,000 during financial year 2016-17.

(ii) She is owning only one house and payment of interest of ₹ 1,75,000 and principal of ₹ 1,00,000 was made for housing loan taken for purchase of house.

(iii) She has also taken a loan of ₹ 2,00,000 from her employer for study of her son. SBI rate for such loan is 10%. Her employer has recovered ₹ 10,000 as interest from her salary for such loan during the year.

Compute taxable income and tax liability for assessment year 2017-18.

Answer

Computation of taxable income of Mrs. Deepali for A.Y. 2017-18

Particulars	₹	₹
Income from Salaries		
Basic salary (₹ 60,000 x 12)		7,20,000
Dearness Allowance (40% of basic salary)		2,88,000
Perquisite value of Concessional Accommodation taken on hire. Lower of:	1,08,000	
(i) actual rent (₹ 15,000 x 12) ₹ 1,80,000		
(ii) 15% of salary (15% of ₹ 7,20,000) ₹ 1,08,000		
(assuming that dearness allowance does not form part of pay for retirement benefits)		
Less: Rent recovered (₹ 2,000×12)	24,000	84,000
Perquisite value of concessional loan [Rule 3(7)(i)] [₹ 20,000 (10% of ₹ 2,00,000) –₹ 10,000]		10,000
Gross Salary		**11,02,000**
Less: Deduction under section 16(iii) - Professional tax paid		6,000
Net Salary		**10,96,000**
Income from house property		
Gross Annual Value (GAV) (Rental income has been taken as GAV in the absence of other information)	1,80,000	
Less: Deduction under section 24		
(a) 30% of ₹ 1,80,000 ₹ 54,000		
(b) Interest on loan ₹ 1,75,000	2,29,000	(49,000)
Gross Total Income		**10,47,000**

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Less: **Deductions under Chapter – VIA**		
80C – Repayment of housing loan		1,00,000
Total Income		**9,47,000**

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

Tax on ₹ 9,47,000	**₹**
Upto ₹ 2,50,000	Nil
250,001 -5,00,000 - 10%	25,000
5,00,001 – 9,47,000 - 20%	89,400
	1,14,400
Add: Education cess @ 2%	2,288
Secondary and higher education cess @ 1%	1,144
Total Tax Liability	**1,17,832**
Total Tax Liability (Rounded off)	**1,17,830**

Note: *Mrs. Deepali cannot claim benefit of self-occupation (i.e., taking the annual value as nil and claiming a higher loss of ₹ 2,00,000) in respect of the house property owned and occupied by her, since the same has been given on rent to her employer, who has allotted the same as residence to Mrs. Deepali.*

Question 8

Shri Madan (age 61 years) gifted a building owned by him to his son's wife Smt. Hema on 01.10.2016. The building fetched a rental income of ₹ 10,000 per month throughout the year. Municipal tax for the first half-year of ₹ 5,000 was paid in June 2016and the municipal tax for the second half-year was not paid till 30.09.2017.

Incomes of Shri Madan and Smt. Hema other than income from house property are given below:

Name	*Business income (₹)*	*Capital gain (₹)*	*Other sources (₹)*
Shri Madan	*1,00,000*	*50,000 (long term)*	*1,50,000*
Smt. Hema	*(75,000)*	*2,00,000 (short term)*	*50,000*

Note: Capital gain does not relate to gain from shares and securities.

Compute the total income of Shri. Madan and Smt. Hema taking into account income from property given above and also compute their income-tax liability for the assessment year 2017-18.

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Answer

Computation of total income and tax liability of Shri Madan for A.Y. 2017-18

Particulars	₹	₹
Income from house property (Refer Note 1)		80,500
Business Income		1,00,000
Long-term Capital Gains		50,000
Income from Other Sources		1,50,000
Total Income		**3,80,500**
Computation of tax liability		
Long-term Capital Gain of ₹ 50,000 @ 20%		10,000
Other income of ₹ 3,30,500 (₹ 3,30,500 – ₹ 3,00,000) × 10% (Refer Note 2)		3,050
		13,050
Less: Rebate under section 87A		5,000
		8,050
Add: Education Cess @ 2%	161	
Secondary and Higher Education Cess @ 1%	81	242
Tax liability		**8,292**
Tax liability (Rounded Off)		**8,290**

Computation of total income and tax liability of Smt. Hema for A.Y. 2017-18

Particulars	₹	₹
Short-term Capital Gains	2,00,000	
Less: Business loss	75,000	1,25,000
Income from Other Sources		50,000
Total Income		**1,75,000**
Tax liability (Since total income is less than basic exemption limit of ₹ 2,50,000)		**Nil**

Notes:

1. As per section 64(1)(vi), the income arising to the son's wife of an individual, directly or indirectly, from assets transferred to her, otherwise than for adequate consideration, by such individual, shall be included in the total income of the individual.

   Therefore, the rental income from building transferred by Shri Madan to his son's wife Smt. Hema without consideration on 01.10.2016is includible in the hands of Shri Madan.

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Computation of Income from House Property

Particulars	Madan (₹)	Hema (₹)
	Period (01.04.2016-30.09.2016)	Period (01.10.2016-31.03.2017)
Gross Annual Value (₹ 10,000 × 6 months) (Rental income taken as GAV in the absence of information relating to Municipal Value, fair value and standard rent)	60,000	60,000
Less: Municipal taxes paid (paid in June for first half year only)	5,000	Nil
Net Annual Value (NAV)	55,000	60,000
Less: Deduction under section 24(a), 30% of NAV	16,500	18,000
Income from House Property	38,500	42,000
Income from House Property of Hema to be clubbed in the hands of Madan as per section 64(1)(vi)	42,000	
Income from house property	80,500	

2. The basic exemption limit for A.Y. 2017-18in respect of an individual who is of the age of 60 years or more during the relevant previous year is ₹ 3,00,000. The same has been considered while calculating Madan's tax liability.

Question 9

Mr. Chandran (aged 38) owned 6 heavy goods vehicles as on 01.04.2016. He acquired 2 more heavy goods vehicles on 1.7.2016. He is solely engaged in the business of plying goods vehicles on hire since financial year 2010-11.

He did not opt for presumptive provision contained in section 44AE for the financial year 2015-16. His books were audited under section 44AB and the return of income was filed on 5.8.2016. He has unabsorbed depreciation of ₹ 70,000 and business loss of ₹ 1,00,000 for the financial year 2015-16.

Following further information is provided to you:

(i) Deposited ₹ 20,000 in Tax Saver Deposit with UCO Bank in the name of married son.

(ii) Paid medical insurance premium of ₹ 33,000 for his parents (both aged above 70) by means of bank demand draft.

(iii) Paid premium on life insurance policy of his married daughter ₹ 25,000. The policy was taken on 1.04.2013and the minimum sum assured is ₹ 2,00,000.

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(iv) Repaid principal of ₹ 40,000 and interest of ₹ 15,000 to Canara Bank towards education loan of his daughter, who completed B.E. two years ago. She is employed after completion of her studies.

Assuming that Mr. Chandran has opted for presumptive provision contained in section 44AE of the Income-tax Act, 1961 for F.Y. 2016-17.Compute the total income of Mr. Chandran for the assessment year 2017-18.

Answer

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

Particulars	₹	₹
Income from business of plying goods vehicle (Refer Note 1)		6,75,000
Less: Brought forward business loss of financial year 2015-16 (Refer Note 2 & 3)		1,00,000
Gross Total Income		**5,75,000**
Less: **Deduction under Chapter VI-A**		
Section 80C:-		
Life insurance premium paid for insurance of married daughter (Refer Note 5)	20,000	
Section 80D:-		
Medical insurance premium paid for insurance of parents (Refer Note 6)	30,000	
Section 80E:-		
Interest paid towards education loan taken for studies of his daughter (Refer Note 7)	15,000	65,000
Total Income		**5,10,000**

Working Notes:

(1) **Computation of income from business of plying goods vehicles under section 44AE**

Particulars	₹
6 heavy goods vehicle held throughout the year (₹ 7,500×6×12)	5,40,000
2 heavy goods vehicle – held for 9 months (₹ 7,500×2×9)	1,35,000
Income under section 44AE	6,75,000

(2) As per section 44AE, any deduction allowable under the provisions of sections 30 to 38 shall be deemed to have been already allowed. Therefore, the unabsorbed depreciation of ₹ 70,000 shall not be allowed as a deduction since it is covered by section 32.

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(3) Brought forward business loss of ₹ 1,00,000 shall be allowed as deduction, by virtue of section 72, as it is allowed to be carried forward for 8 assessment years following the assessment year to which it relates, since the return for A.Y. 2016-17was filed before the due date specified under section 139(1).

(4) Fixed deposit in the name of married son does not qualify for deduction under section 80C.

(5) Premium paid for insurance on the life of any child of the individual, whether married or not, qualifies for deduction under section 80C. In respect of policies issued on or after 1.04.2012, only premium paid to the extent of 10% of "minimum capital sum assured" qualifies for deduction under section 80C. Therefore, out of the life insurance premium of ₹ 25,000 paid for insurance policy of married daughter, only ₹ 20,000 (being 10% of ₹ 2,00,000) is allowed as deduction under section 80C.

(6) Deduction is allowed under section 80D for payment made for medical insurance of parents. Medical insurance premium paid for insuring the health of a person who is a senior citizen i.e. of age 60 years or more, qualifies for deduction under section 80D, subject to a maximum of ₹ 30,000. Hence, deduction of ₹ 30,000 is provided to Mr. Chandran, as his parents are senior citizens and the premium is paid otherwise than by way of cash.

(7) It is only the payment of interest on education loan which qualifies for deduction under section 80E. Deduction under section 80E is allowed in respect of interest on loan taken for education of children of the individual even if they are not dependent. Principal repayment of the education loan is not eligible for deduction under section 80E.

Question 10

Mr. Vidyasagar, a resident individual aged 64, is a partner in Oscar Musicals & Co., a partnership firm. He also runs a wholesale business in medical products. The following details are made available for the year ended 31.3.2017:

Sl. No.	*Particulars*	*₹*	*₹*
(i)	*Interest on capital received from Oscar Musicals & Co., at 15%*		*1,50,000*
(ii)	*Interest from bank on fixed deposit (Net of TDS ₹ 1,500)*		*13,500*
(iii)	*Income-tax refund received relating to assessment year 2015-16including interest of ₹ 2,300*		*34,500*
(iv)	*Net profit from wholesale business*		*5,60,000*
	Amounts debited include the following:		
	Depreciation as per books	*34,000*	
	Motor car expenses	*40,000*	
	Municipal taxes for the shop	*7,000*	
	(For two half years; payment for one half year made		

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	on 12.6.2017and for the other on 14.11.2017)		
	Salary to manager by way of a single cash payment	*21,000*	
(v)	*The WDV of the assets (as on 1.4.2016) used in above wholesale business is as under:*		
	Computers	*1,20,000*	
	Motor car (20% used for personal use)	*3,20,000*	
(vi)	*LIP paid for major son*	*60,000*	
	PPF of his wife	*70,000*	

Compute the total income of the assessee for the assessment year 2017-18. The computation should show the proper heads of income. Also compute the WDV of the different blocks of assets as on 31.3.2017.

Answer

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

Particulars	₹	₹
Profits and gains of business or profession		
Income from wholesale business		
Net profit as per books		5,60,000
Add: Depreciation as per books	34,000	
Disallowance of municipal taxes paid for the second half-yearunder section 43B, since the same was paid after the due date of filing of return (₹ 7,000/2)	3,500	
Disallowance under section 40A(3) in respect of salary paid in cash since the same exceeds ₹ 20,000	21,000	
20% of car expenses for personal use	8,000	66,500
		6,26,500
Less: Depreciation allowable (Note 1)		1,10,400
		5,16,100
Income from firm		
Interest on capital from partnership firm (Note 2)		1,20,000
		6,36,100
Income from other sources		
Interest on bank fixed deposit (Gross)	15,000	
Interest on income-tax refund	2,300	17,300
Gross total income		**6,53,400**
Less: Deduction under Chapter VIA (Note 3)		1,30,000
Total Income		**5,23,400**

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Notes:

(1) **Depreciation allowable under the Income-tax Rules, 1962**

		Opening WDV	Rate		Depre-ciation	Closing WDV
Block 1	Computers	1,20,000	60%		72,000	48,000
Block 2	Motor Car	3,20,000	15%	48,000		
	Less: 20% disallowance for personal use			9,600	38,400	2,81,600
					1,10,400	

(2) Only to the extent the interest is allowed as deduction in the hands of the firm, the same is includible as business income in the hands of the partner. Maximum interest allowable as deduction in the hands of the firm is 12% p.a. It is assumed that the partnership deed provides for the same and hence is allowable to this extent in the hands of the firm. Therefore, interest @12% p.a. amounting to ₹ 1,20,000 would be treated as the business income of Mr. Vidyasagar.

(3) **Deduction under Chapter VI-A**

Particulars	₹	₹
Under section 80C		
LIP for major son	60,000	
PPF paid in wife's name	70,000	
	1,30,000	
Since the maximum deduction under section 80C and 80CCE is ₹ 1,50,000, the entire sum of ₹ 1,30,000 would be allowed as deduction		1,30,000
Total deduction		**1,30,000**

Question 11

Balamurugan furnishes the following information for the year ended 31-03-2017:

Particulars	***₹***
Income from business	*(1,35,000)*
Income from house property	*(15,000)*
Lottery winning (Gross)	*5,00,000*
Speculation business income	*1,00,000*
Income by way of salary	*60,000*
Long term capital gain	*70,000*

Compute his total income, tax liability and advance tax obligations.

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Answer

Computation of total income of Balamurugan for the year ended 31.03.2017

Particulars	₹	₹
Salaries	60,000	
Less: Loss from house property	(15,000)	
Net Salary (after set off of loss from house property)		45,000
Profits and gains of business or profession		
Speculation business income	1,00,000	
Less: Business loss set-off	(1,35,000)	
Net business loss to be set-off against long-term capital gain	(35,000)	
Capital Gains		
Long term capital gain	70,000	
Less: Business loss set-off	(35,000)	
Long term capital gain after set off of business loss		35,000
Income from other sources		
Lottery winnings (Gross)		5,00,000
Total Income		**5,80,000**

Computation of tax liability

Particulars	₹
On total income of ₹ 80,000 (excluding lottery winning)	Nil
On lottery winnings of ₹ 5,00,000 @ 30%	1,50,000
Add: Education Cess @ 2% and Secondary and higher education cess@1%	4,500
Total tax liability	**1,54,500**

The assessee need not pay advance tax since the total income (excluding lottery income) liable to tax is below the basic exemption limit. Further, in respect of lottery income, tax would have been deducted at source @ 30% under section 194B.Since the remaining tax liability of ₹ 4,500 (₹ 1,54,500 – ₹ 1,50,000) is less than ₹ 10,000, advance tax liability is not attracted.

Notes:

(1) The basic exemption limit of ₹ 2,50,000 has to be first exhausted against salary income of ₹ 45,000. The unexhausted basic exemption limit of ₹ 2,05,000 can be adjusted against long-term capital gains of ₹ 35,000 as per section 112, but not against lottery winnings which are taxable at a flat rate of 30% under section 115BB.

2. The first proviso to section 234C(1) provides that since it is not possible for the assessee to estimate his income from lotteries, the entire amount of tax payable (after considering TDS) on such income should be paid in the remaining installments of advance tax which

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are due. Where no such installment is due, the entire tax should be paid by 31st March, 2017.The first proviso to section 234C(1) would be attracted only in case of non-deduction or short-deduction of tax at source under section 194B.

Question 12

Mr. Rajiv, aged 50 years, a resident individual and practicing Chartered Accountant, furnishes you the receipts and payments account for the financial year 2016-17.

Receipts and Payments Account

Receipts	*₹*	*Payments*	*₹*
Opening balance (1.4.2016)		*Staff salary, bonus and stipend to articled clerks*	*21,50,000*
Cash on hand and at Bank	*12,000*	*Other administrative expenses*	*11,48,000*
Fee from professional services	*59,38,000*	*Office rent*	*30,000*
		Housing loan repaid to SBI	
Rent	*50,000*	*(includes interest of ₹ 88,000)*	*1,88,000*
Motor car loan from Canara Bank (@ 9% p.a.)	*2,50,000*	*Life insurance premium*	*24,000*
		Motor car (acquired in Jan. 2017)	*4,25,000*
		Medical insurance premium (for self and wife)	*18,000*
		Books bought (annual publications)	*20,000*
		Computer acquired on 1.11.2016(for professional use)	*30,000*
		Domestic drawings	*2,72,000*
		Public provident fund subscription	*20,000*
		Motor car maintenance	*10,000*
		Closing balance (31.3.2017)	*19,15,000*
		Cash on hand and at Bank	
	62,50,000		*62,50,000*

Following further information is given to you:

(1) He occupies 50% of the building for own residence and let out the balance for residential use at a monthly rent of ₹ 5,000. The building was constructed during the year 1997-98, when the housing loan was taken.

(2) Motor car was put to use both for official and personal purpose. One-fifth of the motor car use is for personal purpose. No car loan interest was paid during the year.

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(3) The written down value of assets as on 1-4-2016 are given below:

Furniture & Fittings	*₹ 60,000*
Plant & Machinery (Air-conditioners, Photocopiers, etc.)	*₹ 80,000*
Computers	*₹ 50,000*

Note: Mr. Rajiv follows regularly the cash system of accounting.

Compute the total income of Mr. Rajiv for the assessment year 2017-18.

Answer

Computation of total income of Mr. Rajiv for the assessment year 2017-18

Particulars		₹	₹	₹
Income from house property				
Self-occupied				
Annual value		Nil		
Less: Deduction under section 24(b) Interest on housing loan 50% of ₹ 88,000 = 44,000 but limited to		30,000		
Loss from self occupied property			(30,000)	
Let out property				
Annual value (Rent receivable has been taken as the annual value in the absence of other information)		60,000		
Less: Deductions under section 24				
(a) 30% of Net Annual Value	18,000			
(b) Interest on housing loan (50% of ₹ 88,000)	44,000	62,000	(2,000)	
Loss from house property				(32,000)
Profits and gains of business or profession				
Fees from professional services			59,38,000	
***Less:* Expenses allowable as deduction**				
Staff salary, bonus and stipend		21,50,000		
Other administrative expenses		11,48,000		
Office rent		30,000		
Motor car maintenance (10,000 x 4/5)		8,000		

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Car loan interest – not allowable (since the same has not been paid and the assessee follows cash system of accounting)	Nil	33,36,000	
		26,02,000	
***Less:* Depreciation**			
Motor car ₹ 4,25,000 x 7.5% x 4/5	25,500		
Books being annual publications @ 100%	20,000		
Furniture and fittings @ 10% of ₹ 60,000	6,000		
Plant and machinery @ 15% of ₹ 80,000	12,000		
Computer @ 60% of ₹ 50,000	30,000		
Computer (New) ₹ 30,000 @ 60% x ½ thereon	9,000	1,02,500	24,99,500
Gross Total income			**24,67,500**
***Less:* Deduction under Chapter VI-A**			
Deduction under section 80C			
Housing loan principal repayment	1,00,000		
PPF subscription	20,000		
Life insurance premium	24,000		
Total amount of₹ 1,44,000 is allowed as deduction since it is within the limit of ₹ 1,50,000		1,44,000	
Deduction under section 80D			
Medical insurance premium paid ₹ 18,000		18,000	1,62,000
Total income			**23,05,500**

Question 13

State under which heads the following incomes are taxable:

(i) Rental income in case of dealer in property

(ii) Dividend on shares in case of a dealer in shares

(iii) Salary received by a partner from his partnership firm

(iv) Rental income of machinery

(v) Winnings from lotteries by a person having the same as business activity

(vi) Salaries payable to a Member of Parliament

(vii) Receipts without consideration

(viii) In case of retirement, interest on employee's contribution if provident fund is unrecognized.

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Answer

	Particulars	Head of Income
(i)	Rental income in case of dealer in property	Income from house property
(ii)	Dividend on shares in case of a dealer in shares	Income from other sources
(iii)	Salary by partner from his partnership firm	Profit and gains of business or profession
(iv)	Rental income of machinery **(See Note below)**	Income from other sources/ Profits and gains of business or profession
(v)	Winnings from lotteries by a person having the same as business activity	Income from other sources
(vi)	Salaries payable to a Member of Parliament	Income from other sources
(vii)	Receipts without consideration	Income from other sources
(viii)	In case of retirement, interest on employee's contribution if provident fund is unrecognized	Income from other sources

Note - *As per section 56(2)(ii), rental income of machinery would be chargeable to tax under the head "Income from Other Sources", if the same is not chargeable to income-tax under the head "Profits and gains of business or profession".*

Question 14

Mr. Devansh, an Indian Resident aged 38 years, carries on his own business. He has prepared the following Profit & Loss A/c for the year ending 31-03-2017:

Particulars	***₹***	***Particulars***	***₹***
Salary	*48,000*	*Gross Profit*	*4,30,400*
Advertisement	*24,000*	*Cash Gift (on the occasion of marriage)*	*1,20,000*
Sundry Expenses	*54,500*	*Interest on Debentures (Listed in recognized stock exchange) Net of Taxes*	*5,400*
Fire Insurance (₹10,000 relates to House Property)	*30,000*		
Income-tax	*27,000*		
Household expenses	*42,500*		
Depreciation (allowable)	*23,800*		
Contribution to an University approved and notified U/s. 35(1)(ii)	*1,00,000*		

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Municipal Taxes paid for house property	*36,000*		
Printing & Stationery	*12,000*		
Repairs & Maintenance	*24,000*		
Net Profit	*1,34,000*		
	5,55,800		***5,55,800***

Other information:

(i) Mr. Devansh owns a House Property which is being used by him for the following purposes:

- *25% of the property for own business*
- *25% of the property for self-residence*
- *50% let out for Residential purpose*

(ii) Rent received from 50% let out portion during the year was ₹ 1,65,000.

(iii) On 1-12-2016 he acquired a vacant site from his friend for ₹ 1,05,000. The State Stamp Valuation Authority fixed the value of the site at ₹ 2,80,000 for stamp duty purpose.

(iv) He received interest on Post Office Savings Bank Account amounting to ₹500

(v) Cash gift on the occasion of marriage includes gift of ₹20,000 from non-relatives.

(vi) LIC premium paid (Policy value ₹ 3,00,000 taken on 01-06-2013) ₹ 60,000 for his handicapped son (suffering from disability mentioned in section 80U)

(vii) He purchased 10,000 shares of X Company Ltd on 01-01-2013 for ₹ 1,00,000 and received a 1:1 bonus on 01-01-2014. He sold 5000 bonus shares in September 2016 for ₹ 2,20,000. (Shares are not listed and STT not paid).

Compute the total income and tax payable by Mr. Devansh for the Assessment Year 2017-18.

Answer

Computation of total income and tax liability of Mr. Devansh for A.Y.2017-18

Particulars	Working Note Nos.	₹
Income from house property	1	1,02,900
Profit and gains of business or profession	2	37,600
Long term capital gains	3	2,20,000
Income from other sources	4	1,81,000
Gross Total Income		**5,41,500**
Less: Deduction under Chapter VI-A	5	45,000
Total Income		**4,96,500**

Tax on total income		
Tax on Long term capital gain @20% (Rs. 2,20,000 x 20%)	44,000	
Tax on balance total income of Rs. 2,76,500	2,650	46,650
Less: Rebate under section 87A (since total income does not exceed ₹ 5,00,000)		5,000
		41,650
Add: Education cess @ 2% and SHEC @ 1%		1,250
Total tax liability		42,900
Less: Tax deducted at source on interest on debentures [₹ 5,400 × 10/90]		600
Net Tax liability		**42,300**

Working Notes:

	Particulars	₹	₹
(1)	**Income from House Property**		
(i)	**Self-occupied portion (25%)**		Nil
	As per section 23(2), income from self-occupied portion is Nil.		
(ii)	**Let-out portion – 50%**		
	Gross Annual Value		1,65,000
	(Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent)		
	Less: Municipal taxes paid in respect of let out portion (50% of ₹36,000)		18,000
	Net Annual Value (NAV)		1,47,000
	Less: Deduction under section 24@30% of NAV		44,100
			1,02,900
(2)	**Profits & Gains of Business or Profession**		
	Net profit as per profit and loss account		1,34,000
	Add: Expenses debited to profit and loss account but not allowable		
	(i) Fire Insurance [relating to let-out and self-occupied house property] (75% of ₹10,000)	7,500	
	(ii) Income-tax [disallowed as per section 40(a)(ii)/(iia)]	27,000	
	(iii) Household expenses (Under section 37, personal	42,500	

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		₹	₹
	expenses are disallowed)		
	(iv) Contribution to university approved under section 35(1)(ii), considered separately	1,00,000	
	(v) Municipal Taxes paid in respect of let-out and self-occupied portions [75% of ₹36,000]	27,000	2,04,000
			3,38,000
	Less: Weighted deduction@175% for contribution to university approved and notified under section 35(1)(ii) [1,00,000 × 175%]		1,75,000
			1,63,000
	Less: Income credited to Profit & Loss Account but not taxable under this head:		
	(i) Cash gift	1,20,000	
	(ii) Interest on debentures **(See Note below)**	5,400	1,25,400
			37,600
(3)	**Capital gains**		
	Sale consideration of bonus shares		2,20,000
	Less: Cost of acquisition [Nil, for bonus shares]		Nil
	Long term capital gain [Since unlisted shares are held by Mr. Devansh for more than 24 months]		**2,20,000**
(4)	**Income from Other Sources**		
	Cash gift on the occasion of marriage is exempt, even if the same is received from a non-relative		Nil
	In case of vacant site received for inadequate consideration, difference between stamp duty value (₹2,80,000) and actual consideration (₹1,05,000) is taxable under section 56(2)(vii), since such difference exceeds ₹50,000.		1,75,000
	Interest of ₹500 on post-office savings bank account [In case of individual account, a sum upto ₹3,500 is exempt under section 10(15)]		Nil
	Interest on debentures (gross) [₹ 5,400 × 100/90] (The rate of TDS under section 194A is 10%) **(See Note below)**		6,000
	Income chargeable under this head		**1,81,000**

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(5)	**Deduction under Chapter VI-A :** **Deduction under section 80C** LIC Premium paid ₹60,000 [Since the policy was taken after 31.3.2013 to insure the life of disabled son, the premium is restricted to 15% of sum assured] [15% of ₹ 3,00,000]		45,000

Question 15

Mr. Raghu, Marketing Manager of KL Ltd., based at Mumbai furnishes you the following information for the year ended 31.03.2017:

Basic salary -	*₹ 1,00,000 per month*
Dearness allowance (Forming part of salary for retirement benefits) -	*₹ 50,000 per month*
Bonus -	*2 months basic salary*
Contribution of employer to Recognized Provident Fund -	*15% of basic salary plus dearness allowance*

Rent free unfurnished accommodation was provided by the company at Mumbai (accommodation owned by the company).

	Particulars	***₹***
(i)	*Recognised Provident Fund contribution made by Raghu*	*1,50,000*
(ii)	*Health insurance premium for insurance of his wife's health*	*30,000*
(iii)	*Health insurance premium in respect of parents (senior citizens)*	*33,000*
(iv)	*Medical expenses of dependent brother with 'severe disability' (covered by Section 2(o) of National Trust for Welfare of Persons with Austism, Cerbral Palsy, Mental Retardation and Multiple Disabilities Act, 1999).*	*6,000*
(v)	*Interest on loan taken for education of his son studying B.Com (full-time) in a recognized college.*	*24,000*
(vi)	*Interest on loan taken for education of a student for whom Mr. Raghu is the legal guardian for pursuing B.Sc. (Physics) (full-time) in a recognized university.*	*20,000*

Compute the total income of Mr. Raghu for the assessment year 2017-18.

Answer

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

Particulars	**₹**	**₹**
Basic salary		12,00,000

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Dearness allowance			6,00,000
Bonus			2,00,000
Employer contribution to recognized provident fund in excess of 12% is taxable (3% of ₹ 18,00,000)			54,000
Rent free accommodation @ 15% of ₹ 20 lakh (basic salary + dearness allowance + bonus)			3,00,000
			23,54,000
***Less:* Deductions under Chapter VI-A**			
Section 80C			
Contribution to recognized provident fund₹ 1,50,000		1,50,000	
Section 80D – Health insurance premium			
Wife₹ 30,000 restricted to	25,000		
Parents (Senior Citizens) ₹ 33,000 restricted to	30,000	55,000	
Section 80DD			
Medical treatment of dependent brother with severe disability (flat deduction irrespective of expenditure incurred)		1,25,000	
Section 80E – Interest on loan taken for full-time education of			
-his son studying B.Com.	24,000		
- a student studying B.Sc. for whom he is the legal guardian	20,000	44,000	3,74,000
Total income			**19,80,000**

Question 16

Determine the total income of Mr. Chand from the following information for the Assessment Year 2017-18:

	Particulars	***₹***
(i)	*Interest received on enhanced compensation (It relates to transfer of land in the financial year 2010-11.Out of the above, ₹ 65,000 relates to financial year 2016-17and the balance relate to preceding years)*	*4,00,000*
(ii)	*Business loss relating to discontinued business of the assessment year 2010-11 brought forward and eligible for set off*	*1,50,000*
(iii)	*Current year business income (i.e. financial year 2016-17) (computed)*	*1,10,000*

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Answer

Computation of total income of Mr. Chand for A.Y.2017-18

Particulars	₹	₹
Profits and gains of business or profession		
Current year business income	1,10,000	
Less: Brought forward business loss of discontinued business ₹ 1,50,000 set-off to the extent of current year business income as per section 72	1,10,000	Nil
Income from other sources		
Interest on enhanced compensation taxable on receipt basis under section 56(2)(viii)	4,00,000	
Less: Deduction under section 57(iv) @ 50%	2,00,000	2,00,000
Total Income		**2,00,000**

The unabsorbed business loss of ₹ 40,000 (₹ 1,50,000 – ₹ 1,10,000) of A.Y.2010-11relating to discontinued business will be carried forward for set-off against income from any business in the next year i.e. A.Y.2018-19.

Question 17

Mr. Dinesh Karthik, a resident individual aged 45, furnishes the following information pertaining to the year ended 31.3.2017:

(i) He is a partner in Badrinath & Co. He has received the following amounts from the firm:

Interest on capital at 15% : ₹ 3,00,000

Salary as working partner (at 1% of firm's sales) (allowed fully to the firm): ₹90,000

(ii) He is engaged in a business of manufacturing wheat flour from wheat. The Profit and Loss account pertaining to this business (summarised form) is as under:

To	*₹*	*By*	*₹*
Salaries	*1,20,000*	*Gross profit*	*12,50,000*
Bonus	*48,000*	*Interest on Bank FD*	*45,000*
Car expenses	*50,000*	*(Net of TDS 5,000)*	
Machinery repairs	*2,34,000*	*Agricultural income*	*60,000*
Advance tax	*70,000*	*Pension from LIC*	
Depreciation on:		*Jeevan Dhara*	*24,000*
- *Car*	*3,00,000*		
- *Machinery*	*1,25,000*		

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Net profit	*4,32,000*		
	13,79,000		*13,79,000*

Opening WDV of assets are as under:

Particulars	***₹***
Car	*3,00,000*
Machinery (Used during the year for 170 days)	*6,50,000*
Additions to machinery:	
New purchased on 23.9.2016	*2,00,000*
New purchased on 12.11.2016	*3,00,000*
Old purchased on 12.4.2016	*1,25,000*

(All assets added during the year were put to use immediately after purchase)

Of the total bonus amount, ₹ 15,000 was paid on 11.10.2016.

One-fifth of the car expenses are towards estimated personal use of the assessee.

(iii) In March, 2015, he had sold a house at Chennai. Arrears of rent relating to this house amounting to ₹ 75,000 was received in February, 2017.

(iv) Details of his Savings and Investments are as under:

Particulars	***₹***
Life insurance premium for policy in the name of his major son employed in LMN Ltd. at a salary of ₹ 6 lacs p.a. (Sum assured ₹ 2,00,000) (Policy taken on 1.07.2013)	*30,000*
Contribution to PPF	*70,000*
Medical Insurance premium for his father aged 70, who is not dependent on him	*32,000*

You are required to compute the total income of Mr. Dinesh Karthik for the assessment year 2017-18.

Answer

Computation of total income of Mr. Dinesh Karthik for the A.Y. 2017-18

Particulars		**₹**	**₹**
Income from house property			
Arrears of rent received in respect of the Chennai house taxable under section 25A	Note 2	75,000	
Less: Deduction @ 30%		22,500	52,500

Profits and gains of business or profession			
(a) Own business	Note 3		5,33,250
(b) Income from partnership firm (See Note 1)			
Interest on capital		2,40,000	
[As per section 28(v), chargeable in the hands of the partner only to the extent allowable as deduction in the firm's hand i.e. @12%]			
Salary of working partner		90,000	3,30,000
Income from other sources			
(a) LIC Jeevan Dhara pension		24,000	
(b) Interest from bank FD (gross)		50,000	74,000
Gross Total Income			**9,89,750**
Less: **Deductions under Chapter VIA**			
Section 80C			
Life insurance premium for policy in the name of major son qualifies for deduction even though he is not dependent on the assessee. However, the same has to be restricted to 10% of sum assured i.e. 10% of₹ 2,00,000.	20,000		
Contribution to PPF	70,000	90,000	
Section 80D			
Mediclaim premium for father, a senior citizen	32,000		
(qualifies for deduction, even though the father is not dependent on the assessee)			
Maximum amount allowable		30,000	1,20,000
Total Income			**8,69,750**

Notes:

(1) The income by way of interest on capital and salary of Mr. Dinesh Karthik from the firm, Badrinath & Co., in which he is a partner, to the extent allowed as deduction in the hands of the firm under section 40(b), has to be included in the business income of the partner as per section 28(v). Accordingly, ₹ 3,30,000 [i.e., ₹ 90,000 (salary) + ₹ 2,40,000 (interest@12%)] should be included in his business income.

(2) As per section 25A, any arrears of rent received will be chargeable to tax, after deducting a sum equal to 30% of such arrears, as income from house property in the year of receipt, whether or not the assessee remains the owner of the house property.

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(3) Computation of income from own business

Particulars	₹	₹
Net profit as per profit and loss account		4,32,000
Less: Items credited to profit and loss account not treated as business income		
Interest on bank FD (net of TDS ₹ 5,000)	45,000	
Agricultural income	60,000	
Pension from LIC Jeevan Dhara	24,000	1,29,000
		3,03,000
Add: Items debited to profit and loss account to be disallowed/considered separately		
Advance tax	70,000	
Depreciation:		
Car	3,00,000	
Machinery	1,25,000	
Car expenses disallowed	10,000	5,05,000
		8,08,000
Less: Depreciation (See Working Note below)		2,74,750
Income from own business		**5,33,250**

Working Note:

Computation of depreciation allowable under the Income-tax Act, 1961

Particulars	₹	₹
On Car:		
15% on 3,00,000	45,000	
Less: 1/5th for personal use	9,000	36,000
On Machinery:		
Opening WDV	6,50,000	
Additions during the year (Used for more than 180 days)	3,25,000	
Depreciation at 15% on	9,75,000	1,46,250
Additions during the year (used for less than 180 days)		
Hence, depreciation at 7.5% on	3,00,000	22,500
Total normal depreciation (A)		2,04,750
Where an asset acquired during the year is put to use for less than 180 days, 50% of the rate of depreciation is		

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allowable. This restriction does not apply to assets acquired in an earlier year.		
Additional depreciation		
New machinery		
Used for more than 180 days at 20%₹ 2,00,000	40,000	
Used for less than 180 days at 10%₹ 3,00,000	30,000	
Total additional depreciation (B)		70,000
Total permissible depreciation (A) + (B)		**2,74,750**

Question 18

From the following details, compute the total income of Siddhant of Delhi and tax payable for the A.Y.2017-18:

Particulars	***₹***
Salary including dearness allowance	*3,35,000*
Bonus	*11,000*
Salary of servant provided by the employer	*12,000*
Rent paid by Siddhant for his accommodation	*49,600*
Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	*11,000*

Siddhant purchased a flat in a co-operative housing society in Delhi for ₹ 4,75,000 in April, 2011, which was financed by a loan from Life Insurance Corporation of India of ₹ 1,60,000 @ 15% interest, his own savings of ₹ 65,000 and a deposit from a nationalized bank for ₹ 2,50,000 to whom this flat was given on lease for ten years. The rent payable by the bank was ₹ 3,500 per month. The following particulars are relevant:

(a) Municipal taxes paid by Mr. Siddhant ₹ 4,300 (per annum)

(b) House Insurance ₹ 860

(c) He earned ₹ 2,700 in share speculation business and lost ₹ 4,200 in cotton speculation business.

(d) In the year 2012-13, he had gifted ₹ 30,000 to his wife and ₹ 20,000 to his son who was aged 11. The gifted amounts were advanced to Mr. Rajesh, who was paying interest @ 19% per annum.

(e) Siddhant received a gift of ₹ 25,000 each from four friends.

(f) He contributed ₹ 50,000 to Public Provident Fund.

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Answer

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

Particulars		₹	₹
Salary Income			
Salary including dearness allowance			3,35,000
Bonus			11,000
Value of perquisites:			
(i) Salary of servant		12,000	
(ii) Free gas, electricity and water		11,000	23,000
			3,69,000
Income from house property			
Gross Annual Value (GAV) (Rent receivable is taken as GAV in the absence of other information) (₹ 3,500 × 12)		42,000	
Less: Municipal taxes paid		4,300	
Net Annual Value (NAV)		37,700	
Less: Deductions under section 24			
(i) 30% of NAV	₹ 11,310		
(ii) Interest on loan from LIC @15% of ₹ 1,60,000 [See Note 2]	₹ 24,000	35,310	2,390
Income from speculative business			
Income from share speculation business		2,700	
Less: Loss from cotton speculation business		4,200	
Net Loss		1,500	
Net loss from speculative business has to be carried forward as it cannot be set off against any other head of income.			
Income from Other Sources			
(i) Income on account of interest earned from advancing money gifted to his minor son is includible in the hands of Siddhant as per section 64(1A)		3,800	
Less: Exempt under section 10(32)		1,500	
		2,300	
(ii) Interest income earned from advancing money gifted to wife has to be clubbed with the income of the assessee as per section 64(1)		5,700	

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(iii) Gift received from four friends (taxable under section 56(2)(vii) as the aggregate amount received during the year exceeds ₹ 50,000)	1,00,000	1,08,000
Gross Total Income		**4,79,390**
Less: Deduction under section 80C		
Contribution to Public Provident Fund		50,000
Total Income		**4,29,390**

Particulars	**₹**
Tax on total income	17,939
Less: Rebate under section 87A	5,000
	12,939
Add: Education cess@2%	259
Add: Secondary and higher education cess@1%	129
	13,327
Tax liability (rounded off)	**13,330**

Notes:

(1) It is assumed that the entire loan of ₹ 1,60,000 is outstanding as on 31.3.2017;

(2) Since Siddhant's own flat in a co-operative housing society, which he has rented out to a nationalised bank, is also in Delhi, he is not eligible for deduction under section 80GG in respect of rent paid by him for his accommodation in Delhi, since one of the conditions to be satisfied for claiming deduction under section 80GG is that the assessee should not own any residential accommodation in the same place.

Question 19

Mr. Janak, working as Finance Manager in Thilagam Realty Ltd., Jaipur, retired from the company on 31.10.2016 at the age of 60. The following amounts were received from the employer from 1st April, 2016to 31st October, 2016:

Basic Salary	*₹ 30,000 p.m.*
Dearness Allowance	*₹ 20,000 p.m. (40% reckoned for superannuation benefits)*
Ex-gratia (lump sum)	*₹ 15,000*

In addition to the above –

(i) The company had taken on lease a residential house at Jaipur, paying a lease rent of ₹ 9,000 p.m. Mr. Janak, who was paying to the company ₹ 6,000 p.m. towards aforesaid rent, vacated the said premises on 31.10.2016.

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(ii) The company had also provided to Mr. Janak a cooking range and micro-wave oven owned by it. The original cost of these assets was ₹ 40,000 and the written down value as on 1.4.2016was ₹ 22,000.

(iii) Mr. Janak has two sons. His second son was studying in a school run by the employer-company throughout the financial year 2016-17. The education facility was provided free of cost. The cost of such education in a similar school is ₹ 1,800 p.m.

(iv) The employer-company was contributing ₹ 7,000 p.m. to Central Government Pension Scheme. Mr Janak contributed an equal amount.

(v) Professional tax paid by the employer ₹ 3,000.

(vi) Subsequent to his retirement, Mr. Janak started his own business on 15-11-2016. The results of the said business from 15.11.2016to 31.3.2017were:

(i) Business loss (excluding current depreciation) ₹ 90,000

(ii) Current year's depreciation ₹ 60,000

(vii) Mr. Janak won a prize in a TV game show. He received a sum of ₹ 2,10,000 after deduction of tax at source to the tune of ₹ 90,000.

(viii) Mr. Janak furnishes the under-mentioned data relating to savings, investments and out-goings:

A. Life insurance premium, with a private insurance company ₹ 30,000 for his son and ₹ 20,000 for his married daughter.

B. Medical insurance premium of ₹ 22,000 for himself and ₹ 26,000 for his mother (aged 82), paid by credit card. His mother is however not dependent on him.

You are required to compute the total income of Mr. Janak (showing clearly the computation under various heads of income) and tax payable by him for the assessment year 2017-18.

Answer

Computation of total income of Mr. Janak for A.Y. 2017-18

Particulars	₹	₹
Basic salary (₹ 30,000 x 7)	2,10,000	
Dearness Allowance (₹ 20,000 x 7)	1,40,000	
Ex-gratia	15,000	
Employers' contribution to Central Government Pension Scheme (₹ 7,000 x 7)	49,000	
Professional tax paid by employer	3,000	
Concessional accommodation **(See Notes 1 & 2)**	150	
Value of furniture **(See Note 3)**	2,333	

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Value of concessional educational facility (₹ 1,800 x 7) **(See Note 4)**	12,600	
Gross salary	**4,32,083**	
Less: Deduction under section 16(iii) Professional tax	 3,000	
Net salary		4,29,083
Income from other sources		
Winnings from TV Game Show (₹ 2,10,000 + ₹ 90,000)		3,00,000
Gross Total Income		**7,29,083**
Less: Deductions under Chapter VI-A		
80C Life insurance premium (₹ 30,000 + ₹ 20,000)	50,000	
80CCD(1) **(See Notes 5)**		
Employee's contribution to pension scheme [to be restricted to 10% of salary i.e. 10% of ₹ 2,66,000 (₹ 30,000+₹ 8,000) x 7]	26,600	
Total deduction under section 80C & 80CCD(1)	**76,600**	
80CCD(1B) Additional employee's contribution to pension scheme [49,000 – 26,600]	22,400	
Employer's Contribution to pension scheme (to be restricted to 10% of salary) [Section 80CCD(2)] **[See Note 5]**	26,600	
80D (₹ 22,000 + ₹ 26,000) **(See Note 6)**	48,000	1,73,600
Total Income (see Note 8)		**5,55,483**
Total income (rounded off)		**5,55,480**

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

Particulars	₹	₹
Tax @ 30% on winnings of ₹ 3,00,000 from game show		90,000
Tax on balance income of ₹ 2,55,480 **(The basic exemption limit of ₹ 3,00,000 is applicable since Mr. Janak is of the age of 60 years** during the P.Y. 2016-17**)**		Nil
		90,000
Add: Education cess @ 2%	1,800	
Secondary and higher education cess @ 1%	900	2,700
Total Tax Liability		92,700
Less: TDS		90,000
Net Tax Payable		**2,700**

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Notes:

(1) For computation of perquisite value of concessional accommodation, 40% of dearness allowance (i.e. ₹ 8,000) should be taken into consideration as forming part of salary, since the question clearly mentions that only 40% is to be reckoned for superannuation benefits. Therefore, salary for the purpose of perquisite valuation would be ₹ 2,81,000 [i.e., (₹ 30,000 + ₹ 8,000) x 7 + 15,000].

(2) In a case where the accommodation is taken on lease or rent by the employer and provided to the employee, the value of perquisite would be lower of the actual amount of lease rental paid or payable by the employer [i.e. ₹ 63,000, being 9,000 x 7) and 15% of salary [i.e., ₹ 42,150, being 15% of ₹ 2,81,000]. This value (i.e. ₹ 42,150) would be reduced by the rent paid by the employee(i.e., ₹ 42,000, being 6,000 x 7).

The value of concessional accommodation is ₹ 150 [i.e. ₹ 42,150 – ₹ 42,000].

(3) The value of furniture owned by employer and provided to the employee is 10% p.a. of actual cost which amounts to ₹ 2,333 [i.e. 10% of 40,000 x 7/12].

Therefore, the value of furnished accommodation will be ₹ 2,483 (₹ 150 + ₹ 2,333) provided to the employee.

It is also possible to consider the cooking range and micro-wave oven provided by employer to the employee as a perquisite on account of use of movable assets of the employer by the employee. Even it is so assumed, there would be no change in the answer since in such a case also, the perquisite value is 10% p.a. of actual cost.

(4) In determining the value of perquisite resulting from the provision of free or concessional educational facilities, from a plain reading of the proviso to Rule 3(5), it is apparent that if the cost of education per child exceeds ₹ 1,000 per month, the entire cost will be taken as the value of the perquisite. Accordingly, the full amount of ₹ 1,800 per month is taxable as perquisite. In such a case, the value of the perquisite would be ₹ 12,600 (i.e. ₹ 1,800 × 7).

Note – *An alternate view possible is that only the sum in excess of ₹ 1,000 per month is taxable. In such a case, the value of perquisite would be ₹ 5,600. The gross salary in that case shall be ₹ 4,25,083 and net salary would be ₹ 4,22,083. The total income and tax liability shall accordingly vary.*

(5) The entire employer's contribution to Central Government Pension scheme should be included in salary and deduction under section 80CCD(2) should be restricted to 10% of salary. The employer's contribution to pension scheme would be outside the overall limit of ₹ 1,50,000 stipulated under section 80CCE. Also, the deduction under section 80CCD(1)for the employee's contribution to the pension scheme is restricted to 10% of salary. Salary means basic salary and dearness allowance, if provided in the terms of employment for retirement benefits. The balance ₹22,400 (₹49,000 – 26,600) can be claimed as deduction under section 80CCD(1B).

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(6) The deduction for medical insurance premium of ₹ 26,000 paid for mother is allowable in full under section 80D, as the maximum limit is ₹ 30,000, since his mother is a senior citizen. Therefore, the total deduction under section 80D would be ₹ 22,000 (for self) + ₹ 26,000 (for mother) = ₹ 48,000.

(7) Winnings from TV game show is chargeable at a flat rate of 30% under section 115BB.No loss can be set-off against such income. Therefore, business loss cannot be set-off against such income.

(8) As per section 71(2A), business loss cannot be set-off against salary income. Section 71(2A) provides that where the net result of the computation under the head "Profits and gains of business or profession" is a loss and the assessee has income chargeable under the head "Salaries", the assessee shall not be entitled to have such loss set-off against such income. From a plain reading of the provisions of section 71(2A), it is possible to take a view that even depreciation cannot be set-off against salary income. Therefore, both business loss and current depreciation cannot be set-off against salary income.

(9) Deduction under section 80GG has not been provided in respect of rent paid by Mr. Janak to his employer. Such deduction can be provided, if it is assumed that all conditions mentioned in section 80GG are satisfied.

Question 20

Mr. Mahesh, a production manager working in ABC Ltd., New Delhi, receives the following emoluments during the previous year 2016-17:

	₹		₹
Basic salary	*1,75,000*	*Bonus*	*8,000*
D.A. (not forming part of salary)	*1,40,000*	*Medical allowance*	*5,000*
Commission on extra production	*12,000*	*Special allowance*	*18,000*

Education Allowance (including allowance for hostel expenditure) for two sons who are engineering students at Mumbai - ₹ 16,000.

(i) His employer has provided rent free house to him in New Delhi. The house is owned by the employer.

(ii) Electricity bills paid by ABC Ltd. for him during the previous year are of ₹ 11,500.

(iii) On 2.1.2017, his employer company has given him a CD player for domestic use and a laptop for office and personal use. Ownership of both the assets have not been transferred. The cost of CD player is ₹ 20,000 and that of laptop is ₹ 40,000.

(iv) His investments during the previous year are:

(1) Units of SEBI registered mutual fund ₹ 25,000

(2) PPF ₹ 15,000

(v) He has paid tuition fees of his sons on 17.12.2016of ₹ 60,000.

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(vi) He has deposited ₹ 10,000 in Five Year Time Deposit Scheme in Post Office on 25.3.2017.

(vii) His agricultural income during the year is ₹ 45,000.

(viii) He has received gift of ₹ 25,000 from his grandfather on 10.6.2016.

(ix) He has gifted his car to his wife on 15.5.2016. She has earned income of ₹ 30,000 from the business of hiring the same during the previous year.

Compute the total income and tax payable of Mr. Mahesh for the A.Y. 2017-18.

Answer

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

Particulars	₹
Income from salary (as per note 3)	4,10,052
Business Income (assuming that his wife carries on the business of hiring of cars) [Income of wife from hiring of car clubbed under section 64(1)(iv)]	30,000
Gross Total Income	**4,40,052**
Less: Deduction under section 80C (as per note 5)	1,10,000
Total income	**3,30,052**
Total income (rounded off)	**3,30,050**

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

Step 1	₹	₹
Add: Agricultural income and Non-agricultural income (₹ 45,000 + ₹ 3,30,050)		
Tax on ₹ 3,75,050	**12,505**	
Step 2		
Add: Basic exemption limit to agricultural income (₹ 2,50,000 +₹ 45,000)		
Tax on ₹ 2,95,000	**4,500**	
Step 3		
Tax on non-agricultural income (Tax under step 1 – Tax under step 2) (₹ 12,505 – ₹ 4,500)		8,005
Less: Rebate under section 87A		5,000
		3,005
Add: Education cess @2% and Secondary and higher education cess @ 1%		90
Total tax liability		**3,095**
Rounded off		**3,100**

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Notes:

1. Valuation of rent free house

Particulars	₹
Basic salary	1,75,000
D.A. (not to be considered as it is not forming part of salary)	Nil
Commission on extra production	12,000
Bonus	8,000
Special allowance	18,000
Education allowance (See Note 4)	6,400
Medical allowance	5,000
Salary for the purpose of valuation of rent-free house	**2,24,400**
Value of rent-free house = 15% of ₹ 2,24,400	33,660

2. Valuation of perquisite of CD Player given for use by the employee

Taxable value of this perquisite is 10% p.a. of cost of the CD player w.e.f. 1.1.2017 (i.e. for 90 days)

10% of ₹ 20,000 = 2,000 x 90/366 = ₹ 492

Provision of laptop by the employer is a tax-free perquisite.

3. Income from salary

Particulars	₹	₹
Basic pay		1,75,000
Dearness allowance		1,40,000
Bonus		8,000
Commission		12,000
Special Allowance		18,000
Taxable education allowance (See Note-4 below)		6,400
Medical Allowance		5,000
Total		**3,64,400**
Add : Taxable perquisites :		
1. Rent free accommodation (Note 1)	33,660	
2. Electricity Bill paid by employer	11,500	
3. CD Player given by employer (Note 2)	492	45,652
Taxable salary		**4,10,052**

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4. **Education allowance exempt under section 10(14)**

   Education allowance of ₹ 100 per month per child for a maximum of 2 children plus hostel allowance of ₹ 300 per month per child for a maximum of 2 children is exempt.

   i.e. (₹ 100×2×12) + (₹ 300×2×12) =₹ 2,400+₹ 7,200 = ₹ 9,600

   Therefore, taxable education allowance would be ₹ 16,000 – ₹ 9,600 = ₹ 6,400.

5. **Investments/payments deductible under section 80C**

Particulars	₹
Units of SEBI registered mutual fund	25,000
Investment in PPF	15,000
Investment in 5 year Time Deposit in Post Office	10,000
Tuition fees of children (assumed to be paid to an eligible educational institution – hence qualifies for deduction under section 80C)	60,000
	1,10,000

   The total deduction under section 80C cannot exceed ₹ 1,50,000. This restriction is contained in section 80CCE.

   Therefore, the permissible deduction under section 80C would be ₹ 1,10,000

6. **Taxability of gift received from grandfather**

   Gift from a relative is not taxable under section 56(2)(vii). Grandfather is a relative as per the definition of "relative" given in the *Explanation* to section 56(2)(vii) and hence₹ 25,000, being gift received from grandfather, is not taxable.

Question 21

Rajat is a Chartered Accountant in practice. He maintains his accounts on cash basis. He is a Resident and ordinarily resident in India. His income and expenditure account for the year ended March 31, 2017reads as follows:

Expenditure	₹	*Income*	₹	₹
Salary to staff	*15,25,000*	*Fees earned:*		
Stipend to articled assistants	*3,18,000*	*Audit*	*26,65,800*	
Incentive to articled assistants	*5,000*	*Taxation services*	*14,68,600*	
Office rent	*13,24,000*	*Consultancy*	*13,82,000*	*55,16,400*
Printing and stationery	*6,600*	*Dividend on shares of Indian companies (gross)*		*9,635*
Meeting, seminar and		*Income from Unit Trust of*		

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conference	*10,38,600*	*India*		*6,600*
Repairs, maintenance and petrol of car	*22,400*	*Profit on sale of shares (STT paid)*		*15,620*
Subscription and periodicals	*2,15,000*	*Honorarium received from various institutions for valuation of answer papers*		*16,350*
Postage, telegram and fax	*2,32,500*	*Rent received from residential flat let out*		*84,000*
Depreciation	*29,500*			
Travelling expenses	*55,000*			
Municipal tax paid in respect of house property	*1,000*			
Net profit	*8,76,005*			
	56,48,605			***56,48,605***

Other information:

(i) The total travelling expenses incurred on foreign tour was ₹ 20,000 which was within the RBI norms.

(ii) Incentive to articled assistants represent amount paid to two articled assistants for passing IPCC Examination at first attempt.

(iii) Repairs and maintenance of car includes ₹ 1,600 for the period from 1.10.2016to 30.09.2017.

(iv) Salary include ₹ 30,000 to a computer specialist in cash for assisting Mr. Rajat in one professional assignment.

(v) ₹ 1,500, interest on loan paid to LIC on the security of his Life Insurance Policy and utilised for repair of computer, has been debited to the drawing account of Mr. Rajat.

(vi) Medical Insurance Premium on the health of:

Particulars	***₹***	***Mode of payment***
Self	*10,000*	*By Cheque*
Dependent brother	*5,000*	*By Cheque*
Major son dependent on him	*3,000*	*By Cash*
Married daughter	*2,000*	*By Cheque*
Wife dependent on assessee	*5,000*	*By Cheque*

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(vii) Shares sold were held for 10 months before sale.

(viii) Rajat paid life membership subscription of ₹ 1,000 to Chartered Accountants Benevolent Fund.The amount was debited to his drawings account. The Chartered Accountants Benevolent Fund is an approved fund under section 80G of Income-tax, 1961.

(ix) Depreciation debited to income and expenditure account is as per the rates of Income-tax Rules, 1962.

Compute the total income and tax payable of Rajat for the Assessment year 2017-18.

Answer

Computation of Total Income of Mr. Rajat for Assessment Year 2017-18

Particulars	Working Note Nos.	₹
Income from House Property	1	58,100
Profit and gains of Business or Profession	2	7,73,300
Short-term capital gains	3	15,620
Income from other sources	4	16,350
Gross Total Income		**8,63,370**
Less: Deduction under Chapter VI-A	5	15,500
Total Income		**8,47,870**
Tax on total income		
Total Income		8,47,870
Less: Short-term capital gains **(See Note 9 below)**		15,620
Normal Income		8,32,250
Tax on normal income		91,450
Tax on short-term capital gains @15%		2,343
		93,793
Add: Education cess @ 2% and SHEC @ 1%		2,814
Total tax liability		96,607
Total tax liability (rounded off)		**96,610**

Notes :

(1)	**Income from House Property**	**₹**	**₹**
	Gross Annual Value	84,000	
	Less: Municipal taxes paid by owner	1,000	
	Net Annual Value (NAV)	83,000	
	Less: Deduction under section 24 @ 30% of NAV	24,900	58,100

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	Rent received has been taken as the Gross Annual Value in the absence of other information relating to Municipal Value, Fair Rent and Standard Rent.		
(2)	**Income under the head "Profits & Gains of Business or Profession"**		
	Net profit as per Profit & Loss Account		8,76,005
	Add: Expenses debited to the Profit & Loss Account but not allowable		
	(i) Salary paid to computer specialist in cash disallowed under section 40A(3), since such cash payment exceeds ₹ 20,000	30,000	
	(ii) Municipal Taxes paid in respect of residential flat let out	1,000	31,000
			9,07,005
	Less: Expenses allowable but not debited to profit and loss account		
	Interest paid on loan taken from LIC used for repair of computer		1,500
			9,05,505
	Less: Income credited to Profit & Loss Account but not taxable under this head:		
	(i) Dividend on shares of Indian companies	9,635	
	(ii) Income from UTI	6,600	
	(iii) Profit on sale of shares	15,620	
	(iv) Honorarium for valuation of answer papers	16,350	
	(v) Rent received from letting out of residential flat	84,000	1,32,205
			7,73,300
(3)	**Capital gains:**		
	Short term capital gain on sale of shares		15,620
(4)	**Income from other sources:**		
	Dividend on shares of Indian companies 9,635		
	Less: Exempt under section 10(34) 9,635	Nil	
	Income from UTI 6,600		
	Less: Exempt under section 10(35) 6,600	Nil	
	Honorarium for valuation of answer papers	16,350	16,350
(5)	**Deductions under Chapter VI-A :**		
	Deduction under section 80D (Medical Insurance Premium)		

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	Policy holder	Amount of Premium (₹)	Amt. eligible for deduction (₹)	
	Self	10,000	10,000	
	Dependent brother	5,000	Nil	
	Major son dependent on him	3,000	Nil	
	Married daughter	2,000	Nil	
	Wife dependent on assessee	5,000	5,000	
			15,000	
				15,000
	Deduction under section 80G (Donation)			
	Donation to CA Benevolent Fund (50% of ₹ 1,000)			500
	Total deduction under Chapter VI-A			**15,500**
	Note *– Premium paid to insure the health of brother is not eligible for deduction under section 80D. Premium paid to insure the health of son is not eligible for deduction since payment is made in cash. Premium paid to insure the health of married daughter is not eligible for deduction as she is not dependent on Mr. Rajat.*			

(6) ₹ 20,000 expended on foreign tour is allowable as deduction assuming that it was incurred in connection with his professional work. Therefore, it requires no further treatment.

(7) Incentive to articled assistants passing IPCC examination in their first attempt is deductible under section 37(1).

(8) Repairs and maintenance paid in advance for the period 1.4.2017to 30.9.2017 i.e. for 6 months amounting to ₹ 800 will be allowed since Mr. Rajat is following the cash system of accounting.

(9) Since securities transaction tax has been paid on the shares and the period of holding of these shares is less than 12 months, the profit arising therefrom is a short-term capital gain chargeable to tax at 15% under section 111A.

(10) Since depreciation debited to income and expenditure account is as per the Income-tax Rules, 1962, no adjustment for the same has been made.

Question 22

Dr. Sparsh Kumar is running a clinic. His Income and Expenditure account for the year ending 31st March, 2017 is given below:

Expenditure	***₹***	***Income***	
To Staff Salary	*14,30,000*	*By Fees Receipts*	*52,63,600*
To Consumables	*9,250*	*By Dividend from Indian*	

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				Companies	*9,500*
To	*Medicine consumed*	*23,64,800*	*By*	*Winning from Lotteries(Net of TDS of ₹ 12,000)*	*28,000*
To	*Depreciation*	*91,000*	*By*	*Income-tax refund*	*2,750*
To	*Administrative Expenses*	*11,46,000*			
To	*Donation to Prime Minister's National Relief Fund*	*15,000*			
To	*Excess of Income over expenditure*	*2,47,800*			
	Total	***53,03,850***		***Total***	***53,03,850***

(i) Depreciation in respect of all assets has been ascertained at ₹ 50,000 as per Income-tax Rules,1962.

(ii) Medicines consumed include medicine of (cost) ₹ 16,000 used for his family.

(iii) Fees Receipts include ₹ 14,000 honorarium for valuing medical examination answer books.

(iv) He has also received ₹ 90,000 on account of Agricultural Income which had not been included in the above Income and Expenditure Account.

(v) He has also received ₹ 57,860 on maturity of one LIC Policy, not included in the above Income and Expenditure Account.

(vi) He received ₹ 6,000 per month as salary from a City Care Centre. This has not been included in the 'Fees Receipts' credited to Income and Expenditure Account.

(vii) He has sold land in June, 2016for ₹ 10,00,000 (valuation as per stamp valuation authority ₹ 14,00,000). The land was acquired by him in October, 1999 for ₹ 4,50,000.

(viii) He has paid premium of ₹ 75,000 for another LIC Policy on his life which was taken on 1.04.2013(sum assured ₹ 5,00,000).

(ix) He has paid ₹ 2,500 for purchase of lottery tickets.

(x) Donation to Prime Minister National Relief Fund has been made by way of an account payee cheque.

(xi) He deposited ₹ 1 lakh in PPF.

From the above, compute the income and tax payable of Dr. Sparsh Kumar for the A.Y.2017-18.

Cost Inflation Index: F.Y. 1999-00 – 389; F.Y. 2016-17–1125.

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Answer

Computation of total income and tax liability of Dr. Sparsh Kumar for the A.Y. 2017-18

Particulars	₹
Income from salary (Working Note – 1)	72,000
Income from business (Working Note – 2)	2,65,550
Long-term capital gains (Working Note – 3)	98,586
Income from other sources (Working Note – 4)	54,000
Gross Total Income	**4,90,136**
Less: Deduction under Chapter VI-A (Working Note – 5)	1,65,000
Total Income	**3,25,136**
Tax on total income (Working Note - 6)	25,372
Less: Rebate under section 87A	5,000
	20,372
Add: Education cess @ 2% and SHEC @1%	611
Total tax liability	20,983
Less: Tax deducted at source (TDS)	12,000
Tax payable	**8,983**
Rounded off	**8,980**

Working Notes:

1. **Computation of salary income**

Particulars	₹
Gross Salary (₹ 6,000×12)	72,000
Less: Deduction under section 16	Nil
Net Salary	**72,000**

2. **Computation of income under the head "Profits and gains of business or profession"**

Particulars	₹	₹
Net Income as per Income and Expenditure Account		2,47,800
Add: Expenses disallowed:		
Depreciation (₹ 91,000 –₹ 50,000)	41,000	
Cost of medicine for self-use	16,000	
Donation to Prime Minister's Relief Fund	15,000	72,000
		3,19,800

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Less: Dividend from Indian companies	9,500	
Income-tax refund	2,750	
Winning from Lotteries	28,000	
Honorarium for valuing answer books	14,000	54,250
		2,65,550

3. Computation of Capital Gains

Particulars	₹	₹
Sale consideration	10,00,000	
Valuation as per Stamp Valuation Authority	14,00,000	
(Value to be taken higher of actual sale consideration or valuation adopted for stamp duty purposes as per section 50C)		
Consideration for the purpose of capital gain		**14,00,000**
Less: Cost of acquisition = ₹ 4,50,000x 1125/389		13,01,414
Long term capital gain		**98,586**

4. Computation of income under the head "Income from other sources"

Particulars	₹	₹
Dividend from Indian Companies [Exempt u/s 10(34)]		-
Honorarium for valuing answer books		14,000
Winning from Lotteries (Net)	28,000	
Add: TDS	12,000	40,000
Income from other sources		**54,000**

Note : As per section 58(4), no expense or deduction is allowable in respect of winnings from lotteries.

5. Computation of deduction under Chapter VI-A

Particulars	₹
U/s 80C Life Insurance Premium (maximum 10% of sum assured)	50,000
PPF	1,00,000
	1,50,000
U/s 80G Donation to Prime Minister's Relief Fund [See Note below]	15,000
Total deduction under Chapter VI-A	**1,65,000**

Note –The donation made to the Prime Minister's National Relief Fund qualifies for 100% deduction under section 80G.

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6. **Computation of tax on total income**

Particulars	₹
Tax on agricultural income plus non-agricultural income i.e. tax on ₹ 4,15,136(being ₹ 90,000 + ₹ 3,25,136) [See Note below]	34,372
Less: Tax on agricultural income plus basic exemption limit i.e. tax on ₹ 3,40,000, (being ₹ 90,000 + ₹ 2,50,000)	9,000
Tax on total income	**25,372**

Note : Tax on ₹ 3,25,136 plus agricultural income of ₹ 90,000 is computed hereunder :

Particulars	₹
Tax on long term capital gain	
₹ 98,586 @ 20%	19,717
Tax on winnings from lotteries	
₹ 40,000 @ 30%	12,000
Tax on balance income of ₹ 2,76,550 (₹ 4,15,136 – ₹ 98,586–₹ 40,000)	2,655
	34,372

Note : Agricultural income is exempt from tax. It is considered for rate purpose only.

7. Any sum received under a life insurance policy is wholly exempt from tax under section 10(10D), subject to satisfaction of conditions given thereunder. In this case, it is presumed that all the conditions are satisfied.

Question 23

Dr. Krishna furnishes you the following information:

Income and Expenditure Account for the year ended 31st March 2017

Particulars	*₹*	*Particulars*	*₹*
To Medicines consumed	*42,42,000*	*By Fee receipts*	*58,47,500*
To Staff salary	*11,65,000*	*By Rent*	*27,000*
To Hospital consumables	*47,500*	*By Dividend from Indian companies*	*9,000*
To Rent paid	*60,000*		
To Administrative expenses	*1,23,000*		
To Net Income	*2,46,000*		
	58,83,500		*58,83,500*

(i) Rent paid includes rent for his residential accommodation of ₹ 30,000 (paid by cheque) at Bangalore.

(ii) Hospital equipments (eligible for depreciation @ 15%)

01.04.2016 Opening WDV ₹ 5,00,000

07.12.2016 Acquire (Cost) ₹ 2,00,000

(iii) Medicines consumed include medicines (cost) ₹ 10,000 used for Dr. Krishna's family.

(iv) Rent received – relates to a property situated at Mysore (Gross Annual Value).The municipal tax of₹ 2,000 paid in December, 2016has been included in the "administrative expenses".

(v) He received ₹ 5,000 per month as salary from Full Cure Hospital. This has not been included in the "fee receipts" credited to income and expenditure account.

(vi) He sold a vacant site in July, 2016for ₹ 6,00,000. It was inherited by him from his father in January, 1998.The site was acquired by his father in December, 1990 for ₹ 1,50,000.

(Cost inflation index for F.Y 1990-91: 182; 1997-98: 331 and 2016-17:1125)

Compute Dr. Krishna's taxable income for the year ended 31.03.2017.

Answer

Computation of taxable income of Dr. Krishna for the previous year ended 31.03.2017

Particulars	₹	₹
Income from Salaries		
Salary received @ ₹ 5,000 per month		60,000
Income from house property		
Gross Annual Value	27,000	
Less: Municipal tax	2,000	
Net Annual Value	25,000	
Less: Deduction under section 24 @ 30%	7,500	17,500
Income from business or profession		
Net income as per income & expenditure account	2,46,000	
Add: Rent paid to residence	30,000	
Medicines consumed – personal use	10,000	
Municipal tax relating to let out property included in administrative expenses – disallowed	2,000	
	2,88,000	
Less: Depreciation (See working note 2)	90,000	
Rent credited to income & expenditure account	27,000	
Dividend from Indian companies [Exempt u/s10(34)]	9,000	1,62,000

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Capital Gains (Long term capital gains)		
Sale consideration	6,00,000	
Less: Indexed cost acquisition (₹ 1,50,000 x 1125/331) **(See Note 3)**	5,09,819	90,181
Gross Total income		**3,29,681**
Less: Deduction under Chapter VIA		
Under section 80GG, rent paid would be allowable as a deduction to the extent of the least of the following		
(i) 25% of total income = 25% of ₹ 2,39,500 **(See Note 1)**	59,875	
(ii) Excess of rent paid over 10% of total income (₹ 30,000 -₹ 23,950)	6,050	
(iii) ₹ 5,000 per month	60,000	
Least of the above		6,050
Total Income		**3,23,631**

Note :

1. Deduction under section 80GG is to be made from Gross Total Income. Gross Total Income as defined under section 80B(5) means the total income computed in accordance with the provisions of this Act, before making any deduction under Chapter VI-A. Under section 112(2), Long term capital gains have to be reduced from Gross Total Income and Chapter VI-A deductions should be allowed as if the Gross Total income so reduced were the Gross Total Income of the assessee. Therefore, in this case, for the purpose of allowing deduction u/s 80GG, Gross Total Income = ₹ 3,29,681 – ₹ 90,181 = ₹ 2,39,500.
2. Depreciation on plant & machinery

	₹
On opening WDV of ₹ 5,00,000 @ 15%	75,000
On equipment acquired ₹ 2,00,000 @ 7.5% (50% thereon, since acquired in December)	15,000
	90,000

3. Since the property was acquired by Dr. Krishna through inheritance, the cost of acquisition to him will be the cost to the previous owner. However, indexation will be from the year in which the assessee (i.e., Dr. Krishna in this case) first held the asset i.e. F.Y. 1997-98.

Alternative view: *In the case of CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.), the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.*

As per this view, this indexed cost of acquisition of property would be ₹ 9,27,198.

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Question 24

Mr. Pankaj, aged 58 years, who retired from the services of the Central Government on 30.6.2016, furnishes particulars of his income and other details as under:

- *Salary @ ₹ 6,000 p.m.*
- *Pension @ ₹ 3,000 p.m. for July2016to Nov2016.*
- *On 1.12.2016, he got 1/3rd of his pension commuted for ₹ 1,20,000.*
- *A house plot at Ernakulam sold on 1.2.2017for ₹ 5,00,000 had been purchased by him on 3.11.1979 for ₹ 10,000. The stamp valuation authority had assessed the value of said house plot at ₹ 6,00,000 which was neither disputed by the buyer nor by him. The value of this house plot as on 1.4.1981 was ₹ 15,000 (The cost inflation index for the financial year 2016-17is 1125).*
- *Received interest on bank FDRs of ₹ 72,500, dividend on mutual fund units of ₹ 15,000 and interest on maturity of NSC of ₹ 50,000 out of which an amount of ₹ 40,000 was already disclosed by him on accrual basis in the returns upto assessment year 2016-17.*
- *Investment in purchase of NSC for ₹ 30,000 and payment for mediclaim insurance for self and wife of ₹ 22,500.Made investment in PPF of₹ 80,000.*

Compute the total income of Mr. Pankaj for A.Y. 2017-18.

In the event of Mr. Pankaj being ready to make appropriate investment for availing exemption in respect of capital gain arising from sale of house plot, what will be the amount to be invested and the period within which the same should be invested?

(a) if he wishes to avail exemption under section 54F by constructing a new residential house;

(b) if he wants to avail exemption under section 54EC.

Answer

Computation of total income of Mr. Pankaj for A.Y.2017-18

Particulars	₹
Income from salaries (See Working Note 1)	41,000
Capital gains (See Working Note 2)	4,31,250
Income from other sources (See Working Note 3)	82,500
Gross Total Income	**5,54,750**
Less: Deductions under Chapter VI-A (See Working Note 4)	1,23,500
Total Income	**4,31,250**

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Working Notes:

1. **Income from salaries**

Particulars	₹
Salary for 3 months received from Government of India (₹ 6000 x 3)	18,000
Pension for 5 months from July 2016 to Nov2016 @ ₹ 3000 p.m. (₹ 3000 x 5)	15,000
Pension for 4 months from Dec 2016 to March2017@ ₹ 2,000 p.m.(₹ 2,000 x 4)	8,000
	41,000

Note : Commuted value of pension of ₹ 1,20,000 received from the Central Government is fully exempt under section 10(10A).

2. **Capital gains**

Particulars	₹
Long term capital gains on sale of house plot at Ernakulam on 01.02.2017	
Sale consideration received is ₹ 5,00,000. However, since the value assessed by the stamp valuation authority (i.e. ₹ 6,00,000) is higher than the sale consideration, such value assessed is deemed to be the full value of the consideration received or accruing as a result of such transfer as per section 50C	6,00,000
Less: Indexed cost of acquisition	
₹ 15,000 x1125/100	1,68,750
	4,31,250

3. **Income from other sources**

Particulars	₹	₹
Interest on bank FDRs		72,500
Dividend of ₹ 15,000 on units of Mutual Fund [exempt under section 10(35)]		-
Interest on maturity of NSC	50,000	
Less: Interest already shown on accrual basis in the past returns	40,000	10,000
		82,500

4. **Deductions under Chapter VI-A**

Particulars	₹	₹
Under section 80C		
Purchase of NSC	30,000	

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Investment in PPF	80,000	1,10,000
Under section 80D		
Medical insurance premium paid ₹ 22,500 (assumed to have been paid by cheque)		22,500
		1,32,500
Restricted to Gross total income (excluding Long Term Capital Gains)		**1,23,500**

Investment in approved modes

Section 54F (by constructing a new house)

In order to avail exemption under section 54F by constructing a new residential house, the assessee should construct a residential house within three years from the date of transfer of house plot. To avail the maximum exemption, the entire net consideration received from sale of house plot should be invested. If only part of the net consideration is invested, then proportionate exemption of long term capital gains would be available i.e.

$$\text{Long term capital gain} \times \frac{\text{Amount invested in new residential house}}{\text{Net sale consideration}}$$

Section 54EC

In order to avail maximum exemption under section 54EC, the assessee should invest the entire long-term capital gain arising from transfer of the house plot, i.e. ₹ 4,31,250, within six months from the date of sale of house plot, in bonds of National Highways Authority of India (NHAI) or Rural Electrification Corporation Ltd. (RECL).If only part of the capital gain is invested, then the exemption would be restricted to the amount invested in such bonds.

Question 25

The broad break-up of tax and allied details of Mrs. Rinku, born on 30th March, 1956 are as under:

Particulars	₹
Long-term capital gains on sale of house	*2,00,000*
Short-term capital gains on sale of shares in B Pvt. Ltd.	*30,000*
Prize winning from a T.V. show	*20,000*
Business income	*2,20,000*
Net agricultural income	*40,000*
Mrs. Rinku has paid the following:	
LIC premium of self	*40,000*
LIC premium of husband	*20,000*

Compute the tax payable by Mrs. Rinku for the assessment year 2017-18.

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Answer

Computation of tax payable by Mrs. Rinku for the A.Y.2017-18

	Particulars	**₹**	**₹**
	Step 1		
	Agricultural income and Non-agricultural income (₹ 40,000 + ₹ 4,10,000) [For computation of non-agricultural income, see Note 1 below]	4,50,000	
	Tax on the above income		
(i)	Tax on long-term capital gain of₹ 1,30,000 @ 20% [₹ 2,00,000 –₹ 70,000 (unexhausted basic exemption limit i.e. ₹ 3,00,000 - ₹ 2,30,000)	26,000	
(ii)	Tax on winnings of ₹ 20,000 from a T.V. show @ 30%	6,000	
(iii)	Tax on balance income of ₹ 2,30,000	Nil	32,000
	Total tax on ₹ 4,50,000		**32,000**
	Step 2		
	Basic exemption limit to agricultural income (₹ 3,00,000 + ₹ 40,000)	3,40,000	
	Tax on ₹ 3,40,000		**4,000**
	Step 3		
	Tax on non-agricultural income (Tax under step 1 – Tax under step 2) (₹ 32,000 – ₹ 4,000)		28,000
	Less: Rebate under section 87A		5,000
			23,000
	*Add:*Education cess @ 2%		460
	Add: Secondary and higher education cess @ 1%		230
	Tax payable by Mrs. Rinku		**23,690**

Notes:

1. **Computation of total income of Mrs. Rinku for the A.Y.2017-18**

Particulars	**₹**	**₹**
Business income		2,20,000
Long term capital gains on sale of house		2,00,000
Short term capital gains on sale of shares in B Pvt. Ltd		30,000
Prize winnings from a T.V. show		20,000

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Gross Total Income		**4,70,000**
Less: **Deduction under section 80C**		
Life insurance premium of self	40,000	
Life insurance premium of husband	20,000	60,000
Total Income		**4,10,000**

2. Mrs. Rinku turns60years of age on 30.03.2017 Therefore, she is a senior citizen for the P.Y. 2016-17 and is entitled to the higher basic exemption limit of ₹ 3,00,000.

3. Short-term capital gains on sale of shares in B Pvt. Ltd. is taxable at normal rates.

Question 26

Ramdin working as Manager (Sales) with Frozen Foods Ltd., provides the following information for the year ended 31.03.2017:

– *Basic Salary*	*₹ 15,000 p.m.*
– *DA (50% of it is meant for retirement benefits)*	*₹ 12,000 p.m.*
– *Commission as a percentage of turnover of the Company*	*0.5 %*
– *Turnover of the Company*	*₹ 50 lacs*
– *Bonus*	*₹ 50,000*
– *Gratuity*	*₹ 30,000*
– *Own Contribution to R.P.F.*	*₹ 30,000*
– *Employer's contribution to R.P.F.*	*20% of basic salary*
– *Interest credited in the R.P.F. account @ 15% p.a..*	*₹ 15,000*

- *Gold Ring worth ₹ 10,000 was given by employer on his 25th wedding anniversary.*
- *Music System purchased on 01.04.2016by the company for ₹ 85,000 and was given to him for personal use.*
- *Two old heavy goods vehicles owned by him were leased to a transport company against the fixed charges of ₹ 6,500 p.m. Books of account are not maintained.*
- *Received interest of ₹ 5,860 on bank FDRs, dividend of ₹ 1,260 from shares of Indian Companies and interest of ₹ 7,540 from the debentures of Indian Companies.*
- *Made payment by cheques of ₹ 15,370 towards premium of Life Insurance policies and ₹ 12,500 for Mediclaim Insurance policy.*
- *Invested in NSC ₹ 30,000 and in FDR of SBI for 5 years ₹ 50,000.*
- *Donations of ₹ 11,000 to an institution approved u/s 80G and of ₹ 5,100 to Prime Minister's National Relief Fund were given during the year by way of cheque.*

Compute the total income and tax payable thereon for the A.Y. 2017-18.

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Answer

Computation of Total Income for the A.Y.2017-18

Particulars	₹	₹
Income from Salaries		
Basic Salary (₹ 15,000 x 12)		1,80,000
Dearness Allowance (₹ 12,000 x12)		1,44,000
Commission on Turnover (0.5% of ₹ 50 lacs)		25,000
Bonus		50,000
Gratuity (Note 1)		30,000
Employer's contribution to recognized provident fund		
Actual contribution [20% of ₹ 1,80,000]	36,000	
Less: Exempt (Note 2)	33,240	2,760
Interest credited in recognized provident fund account @15% p.a.	15,000	
Less: Exempt upto 9.5% p.a.	9,500	5,500
Gift of gold ring worth ₹ 10,000 on 25th wedding anniversary by employer (See Note 3)		10,000
Perquisite value of music system given for personal use (being 10% of actual cost) i.e. 10% of ₹ 85,000		8,500
		4,55,760
Profits and Gains of Business or Profession		
Lease of 2 trucks on contract basis against fixed charges of ₹ 6,500 p.m. In this case, presumptive tax provisions of section 44AE will apply i.e. ₹ 7,500 p.m. for each of the two trucks (7,500x 2 x12). He cannot claim lower profits and gains since he has not maintained books of account.		1,80,000
Income from Other Sources		
Interest on bank FDRs	5,860	
Interest from debentures	7,540	
Dividend on shares [Exempt under section 10(34)]	Nil	13,400
Gross total Income		**6,49,160**
Less: **Deductions under Chapter VI-A**		
Section 80C		
Premium on life insurance policy	15,370	
Investment in NSC	30,000	
FDR of SBI for 5 years	50,000	

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Employee's contribution to recognized provident fund	30,000	**1,25,370**
Section 80D - Mediclaim Insurance		12,500
Section 80G (Note 4)		10,600
Total Income		**5,00,690**
Tax on total income		
Income-tax		25,138
Add: Education cess @ 2%		503
Add: Secondary and higher education cess @ 1%		251
Total Tax Payable		**25,892**
Tax Payable (rounded off)		**25,890**

Notes:

1. Gratuity received during service is fully taxable.
2. Employer's contribution in the recognized provident fund is exempt up to 12% of the salary i.e. 12% of (Basic Salary + DA for retirement benefits + Commission based on turnover)

   =12% of (₹ 1,80,000+ (50% of ₹ 1,44,000)+ ₹ 25,000)

   =12% of 2,77,000 = ₹ 33,240
3. An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable in view of the language of *Circular No.15/2001 dated 12.12.2001* that such gifts upto ₹ 5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹ 5,000. In such a case the Income from Salaries would be ₹ 4,50,760.
4. Deduction under section 80G is computed as under:

Particulars	₹
Donation to PM National Relief Fund (100%)	5,100
Donation to institution approved under section 80G (50% of ₹ 11,000) (amount contributed ₹ 11,000 or 10% of Adjusted Gross Total Income i.e. ₹ 51,129, whichever is lower)	5,500
Total deduction	10,600

Adjusted Gross Total Income =Gross Total Income – Deductions under section 80C and 80D=₹ 6,49,160–₹ 1,37,870 =₹ 5,11,290.

Question 27

Dr. Niranjana, a resident individual, aged 60 years is running a clinic. Her Income and Expenditure Account for the year ending March 31st, 2017is as under:

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Expenditure	₹	Income	₹
To Medicine consumed	35,38,400	By Consultation and Medical charges	58,85,850
To Staff salary	13,80,000	By Income-tax refund (Principal ₹ 5,000, interest ₹ 450)	5,450
To Clinic consumables	1,10,000	By Dividend from units of UTI	10,500
To Rent paid	90,000	By Winning from game show on T.V. (net of TDS of ₹ 15,000)	35,000
To Administrative expenses	2,55,000	By Rent	27,000
To Amount paid to scientific research association approved under section 35	1,50,000		
To Net profit	4,40,400		
	59,63,800		**59,63,800**

(i) *Rent paid includes ₹ 30,000 paid by cheque towards rent for her residential house in Surat.*

(ii) *Clinic equipments are:*

1.4.2016 Opening W.D.V. - ₹ 5,00,000

7.12.2016 Acquired (cost) - ₹ 2,00,000

(iii) *Rent received relates to property situated at Surat. Gross Annual Value ₹ 27,000. The municipal tax of ₹ 2,000, paid in December, 2016, has been included in "administrative expenses".*

(iv) *She received salary of ₹ 7,500 p.m. from "Full Cure Hospital" which has not been included in the "consultation and medical charges".*

(v) *Dr. Niranjana availed a loan of ₹ 5,50,000 from a bank for higher education of her daughter. She repaid principal of ₹ 1,00,000, and interest thereon ₹ 55,000 during the year 2016-17.*

(vi) *She paid ₹ 1,00,000 as tuition fee (not in the nature of development fees/ donation) to the university for full time education of her daughter.*

(vii) *An amount of ₹ 28,000 has also been paid by cheque on 27th March, 2017for her medical insurance premium.*

From the above, compute the total income of Dr. Smt. Niranjana for the A.Y.2017-18.

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Answer

Computation of total income and tax liability of Dr. Niranjana for A.Y. 2017-18

	Particulars	₹	₹	₹
I	**Income from Salary**			
	Basic Salary (₹ 7,500 x 12)			90,000
II	**Income from house property**			
	Gross Annual Value (GAV)		27,000	
	Less : Municipal taxes paid		2,000	
	Net Annual Value (NAV)		25,000	
	Less: Deduction u/s 24 @ 30% of₹ 25,000		7,500	17,500
III	**Income from profession**			
	Net profit as per Income and Expenditure account		4,40,400	
	Less : Items of income to be treated separately			
	(i) Rent received	27,000		
	(ii) Dividend from units of UTI	10,500		
	(iii) Winning from game show on T.V.(net of TDS)	35,000		
	(iv) Income tax refund	5,450	77,950	
			3,62,450	
	Less : Allowable expenditure			
	Depreciation on Clinic equipments			
	on ₹ 5,00,000 @ 15%	75,000		
	on ₹ 2,00,000 @ 7.5%	15,000		
	(On equipments acquired during the year after September 2016 she is entitled to depreciation @ 50% of normal depreciation)			
	Additional deduction of 75% for amount paid to scientific research association (Since weighted deduction of 175% is available in respect of such payment)	1,12,500	2,02,500	
			1,59,950	
	Add: Items of expenditure not allowable while computing business income			
	(i) Rent for her residential accommodation included in Income and Expenditure A/c	30,000		

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	(ii) Municipal tax paid relating to residential house at Surat included in administrative expenses	2,000	32,000	1,91,950
IV	**Income from other sources**			
	(a) Interest on income-tax refund		450	
	(b) Dividend from UTI	10,500		
	Less : Exempt under section 10(35)	10,500	Nil	
	(c) Winnings from the game show on T.V. (₹ 35,000 + ₹ 15,000)		50,000	50,450
	Gross Total Income			**3,49,900**
	Less: Deductions under Chapter VI A:			
	(a) Section80C - Tuition fee paid to university for full time education of her daughter		1,00,000	
	(b) Section 80D - Medical insurance premium (fully allowed since she is a senior citizen)		28,000	
	(c) Deduction under section 80E - Interest on loan taken for higher education is deductible		55,000	1,83,000
	Total income			**1,66,900**

Notes:

(i) The principal amount received towards income-tax refund will be excluded from computation of total income. Interest received will be taxed under the head "Income from other sources".

(ii) Winnings from game show on T.V. should be grossed up for the chargeability under the head "Income from other sources" (₹ 35,000 + ₹ 15,000). Thereafter, while computing tax liability, TDS of ₹ 15,000 should be deducted to arrive at the tax payable. Winnings from game show are subject to tax @30% as per section 115BB.

(iii) Since Dr. Niranjana is staying in a rented premise in Surat itself, she would not be eligible for deduction u/s 80GG, since she owns a house in Surat which she has let out.

Question 28

Dr. Parekh is a resident individual. His Income and Expenditure Account for the year ending 31st March, 2017is given below:

To	*₹*	*By*	*₹*
Salary to staff	*3,78,000*	*Consultation fees*	*51,85,000*
Cost of medicine	*36,35,000*	*Cost of medicines recovered*	*7,85,000*

Rent	*66,000*	*Stock of medicine*	*25,000*
Administrative cost	*11,98,000*	*Interest on Post Office MIS*	*86,400*
Advance tax	*1,40,000*	*Interest on Time Deposit with bank (Net of TDS ₹ 3,000)*	*27,000*
Membership fees	*5,000*	*Rent received*	*20,000*
Depreciation on apparatus	*42,500*	*Winning from lotteries (Net of TDS ₹ 3,000)*	*7,000*
Net profit	*6,70,900*		
	61,35,400		*61,35,400*

(i) He has deposited ₹ 1,20,000 in PPF.

(ii) He received salary of ₹ 1,50,000 and commission of ₹ 50,000 from a nursing home in which Dr. (Mrs.) Parekh is also an equal partner.

(iii) He received fees of ₹ 50,000 from University of Trividad as lecturer.

(iv) Received pension of ₹ 84,000 from LIC Jeevan Suraksha.

(v) Paid ₹ 32,500 by cheque as mediclaim insurance premium for his medical treatment.

(vi) He paid LIC premium of ₹ 80,000 for his own life.

(vii) Cost of administration includes ₹ 3,000 paid for municipal tax for the house let out to a tenant.

(viii) Depreciation as per Income-tax Rules, 1962 to be computed as follows:

WDV as on 1.4.2016	*₹3,00,000*
Rate of depreciation	*@ 15%*

(ix) Cost of lottery tickets amounting to ₹ 350 has not been debited to Income and Expenditure account.

You are required to compute the total income and tax payable thereon by Dr. Parekh for the assessment year 2017-18.

Answer

Computation of total Income and tax payable by Dr. Parekh for the A.Y. 2017-18

Particulars	**₹**	**₹**
Income from House Property (Note 1)		11,900
Profits and gains of business or profession (Note 2)		8,71,000
Income from other sources (Note 3)		2,60,400
Gross Total income		**11,43,300**

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Less: Deductions under Chapter VIA		
(i) Deduction under section 80C		
Investment in PPF	1,20,000	
Life insurance premium paid	80,000	
	2,00,000	
Deduction restricted to	1,50,000	
(ii)Deduction under section 80D		
Mediclaim premium of ₹ 32,500 paid by cheque for himself. However, deduction restricted to	25,000	1,75,000
Total income		**9,68,300**
Components of Total Income		
Special income :		
Winning from lotteries (chargeable at special rate @ 30% under section 115BB)		10,000
Normal income		9,58,300
		9,68,300
Computation of Tax		
Tax on winnings from lotteries @ 30%		3,000
Tax on normal income (₹ 9,58,300)		
First ₹ 2,50,000 Nil	NIL	
Next ₹ 2,50,000 10%	25,000	
Balance ₹ 4,58,300 20%	91,660	1,16,660
Income tax payable		1,19,660
Add: Education cess @2%		2,393
Secondary and higher education cess @1%		1,197
Total Tax Payable		**1,23,250**
Less: Tax deducted at source		
From Interest	3,000	
From lottery income	3,000	6,000
		1,17,250
Less : Advance tax paid		1,40,000
Refund		**(-) 22,750**

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Notes:

1. **Computation of Income from House Property**

Particulars	₹
Gross Annual Value – Rent received (treated as fair rent)	20,000
Less : Municipal taxes paid	3,000
Net Annual Value (NAV)	**17,000**
Less : Statutory deduction under section 24 @ 30% of NAV	5,100
Income from House Property	**11,900**

2. **Computation of Profits and gains of business or profession**

Particulars	₹	₹
Net Profit as per Income & Expenditure Account		6,70,900
Add : Depreciation charged	42,500	
Municipal Taxes paid	3,000	
Advance Tax (See Note-4)	1,40,000	1,85,500
		8,56,400
Less: Rent received	20,000	
Interest on Post Office MIS	86,400	
Interest on Term Deposit with bank (Net of TDS)	27,000	
Winning from lotteries (Net of TDS)	7,000	
Depreciation as per Income-tax Act, 1961	45,000	1,85,400
		6,71,000
Salary from Nursing Home as partner	1,50,000	
Commission from Nursing home as partner	50,000	2,00,000
Income from business		**8,71,000**

3. **Computation of Income from Other Sources**

Particulars	₹
Interest Post Office MIS	86,400
Interest on Term Deposit with Bank (Gross)	30,000
Winning from lotteries (Gross)	10,000
Fees from University of Trividad	50,000
Pension from LIC Jeevan Suraksha	84,000
Income from Other Sources	**2,60,400**

4. Advance Tax is not allowable as deduction.

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5. Depreciation of Apparatus :

	₹
WDV as on 1.4.2016	3,00,000
Depreciation @15%	45,000
WDV as on 31.3.2017	2,55,000

6. Any salary, bonus, commission or remuneration by whatever name called due to or received by a partner of a firm from the firm shall not be treated as salary but it shall be treated as income from business or profession for the purposes of section 28.

7. As per section 58(4), no expenditure can be allowed against winnings from lotteries. Therefore, amount spent on lottery tickets being ₹ 350, cannot be allowed as deduction from income from winnings of lotteries.

8. Pension from LIC Jeevan Suraksha is taxable as Income from other sources.

Question 29

From the following particulars furnished by Mr. X for the year ended 31.3.2017, you are requested to compute his total income and tax payable for the assessment year 2017-18.

(a) Mr. X retired on 31.12.2016at the age of 58, after putting in 25 years and 9 months of service, from a private company at Mumbai.

(b) He was paid a salary of ₹ 25,000 p.m. and house rent allowance of ₹ 6,000 p.m. He paid rent of ₹ 6,500 p.m. during his tenure of service.

(c) On retirement, he was paid a gratuity of ₹ 3,50,000.He was not covered by the payment of Gratuity Act. His average salary in this regard may be taken as ₹ 24,500.Mr. X had not received any other gratuity at any point of time earlier, other than this gratuity.

(d) He had accumulated leave of 15 days per annum during the period of his service; this was encashed by Mr. X at the time of his retirement. A sum of ₹ 3,15,000 was received by him in this regard. His average salary may be taken as ₹ 24,500. Employer allowed 30 days leave per annum.

(e) After retirement, he ventured into textile business and incurred a loss of ₹ 80,000 for the period upto 31.3.2017.

(f) Mr. X has invested ₹ 62,500 in public provident fund and ₹ 37,500 in National Savings Certificates.

Answer

Computation of total income of Mr. X for A.Y.2017-18

Particulars	₹	₹
Income from Salaries		
Basic salary (₹ 25,000 x 9 months)		2,25,000
House rent allowance		

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Actual amount received	54,000	
Less : Exemption under section 10(13A)(Note 1)	36,000	18,000
Gratuity		
Actual amount received	3,50,000	
Less: Exemption under section 10(10)(iii) (Note 2)	3,06,250	43,750
Leave encashment		
Actual amount received	3,15,000	
Less : Exemption under section 10(10AA) (Note 3)	2,45,000	70,000
Gross Salary		**3,56,750**
Profits and gains of business or profession		
Business loss of ₹ 80,000 to be carried forward as the same cannot be set off against salary income		Nil
Gross Total income		**3,56,750**
Less : Deduction under section 80C		
Investment in public provident fund	62,500	
Investment in NSC	37,500	1,00,000
Total income		**2,56,750**
Tax on total income		675
Less: Rebate under section 87A		675
Tax payable		**Nil**

Note :

(1) As per section 10(13A), house rent allowance will be exempt to the extent of least of the following three amounts:

(i)	HRA actually received (6,000 x 9)	54,000
(ii)	Rent paid in excess of 10% of salary (₹ 6,500 – ₹ 2,500) x 9 months	36,000
(iii)	50% salary	1,12,500

(2) Gratuity of ₹ 3,06,250 is exempt under section 10(10)(iii), being the minimum of the following amounts :

(i)	Actual amount received	3,50,000
(ii)	Half month average salary for each year of completed service(1/2 x 24,500 x 25)	3,06,250
(iii)	Statutory limit	10,00,000

(3) Leave enchashment is exempt upto the least of the following:

(i)	Actual amount received	3,15,000

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(ii)	10 months average salary (24,500 x 10)	2,45,000
(iii)	Cash equivalent of unavailed leave calculated on the basis of maximum 30 days for every year of actual service rendered to the employer from whose service he retired (See Note 4 below)	3,06,250
(iv)	Statutory limit	3,00,000

(4) Since the leave entitlement of Mr. X as per his employer's rules is 30 days credit for each year of service and he had accumulated 15 days per annum during the period of his service, he would have availed/taken the balance 15 days leave every year.

Leave entitlement of Mr. X on the basis of 30 days for every year of actual service rendered by him to the employer	= 30 days/year x 25= 750 days
Less: Leave taken /availed by Mr. X during the period of his service	= 15 days/year x 25= 375 days
Earned leave to the credit of Mr. X at the time of his retirement	375 days
Cash equivalent of earned leave to the credit of Mr. X at the time of his retirement	= 375 × 24,500 /30= ₹ 3,06,250

Question 30

(i) Smt. Savita Rani was born on 01.07.1950.She is a Deputy Manager in a Company in Mumbai. She is getting a monthly salary and D.A. of ₹ 45,000 and ₹ 12,000 respectively.50% of DA forms part of pay. She also gets a House Rent Allowance of ₹ 6,000 per month. She is a member of Recognised P.F. wherein she contributes 15% of her salary of ₹ 51,000 p.m. (45,000 + 6,000, being 50% of DA).Her employer also contributes an equal amount.

(ii) She is living in the house of her minor son in Mumbai.

(iii) During the previous year 2016-17, her minor son has earned an income of ₹ 30,000 (computed) as rent from a House Property, which had been transferred to him by Smt. Savita Rani without consideration a few years back.

(iv) During the previous year 2016-17, she sold Government of India Capital Indexed Bonds for ₹ 1,50,000 on 30.09.2016, which she purchased on 01.07.2001 for ₹ 80,000 (Cost inflation index – F.Y. 2001-2002: 426 and for the F.Y. 2016-17: 1125).

(v) Her employer gave her an interest free loan of ₹ 1,50,000 on 01.10.2016 to one of her son's wife for the purchase of an Alto Maruti Car. Nothing has been repaid to the company towards the loan. The lending rate on SBI for a similar loan is 8% as on 01.04.2016.

(vi) During the previous year 2016-17she paid ₹ 15,000 by cheque to GIC towards Medical Insurance Premium of her dependent mother.

Compute the taxable income and tax liability of Mrs. Savita Rani for the A.Y. 2017-18.

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Answer

Computation of taxable income and tax liability of Smt. Savita Rani for A.Y. 2017-18

Particulars	₹	₹
Income from salary		
Basic salary (₹ 45,000 x 12)		5,40,000
Dearness Allowance (₹ 12000 x 12)		1,44,000
House Rent allowance (fully taxable)		72,000
Employer's contribution to recognized provident fund in excess of 12% is taxable as salary income		
12% of salary is ₹ 73,440. Employer's contribution is 15% of salary, which is ₹ 91,800		
Excess contribution is (₹ 91,800 – ₹ 73,440)		18,360
Perquisite in respect of interest free loan (₹ 1,50,000 x 8%x ½)		6,000
Net Salary		**7,80,360**
Income from house property (See Note below)		30,000
Long term Capital Gain:		
Sale consideration of GOI capital indexed bonds	1,50,000	
Less: Indexed cost of acquisition (₹ 80,000 x 1125/426)	2,11,268	
Long-term capital loss (to be carried forward)	61,267	
Gross Total Income		**8,10,360**
Deduction under section 80C – in respect of recognized provident fund contribution	91,800	
Deduction under section 80D – Mediclaim	15,000	1,06,800
Total Income		**7,03,560**
Tax Payable on ₹ 7,03,560		60,712
Add : Education cess and Secondary and higher education cess @ 3%		1,821
Total tax payable		**62,533**
Total tax payable (rounded off)		**62,530**

Note: *As per section 27, any property transferred to the minor child without adequate consideration would be deemed to be the property of the assessee. Therefore, the income from house property of ₹ 30,000 (computed) is to be assessed in the hands of Smt. Savita Rani.*

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Question 31

Ramesh retired as General manager of XYZ Co. Ltd. on 30.11.2016after rendering service for 20 years and 10 months. He received ₹ 3,00,000 as gratuity from the employer. (He is not covered by Gratuity Act, 1972).

His salary particulars are given below :

Basic pay	*₹ 10,000 per month up to 30.6.2016*
Basic pay	*₹ 12,000 per month from 1.7.2016*
Dearness allowance (Eligible for retirement benefits)	*50% of basic pay*
Transport allowance	*₹ 2,300 per month*

He resides in his own house. Interest on monies borrowed for the self occupied house is ₹ 24,000 for the year ended 31.03.2017.

From a fixed deposit with a bank, he earned interest income of ₹ 18,000 for the year ended 31.03.2017.

Compute taxable income of Ramesh for the year ended 31.03.2017.

Answer

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

Particulars	₹	₹
Income from salary		
Basic pay : April to June(₹ 10,000 x 3)		30,000
Basic pay : July to November (₹ 12,000 x 5)		60,000
Dearness allowance @ 50% basic pay		45,000
Transport allowance (₹ 2,300 x 8) less exemption @ ₹ 1,600 per month (₹ 18,400 – ₹ 12,800)		5,600
Gratuity		
(i) Statutory limit ₹ 10,00,000		
(ii) Half month average salary [See Note below] ₹ 8,100 x 20 yrs = ₹ 1,62,000		
(iii) Actual amount received = ₹ 3,00,000		
Least of the above i.e. ₹ 1,62,000 is exempt. Balance is taxable (₹ 3,00,000 – ₹ 1,62,000)		1,38,000
		2,78,600
Income from house property:		
Self occupied – ALV	Nil	

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Less: Interest on monies borrowed under section 24(b)	24,000	(24,000)
Income from other sources:		
Fixed deposit interest		18,000
Total income		**2,72,600**

Note :

Average salary of 10 months preceding the month of retirement is to be computed :₹

Basic pay ₹ 10,000 x 6	60,000
Basic pay ₹ 12,000 x 4	48,000
Total	1,08,000
Add: 50% of Dearness Allowance–eligible for retirement benefits	54,000
	1,62,000
Average salary : ₹ 1,62,000/10	16,200
Half month average salary ₹ 16,200 / 2	8,100

Question 32

Rosy and Mary are sisters, born and brought up at Mumbai. Rosy got married in 1982 and settled at Canada since 1982.Mary got married and settled in Mumbai. Both of them are below 60 years. The following are the details of their income for the previous year ended 31.3.2017:

S.No.	***Particulars***	***Rosy*** ₹	***Mary*** ₹
1.	*Pension received from State Government*	*--*	*10,000*
2.	*Pension received from Canadian Government*	*20,000*	*--*
3.	*Long-term capital gain on sale of land at Mumbai*	*1,00,000*	*50,000*
4.	*Short-term capital gain on sale of shares of Indian listed companies in respect of which STT was paid*	*20,000*	*2,50,000*
5.	*LIC premium paid*	*--*	*10,000*
6.	*Premium paid to Canadian Life Insurance Corporation at Canada*	*40,000*	*--*
7.	*Mediclaim policy premium paid*	*--*	*25,000*
8.	*Investment in PPF*	*--*	*20,000*
9.	*Rent received in respect of house property at Mumbai*	*60,000*	*30,000*

Compute the taxable income and tax liability of Mrs. Rosy and Mrs. Mary for the Assessment Year 2017-18and tax thereon.

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Answer

Computation of taxable income of Mrs. Rosy and Mrs. Mary for the A.Y.2017-18

S. No.	Particulars	Mrs. Rosy	Mrs. Mary
		₹	₹
(I)	**Salaries**		
	Pension received from State Government	-	10,000
	Pension received from Canadian Government is not taxable in the case of a non-resident since it is earned and received outside India		
		-	**10,000**
(II)	**Income from house property**		
	Rent received from house property at Mumbai (assumed to be the annual value in the absence of other information i.e. municipal value, fair rent and standard rent)	60,000	30,000
	Less: Deduction under section 24(a) @ 30%	18,000	9,000
		42,000	**21,000**
(III)	**Capital gains**		
	Long-term capital gain on sale of land at Mumbai	1,00,000	50,000
	Short term capital gain on sale of shares of Indian listed companies in respect of which STT was paid	20,000	2,50,000
		1,20,000	**3,00,000**
(A)	**Gross Total Income [(I)+(II)+(III)]**	**1,62,000**	**3,31,000**
	Less: Deductions under Chapter VIA		
1.	Deduction under section 80C		
	1. LIC Premium paid	-	10,000
	2. Premium paid to Canadian Life Insurance Corporation	40,000	
	3. Investment in PPF	-	20,000
		40,000	**30,000**
2.	Deduction under section 80D – Mediclaim premium paid (assuming that the same is paid by cheque)		25,000
		40,000	**55,000**

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(B)	Total deduction under Chapter VIA is restricted to income other than capital gains taxable under sections 111A & 112	40,000	31,000
(C)	**Total income (A-B)**	**1,22,000**	**3,00,000**
	Tax liability of Mrs. Rosy for A.Y. 2017-18		
	Tax on long-term capital gains @ 20%	20,000	
	Tax on short-term capital gains @ 15%	3,000	
		23,000	
	Tax liability of Mrs. Mary for A.Y.2017-18		
	Tax on short-term capital gains @ 15% of ₹ 50,000 [i.e. ₹ 2,50,000 less ₹ 2,00,000, being the unexhausted basic exemption limit as per proviso to section 111A]		7,500
	Less: Rebate under section 87A		5,000
			2,500
	Education cess @ 2% & SHEC@ 1%	690	75
	Total tax payable	**23,690**	**2,575**

Notes :

(1) Long-term capital gains is chargeable to tax @ 20% as per section 112.

(2) Short-term capital gains on transfer of equity shares in respect of which securities transaction tax is paid is subject to tax @ 15% as per section 111A.

(3) In case of resident individuals, if the basic exemption limit is not fully exhausted against other income, then the long-term capital gains/short-term capital gains will be reduced by the unexhausted basic exemption limit and only the balance will be taxed at 20%/15% respectively. However, this benefit is not available to non-residents. Therefore, while Mrs. Mary can adjust there unexhausted basic exemption limit against long-term capital gains and short-term capital gains taxable under section 111A, Mrs. Rosy cannot do so.

(4) Since long-term capital gains is taxable at the rate of 20% and short-term capital gains is taxable at the rate of 15%, it is more beneficial for Mrs. Mary to first exhaust her basic exemption limit of ₹ 2,50,000 against long-term capital gains of ₹ 50,000 and the balance limit of ₹ 2,00,000 (i.e., 2,50,000 – 50,000) against short-term capital gains.

Question 33

Mr. Rajesh is serving in a public limited company as General Manager (Finance). His total emoluments for the year ended 31st March, 2017are as follows:

Basic Salary	*₹ 5,40,000*
HRA (Computed)	*₹ 1,80,000*
Transport allowance	*₹ 22,000*

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Apart from the above, his employer has sold the following assets to him on 1st January, 2017:

(i) Laptop computer for ₹ 20,000 (Acquired in September, 2015 for ₹ 1,20,000)

(ii) Car 1800 cc for ₹ 3,20,000 (purchased in April, 2014 for ₹ 8,50,000)

He also owns a residential house, let out for a monthly rent of ₹ 15,000. The fair rental value of the property for the let out period is ₹ 1,50,000. The house was self-occupied by him from 1st January, 2017to 31st March, 2017.He has taken a loan from bank of ₹ 20 lacs for the construction of the property, and has repaid ₹ 1,05,000 (including interest ₹ 40,000) during the year.

Mr. Rajesh sold shares of different Indian companies on 14th April, 2016:

Name	***Sale value (per share)***	***Purchase price (per share)***	***Acquired on***	***No. of shares***
A Ltd.	*₹ 150*	*₹ 120*	*2nd May, 2009*	*200*
B Ltd.	*₹ 82*	*₹ 65*	*16th April, 2015*	*125*

Sale proceeds were subject to brokerage of 0.1% and securities transaction tax of 0.125% on the gross consideration. He received income-tax refund of ₹ 5,750 (including interest ₹ 750) relating to the assessment year2015-16.

Compute the total income of Mr. Rajesh for the Assessment Year 2017-18.

Answer

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

Particulars	**₹**
Income from salaries (Working Note 1)	9,86,800
Income from house property (Working Note 2)	1,00,000
Capital gains	
Short-term capital gains (Working Note 3)	2,115
Income from other sources: Interest on Income-tax refund	750
Gross Total Income	**10,89,665**
Less: **Deduction under Chapter VIA**	
Deduction under section 80C	
Repayment of housing loan (principal) [See Note below]	65,000
Total Income	**10,24,665**
Total Income (rounded off)	**10,24,670**

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Working Notes:

	Particulars	₹	₹
1.	**Income from salaries**		
	Basic Salary		5,40,000
	HRA (computed)		1,80,000
	Transport allowance	22,000	
	Less: Exempt under section 10(14) [₹ 1,600 ×12]	19,200	2,800
	Perquisites (relating to sale of movable assets by employer)		
	Laptop Computer		
	Cost [September, 2015]	1,20,000	
	Less: Depreciation at 50% for one completed year	60,000	
	WDV [September, 2016]	60,000	
	Less: Amount paid to the employer	20,000	
	Perquisite value of laptop (A)	**40,000**	
	Car		
	Cost [April, 2014]	8,50,000	
	Less: Depreciation for the 1st year (April'14 to March'15) @ 20% of WDV	1,70,000	
	WDV [April, 2015]	6,80,000	
	Less: Depreciation for the 2nd year (April'15 to March'16) @ 20% of WDV	1,36,000	
	WDV [April, 2016]	5,44,000	
	Less: Amount paid to the employer	3,20,000	
	Perquisite value of car (B)	**2,24,000**	
	Perquisite value (A) + (B)		2,64,000
	Income chargeable under the head "Salaries"		**9,86,800**
2.	**Income from house property**		
	Section 23(2) provides that the annual value of a self-occupied house shall be taken as Nil. However, section 23(3) provides that the benefit of self-occupation would not be available if the house is actually let during the whole or part of the previous year. This implies that the benefit of taking the annual value as nil would be available only if the house is self-occupied for the whole year.		

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	In this case, therefore, the benefit of taking annual value as Nil is not available since the house is self-occupied only for 3 months. In such a case, the gross annual value has to be computed as per section 23(1). Accordingly, the fair rent for the whole year should be compared with the actual rent for the let-out period and whichever is higher shall be adopted as the Gross Annual Value.

Particulars	₹	₹
Gross Annual Value (higher of fair rent for the whole year and actual rent for the let-out period)		2,00,000
Fair rent for the whole year = ₹ 1,50,000 × 12/9	2,00,000	
Actual rent received = ₹ 15,000 × 9	1,35,000	
Less: Municipal taxes		Nil
Net Annual Value (NAV)		**2,00,000**
Less: Deductions under section 24		
30% of NAV	60,000	
Interest on loan [See Note below]	40,000	1,00,000
Income from house property		**1,00,000**

Note *: It is presumed that the interest of ₹ 40,000 paid on housing loan represents the interest actually due for the year.*

3. Income chargeable as "Capital Gains"

Section 10(38) exempts long-term capital gain on sale of equity shares of a company, if such transaction is chargeable to securities transaction tax. Since Mr. Rajesh has held shares of A Ltd. for more than 12 months, the gains arising from sale of such shares is a long-term capital gain, which is exempt under section 10(38), since securities transaction tax has been paid on such sale.

Shares in B Ltd. are held for less than 12 months and hence the capital gains arising on sale of such shares is a short-term capital gain chargeable to tax @15% as per section 111A, since the transaction is subject to securities transaction tax. It may be noted, however, that securities transaction tax is not a deductible expenditure.

Short-term capital gains arising from sale of shares of B Ltd.

Sale consideration (82 × 125)	10,250	
Less: Brokerage @ 0.1%	10	
Net sale consideration	10,240	
Cost of acquisition (65 x 125)	8,125	
Short-term capital gains	**2,115**	

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Question 34

Mr. Ram, who does not maintain books of account for the year ended 31.3.2017, requests you to compute his total income and the tax payable thereon for the assessment year 2017-18from the following: ₹

(i) Basic Salary - 20,000 p.m.

CCA - 1,000 p.m.

HRA - 5,000 p.m.

(ii) Ram resides in Chennai, paying a rent of ₹ 6,000 per month.

(iii) Ram is paid an education allowance of ₹ 500 per month per child for all the three of his children. Actual expenses (tuition fees only) amounts to ₹ 15,000, ₹ 10,000 and ₹ 5,000 respectively.

(iv) He bought a heavy goods vehicle on 7.6.2016and has been letting it on hire from the same date. He declares an income of ₹ 34,900 from the same.

(v) Interest from company deposits is ₹ 15,000 and bank interest from saving bank account is ₹ 5,000.

(vi) Interest is payable on bank loans availed for buying the truck and making company deposits as follows:-

Purpose	***Date of loan***	**Amount**	**Interest rate**
Truck purchase	*1.4.2016*	*5 lakhs*	*10% p.a.*
Company deposit	*1.10.2016*	*1 lakh*	*9 % p.a.*

(vii) Loss carried forward arising from speculating in shares during the preceding previous year and eligible for set-off is ₹ 1,00,000.

(viii) Ram has invested ₹ 12,000 in notified equity linked saving scheme of UTI, ₹ 52,000 in PPF, ₹ 9,000 as premium on life insurance policy taken on 31.07.2013 on his own life (sum assured ₹ 40,000) and ₹ 15,000 towards pension fund of LIC.

Answer

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

Particulars	**₹**	**₹**
Income from Salary		
Basic Salary (₹ 20,000 × 12)		2,40,000
CCA (₹ 1,000 × 12)		12,000
HRA (₹ 5,000 × 12)	60,000	
Less: Exempt under section 10(13A) [See Note 1 below]	48,000	12,000

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Education Allowance (₹ 500×12×3)	18,000	
Less: Exempt under section 10(14) (₹ 100×12×2)	2,400	15,600
Income from Salary		**2,79,600**
Profits and gains from business or profession		
Income from the business of letting on hire, a heavy vehicle under section 44AE (₹ 7,500×10) [See Note 2 below]		75,000
Income from Other Sources		
Interest from company deposits	15,000	
Interest from Saving Bank Account	5,000	
	20,000	
Less: Deduction under section 57		
₹ 1,00,000 @ 9% for 6 months–towards loan interest	4,500	15,500
Gross Total Income		**3,70,100**
Less: Deduction under Chapter VI-A		
Under section 80C [See Note 4 below]	93,000	
Under section 80CCC	15,000	
	1,08,000	
Under section 80TTA- Interest from Saving Bank Account(See Note-6 below)	5,000	1,13,000
Total Income		**2,57,100**

Computation of tax payable for the A.Y.2017-18

Tax on ₹ 2,57,100	710
Less: Rebate under section 87A	710
	Nil
Add: Education cess @ 2% and SHEC @ 1%	Nil
Tax Payable	**Nil**

Notes :

(1) HRA is exempt to the extent of the least of the following under section 10(13A)

(1) 50% of salary (as the city is Chennai) i.e. 50% of ₹ 2,40,000=₹ 1,20,000

(2) Excess of rent paid over 10% of salary = ₹ 72,000 – ₹ 24,000 = ₹ 48,000

(3) Actual HRA received =5,000 × 12 = ₹ 60,000

Least of the above i.e.₹ 48,000 is exempt under section 10(13A)

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(2) In the case of a person owning not more than 10 vehicles at any time during the previous year, estimated income from each vehicle, whether heavy goods vehicle or not, will be deemed to be ₹ 7,500/- for every month or part of the month during which the heavy vehicle is owned by the assessee during the previous year [Section 44AE].

Presumptive income = ₹ 7,500 × 10 = 75,000

If, however, the assessee declares a higher amount, such amount will be considered as income. In the instant case, since the assessee declares a lower amount, it cannot be considered, since no books of account are maintained. Also, interest is not deductible, since under section 44AE, all deductions under sections 30 to 38 are deemed to have been allowed.

(3) Brought forward loss from speculation business can be set off only against income from speculation business and not against other business income.

(4) Deduction under section 80C:

Investment in notified equity linked saving scheme of UTI	12,000
Investment in PPF	52,000
Life insurance premium on own life restricted to 10% of sum assured	4,000
Tuition fees paid for two of his children (Most favourable to Ram)	25,000
	93,000

(5) Contribution to pension fund of LIC ₹ 15,000 is deductible under section 80CCC.

(6) Deduction under section 80TTA is allowed in respect of interest from Saving Bank Account upto a maximum of ₹ 10,000. Therefore, interest from Saving Bank Account of ₹ 5,000 is allowed as deduction.

Question35

Mr. Ashok owns a property consisting of two blocks of identical size. The first block is used for business purposes. The other block has been let out from 1.4.2016 to his cousin for ₹ 10,000 p.m. The cost of construction of each blockis ₹ 5 lacs (fully met from bank loan), rate of interest on bank loan is 10% p.a. The construction was completed on 31.3.2016. During the year ended 31.3.2017, he had to pay a penal interest of ₹ 2,000 in respect of each block on account of delayed payments to the bank for the borrowings. The normal interest paid by him in respect of each block was ₹ 42,000.Principal repayment for each block was ₹ 23,000 made at the end of the year. An identical block in the same neighbourhood fetches a rent of ₹ 15,000 per month. Municipal tax paid in respect of each block was ₹ 12,000.

The income computed in respect of business prior to adjustment towards depreciation on any asset is ₹ 2,20,000.

Depreciation on equipments used for business is ₹ 30,000.

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On 23.3.2017, he sold shares of B Ltd., a listed share in BSE for ₹ 2,30,000. The share had been purchased 10 months back for ₹ 1,80,000.Securities transaction tax paid may be taken as ₹ 220.

Brought forward business loss of a business discontinued on 12.1.2016is ₹ 80,000.This loss has been determined in pursuance of a return of income filed in time and the current year is the seventh year.

The following payments were effected by him during the year :

(i) LIP of ₹ 20,000 on his life and ₹ 12,000 for his son aged 22, engaged as a software engineer and drawing salary of ₹ 25,000 p.m.

(ii) Mediclaim premium of ₹ 6,000 for himself and ₹ 5,000 for above son. The premiums were paid by cheque.

You are required to compute the total income for the assessment year 2017-18.The various heads of income should be properly shown. Ignore the interest on bank loan for the period prior to 1.4.2016, as the bank had waived the same.

Answer

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

Particulars	₹	₹	₹
Income from house property [See Note I]			
House block 2 let out (higher of fair rent and rent receivable)		1,80,000	
Less: Municipal tax paid		12,000	
Net annual value (NAV)		**1,68,000**	
Less: Deductions under section 24			
(a) 30% of NAV	50,400		
(b) Interest on bank loan @ 10% on ₹ 5,00,000	50,000	1,00,400	67,600
Profits and gains of business or profession [See Note II]			
Income prior to adjustment for depreciation		2,20,000	
Less: Depreciation on equipments used for business	30,000		
Depreciation on building ₹ 5,00,000 @ 10%	50,000	80,000	
		1,40,000	
Less: Set off of brought forward business lossrelating to discontinued business**[See Note III]**		80,000	60,000
Capital Gains[See Note IV]			
Short term capital gains from sale of listed shares			

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Full value of consideration		2,30,000	
Less : Cost of acquisition		1,80,000	50,000
Gross Total Income			**1,77,600**
Less : Deduction under section 80C in respect of LIP ₹ 32,000 and housing loan repayment in respect of II block ₹ 23,000	55,000		
Deduction under section 80D (for self)	6,000		61,000
Total income			**1,16,600**

Notes :

I – On computation of Income from house property

(i) The annual value of the house property which is used for business would not fall under the head "Income from house property". Therefore, the annual value of the first block is not chargeable to tax under the head "Income from house property". However, depreciation there on at 10% has been claimed while computing the income from business.

(ii) As regards the second block, the sum for which the property may be reasonably expected to be let is ₹ 15,000 per month. The Gross Annual Value (GAV) of the block is the higher of fair rent (i.e., ₹ 15,000 p.m.) or the actual rent received (₹ 10,000 p.m.)Hence, the GAV of the second block is ₹ 1,80,000 (i.e. ₹ 15,000 p.m.)

(iii) Under section 24(b), interest on bank loan for construction of house is deductible. However, penal interest is not deductible. Interest due during the year in respect of the second block is ₹ 50,000 (i.e. 10% of ₹ 5 lakhs), which is allowable as deduction under section 24(b).

II – On computation of Profits and gains of business or profession: Mr. Ashok can claim depreciation @ 10% on the building used by him for business purposes. The depreciation on the first block is ₹ 50,000 (being 10% of ₹ 5,00,000) and depreciation on equipments used for business is ₹ 30,000.Hence the depreciation allowable during the year is ₹ 80,000.

III – On set off of business loss: As per section 72, business loss relating to discontinued business is eligible for set off.

IV – On treatment of short-term capital gains (STCG): The listed shares have been sold and securities transaction tax is paid, hence it is taxable at 15% as per section 111A.For the purpose of providing deduction under Chapter VI-A, the gross total income should be reduced by the STCG on listed shares.

V – On computation of deductions under sections 80C and 80D: Deduction under section 80C can be claimed in respect of life insurance premium paid for major son, even though he is not dependent on the assessee. It is assumed Block 2 let out to cousin was used

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for residential purpose and accordingly principal repayment was considered for deduction under section 80C.

However, deduction under section 80D cannot be claimed in respect of mediclaim premium paid for non-dependant son. Mediclaim premium paid for self of ₹ 6,000 is eligible for deduction.

Question 36

Total income of Mrs. Priti, aged 59, a resident of Mumbai for the financial year 2016-17is ₹ 21,05,000. It includes an income of ₹ 2,20,000 from the business of dealing in shares on which she has paid securities transaction tax of ₹ 15,000. She has also deposited ₹ 1,50,000 in her PPF. account with the State Bank of India. Compute her tax liability for the A.Y. 2017-18.

Answer

Computation of tax liability of Mrs. Priti for A.Y. 2017-18

Particulars		₹
Total income other than business of dealing in shares(₹ 21,05,000 – ₹ 2,20,000) (before deduction under section 80C)		18,85,000
Income from business of dealing in shares [See Note below]		2,05,000
Gross Total Income		**20,90,000**
Less : Deduction under section 80C in respect of PPF deposit		1,50,000
Total income		**19,40,000**
Tax on total income		4,07,000
Add: Education cess @ 2%		8,140
Add: Secondary and Higher Education cess @1%		4,070
Tax Liability		**4,19,210**

Note: ₹ 2,20,000 less amount of ₹ 15,000 paid towards securities transaction tax eligible for deduction under section 36(1)(xv).

Question 37

Mr. A, a senior citizen, has furnished the following particulars relating to his house properties:

Nature of occupation	*House I Self occupied ₹*	*House II Let out ₹*
Municipal valuation	*60,000*	*1,20,000*
Fair rent	*90,000*	*1,50,000*
Standard rent	*75,000*	*90,000*

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Actual rent per month		*9,000*
Municipal taxes paid	*6,000*	*12,000*
Interest on capital borrowed	*70,000*	*90,000*

Loan for both houses were taken on 1.4.2008.House II remained vacant for 4 months.

Besides the above two houses, A has inherited during the year an old house from his grandfather. Due to business commitments, he sold the house immediately for a sum of ₹ 250 lakhs. The house was purchased in 1960 by his grandfather for a sum of ₹ 2 lakhs. However, the fair market value as on 1.4.1981 was ₹ 20 lakhs. With the sale proceeds, A purchased a new house in March, 2017for a sum of ₹ 100 lakhs and the balance was used in his business.

The other income particulars of Mr. A besides the above are as follows (A.Y.2017-18)

Business loss	*₹ 2 lakhs*
Income from other sources (Fixed Deposit interest)	*₹ 1 lakh*
Investments made during the year : PPF	*₹ 1,00,000*
Cost inflation index (F.Y. 2016-17)	*1125*

Compute total income of Mr. A and his tax liability for the assessment year 2017-18

Answer

Computation of Total Income and Tax liability of Mr. A for A.Y. 2017-18

Particulars	₹	₹
1. Income from house property –House I	(70,000)	
– House II	(48,000)	
(See Working Note 1)		(1,18,000)
2. Profits and gains of business		(2,00,000)
3. Capital gains – long term (See Working Note 2)		1,30,00,000
4. Income from other sources – Bank interest		1,00,000
Gross total income		1,27,82,000
Less : Deduction under Chapter VI-A		
Deduction under section 80C (PPF)		1,00,000
Total income		**1,26,82,000**
Tax liability		
Total income other than long term capital gain is Nil.		
Taxable long term capital gain is ₹ 1,23,82,000		
[i.e. ₹ 1,30,00,000 – ₹ 3,18,000 – basic exemption limit of ₹ 3,00,000]		
On long term capital gains of ₹ 1,23,82,000 @ 20%		24,76,400
Surcharge @ 15%		3,71,460
		28,47,860

Education cess @ 2% and Secondary and higher education cess@1%		85,436
Total tax payable		**29,33,296**

Working notes:

1. **Calculation of income from house property**

House I – Self occupied		₹
Annual value		Nil
Less : Interest as per section 24(b)		70,000
Loss from house property (House I)		(70,000)
House II- Let out		₹
Gross annual value(₹ 9,000 x 8)		72,000
Less :Municipal taxes		12,000
Net Annual Value (NAV)		60,000
Less : Deductions under section 24		
30% of NAV	18,000	
Interest on borrowed capital	90,000	1,08,000
Loss from house property (house II)		(48,000)

Note : Interest on capital borrowed will be allowed in full for let out properties. As per section 23(1)(c), where the property or any part of the property is let and was vacant during the whole or any part of the previous year and owing to such vacancy the actual rent received or receivable by the owner in respect thereof is less than the expected rent (in this case, standard rent of ₹ 90,000), then, the actual rent received or receivable would be the Gross Annual Value of the property. In this case, the actual rent received (i.e. ₹ 72,000) is less than the expected rent(i.e. ₹ 90,000) on account of vacancy and therefore, the actual rent received is taken as the Gross Annual Value.

2. **Computation of Capital Gains**

Particulars	₹	₹
Sale consideration	2,50,00,000	
Less: Indexed cost of acquisition(₹ 20,00,000 x 1125/1125)	20,00,000	
	2,30,00,000	
Less : Exemption under section 54	1,00,00,000	
Taxable long term capital gain		**1,30,00,000**

As per the definition of the indexed cost of acquisition under clause (iii) of *Explanation to* section 48, indexation benefit will be available only from the previous year in which Mr. A first held the asset i.e. P.Y. 2016-17. Since Mr. A sold the asset in the same year in

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which it was held by him, cost of acquisition and indexed cost of acquisition would be same.

Note: *As per the view expressed by Bombay High Court, in the case of CIT v. Manjula J. Shah 16 Taxmann 42, in case the cost of acquisition of the capital asset in the hands of the assessee is taken to be cost of such asset in the hands of the previous owner, the indexation benefit would be available from the year in which the capital asset is acquired by the previous owner. If this view is taken, the indexed cost of acquisition would be ₹ 2,25,00,000 and long term capital gain (before exemption under section 54) would be ₹ 25,00,000. Therefore, exemption under section 54 would be restricted to ₹ 25,00,000 and the taxable long term capital gain would be Nil.*

3. It has been assumed that the loss from house property and business loss have been set-off fully against long term capital gains. Therefore, ₹ 1 lakh relating to section 80C investments are deducted against "Income from other sources". The taxable income represents long term capital gains only and the tax liability is computed accordingly.

Question 38

Mr. Rahul, an assessee aged 61 years, gives the following information for the previous year ended 31-03-2017:

Sl. No.	***Particulars***	**₹**
a.	*Loss from profession*	*1,05,000*
b.	*Capital loss on the sale of property - short term*	*55,000*
c.	*Capital gains on sale of unlisted shares - long term*	*2,05,000*
d.	*Loss in respect of self occupied property*	*15,000*
e.	*Loss in respect of let out property*	*30,000*
f.	*Share of loss from firm*	*1,60,000*
g.	*Income from card games*	*55,000*
h.	*Winnings from lotteries*	*1,00,000*
i.	*Loss from horse races in Mumbai*	*40,000*
j.	*Medical Insurance premium paid by cheque*	*18,000*

Compute the total income of Mr. Rahul for the assessment year 2017-18.

Answer

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

Particulars	**₹**	**₹**
Income from house property		
Loss (₹ 15,000 + ₹ 30,000)	(45,000)	

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Profits and gains from business or profession		
Loss from profession	(1,05,000)	
Capital Gains		
Long-term capital gains on sale of shares		2,05,000
Less: Short-term capital loss on sale of property **(Note 1)**		55,000
Income under the head "Capital Gains"		1,50,000
Less: Set-off of losses under other heads of income **(Note 2)**		
Loss from profession	1,05,000	
Loss under the head "Income from house property" (₹ 15,000 + ₹ 30,000)	45,000	1,50,000
		Nil
Income from other sources		
Income from card games	55,000	
Winnings from lotteries	1,00,000	1,55,000
Gross total income		**1,55,000**
Less: Deductions under Chapter VIA **(Note 4)**		Nil
Total Income		**1,55,000**

Notes:

(1) As per section 74, short-term capital loss can be set-off against both short-term capital gains and long-term capital gains. Hence, short term capital loss of ₹ 55,000 can be set-off against long-term capital gains of ₹ 2,05,000 on sale of shares. The net income under the head "Capital gains" would be ₹ 1,50,000.

(2) Section 71 provides for set-off of loss from one head against income from another. As per section 71(2), loss under any head of income, other than capital gains, can be set-off against income under any head, including capital gains. Therefore, loss of ₹ 1,05,000 from profession and loss of ₹ 45,000 from house property (both let out and self-occupied) can be set-off against the net income of ₹ 1,50,000 under the head "Capital Gains".

(3) Loss from an exempt source cannot be set-off against profit from a taxable source. Therefore, share of loss from a firm cannot be set-off against any other income, since share of profit from firm is exempt under section 10(2A).

(4) As per section 58(4), no deduction in respect of any expenditure or allowance in connection with income by way of winnings from lotteries and income from card games is allowable under any provision of the Income-tax Act, 1961. Therefore, since the total income comprises only of income from card games and winnings from lotteries, deduction under Chapter VI-A is not allowable from such income. Therefore, Mr. Rahul will not be entitled to claim deduction under section 80D in respect of medical insurance premium paid by cheque.

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(5) Further, loss from horse races can neither be set-off against winnings from lotteries and income from card games nor can it be carried forward.

Question 39

Mr. Vishal is a resident individual. His Profit & Loss Account for the year ended 31st March, 2017is given below:

	₹		₹
To Staff Salary	*3,57,500*	*By Gross profit*	*13,55,500*
To Office Rent	*78,000*	*By Interest on Post Office Monthly Income scheme*	*98,400*
To Administrative Expenses	*2,14,000*	*By Bank F.D. interest (Net of TDS 7,000)*	*63,000*
To Income-tax	*1,60,000*	*By Rent (on let out property)*	*66,000*
To Depreciation	*67,500*	*By Winning from lotteries(Net of TDS 7,500)*	*17,500*
To Net Profit	*7,23,400*		
	16,00,400		***16,00,400***

Following further information is given to you:

(i) During the financial year 2016-17, he deposited ₹ 1,50,000 into his Public Provident Fund Account (i.e. on 27-3-2017)

(ii) He received annual salary of ₹ 1,20,000 and annual Commission of ₹ 60,000 from a partnership firm in the capacity of working partner. It is fully chargeable to tax under section 28 (v).

(iii) Received annuity pension of ₹ 72,500 from LIC of India.

(iv) Paid medical insurance premium of ₹ 26,850. The medical insurance was on self. Mr. Vishal is not a senior citizen.

(v) Life Insurance Premium of ₹ 25,000 was paid on the policy standing in the name of his wife Sujatha.

(vi) Administrative expenses include ₹ 5,000 being municipal tax on let out property.

(vii) Depreciation eligible as per the Income-tax Act, 1961 amounts to ₹ 57,000.

Compute the total income of Mr. Vishal for the Assessment year 2017-18.

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Answer

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

Particulars	₹	₹	₹
Income from House Property			
Gross Annual Value – Rent received **(Note 1)**		66,000	
Less: Municipal taxes paid		5,000	
Net Annual Value		61,000	
Less: Deduction under section 24 @ 30% of NAV		18,300	42,700
Profits and gains of business or profession			
Net Profit as per Profit & Loss Account		7,23,400	
Add: **Expenses not allowable**			
Income-tax	1,60,000		
Depreciation charged	67,500		
Municipal Taxes paid on let out property	5,000	2,32,500	
		9,55,900	
Less: **Income not forming part of business income**			
Interest on Post Office Monthly Income scheme	98,400		
Interest on Bank Fixed Deposit	63,000		
Rent received	66,000		
Winning from lotteries	17,500	2,44,900	
		7,11,000	
Less: Depreciation as per Income-tax Act, 1961		57,000	
		6,54,000	
Add: Salary received from partnership firm **(Note 2)**		1,20,000	
Commission received from partnership firm (**Note 2)**		60,000	8,34,000
Income from other sources			
Interest on Post Office Monthly Income scheme		98,400	
Interest on Bank Fixed Deposit (₹63,000 + ₹7,000)		70,000	
Winning from lotteries (₹17,500 + ₹7,500)		25,000	
Annuity pension received from LIC of India		72,500	2,65,900
Gross Total income			**11,42,600**
Less: **Deductions under Chapter VI-A**			
(i) **Deduction under section 80C**			

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	Deposit in PPF	1,50,000	
	Life insurance premium paid for his wife	25,000	
		1,75,000	
	Restricted to	1,50,000	
(ii)	**Deduction under section 80D**		
	Mediclaim premium of ₹ 26,850 paid for insurance on self. However, the deduction is restricted to ₹ 25,000.	25,000	1,75,000
Total income			**9,67,600**

Notes:

(1) Rent received is assumed to be the gross annual value of the let out property in absence of any information regarding municipal value, fair rental value and standard rent.

(2) Any salary, bonus, commission or remuneration, by whatever name called, due to or received by a partner of a firm shall not be treated as salary but it shall be treated as income from business or profession for the purposes of section 28.

Question 40

Mr. Vinod Kumar, resident, aged 62, furnishes the following information pertaining to the year ended 31-3-2017:

		(₹)
(i)	*Pension received (Net of TDS)*	*6,27,000*
(ii)	*Short-term capital gains (from sale of listed shares)*	*65,000*
(iii)	*Long-term capital gains (from sale of listed shares)*	*1,24,000*
(iv)	*Interest on fixed deposit from bank*	*1,60,000*
(v)	*Pertaining to technical consultancy services provided by him:*	
	Gross receipts	*51,60,000*
	Expenses:	
	Rent for premises	*5,44,000*
	Salaries	*11,20,000*
	Miscellaneous expenditure (revenue)	*3,91,000*
	Conveyance	*3,00,000*
(vi)	*Contribution to PPF*	*1,10,000*
(vii)	*Premium on life insurance policy taken on 10-1-2017 (sum assured ₹ 5,00,000)*	*60,000*
(viii)	*Mediclaim Insurance Premium for self (paid otherwise than by cash)*	*27,000*

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	Preventive health checkup expenses (in cash)	*6,000*
(ix)	*Donation given in cash to a charitable trust registered under Section 12AA (eligible for deduction under section 80G) of the Income-tax Act, 1961*	*14,000*
(x)	*Interest received from Post Office Savings A/c*	*18,000*

Additional information:

- *TDS from pension* *25,000*
- *1/4th of conveyance expenses is estimated for personal use.*

Listed shares were sold in recognized stock exchange.

Compute the total income of the assessee for the assessment year 2017-18, under proper heads of income.

Answer

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

Particulars	₹	₹	₹
Income from Salary			
Pension received (net of TDS)		6,27,000	
Add: Tax deducted at source		25,000	6,52,000
Profits and gains from business or profession			
Gross Receipts		51,60,000	
***Less:* Expenses**			
Rent for premises allowable under section 30(a)	5,44,000		
Salaries	11,20,000		
Miscellaneous expenditure[2]	3,91,000		
Conveyance for official use [3/4th of ₹ 3,00,000]	2,25,000	22,80,000	28,80,000
Capital Gains			
Long-term capital gains on sale of listed shares – exempt under section 10(38), since securities transaction tax would have been paid as the same have been sold in a recognized stock exchange		-	
Short-term capital gains on sale of listed shares – taxable @15% under section 111A, since securities transaction tax would have been paid as the same			

[2] Assuming that the same incurred wholly and exclusively for the purpose of the profession

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have been sold in a recognized stock exchange		65,000	65,000
Income from Other Sources			
Interest on fixed deposit from bank		1,60,000	
Interest on Post Office Savings Account	18,000		
Less: Exempt under section 10(15)	3,500	14,500	
			1,74,500
Gross Total Income			**37,71,500**
***Less*: Deductions under Chapter VI-A**			
Under section 80C			
Contribution to PPF	1,10,000		
Life insurance premium paid ₹ 60,000 (restricted to 10% of sum assured, since the policy was taken after 31.3.2012)	50,000		
	1,60,000		
Restricted to		1,50,000	
Under section 80D			
Medical insurance premium (paid otherwise than by cash)	27,000		
Preventive health check-up (allowed even if paid by cash), ₹6,000, restricted to	5,000		
	32,000		
Restricted to ₹ 30,000, since Mr. Vinod Kumar is a resident individual of the age of 62 years (i.e., 60 years or more at any time during the previous year)		30,000	
Under section 80G			
As per section 80G(5D), cash donation to charitable trust of an amount exceeding ₹ 10,000 is not allowable as deduction		-	
Under section 80TTA			
Interest from Post Office Savings Account, ₹ 14,500, restricted to		10,000	
			1,90,000
Total Income			**35,81,500**

Mr. Vinod Kumar is engaged in Technical Consultancy services which is specified under section 44AA.

Since Mr. Vinod Kumar's Gross Receipts exceed ₹ 50 lakhs, he cannot opt for presumptive taxation u/s 44ADA. He has to get then audited u/s 44AB.

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Question 41

Mrs. Ann provides the following information for the financial year ending 31-3-2017. Compute her total income and tax payable thereon for A.Y.2017-18 as per Income-tax Act 1961.

Income / Receipts:

(1) Salary from M/s. Prominent Technologies - ₹ 60,000 per month (Joined from 1st March, 2016).

(2) She is in receipt of HRA, ₹ 15,000 per month and also educational allowance of ₹ 1,500 per month for all the three of her children.

(3) She bought a truck on 01-08-2016 and has been letting it on hire. She does not maintain books of account for this business. But she declares for income tax purpose, that she is earning net income of ₹ 11,000 per month from this business.

(4) She received ₹ 8,500 as interest on Post Office Savings Bank Account.

(5) She received ₹ 25,000 as interest from Company Deposits.

(6) Amounts withdrawn from National Savings Scheme, 1992 (Principal ₹ 20,000 & Interest ₹ 35,000)

Expenses / Payments:

(1) Interest payable to bank ₹ 1,000 per month on loan for the purchase of truck.

(2) Total interest paid to bank for loan borrowed for investing in company deposits is ₹ 5,000.

(3) Rent paid for residence is ₹ 18,000 per month.

(4) Tuition fees paid for the year 2016-17 for her three children is ₹ 50,000, ₹ 30,000 and ₹ 20,000, respectively, to educational institution situated in India.

(5) Medical insurance premium for her and for her husband is ₹ 30,000 (paid by cheque) and ₹ 25,000 (paid by cash), respectively.

(6) She has deposited during the year, in 5 year Post Office Recurring Deposit Scheme, ₹ 20,000.

Answer

Computation of total income of Mrs. Ann for the Assessment Year 2017-18

Particulars	₹	₹
Income from Salary		
Basic Salary (₹ 60,000 × 12)		7,20,000
HRA (₹ 15,000 × 12)	1,80,000	
Less: Exempt under section 10(13A) **[See Note 1 below]**	1,44,000	36,000

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Education Allowance (₹1,500×12)		18,000	
Less: Exempt under section 10(14)@₹100 per month per child and maximum for 2 child (₹100 × 12 × 2)		2,400	15,600
			7,71,600
Profits and gains from business or profession			
Income from the business of letting on hire a truck under section 44AE **[See Note 2 below]**			88,000
Income from Other Sources	₹		
Interest on Post Office Savings Bank Account	8,500		
Less: Exempt under section 10(15)	3,500	5,000	
Interest from company deposits	25,000		
Less: Deduction u/s 57 in respect of interest on loan paid for investing in company deposits	5,000	20,000	
Interest on National Savings Scheme, 1992		35,000	60,000
Gross Total Income			**9,19,600**
Less: **Deductions under Chapter VI-A**			
Under section 80C [Tuition fees paid for two children – most favorable to Mrs. Ann being ₹ 50,000 + ₹ 30,000]		80,000	
Deposit in 5 year Post Office Recurring Deposit Scheme does not qualify for deduction under section 80C.		Nil	
Under section 80D [Medical Insurance Premium paid by cheque for insurance of self and spouse together would qualify for deduction upto a maximum of ₹ 25,000]		25,000	
Under section 80TTA [Interest from Post Office Saving Bank Account – **See Note 3 below**]		5,000	
			1,10,000
Total Income			**8,09,600**

Computation of tax payable for the A.Y.2017-18

Particulars	₹
Tax on ₹ 8,09,600 [₹ 61,920 (20% of ₹ 3,09,600) + ₹ 25,000]	86,920
Add: Education cess @ 2% and SHEC @ 1%	2,608
Tax Payable	**89,528**

Notes:

(1) HRA is exempt to the extent of the least of the following under section 10(13A) -

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(1) 50% of salary i.e., 50% of ₹ 7,20,000 = ₹ 3,60,000 (in case Mrs. Ann resides in Delhi, Mumbai, Calcutta or Chennai) **(or)** 40% of salary i.e., 40% of ₹ 7,20,000 = ₹ 2,88,000 (in case Mrs. Ann resides in any other place)

(2) Excess of rent paid over 10% of salary = (₹ 18,000 – ₹ 6,000) × 12 = ₹ 1,44,000

(3) Actual HRA received = ₹ 15,000 × 12 = ₹ 1,80,000

Least of the above i.e., ₹ 1,44,000 is exempt under section 10(13A)

(2) In the case of a person owning not more than 10 vehicles at any time during the previous year, estimated income from each vehicle will be deemed to be ₹ 7,500 for every month or part of the month during which such vehicle is owned by the assessee in the previous year or an amount claimed to have been actually earned from such vehicle, whichever is higher [Section 44AE].

In this case, since the assessee declares a higher amount of ₹ 11,000 per month as the net income actually earned by her from letting on hire truck, such amount will be considered as income under section 44AE. Interest paid @ ₹ 1,000 p.m. is not deductible, since under section 44AE, all deductions as per sections 30 to 38 are deemed to have been allowed.

Truck was plied for the period 01.08.2016 to 31.03.2017 for 8 months.

Therefore, in this case, income under section 44AE is ₹11,000 × 8 = ₹ 88,000

(3) Interest upto ₹ 3,500 on post office savings bank account is exempt under section 10(15). The balance interest of ₹ 5,000 would be included under the head "Ïncome from other sources" and form part of gross total income. However, the same would qualify for deduction under section 80TTA, since interest upto ₹ 10,000 from, *inter alia,* post office savings bank account qualifies for deduction thereunder.

Question 42

Mr. Venus provides the following details for the previous year ending 31-3-2017

(i)	*Salary from HNL Ltd.*	*₹ 50,000 per month*
(ii)	*Interest on FD with SBI for the financial year 2016-17*	*₹ 72,000 (Net of TDS)*
(iii)	*Determined long term capital loss of A Y 2015-16 (to be carried forward)*	*₹ 96,000*
(iv)	*Long term capital gain*	*₹ 75,000*

(v) *Loss of minor son ₹ 90,000 computed in accordance with the provisions of Income- tax Act, 1961. Mr. Venus transferred his own house to his minor son without adequate consideration few years back and minor son let it out and suffered loss.*

(vi)	*Loss of his wife's business*	*₹ (2,00,000)*

She carried business with funds which Mr. Venus gifted to her.

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You are required to compute taxable income of Mr. Venus for the AY 2017-18.

Answer

Computation of Taxable Income of Mr. Venus for the A.Y. 2017-18

Particulars	₹	₹
Salaries		
Income from Salary (₹ 50,000 × 12)	6,00,000	
Less: Loss from house property in respect of which Mr. Venus is the deemed owner to be set off against his salary income as per section 71(1) **[See Note 1]**	90,000	5,10,000
Capital Gains		
Long term capital gain	75,000	
Less: Brought forward long term capital loss of A.Y. 2015-16 set off against current year long-term capital gain as per section 74(1) & (2) **[See Note 2]**	75,000	Nil
Balance long-term capital loss of ₹ 21,000 (₹ 96,000 – ₹ 75,000) of A.Y.2015-16 to be carried forward to A.Y.2018-19 **[See Note 2]**		
Income from Other Sources		
Interest on fixed deposit with SBI (₹ 72,000 × 100/90)	80,000	
Less: Business loss incurred by wife includible in Mr. Venus's hands set off against interest income as per section 71(1) **[See Notes 3 & 4]**	80,000	Nil
Balance business loss of ₹ 1,20,000 (₹ 2,00,000 – ₹ 80,000) to be carried forward to A.Y. 2018-19		
Taxable Income		**5,10,000**

Notes:

(1) As per section 27(i), Mr. Venus is the deemed owner of the house transferred to his minor son without adequate consideration. Hence, the income from house property would be assessable in Mr. Venus's hands. Since there is a loss from house property transferred to minor son without adequate consideration, Mr. Venus can set-off the same against salary income, since he is the deemed owner of such property.

(2) As per section 74(1) and 74(2), brought forward long-term capital loss can be set-off only against long-term capital gains. Unabsorbed long-term capital loss can be carried forward for a maximum of eight assessment years (upto A.Y.2023-24, in this case) for set-off against long-term capital gains.

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(3) As per section 64(1)(iv), income from funds gifted to spouse by an individual and invested in business by the spouse is includible in the hands of the individual. As per *Explanation 2* to section 64, income includes "loss". Hence, in the given case, loss arising out of the business carried on by Mr. Venus's wife is to be included in the income of Mr. Venus, as she has carried on business with the funds gifted to her by Mr. Venus.

(4) As per section 71(2A), business loss cannot be set-off against salary income. However, the same can be set-off against income from other sources (consisting of interest on fixed deposit).

Exercise

1. *Income under the Income-tax Act, 1961, is to be computed under -*
   - *(a) five heads*
   - *(b) six heads*
   - *(c) four heads*
2. *What is the basic exemption limit for a woman assessee for A.Y. 2017-18, who turned 60 years on 2.4.2017?*
   - *(a). ₹ 2,00,000*
   - *(b). ₹ 3,00,000*
   - *(c). ₹ 2,50,000*
3. *What is the rate of surcharge applicable to individuals having total income exceeding ₹ 1 crore?*
   - *(a). 15%*
   - *(b). 12%*
   - *(c). 10%*
4. *What is the basic exemption limit for Mrs. X, a resident individual who is of the age of 80 years as on 30.3.2017?*
   - *(a). ₹ 5,00,000*
   - *(b). ₹ 2,40,000*
   - *(c). ₹ 3,00,000*
5. *Share of profit of Mr. P, who is a partner in M/s PQR is –*
   - *(a) exempt from tax*
   - *(b) taxable as his business income*
   - *(c) taxable as his salary*
6. *Explain briefly the tax treatment of the following income of Mr. X, who is a partner in the firm M/s. XYZ –*

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(i) Salary received by Mr. X from M/s. XYZ.

(ii) Interest (on loan) received from M/s. XYZ.

(iii) Share of profit from the firm.

7. *Discuss the tax treatment of the following income of Mr. A, who is a member of a HUF-*

   (i) Share of income from HUF.

   (ii) Income from an impartible estate of the HUF.

   (iii) Income from self-acquired property converted into joint family property.

Answers

1. a; **2.**c; **3.**a; **4.**a; **5.**a

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9 Provisions Concerning Advance Tax and Tax Deducted at Source

Key Points

Advance Tax

Common advance tax payment schedule for corporates and non-corporates (other than an eligible assessee in respect of eligible business referred to in section 44AD) from 1st June, 2016:

Due date of installment	Amount payable
On or before 15th June	Not less than 15% of advance tax liability.
On or before 15th September	Not less than 45% of advance tax liability *less* amount paid in earlier installment.
On or before 15th December	Not less than 75% of advance tax liability *less* amount paid in earlier installment or installments.
On or before 15th March	Whole amount of advance tax liability *less* amount paid in earlier installment or installments.

Eligible assessee computing profits on presumptive basis under section 44AD to pay advance tax by 15th March

An eligible assessee, opting for computation of profits or gains of business on presumptive basis in respect of eligible business referred to in section 44AD, shall be required to pay advance tax of the whole amount in one instalment on or before the 15th March of the financial year.

However, any amount paid by way of advance tax on or before 31st March shall also be treated as advance tax paid during each financial year on or before 15th March.

Interest for non-payment or short-payment of advance tax [Section 234B]

(1)	Interest under section 234B is attracted for non-payment of advance tax or payment of advance tax of an amount less than 90% of assessed tax.
(2)	The interest liability would be 1% per month or part of the month from 1st April following the financial year upto the date of determination of income under section 143(1).

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(3)	Such interest is calculated on the amount of difference between the assessed tax and the advance tax paid.
(4)	Assessed tax is the tax calculated on total income less tax deducted at source.
Interest payable for deferment of advance tax [Section 234C]	
(a)	**Manner of computation of interest under section 234C for deferment of advance tax by corporate and non-corporate assessees**: In case an assessee, other than an eligible assessee in respect of the eligible business referred to in section 44AD, who is liable to pay advance tax under section 208 has failed to pay such tax or the advance tax paid by such assessee on its current income on or before the dates specified in column (1) is less than the specified percentage [given in column (2)] of tax due on returned income, then simple interest@1% per month for the period specified in column (4) on the amount of shortfall, as per column (3) is leviable under section 234C.

Specified date	Specified %	Shortfall in advance tax	Period
(1)	**(2)**	**(3)**	**(4)**
15th June	15%	15% of tax due on returned income (-) advance tax paid up to 15th June	3 months
15th September	45%	45% of tax due on returned income (-) advance tax paid up to 15th September	3 months
15th December	75%	75% of tax due on returned income (-) advance tax paid up to 15th December	3 months
15th March	100%	100% of tax due on returned income (-) advance tax paid up to 15th March	1 month

Note *– However, if the advance tax paid by the assessee on the current income, on or before 15th June or 15th September, is not less than 12% or, as the case may be, 36% of the tax due on the returned income, then, the assessee shall not be liable to pay any interest on the amount of the shortfall on those dates.*

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(b)	**<u>Computation of interest under section 234C in case of an eligible assessee in respect of eligible business referred to in section 44AD</u>**: In case an eligible assessee in respect of the eligible business referred to in section 44AD, who is liable to pay advance tax under section 208 has failed to pay such tax or the advance tax paid by the assessee on its current income on or before 15th March is less than the tax due on the returned income, then, the assessee shall be liable to pay simple interest at the rate of 1% on the amount of the shortfall from the tax due on the returned income.
(c)	**<u>Non-applicability of interest under section 234C in certain cases</u>**: Interest under section 234C shall not be leviable in respect of any shortfall in payment of tax due on returned income, where such shortfall is on account of under-estimate or failure to estimate – (i) the amount of capital gains; (ii) income of nature referred to in section 2(24)(ix) i.e., winnings from lotteries, crossword puzzles etc.; (iii) income under the head "Profits and gains of business or profession" in cases where the income accrues or arises under the said head for the first time. However, the assessee should have paid the whole of the amount of tax payable in respect of such income referred to in (i), (ii) and (iii), as the case may be, had such income been a part of the total income, as part of the remaining instalments of advance tax which are due or where no such instalments are due, by 31st March of the financial year.

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Deduction of Tax at source

Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
192	Salary	Basic exemption limit (₹2,50,000/ ₹3,00,000, as the case may be)	Any person	Individual	Average rate of income-tax computed on the basis of the rates in force.	At the time of payment	Allowances, to the extent exempt under section 10, and exempt perquisites would be excluded.
193	Interest on Securities	8% Savings (Taxable) Bonds, 2003 – ₹ 10,000 Interest on debentures issued by a company in which the public are substantially interested, paid or credited to a resident individual or HUF - ₹ 5,000	Any person	Any resident	10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	Some exempted interest payments are interest – - On any security of the Central Government or a State Government. - Payable to LIC, GIC or any of the four public sector insurance companies formed by GIC in respect of any securities owned by it or in which it has full beneficial interest. - Payable to any other insurer in respect of any securities owned by it or in which it has full beneficial interest. - Payable on any security issued by a company, where such security is in dematerialized form and is listed on a recognized stock exchange in India.

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Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194	Dividend	₹ 2,500 in a financial year	The Principal Officer of a domestic company	Resident Individual	10%	At the time of payment	Dividend credited or paid to LIC, GIC or any of the four public sector insurance companies formed by GIC, or any other insurer, in respect of shares owned by it or in which it has full beneficial interest. Dividend referred to in section 115-O, since the domestic company distributing dividend has paid dividend distribution tax on such dividend.
194A	Interest other than interest on securities	₹ 10,000 in a financial year, in case of interest paid by – (i) a banking company; (ii) a co-operative society engaged in banking business; and (iii) deposits with post office.	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any Resident	10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	Interest credited or paid to: - any banking company, or a cooperative society engaged in the business of banking - any financial corporation established by or under a Central, State or Provincial Act. - the Life Insurance Corporation of India. - the Unit Trust of India; - any company and cooperative society carrying on the business of insurance. - notified institution, association, body or class of institutions, associations or bodies Interest credited or paid by a firm to a partner

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Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
		₹ 5,000 in a financial year, in other cases.					Interest credited or paid by a co-operative society to its member or to any other co-operative society, etc.
194B	Winnings from any lottery, crossword puzzle or card game or other game of any sort	₹ 10,000	Any Person	Any Person	30%	At the time of payment	-
194BB	Winnings from horse race	₹ 10,000 (₹ 5,000 upto 31.5.2016)	Book Maker or a person holding licence for horse racing, wagering or betting in any race course.	Any Person	30%	At the time of payment	-

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Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194C	Payments to Contractors	Single sum credited or paid - ₹ 30,000 **or** The aggregate of sums credited or paid during the financial year - ₹ 1,00,000 (₹ 75,000 upto 31.5.2016)	Central / State Govt., Local authority, Central/ State/Provin-cial Corpn., company, firm, trust, co-operative society, individuals/ HUFs liable to tax audit in the immediately preceding financial year.	Any Resident contractor for carrying out any work (including supply of labour)	1% of sum paid or credited, if the payee is an Individual or HUF 2% of sum paid or credited, if the payee is any other person.	At the time of credit of such sum to the account of the contractor or at the time of payment, whichever is earlier.	Any sum credited or paid to a contractor in transport business, who owns ten or less goods carriages at any time during the previous year if the contractor furnishes a declaration to that effect alongwith his PAN to the person paying or crediting such sum. Any sum credited or paid by an individual or HUF exclusively for personal purposes of such individual or HUF.
194D	Insurance Commission	₹ 15,000 in a financial year (₹ 20,000 upto 31.5.2016)	Any person	Any Resident	10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	

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Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194DA	Any sum under a Life Insurance Policy	Less than ₹ 1,00,000 (aggregate amount of payment to a payee in a financial year)	Any person	Any resident	1% (2% upto 31.5.2016)	At the time of payment	Sums which are exempt under section 10(10D)
194H	Commission or brokerage	₹ 15,000 in a financial year (₹ 5,000 upto 31.5.2016)	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any resident	5% (10% upto 31.5.2016)	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	Commission or brokerage payable by BSNL or MTNL to their PCO franchisees.
194-I	Rent	₹ 1,80,000 in a financial year	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any resident	For P & M or equipment- 2% For land, building, furniture or fixtures -10%	At the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier.	-

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Section	Description	Threshold Limit	Payer	Type of Payee	Rate of TDS	Time of deduction	Payments / Income exempted from TDS
194-IA	Payment on transfer of certain immovable property	Less than ₹ 50 lakh (Consideration for transfer)	Any person, being a transferee	Resident transferor	1%	At the time of credit of such sum to the account of the transferor or at the time of payment, which-ever is earlier.	Payment for transfer of agricultural land
194J	Fees for professional or technical services/ Royalty/ Non-compete fees/ Director remuneration	₹ 30,000 in a financial year, for each category of income. (However, this limit does not apply in case of payment made to director of a company).	Any person, other than an individual or HUF not liable to tax audit u/s 44AB in the immediately preceding financial year.	Any Resident	10%	At the time of credit of such sum to the account of the payee or at the time of payment, whichever is earlier.	Any sum by way of fees for professional services credited or paid by an individual or HUF exclusively for personal purposes of such individual or any member of HUF.
194LA	Compensation on acquisition of certain immovable property	₹ 2,50,000 in a financial year (₹ 2,00,000 upto 31.5.2016)	Any person	Any Resident	10%	At the time of payment	Compensation on acquisition of agricultural land.

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Question 1

Compute the amount of tax deduction at source on the following payments made by M/s. S Ltd. during the financial year 2016-17 as per the provisions of the Income-tax Act, 1961.

Sr. No.	*Date*	*Nature of Payment*
(i)	*1-10-2016*	*Payment of ₹ 2,00,000 to Mr. "R" a transporter who owns 8 goods carriages throughout the previous year and furnishes a declaration to this effect alongwith his PAN.*
(ii)	*1-11-2016*	*Payment of fee for technical services of ₹ 25,000 and Royalty of ₹ 20,000 to Mr. Shyam who is having PAN.*
(iii)	*30-06-2016*	*Payment of ₹ 25,000 to M/s X Ltd. for repair of building.*
(iv)	*01-01-2017*	*Payment of ₹ 2,00,000 made to Mr. A for purchase of diaries made according to specifications of M/s S Ltd. However, no material was supplied for such diaries to Mr. A by M/s S Ltd.*
(v)	*01-01-2017*	*Payment made ₹ 1,80,000 to Mr. Bharat for compulsory acquisition of his house as per law of the State Government.*
(vi)	*01-02-2017*	*Payment of commission of ₹ 14,000 to Mr. Y.*

Answer

(i) No tax is required to be deducted at source under section 194C by M/s S Ltd. on payment to transporter Mr. R, since he satisfies the following conditions:

(1) He owns ten or less goods carriages at any time during the previous year.

(2) He is engaged in the business of plying, hiring or leasing goods carriages;

(3) He has furnished a declaration to this effect along with his PAN.

(ii) As per section 194J, liability to deduct tax is attracted only in case the payment made as fees for technical services and royalty, individually, exceeds ₹ 30,000 during the financial year. In the given case, since, the individual payments for fee of technical services i.e. ₹ 25,000 and royalty ₹ 20,000 is less than ₹ 30,000 each, there is no liability to deduct tax at source. It is assumed that no other payment towards fees for technical services and royalty were made during the year to Mr. Shyam.

(iii) Provisions of section 194C are not attracted in this case, since the payment for repair of building on 30.06.2016 to M/s. X Ltd. is less than the threshold limit of ₹ 30,000**.**

(iv) According to section 194C, the definition of "work" does not include the manufacturing or supply of product according to the specification by customer in case the material is purchased from a person other than the customer.

Therefore, there is no liability to deduct tax at source in respect of payment of ₹ 2,00,000 to Mr. A, since the contract is a contract for 'sale'.

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(v) As per section 194LA, any person responsible for payment to a resident, any sum in the nature of compensation or consideration on account of compulsory acquisition under any law, of any immovable property, is responsible for deduction of tax at source if such payment or the aggregate amount of such payments to the resident during the financial year exceeds ₹ 2,50,000.

In the given case, no liability to deduct tax at source is attracted as the payment made does not exceed ₹ 2,50,000.

(vi) As per section 194H, any person (other than an individual or HUF) who is responsible for paying commission or brokerage to a resident shall deduct tax at source @5% if the amount of such income or the aggregate of the amounts of such income credited or paid during the financial year exceeds ₹ 15,000.

Since the commission payment made to Mr. Y does not exceeds ₹ 15,000, the provisions of section 194H are not attracted.

Question 2

State the applicability of TDS provisions and TDS amount in the following cases:

(a) Rent paid for hire of machinery by B Ltd. to Mr. Raman ₹ 2,10,000.

(b) Fee paid to Dr. Srivatsan by Sundar (HUF) ₹ 35,000 for surgery performed on a member of the family.

Answer

(a) Since the rent paid for hire of machinery by B. Ltd. to Mr. Raman exceeds ₹ 1,80,000, the provisions of section 194-I for deduction of tax at source are attracted.

The rate applicable for deduction of tax at source under section 194-I on rent paid for hire of plant and machinery is 2% assuming that Mr. Raman had furnished his permanent account number to B Ltd.

Therefore, the amount of tax to be deducted at source:

= ₹ 2,10,000 x 2% = ₹ 4200.

Note: In case Mr. Raman does not furnish his permanent account number to B Ltd., tax shall be deducted @ 20% on ₹ 2,10,000, by virtue of provisions of section 206AA.

(b) As per the provisions of section 194J, a Hindu Undivided Family is required to deduct tax at source on fees paid for professional services only if it is subject to tax audit under section 44AB in the financial year preceding the current financial year.

However, if such payment made for professional services is exclusively for the personal purpose of any member of Hindu Undivided Family, then, the liability to deduct tax is not attracted.

Therefore, in the given case, even if Sundar (HUF) is liable to tax audit in the immediately preceding financial year, the liability to deduct tax at source is not attracted

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in this case since, the fees for professional service to Dr. Srivatsan is paid for a personal purpose i.e. the surgery of a member of the family.

Question 3

What are the provisions relating to tax deduction at source in respect of:

(a) ABC and Co. Ltd. paid ₹ 19,000 to one of its Directors as sitting fees on 1-01-2017.

(b) Mr. X sold his house to Mr. Y on 01-02-2017 for ₹ 60 lacs?

Answer

(a) Section 194J provides for deduction of tax at source @10% from any sum paid by way of any remuneration or fees or commission, by whatever name called, to a resident director, which is not in the nature of salary on which tax is deductible under section 192. The threshold limit of ₹ 30,000 upto which the provisions of tax deduction at source are not attracted in respect of every other payment covered under section 194J is, however, not applicable in respect of sum paid to a director.

Therefore, tax@10% has to be deducted at source under section 194J in respect of the sum of ₹ 19,000 paid by ABC Ltd. to its director.

(b) Section 194-IA requires every person, being a transferee, responsible for paying any sum as consideration for transfer of any immovable property (other than agricultural land), to deduct tax@1% of such sum, at the time of credit of such sum to the account of the resident transferor or at the time of payment of such sum to a resident transferor, whichever is earlier.

Such tax is required to be deducted at source where the consideration for transfer of immovable property is ₹ 50 lakhs or more.

In this case, since the consideration for transfer of house exceeds ₹ 50 lakhs, Mr. Y is liable to deduct tax at source@1% under section 194-IA on the consideration of ₹ 60 lakhs payable for transfer of house to Mr. X.

Question 4

Ashwin doing manufacture and wholesale trade furnishes you the following information :

Total turnover for the financial year

Particulars	***₹***
2015-16	*2,05,00,000*
2016-17	*95,00,000*

State whether tax deduction at source provisions are attracted for the below said expenses incurred during the financial year 2016-17:

Particulars	***₹***
Interest paid to UCO Bank	*41,000*

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Contract payment to Raj (2 contracts of ₹ 12,000 each)	*24,000*
Shop rent paid (one payee)	*1,90,000*
Commission paid to Balu (on 1.8.2016)	*7,000*

Answer

As the turnover of Ashwin for F.Y.2015-16, i.e. ₹ 205 lakh, has exceeded the monetary limit of ₹ 100 lakh prescribed under section 44AB, he has to comply with the tax deduction provisions during the financial year 2016-17, subject to, however, the exemptions provided for under the relevant sections for applicability of TDS provisions.

Interest paid to UCO Bank

TDS under section 194A is not attracted in respect of interest paid to a banking company.

Contract payment of ₹ 24,000 to Raj for 2 contracts of ₹ 12,000 each

TDS provisions under section 194C would not be attracted if the amount paid to a contractor does not exceed ₹ 30,000 in a single payment or ₹ 1,00,000 in the aggregate during the financial year. Therefore, TDS provisions under section 194C are not attracted in this case.

Shop Rent paid to one payee – Tax has to be deducted under section 194-I as the rental payment exceeds ₹ 1,80,000.

Commission paid to Balu – No, tax has to be deducted under section 194-H in this case as the commission does not exceed ₹ 15,000.

Question 5

State in brief the applicability of tax deduction at source provisions, the rate and amount of tax deduction in the following cases for the financial year 2016-17:

(i) Winning by way of jackpot in a horse race ₹ 1,00,000.

(ii) Payment made by a firm to sub-contractor ₹ 3,00,000 with outstanding balance of ₹ 1,20,000 shown in the books as on 31-03-2017.

(iii) Rent paid for plant and machinery ₹ 1,50,000 by a partnership firm having sales turnover of ₹ 20,00,000 and net loss of ₹ 15,000.

(iv) Payment made to Ricky Ponting, an Australian cricketer, by a newspaper for contribution of articles ₹ 25,000.

Answer

(i) Provisions for tax deduction at source under section 194BB @ 30% are attracted if the amount exceeds ₹ 10,000 in respect of income arising by way of winning a jackpot in horse races.

Tax to be deducted = ₹ 1,00,000 x 30% = ₹ 30,000

(ii) Provisions of tax deduction at source under section 194C are attracted in respect of

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payment by a firm to a sub-contractor. Under section 194C, tax is deductible at the time of credit or payment, whichever is earlier @ 1% if the payment is made to an individual or HUF and 2% for others.

Assuming that sub-contractor to whom payment has been made is an individual and the aggregate amount credited during the year is ₹ 4,20,000, tax is deductible @ 1% on ₹ 4,20,000.

Tax to be deducted = ₹ 4,20,000 x 1% = ₹ 4,200

(iii) As per section 194-I, tax is to be deducted @ 2% on payment of rent for plant and machinery, only if the payment exceeds ₹ 1,80,000 during the financial year. Since rent of ₹ 1,50,000 paid by a partnership firm does not exceed ₹ 1,80,000, tax is not deductible.

(iv) Under section 194E, the person responsible for payment of any amount to a non-resident sportsman for contribution of articles relating to any game or sport in India in a newspaper shall deduct tax @ 20%. Further, since Ricky Ponting is a non-resident, education cess @2% and secondary and higher education cess @ 1% on TDS would also be added.

Therefore, tax to be deducted = ₹ 25,000 x 20.60% = ₹ 5,150.

Question 6

State in brief the applicability of tax deduction at source provisions, the rate and amount of tax deduction in the following cases for the financial year 2016-17:

(1) Payment of ₹ 27,000 made to Jacques Kallis, a South African cricketer, by an Indian newspaper agency on 02-07-2016 for contribution of articles in relation to the sport of cricket.

(2) Rent of ₹ 1,70,000 paid by a partnership firm for use of plant and machinery.

(3) Winning from horse race ₹ 1,50,000.

(4) ₹ 2,00,000 paid to Mr. A, a resident individual, on 22-02-2017 by the State of Uttar Pradesh on compulsory acquisition of his urban land.

Answer

(1) Section 194E provides that the person responsible for payment of any amount to a non-resident sportsman for contribution of articles relating to any game or sport in India in a newspaper **has to deduct tax at source** @ 20%. Further, since Jacques Kallis, a South African cricketer, is a non-resident, education cess @2% and secondary and higher education cess @1% on TDS should also be added.

Therefore, tax to be deducted = ₹ **27,000 x 20.60% = ₹ 5,562.**

(2) As per section 194-I, tax is to be deducted at source @ 2% on payment of rent for use of plant and machinery, only if the payment exceeds ₹ 1,80,000 during the financial year.

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Since rent of ₹ 1,70,000 paid by a partnership firm does not exceed ₹1,80,000, **tax is not deductible**.

(3) Under section 194BB, tax is to be deducted at source, if the winnings from horse races exceed ₹ 10,000. The **rate of deduction of tax at source is 30%**. Assuming that winnings are paid to the residents, education cess@2% and secondary and higher education cess@1% has not been added to the tax rate of 30%.

Hence, tax to be deducted = ₹ 1,50,000 x 30% = **₹ 45,000.**

(4) As per section 194LA, any person responsible for payment to a resident, any sum in the nature of compensation or consideration on account of compulsory acquisition under any law, of any immovable property, is required to deduct tax at source @ 10%, if such payment or the aggregate amount of such payments to the resident during the financial year exceeds ₹ 2,50,000.

In the given case, there is no liability to deduct tax at source as the payment made to Mr. A does not exceed ₹ 2,50,000.

Question 7

Mr. Madan sold his house property in Surat as well as his rural agricultural land for a consideration of ₹ 65 lakhs and 20 lakhs, respectively, to Mr. Raman on 01-10-2016. He has purchased the house property for ₹ 40 lakhs and the land for ₹ 15 lakhs, in the year 2014. There was no difference in the stamp valuation. You are required to determine TDS implications, if any, assuming both persons are resident Indians.

Answer

As per section 194-IA, any person, being a transferee, responsible for paying to a resident transferor any sum by way of consideration for transfer of any immovable property (other than rural agricultural land) is required to deduct tax at source@1% of such sum, if the consideration for transfer is ₹ 50 lakhs or more. The deduction of tax at source has to be made at the time of credit of such sum to the account of the transferor or at the time of payment of such sum, whichever is earlier.

Accordingly, in this case, since the sale consideration of house property exceeds ₹ 50 lakh, Mr. Raman, the transferee, is required to deduct tax at source at 1% of ₹ 65 lakhs, being the consideration for transfer of house property.

The tax to be deducted under section 194-IA would be ₹ 65,000, being 1% of ₹ 65 lakh.

Since TDS provisions under section 194-IA are attracted in respect of transfer of any immovable property, other than rural agricultural land, no tax is required to be deducted by Mr. Raman from the sale consideration payable for transfer of rural agricultural land.

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Question 8

State the concessions granted to transport operators onwards in the context of cash payments under section 40A(3) and deduction of tax at source under section 194-C.

Answer

Section 40A(3) provides for disallowance of expenditure incurred in respect of which payment or aggregate of payments made to a person in a day exceeds ₹ 20,000, and such payment or payments are made otherwise than by account payee cheque or account payee bank draft.

However, in case of payment made to transport operators for plying, hiring or leasing goods carriages, the disallowance will be attracted only if the payments made to a person in a day exceeds ₹ 35,000. Therefore, payment or aggregate of payments up to ₹ 35,000 in a day can be made to a transport operator otherwise than by way of account payee cheque or account payee bank draft, without attracting disallowance under section 40A(3).

Under section 194C, tax had to be deducted in respect of payments made to contractors at the rate of 1% in case the payment is made to individual or Hindu Undivided Family or at the rate of 2% in any other case.

However, no deduction is required to be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor, during the course of the business of plying, hiring or leasing goods carriages, if the following conditions are fulfilled:-

(1) He owns ten or less goods carriages at any time during the previous year.

(2) He is engaged in the business of plying, hiring or leasing goods carriages;

(3) He has furnished a declaration to this effect along with his PAN.

Question 9

Mrs. Indira, a landlord, derived income from rent from letting a house property to M/s Vaibhav Corporation Ltd. of ₹ 1,00,000 per month. She charged service tax @ 15% on lease rent charges. Calculate the deduction of tax at source (TDS) to be made by M/s Vaibhavi Corporation Ltd. on payment made to Mrs. Indira and narrate related formalities in relation to TDS.

Answer

(1) As per *Circular No. 4/2008 dated 28th April, 2008* issued by the CBDT, the service tax paid by the tenant does not partake the nature of income of the landlord. The landlord only acts as a collecting agency for collection of service tax. Therefore, tax deducted at source under section 194-I would be required to be made on the amount of rent paid or payable excluding the amount of service tax, i.e. tax has to be deducted under section 194-I on ₹ 12 lakh.

(2) Tax is deductible @ 10% under section 194-I.

(3) Hence, in the given case, TDS under section 194-I would amount to ₹ 10,000, to be deducted every month.

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(4) Tax deducted should be deposited within prescribed time i,.e. on or before seven days from the end of the month in which the deduction is made and upto 30th April for the month of March.

Question 10

Bharghav doing textiles business furnishes you the following information:

Total turnover for the financial year:

	₹
2015-16	*205,00,000*
2016-17	*95,00,000*

State whether the provisions of tax deduction at source are attracted for the following expenses incurred during the financial year 2016-17:

	₹
Interest paid to Indian Bank on Term Loan	*92,800*
Advertisement expenses to R (two individual payments of ₹ 24,000 and ₹ 34,000)	*58,000*
Factory rent paid to C	*1,85,000*
Brokerage paid to B, a sub-broker (on 10.11.2016)	*16,000*

Answer

Since the turnover of Mr. Bharghav for F.Y.2015-16, i.e., ₹ 205 lakhs, has exceeded the monetary limit of ₹ 100 lakhs prescribed under section 44AB, he has to comply with the tax deduction provisions during the financial year 2016-17, subject to, however, the exemptions provided for under the relevant sections for applicability of TDS provisions.

(i) **Interest paid to Indian Bank on term loan**

TDS under section 194A is not attracted in respect of interest paid to a banking company.

(ii) **Advertisement expenses to R (two individual payments of ₹ 24,000 and ₹ 34,000)**

Under section 194C, the provisions for tax deduction at source would not be attracted if the amount paid to a contractor does not exceed ₹ 30,000 in a single payment or ₹ 100,000 in the aggregate during the financial year. Therefore, provisions for deduction of tax at source under section 194C are not attracted in respect of payment of ₹ 24,000 to R.

However, payment of ₹ 34,000 to R would attract TDS@1% under section 194C, since it exceeds ₹ 30,000.

Note - *The tax to be deducted would be ₹ 340, being 1% of ₹ 34,000.*

(iii) **Factory rent of ₹ 1,85,000 paid to C**

Tax has to be deducted under section 194-I as the rental payment exceeds ₹ 1,80,000.

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Note - The tax to be deducted is ₹ 18,500, being 10% of ₹ 1,85,000.

(iv **Brokerage of ₹ 16,000 paid to B, a sub-broker**

Tax has to be deducted @5% under section 194-H as the brokerage exceeds ₹ 15,000 during the F.Y. 2016-17.

Note - *The tax to be deducted is ₹ 800, being 5% of ₹ 16,000.*

Question 11

What is the difference between TDS and TCS under the Income-tax Act, 1961?

Answer

Difference between TDS and TCS

	TDS	TCS
(1)	TDS is tax deduction at source	TCS is tax collection at source.
(2)	Person responsible for paying is required to deduct tax at source at the prescribed rate.	Seller of certain goods or provider of certain services is responsible for collecting tax at source at the prescribed rate from the buyer. Person who grants licence or lease (in respect of any parking lot, toll plaza, mine or quarry) is responsible for collecting tax at source at the prescribed rate from the licensee or lessee, as the case may be.
(3)	Generally, tax is required to be deducted at the time of credit to the account of the payee or at the time of payment, whichever is earlier. However, in case of payment of salary and payment in respect of life insurance policy, tax is required to be deducted at the time of payment.	Generally, tax is required to be collected at source at the time of debiting of the amount payable by the buyer of certain goods to the account of the buyer or at the time of receipt of such amount from the said buyer, whichever is earlier. However, in case of sale of jewellery or bullion or any other goods or any services, tax collection at source is required at the time of receipt of sale consideration in cash exceeding specified threshold limit. Further, in case of sale of Motor Vehicle of value exceeding ₹ 10 lakhs tax has to be collected at the prescribed rate at the time of receipt.

Question 12

Who is liable to pay advance tax? What is the procedure to compute the advance tax payable?

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Answer

Persons liable to pay advance tax

As per section 207(1), tax shall be payable in advance during any financial year in accordance with the provisions of sections 208 to 219, in respect of an assessee's current income i.e., the total income of the assessee which would be chargeable to tax for the assessment year immediately following that financial year.

In order to reduce the compliance burden on senior citizens having passive sources of income like interest, rent etc., section 207(2) provides exemption from payment of advance tax to a resident individual-

(1) not having any income chargeable under the head "Profits and gains of business or profession"; and

(2) of the age of 60 years or more at any time during the previous year.

As per section 208, the obligation to pay advance tax arises in every case where such tax payable by the assessee during that year is ₹10,000 or more.

Procedure for computing advance tax payable [Section 209]

(1) An assessee has to **first estimate his current income** (under five heads of income after applying the provisions of aggregation of income and set-off or carry forward of losses and allowing deductions under Chapter VI-A).

(2) The assessee shall then compute the income-tax payable on his current income **at the rates in force in the financial year**.

(3) The tax so calculated shall be reduced by the amount of tax which has been actually deducted at source.

(4) Net agricultural income is also to be considered for the purpose of computing advance tax in case of specified classes of assessees.

The specified percentage of advance tax shall be paid by the assessee on his accord on or before the due date of each installment. A person who pays any installment or installments may, increase or reduce the amount of advance tax payable in subsequent installment(s) in accordance with his estimate of current income and the advance tax payable thereon [Sections 210(1) and (2)].

Question 13

Briefly discuss the provisions relating to payment of advance tax on income arising from capital gains and casual income.

Answer

The proviso to section 234C contains the provisions for payment of advance tax in case of capital gains and casual income.

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Advance tax is payable by an assessee on his/its total income, which includes capital gains and casual income like income from lotteries, crossword puzzles, etc.

Since it is not possible for the assessee to estimate his capital gains, or income from lotteries etc., it has been provided that if any such income arises after the due date for any installment, then, the entire amount of the tax payable (after considering tax deducted at source) on such capital gains or casual income should be paid in the remaining installments of advance tax, which are due.

Where no such installment is due, the entire tax should be paid by 31st March of the relevant financial year.

No interest liability on late payment would arise if the entire tax liability is so paid.

Note: *In case of casual income the entire tax liability is fully deductible at source @30% under section 194B and 194BB. Therefore, advance tax liability would arise only in respect of the education cess and secondary and higher education cess element of such tax, if the same along with tax liability in respect of other income, if any, is ₹ 10,000 or more.*

Question 14

Briefly discuss the provisions of section 234B of the Income-tax Act, 1961 for short-payment or non-payment of advance tax.

Answer

Provisions of section 234B for short-payment or non-payment of advance tax

(1) Interest under section 234B is attracted for non-payment of advance tax or payment of advance tax of an amount less than 90% of assessed tax.

(2) The interest liability would be 1% per month or part of the month for the period from 1st April next following the financial year upto the date of determination of total income under section 143(1) and where a regular assessment is made, upto the date of such regular assessment.

(3) Such interest is calculated on an amount equal to the assessed tax; in a case where advance tax is paid in part, such interest is calculated on the amount of difference between the assessed tax and the advance tax paid.

Question 15

What are the consequences of failure to deduct or pay the tax under section 201 of the Income-tax Act, 1961?

Answer

Any person, including principal officer of a company, responsible for deducting tax at source shall be deemed to be an assessee in default in respect of such tax, if he does not deduct or

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after deducting fails to pay, the whole or any part of the tax as required by or under the provisions of the Income-tax Act, 1961.

However, no penalty shall be charged under section 221 from such person, unless the Assessing Officer is satisfied that such person, without good and sufficient reasons, has failed to deduct and pay such tax.

As per section 201(1A), a person who fails to deduct tax or after deduction, fails to pay the tax, is liable to pay simple interest@1% for every month or part of a month on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually deducted and simple interest @ 1½% for every month or part of month from the date on which tax was deducted to the date on which such tax is actually paid. Such interest should be paid before furnishing the statement of tax deducted at source under section 200(3).

Where such tax has not been paid after it is deducted, the amount of tax together with the amount of simple interest thereon shall be a charge upon all the assets of the person, or the company, as the case may be.

Exercise

1. *Any person responsible for paying to a resident any sum exceeding ₹ 2.5 lakh towards compensation for compulsory acquisition of his urban industrial land under any law has to deduct income-tax at the rate of -*

   (a). 10%

   (b). 15%

   (c). 20%

2. *The rate of TDS on rental payments of plant, machinery or equipment is -*

   (a). 2%

   (b). 5%

   (c). 10%

3. *For non-payment or short payment of advance tax -*

   (a). interest is payable under section 234A

   (b) interest is payable under section 234B

   (c) interest is payable under section 234C

4. *For deferment of advance tax -*

   (a) interest is payable under section 234A

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(b) interest is payable under section 234B

(c) interest is payable under section 234C

5. *Write short notes on -*

   (a) Certificate for deduction of tax at lower rate

   (b) Installments of advance tax and due dates for payment of advance tax

   (c) Payment of advance tax in case of capital gains

6. *Explain the meaning of the following terms in the context of section 194J -*

   (a) Professional services

   (b) Fees for technical services

7. *Who are the "persons responsible for paying" taxes deducted at source as per section 204?*

8. *Which are the payments for which individuals and HUFs, who are liable to get their accounts audited under section 44AB, are vested with the liability to deduct tax at source? Discuss.*

Answers

1. a; **2.** a; **3.** b; **4.** c.

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10 Provisions for Filing Return of Income

Key Points	
Section	**Particulars**
139(1)	**Assessees required to file return of income compulsorily** (i) Companies and firms (whether having profit or loss or nil income); (ii) a person, being a resident other than not ordinarily resident, having any asset (including any financial interest in any entity) located outside India or signing authority in any account located outside India, whether or not having income chargeable to tax; (iii) Individuals, HUFs, AOPs or BOIs and artificial judicial persons whose total income before giving effect to the provisions of section 10(38) or Chapter VI-A exceeds the basic exemption limit. **Due date of filing return of income** 30th September of the assessment year, in case the assessee is: (i) a company; (ii) a person (other than company) whose accounts are required to be audited; or (iii) a working partner of a firm whose accounts are required to be audited. 31st July of the assessment year, in case of any other assessee (other than assessees who are required to furnish report under section 92E, for whom the due date is 30th November of the assessment year).
139(3)	**Return of loss** An assessee can carry forward or set off his/its losses provided he/it has filed his/its return under section 139(3), within the due date specified under section 139(1). **Exceptions** Loss from house property and unabsorbed depreciation can be carried forward for set-off even though return has not been filed before the due date.

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139(4)	**<u>Belated Return</u>** A return of income for any previous year, which has not been furnished within the time allowed u/s 139(1), may be furnished at any time before the: (i) end of the relevant assessment year; or (ii) completion of the assessment, whichever is earlier. A belated return can also be revised.
139(5)	**<u>Revised Return</u>** If any omission or any wrong statement is discovered in a return furnished u/s 139(1) or belated return u/s 139(4), a revised return may be furnished by the assessee at any time: (i) before the expiry of one year from the end of the relevant assessment year; or (ii) before the completion of assessment, whichever is earlier.
139(4A)	**<u>Return of Income of Charitable Trusts and Institutions</u>** Every person in receipt of income derived - (i) from property held under trust wholly or partly for charitable or religious purpose; or (ii) by way of voluntary contributions on behalf of such trust or institution, must furnish a return of income if the total income, in respect of which he is assessable as a representative assessee (computed before allowing any exemption u/s 11 &12) exceeds the basic exemption limit.
139(4B)	**<u>Return of Income of Political Parties</u>** A political party is required to file a return of income if its total income (before claiming any exemption u/s 13A) exceeds the basic exemption limit. Grant of exemption under section 13A is subject to the condition of the political party filing a return of income within the time limit prescribed u/s 139(1).
139(4C)	**<u>Mandatory filing of returns by Scientific Research Associations, News agency, Trade unions etc</u>.** It is mandatory for a research association, news agency or trade union or mutual fund referred to in section 10(23D) or securitization trust or venture capital company/venture capital fund to file a return of income on or before the due date under section 139(1), if its total income (before giving effect to the exemption under section 10) exceeds the basic exemption limit.

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	Persons authorized to verify the Return of Income [Section 140]		
	This section specifies the persons who are authorized to verify the return of income under section 139.		
	Assessee	**Circumstance**	**Authorised Persons**
1.	Individual	(i) In circumstances not covered under (ii), (iii) & (iv) below	- the individual himself
		(ii) where he is absent from India	- the individual himself; or - any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
		(iii) where he is mentally incapacitated from attending to his affairs	- his guardian; or - any other person competent to act on his behalf
		(iv) where, for any other reason, it is not possible for the individual to verify the return	- any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
2.	Hindu Undivided Family	(i) in circumstances not covered under (ii) and (iii) below	- the karta
		(ii) where the karta is absent from India	- any other adult member of the HUF
		(iii) where the karta is mentally incapacitated from attending to his affairs	- any other adult member of the HUF
3.	Company	(i) in circumstances not covered under (ii) to (v) below	- the managing director of the company
		(ii) (a) where for any unavoidable reason such managing director is not able to verify the return; or (b) where there is no managing director	- any director of the company - any director of the company

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		(iii) where the company is not resident in India	- a person who holds a valid power of attorney from such company to do so (such power of attorney should be attached to the return).
		(iv) (a) Where the company is being wound up (whether under the orders of a court or otherwise); or	- Liquidator
		(b) where any person has been appointed as the receiver of any assets of the company	- Liquidator
		(v) Where the management of the company has been taken over by the Central Government or any State Government under any law	- the principal officer of the company
4.	Firm	(i) in circumstances not covered under (ii) below	- the managing partner of the firm
		(ii) (a) where for any unavoidable reason such managing partner is not able to verify the return; or	- any partner of the firm, not being a minor
		(b) where there is no managing partner.	- any partner of the firm, not being a minor
5	Local authority	-	- the principal officer
6	Political party [referred to in section 139(4B)]	-	- the chief executive officer of such party (whether he is known as secretary or by any other designation)
7	Any other association	-	- any member of the association or the principal officer of such association
8	Any other person	-	- that person or some other person competent to act on his behalf.

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Question 1

Paras is resident of India. During the F.Y. 2016-17, interest of ₹ 2,88,000 was credited to his Non-resident (External) Account with SBI. ₹ 30,000, being interest on fixed deposit with SBI, was credited to his saving bank account during this period. He also earned ₹ 3,000 as interest on this saving account. Is Paras required to file return of income?

What will be your answer, if he owns one shop in Kerala having area of 150 sq. ft.?

Answer

An individual is required to furnish a return of income under section 139(1) if his total income, before giving effect to the deductions under Chapter VI-A, exceeds the maximum amount not chargeable to tax i.e. ₹ 2,50,000 (for A.Y. 2017-18).

Computation of total income of Mr. Paras for A.Y. 2017-18

Particulars	₹
Income from other sources	
Interest earned from Non-resident (External) Account ₹ 2,88,000 [Exempt under section 10(4)(ii), assuming that Mr. Paras has been permitted by RBI to maintain the aforesaid account]	NIL
Interest on fixed deposit with SBI	30,000
Interest on savings bank account	3,000
Gross Total Income	33,000
Less: Deduction under section 80TTA (Interest on saving bank account)	3,000
Total Income	**30,000**

Since the total income of Mr. Paras for A.Y.2017-18, before giving effect to the deductions under Chapter VI-A, is less than the basic exemption limit of ₹ 2,50,000, he is not required to file return of income for A.Y.2017-18.

Owning a shop having area of 150 sq.ft in Kerala would not make any difference to the answer.

Note: *In the above solution, interest of ₹ 2,88,000 earned from Non-resident (External) account has been taken as exempt on the assumption that Mr. Paras, a resident, has been permitted by RBI to maintain the aforesaid account. However, in case he has not been so permitted, the said interest would be taxable. In such a case, his total income, before giving effect to the deductions under Chapter VIA, would be ₹ 3,21,000 (₹ 30,000 + ₹ 2,88,000 + ₹ 3,000), which is higher than the basic exemption limit of ₹ 2,50,000. Consequently, he would be required to file return of income for A.Y.2017-18. Here again, ownership of shop in Kerala is immaterial.*

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Question 2

State with reasons whether you agree or disagree with the following statements:

(a) Return of income of Limited Liability Partnership (LLP) could be verified by any partner.

(b) Time limit for filing return under section 139(1) in the case of Mr. A having total turnover of ₹ 160 lakhs for the year ended 31.03.2017, whether or not opting to offer presumptive income under section 44AD, is 30th September 2017.

Answer

(a) Disagree

The return of income of LLP should be verified by a designated partner.

Any other partner can verify the Return of Income of LLP **only in** the following cases:-

(i) where for any unavoidable reason such designated partner is not able to verify the return, or,

(ii) where there is no designated partner.

(b) Disagree

In case Mr. A opts to offer his income as per the presumptive taxation provisions of section 44AD, then, the due date under section 139(1) for filing of return of income for the year ended 31.03.2017, shall be 31st July, 2017.

In case Mr. A does not opt for presumptive taxation provisions under section 44AD and, he has to get his accounts audited under section 44AB, in which case the due date for filing return would be 30th September, 2017.

Question 3

Specify the persons who are authorized to verify under section 140, the return of income filed under section 139 of the Income-tax Act, 1961 in the case of:

(i) Political party;

(ii) Local authority;

(iii) Association of persons, and

(iv) Limited Liability Partnership (LLP).

Answer

The following persons (mentioned in Column III below) are authorised as per section 140, to verify the return of income filed under section 139:

I	II	III
(i)	Political party	Chief Executive Officer of such party (whether known as secretary or by any other designation).

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(ii)	Local authority	Principal Officer thereof.
(iii)	Association of Persons	Any member of the association or the principal officer thereof.
(iv)	LLP	Designated partner, or Any partner, - where the designated partner is not able to verify the return for any unavoidable reason; - where there is no designated partner.

Question 4

Mr. Vineet submits his return of income on 12-09-2017 for A.Y 2017-18 consisting of income under the head salaries, "Income from house property" and bank interest. On 21-01-2018, he realized that he had not claimed deduction under section 80TTA in respect of his interest income on the Savings Bank Account. He wants to revise his return of income, since one year has not elapsed from the end of the relevant assessment year. Discuss.

Answer

Since Mr. Vineet has income only under the heads "Salaries", "Income from house property" and "Income from other sources", he does not fall under the category of a person whose accounts are required to be audited under the Income-tax Act, 1961 or any other law in force. Therefore, the due date of filing return for A.Y.2017-18 under section 139(1), in his case, is 31st July, 2017. Since Mr. Vineet had submitted his return only on 12.9.2017, the said return is a belated return under section 139(4).

As per section 139(5), a return furnished under section 139(1) or a belated return u/s 139(4) can be revised. Thus, a belated return under section 139(4) can also be revised. Therefore, Mr. Vineet can revise the return of income filed by him under section 139(4), to claim deduction under section 80TTA, since the time limit of one year from the end of the relevant assessment year has not elapsed.

Question 5

State whether filing of income-tax return is mandatory for the assessment year 2017-18 in respect of the following cases:

(i) Research association eligible for exemption under section 10(21) having total income of ₹ 3,10,000

(ii) Registered trade union eligible for exemption under section 10(24) having following incomes:

Income from house property (computed)	*₹ 60,000*
Income from other sources (computed)	*₹ 40,000*

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(iii) A charitable trust registered under section 12AA, having total income of ₹ 2,60,000.

(iv) A Limited Liability Partnership (LLP) with business loss of ₹ 1,30,000.

Answer

(i) As per section 139(4C), a research association referred to in section 10(21) must file its return of income within the due date under section 139(1) if its total income, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to income-tax.

Since the total income of the research association exceeds the basic exemption limit of ₹ 2,50,000, it has to file its return of income for the A.Y.2017-18.

(ii) As per section 139(4C), a registered trade union referred to in section 10(24) must file its return of income if the total income exceeds the basic exemption limit without giving effect to the provisions of section 10.

Since the total income of the trade union is less than the basic exemption limit of ₹ 2,50,000, it need not file its return of income for the A.Y. 2017-18.

(iii) As per section 139(4A), a charitable trust registered under section 12AA must file its return of income, if its total income computed as per the provisions of the Income-tax Act, 1961, without giving effect to the provisions of sections 11 and 12, exceeds the maximum amount which is not chargeable to income-tax. Since the total income of the charitable trust exceeds ₹ 2,50,000, it has to file its return of income for the A.Y. 2017-18.

(iv) As per third proviso to section 139(1), every company or firm shall furnish on or before the due date the return in respect of its income or loss in every previous year. Since LLP is included in the definition of "firm" under the Income-tax Act, 1961, it has to file its return mandatorily, even though it has incurred a loss.

Question 6

State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

(i) The Assessing Officer has the power, inter alia, to allot PAN to any person by whom no tax is payable.

(ii) Where the Karta of a HUF is absent from India, the return of income can be verified by any male member of the family.

Answer

(i) **True :** Section 139A(2) provides that the Assessing Officer may, having regard to the nature of transactions as may be prescribed, also allot a PAN to any other person, whether any tax is payable by him or not, in the manner and in accordance with the procedure as may be prescribed.

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(ii) False : Section 140(b) provides that where the Karta of a HUF is absent from India, the return of income can be verified by any other adult member of the family; such member can be a male or female member.

Question 7

The total income of a university without giving effect to exemption under section 10(23C) is ₹ 46 lacs. Its total income, however, is nil. Should the University file its return of income?

Answer

Section 139(4C) enjoins that, a university referred to in section 10(23C), should file the return of income if its total income without giving effect to the exemption under section 10, exceeds the basic exemption limit. The provisions of the Act will apply as if it were a return required to be furnished under section 139(1). In the given case, since the total income of the University before giving effect to the exemption exceeds the basic exemption limit, it has to file its return of income.

Question 8

Mrs. Hetal, an individual engaged in the business of Beauty Parlour, has got her books of account for the Financial year ended on 31st March, 2017 audited under section 44AB. Her total income for the assessment year 2017-18 is ₹ 3,35,000. She wants to furnish her return of income for assessment year 2017-18 through a tax return preparer. Can she do so?

Answer

Section 139B provides a scheme for submission of return of income for any assessment year through a tax return preparer. However, it is not applicable to persons whose books of account are required to be audited under section 44AB. Therefore, Mrs. Hetal cannot furnish her return of income for A.Y.2017-18 through a tax return preparer.

Question 9

Can an individual, who is not in India, verify the return of income from outside India? Is there any other option?

Answer

As per section 140, return of income can be verified by an individual even if he is absent from India. Hence, an individual can himself verify the return of income from a place outside India. Alternatively, any person holding a valid power of attorney and duly authorised by the individual can also verify the return of income. However, such power of attorney should be attached along with the return of income.

Question 10

Explain with brief reasons whether the return of income can be revised under section 139(5) of the Income-tax Act, 1961 in the following cases:

(i) Belated return filed under section 139(4).

(ii) Return already revised once under section 139(5).

(iii) Return of loss filed under section 139(3).

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Answer

Any person who has furnished a return under section 139(1) or 139(4) can file a revised return at any time before the expiry of one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier, if he discovers any omission or any wrong statement in the return filed earlier. Accordingly,

(i) A belated return filed under section 139(4) can be revised.

(ii) A return revised earlier can be revised again as the first revised return replaces the original return. Therefore, if the assessee discovers any omission or wrong statement in such a revised return, he can furnish a second revised return within the prescribed time i.e. within one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier.

(iii) A return of loss filed under section 139(3) is deemed to be return filed under section 139(1), and therefore, can be revised under section 139(5).

Question 11

Enumerate the circumstances in which an individual assessee is empowered to verify his return of income under section 139 by himself or otherwise by any authorized person.

Answer

The following table enumerates the specific circumstances and the authorized persons empowered to verify the return of income of an individual assessee filed under section 139(1) in each such circumstance:

	Circumstance	Return of income, to be verified by
(i)	Where he is absent from India	- the individual himself; or - any person duly authorised by him in this behalf holding a valid power of attorney from the individual. (Such power of attorney should be attached to the return of income)
(ii)	Where he is mentally incapacitated from attending to his affairs	- his guardian; or - any other person competent to act on his behalf.
(iii)	Where, for any other reason, it is not possible for the individual to verify the return	- any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
(iv)	In circumstances not covered under (i), (ii) & (iii) above	- the individual himself

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Question 12

Explain the term "return of loss" under the Income-tax Act, 1961. Can any loss be carried forward even if return of loss has not been filed as required?

Answer

A return of loss is a return which shows certain losses. Section 80 provides that the losses specified therein cannot be carried forward, unless such losses are determined in pursuance of return filed under the provisions of section 139(3).

Section 139(3) states that to carry forward the losses specified therein, the return should be filed within the time specified in section 139(1).

Following losses are covered by section 139(3):

- business loss to be carried forward under section 72(1),
- speculation business loss to be carried forward under section 73(2),
- loss from specified business to be carried forward under section 73A(2).
- loss under the head "Capital Gains" to be carried forward under section 74(1); and
- loss incurred in the activity of owning and maintaining race horses to be carried forward under section 74A(3)

However, loss from house property to be carried forward under section 71B and unabsorbed depreciation can be carried forward even if return of loss has not been filed as required under section 139(3).

Question 13

Is a political party required to file return of Income? State the provisions applicable under the Income-tax Act, 1961.

Answer

Yes, a political party is required to file return of income if, without giving effect to the exemption provisions under section 13A, the total income of the political party exceeds the basic exemption limit.

In such cases, as per section 139(4B), the chief executive officer of the political party is required to furnish a return of income of the party of the previous year within the due date prescribed under section 139(1).

For the purpose of claiming exemption under section 13A, the accounts of the political party have to be audited by a Chartered Accountant. Consequently, the due date of filing return for such political parties would be 30th September of the assessment year.

In other cases, the due date of filing of return would be 31st July of the assessment year.

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The return must be filed in the prescribed form and verified in the prescribed manner setting forth such other particulars as may be prescribed by the CBDT.

The provisions of the Income-tax Act, 1961 would apply as if it were a return required to be furnished under section 139(1).

Question 14

Who are the persons authorized to verify return of income in the case of individual under section 139 of the Income-tax Act, 1961?

Answer

As per section 140(a), the persons authorised to verify the return of income of an individual assessee filed under section 139(1) under different circumstances are as follows:

	Circumstance	**Return of income, to be verified by**
(i)	Where he is absent from India	- the individual himself; or - any person duly authorised by him in this behalf holding a valid power of attorney from the individual to do so.
(ii)	Where he is mentally incapacitated from attending to his affairs	- his guardian; or - any other person competent to act on his behalf.
(iii)	Where, for any other reason, it is not possible for the individual to verify the return	- any person duly authorised by him in this behalf holding a valid power of attorney from the individual to do so.
(iv)	In circumstances not covered under (i), (ii) & (iii) above	- the individual himself

Exercise

1. *Akash, who is 32 years old, has long-term capital gains of ₹ 25,000 which is exempt under section 10(38) and deduction of Rs.80,000 under section 80C. He has to file a return of income for A.Y.2017-18, if his total income is -*

   (a) ₹ 1,00,000

   (b) ₹ 1,25,000

   (c) ₹ 1,50,000

2. *The due date for filing of a return of income for a company for Assessment year 2017-18 is -*

   (a) 31st July, 2017

   (b) 30th September, 2017

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(c) 31st October, 2017

(d) 31st August, 2017

3. *For filing returns of income in respect of various entities, the Income-tax Act, 1961 has prescribed -*

   (a) *Two due dates*

   (b) *Three due dates*

   (c) *Four due dates*

4. *Political parties -*

   (a) *need not file their return of income*

   (b) *should always file their return of income*

   (c) *should file their return of income if the total income computed without giving effect to the provisions of section 13A exceeds the basic exemption limit.*

5. *The return of a company has to be verified by -*

   (a) *the Managing Director or Director*

   (b) *the General Manager*

   (c) *The Secretary*

6. *An assessee can file a revised return of income at any time before the completion of assessment or before expiry of the following period, whichever is earlier -*

   (a). *one year from the end of the relevant assessment year*

   (b). *two years from the end of the relevant assessment year*

   (c). *six months from the end of the relevant assessment year*

7. *As per section 139(1), filing of returns is compulsory for -*

   (a) *companies only*

   (b) *firms only*

   (c) *both companies and firms*

8. *Write short notes on the following -*

   (a) *Belated return*

   (b) *Revised return*

9. *Filing of return of income on or before due date is necessary for carry forward of losses - Discuss the correctness of this statement.*

10. *Who are the persons authorised to verify the return of income in the case of -*

    (a) *Hindu Undivided Family*

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(b) Company

(c) Partnership firm

11. *List ten transactions for which quoting of permanent account number is mandatory.*

12. *Briefly discuss about the interest chargeable under section 234A for delay or default in furnishing return of income.*

Answers

1. c; **2.** b; **3.** b; **4.** c; **5.** a; **6.** a; **7.** c.

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INTERMEDIATE (IPC) COURSE
PRACTICE MANUAL

PAPER : 4

Taxation

Part – II : Indirect Taxes

[Relevant for May, 2017 and November, 2017 Examinations]

As amended by the Finance Act, 2016

BOARD OF STUDIES
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

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This Practice Manual has been prepared by the faculty of the Board of Studies. The objective of the Practice Manual is to provide teaching material to the students to enable them to obtain knowledge and skills in the subject. In case students need any clarifications or have any suggestions to make for further improvement of the material contained herein, they may write to the Director of Studies.

All care has been taken to provide interpretations and discussions in a manner useful for the students. However, the Practice Manual has not been specifically discussed by the Council of the Institute or any of its Committees and the views expressed herein may not be taken to necessarily represent the views of the Council or any of its Committees.

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SYLLABUS

PAPER – 4 : TAXATION

(One paper — Three hours – 100 Marks)

Level of Knowledge: Working knowledge

PART II – INDIRECT TAXES (50 MARKS)

Objective: To develop an understanding of the basic concepts of the different types of indirect taxes and to acquire the ability to analyse the significant provisions of service tax.

1. **Introduction to excise duty, customs duty, central sales tax and VAT – Constitutional aspects, Basic concepts relating to levy, taxable event and related provisions**
2. **Significant provisions of service tax**
   (i) Constitutional Aspects
   (ii) Basic Concepts and General Principles
   (iii) Charge of service tax including negative list of services
   (iv) Point of taxation of services
   (v) Exemptions and Abatements
   (vi) Valuation of taxable services
   (vii) Invoicing for taxable services
   (viii) Payment of service tax
   (ix) Registration
   (x) Furnishing of returns
   (xi) CENVAT Credit [Rule 1 -9 of CENVAT Credit Rules, 2004]

Note – If new legislations are enacted in place of the existing legislations the syllabus will accordingly include the corresponding provisions of such new legislations in place of the existing legislations with effect from the date to be notified by the Institute. Students shall not be examined with reference to any particular State VAT Law.

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A WORD ABOUT PRACTICE MANUAL

The distinctive characteristic of the Chartered Accountancy Course i.e., distance learning, emphasizes the need for bridging the gap between the students and the Institute. For this purpose, Board of Studies, the academic wing of the Institute, provides a variety of educational inputs to the students. Subject-wise Practice Manual is one among the many of such inputs provided by the Board of Studies. Practice Manual of a subject is basically a comprehensive question bank comprising of a variety of questions along with model answers on all Chapters covered in the Study Material. They are highly useful to the students preparing for the examinations, since the students get answers to all significant questions relating to a subject at one place and that too, grouped chapter-wise.

Paper 4: Taxation of Intermediate (IPC) Course has two parts; Part – I : Income-tax and Part – II : Indirect Taxes.

Practice Manual of Part II: Indirect Taxes is divided into seven chapters in line with the Study Material on Indirect Taxes to enable the students to co-relate the Practice Manual with the Study Material and facilitate in revision of each chapter. "Key Points" have been included at the beginning of Chapter 1, Chapter 3 and Chapter 4 in order to facilitate the students in answering the questions and solving the problems in respect of topics contained therein. Such "Key Points" would also facilitate quick revision of these chapters. **The questions included in this Practice Manual have been adapted and answered on the basis of the indirect tax laws as amended by the Finance Act, 2016 and Notifications/Circulars issued till 1st June, 2016.**

This Practice Manual will serve as a useful and handy reference guide to the students preparing for Intermediate (IPC) Examination and would facilitate in understanding the application of the provisions contained in the Chapters of the Study Material. Further, it will also enable the students to answer the questions in the best possible manner and would thus, guide them in improving their performance in the examinations. Students should strive to attempt these questions on their own and compare their answers with the model answers given in the Practice Manual to identify their gray areas and plan a strategy to tackle theoretical as well as practical problems. For further clarifications/guidance, students may send their queries at swati.bos@icai.in

Happy Reading and Best Wishes!

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1 Basic Concepts of Indirect taxes

UNIT – 1: INTRODUCTION

<table>
<tr><th colspan="4">KEY POINTS</th></tr>
<tr><td>What is a tax?</td><td colspan="3">Tax is money that people have to pay to the Government, which is used to provide public services.</td></tr>
<tr><td rowspan="2">Direct tax v. Indirect Tax</td><td>Direct Tax</td><td colspan="2">Indirect Tax</td></tr>
<tr><td>Direct tax is imposed directly on the taxpayer and paid directly to the Government by the persons on whom it is imposed. Its burden cannot be shifted.
E.g.: Income-tax</td><td colspan="2">The incidence of indirect tax is borne by the consumers who ultimately consume the product or the service, while the immediate liability to pay the tax may fall upon manufacturer or provider of service or seller of goods.
Its burden can be shifted by the taxpayer to someone else.
E.g.: Excise Duty, Customs Duty, Service Tax, Central Sales Tax (CST), Value Added Tax (VAT), etc.</td></tr>
<tr><td>Constitution of India</td><td colspan="3">♦ Power to levy and collect taxes whether, direct or indirect emerges from the Constitution of India.
♦ In case any act, rule, notification or order is not in conformity with the Constitution, it is called ultra vires the Constitution and is illegal and void.</td></tr>
<tr><td rowspan="2">Seventh Schedule to Article 246 of Constitution</td><td>Union List (List I)</td><td>State List (List II)</td><td>Concurrent List (List III)</td></tr>
<tr><td>It contains the matters in respect of which the Parliament (Central Government) has the exclusive right to make laws.</td><td>It contains the matters in respect of which the State Government has the exclusive right to make laws.</td><td>It contains the matters in respect of which both the Central & State Governments have power to make laws.</td></tr>
</table>

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	Taxation Entries: 82 to 92C	**Taxation Entries:** 45 to 63	**No head of taxation**
	Taxes under Union List: Income-tax, Customs Duty, Service Tax, Central Excise Duty, Central Sales Tax etc.	**Taxes under State List:** State Level VAT, State Excise Duties	

Question 1

Mr. A's service tax liability for half year ended on March 31, 20XX is ₹ 50,000. However, Mr. A has suffered unexpected loss in his business and is short of cash. Therefore, he decides not to pay service tax for the said half year. Examine whether Mr. A's contention is valid.

Answer

No, Mr. A's contention is not valid as tax is **not a voluntary payment** or donation, but an enforced contribution, exacted pursuant to legislative authority. Thus, Mr. A will have to **compulsorily** pay service tax of ₹ 50,000 for half year ended on March 31, 20XX in accordance with the applicable provisions of service tax law irrespective of his financial position.

Question 2

Goods are imported at a port city. State Government of the port city intends to levy customs duty on such imported goods as they have landed at a port which comes under its (State Government's) jurisdiction. Examine whether the State Government's stand is correct in law.

Answer

No, the State Government's stand is not correct in law. Power to levy customs duty is vested with Central Government by virtue of Entry 83 of Union List of Seventh Schedule to Article 246 of Constitution of India. Union List or List-I contains the matters in respect of which Parliament (Central Government) has the exclusive right to make laws.

Question 3

Examine with reasons whether following statements are true or false:

(i) A State Government and the Central Government together can make laws in respect of taxes covered under Concurrent List.

(ii) In case of a Union Territory, Parliament can make laws in respect of a matter included in State List.

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Answer

(i) **False.** Since, there is no head of taxation in Concurrent List (List – III), there does not arise any question of State Government and the Central Government together making laws in respect of any tax.

(ii) **True.** Parliament has a further power to make any law for any part of India not comprised in a State even if such matter is included in State List.

Question 4

Examine the validity of following statements:

(i) *Central Government is empowered to make laws in respect of excise duty leviable on liquors (meant for human consumption) containing alcohol.*

(ii) *Taxes on intra-State sale or purchase of goods are covered under Entry 92A of Union List of the Constitution.*

Answer

(i) **Invalid.** Duties of excise on alcoholic liquors meant for human consumption are covered under Entry 51 of State List (List II). Thus, only State Governments are authorized to make laws in respect of such excise duty.

(ii) **Invalid.** Taxes on intra-State sale or purchase of goods are covered under Entry 54 of State List of the Constitution. Entry 92A of Union List of the Constitution covers central sales tax.

Exercise

1. *Differentiate between direct and indirect taxes.*
2. *Enumerate different types of direct and indirect taxes.*
3. *Explain the salient features of indirect taxes.*
4. *Write a short note on various Lists provided under Seventh Schedule to the Constitution of India.*
5. *Which Governmental bodies control and administer direct and indirect taxes in India?*

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UNIT – 2 : CENTRAL EXCISE DUTY

For the sake of brevity, Central Excise Act, 1944 and Central Excise Tariff Act, 1985 has been referred to as CEA and CETA respectively in the key points given below.

<table>
<tr><th colspan="3">KEY POINTS</th></tr>
<tr><td>What is excise duty?</td><td colspan="2">Excise duty is a tax upon manufacture of goods and not upon sale of goods.</td></tr>
<tr><td rowspan="3">Constitutional provisions</td><td colspan="2">Central excise duty is levied vide Entry 84 of the Union List.</td></tr>
<tr><td>Entry 84 includes excise duty on</td><td>❖ Tobacco
❖ Other goods manufactured or produced in India
❖ Medicinal and toilet preparations containing alchohol, opium, Indian hemp or other narcotic drugs and narcotics</td></tr>
<tr><td>Entry 84 excludes excise duty on</td><td>❖ Alcoholic liquors for human consumption
❖ Opium, Indian hemp and other narcotic drugs and narcotics</td></tr>
<tr><td rowspan="3">Applicable excise duties</td><td>Basic Excise Duty (CENVAT)</td><td>❖ Leviable u/s 3(1)(a) of CEA at the rates specified in First Schedule of CETA
❖ Applicable on majority of goods
❖ General rate: 12.5%</td></tr>
<tr><td>National Calamity Contingent duty (NCCD)</td><td>❖ Leviable u/s 136 of the Finance Act, 2001
❖ Applicable on pan masala, branded chewing tobacco, cigarettes, domestic crude oil and mobile phones</td></tr>
<tr><td>Additional Duty of Excise</td><td>❖ Leviable u/s 85 of the Finance Act, 2005 by way of surcharge
❖ Applicable on pan masala and certain specified tobacco products</td></tr>
<tr><td colspan="3">Levy of duty</td></tr>
<tr><td>Application of central excise law</td><td colspan="2">CEA and CETA apply to
♣ whole of India (including Jammu and Kashmir) and
♣ also extends to designated areas in the Continental Shelf and Exclusive Economic Zone of India (EEZ)</td></tr>
</table>

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<table>
<tr><td>Taxable event</td><td>♦ Taxable event for levy of excise duty is manufacture. However, all manufacturing processes do not attract levy of excise duty unless some basic conditions are met.
♦ Excise duty is not concerned with ownership or sale.</td></tr>
<tr><td>Charge of excise duty [Section 3]</td><td>Excise duty is leviable when the following four conditions are satisfied cumulatively:
♣ There is a manufacture
♣ Such manufacture is in India (excluding SEZ)
♣ Such manufacture results in ‘goods’, and
♣ Such goods are excisable goods
Other propositions of charging section:
♦ No distinction between excisable goods produced by Government and those produced by others, with regard to payment of excise duty.
♦ Excise duty leviable on goods sold by an EOU in DTA = Total customs duties leviable under the Customs Act/other applicable law on like goods produced/manufactured outside India, if imported into India.
▪ Value of such goods is determined in accordance with Customs Act, 1962 if the duty to be levied is based on the value of such goods (ad valorem).
▪ Where in respect of any such like goods, customs duty is leviable at different rates, then, highest of those rates is taken.</td></tr>
<tr><td colspan="2">Goods, Excisable goods, Non-excisable goods, Non-dutiable goods, Exempted goods</td></tr>
<tr><td>Goods</td><td>• Two fundamental aspects of the term ‘goods’ are that they should be (a) ‘moveable’ and (b) ‘marketable’.
Marketability
♦ Explanation to section 2(d) of CEA provides that ‘goods’ includes any article, material or substance which is being capable of brought and sold for a consideration and such goods shall be deemed to be marketable.
♦ Even one purchaser is enough for establishing marketability.
♦ Actual sale is not necessary for being marketable.</td></tr>
</table>

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	♦ Marketability is a question of fact to be decided on the basis of the facts of each case. ♦ Goods of short-shelf life will be deemed to be marketable only if they are capable of being brought and sold during that period.
Excisable goods	♦ Excisable goods are the 'goods' which are specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985 as being subject to a duty of excise and includes salt [Section 2(d) of CEA]. ♦ Since Nil rate is a rate of duty, goods specified in the Tariff as being subject to Nil rate of duty are also excisable goods.
Non-excisable goods, Non-dutiable goods, Exempted goods	♦ Goods not specified in the Tariff are non-excisable goods. ♦ Non-dutiable goods are excisable goods but are not liable to duty either on account of rate of duty being 'NIL' in the Tariff or on account of 100% exemption granted by any exemption notification. ♦ Exempted goods are excisable goods which have been exempted from payment of duty by way of an exemption notification.
Manufacture	
Definition of manufacture [Section 2(f) of CEA]	Manufacture includes any process, (i) incidental or ancillary to the completion of a manufactured product; (ii) which is specified in relation to any goods in the Section or Chapter Notes of the Schedule to the Central Excise Tariff Act, 1985 as amounting to manufacture; or (iii) which, in relation to goods specified in the Third Schedule, involves packing or repacking of such goods in a unit container or labelling or re-labelling of containers including the declaration or alteration of retail sale price on it or adoption of any other treatment on the goods to render the product marketable to consumer. and the term manufacturer shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also any person who engages in their production or manufacture on his own account.
Judicial interpretation	An activity or process would amount to "manufacture" if it leads to emergence of a new commercial product, different from the one with which the process started. In other words, it must be an article with different name, character or use.

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Deemed manufacture	Clauses (ii) and (iii) of the definition of manufacture as provided in section 2(f) of CEA are termed as 'deemed manufacture'. The aforesaid definition gives a wider meaning to the expression "manufacture" as several processes which would not ordinarily be understood as amounting to manufacture are specifically included therein.
Levy of excise duty on captive consumption	♦ Intermediate goods produced will be chargeable to duty if they arise in the course of manufacture/production, are moveable and marketable in such intermediate stage, listed in the Tariff, and are subject to duty of excise in the Tariff. ♦ However, if duty is payable on final product, excise duty is exempted on intermediate product used in manufacture of such final products.
Assembly *vis a vis* manufacture	♦ Assembly would not amount to manufacture in as much as an already manufactured item may be put in a readily usable form. ♦ However, if the assembly results in new commercial commodity with a distinct name, character and use, then it would amount to manufacture.
Dutiability of waste and scrap	♦ Waste/scrap can be 'excisable goods' if they are known in commercial parlance, are marketable and specified in Central Excise Tariff. ♦ Since excise duty is leviable on manufacture, waste and scrap (which are excisable goods) actually generated in the course of manufacture alone is chargeable to duty and waste and scrap generated without any process is not liable to excise duty. ♦ Waste of exempted goods is exempt from excise duty.
Manufacturer	
Who is a manufacturer?	A person carrying out manufacture in terms of any of the three clauses of section 2(f) of CEA is the manufacturer. Following are also included in the definition of manufacturer: ♣ a manufacturer who manufactures through hired labour ♣ a manufacturer who manufactures on his own account
Raw material supplier/ Brand name owner *vis a vis* manufacturer	♦ Person carrying out actual manufacturing process is manufacturer even if raw material is supplied by someone else and goods have been manufactured as per his specifications. ♦ Person actually undertaking manufacturing process is the manufacturer and not the brand name owner under whose brand name, such person manufactures the final product.

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	♦ If the relationship between raw material supplier/brand name owner and person carrying out actual manufacturing process is that of a principal and agent, raw material supplier will be the manufacturer. ♦ A person supplying raw material/brand name owner will be considered as hiring job worker only if he supervises and controls the activities of the job worker. ♦ If manufacturer is a dummy or fake unit, then raw material supplier or the brand name owner will be deemed to be the actual manufacturer.
Collection of duty	
Time for payment of duty	♦ Taxable event for levy of excise duty is manufacture, but collection thereof is postponed to the stage of removal. ♦ Excisable goods cannot be removed from the place of manufacture or from warehouse (when the goods are stored in warehouse) without payment of duty whether for consumption, or export, or manufacture of any other commodity in or outside the place of manufacture until the excise duty leviable thereon has been paid in the prescribed manner.
Person liable to pay duty	♦ Every person who produces or manufactures any excisable goods, or who stores such goods in a warehouse is liable to pay excise duty. ◘ **Exception**: Where molasses are produced in a Khandsari sugar factory, the person who procures such molasses (not the person who produces the same) for use in the manufacture of any commodity is liable to pay duty on such molasses.
Relevant date for determination of rate of duty	♦ For excisable goods other than khandsari molasses, relevant date is the date when such goods are removed from the factory or the warehouse. ♦ For khandsari molasses, relevant date is the date of receipt of such molasses in the factory of the procurer of such molasses. ♦ In case of captive consumption, relevant date is the date on which the goods are issued for such use.
Some special aspects	♦ When there is a change in rate of duty between date of manufacture and date of removal, duty will be leviable at the rate prevalent on the date of removal. ♦ Non-excisable goods will not be chargeable to duty even though subsequent to manufacture but before removal such goods are bought within the purview of the Tariff or are made chargeable to a specified rate of duty under the Tariff.

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<table>
<tr><td></td><td colspan="2">♦ Exempted goods will be chargeable to duty at the time of removal (at rate prevalent on the date of removal) if, subsequent to manufacture but before removal, the exemption from duty is withdrawn.</td></tr>
<tr><td colspan="3">Classification of excisable goods</td></tr>
<tr><td>Concept</td><td colspan="2">♦ Classification of excisable goods is essential for determining applicable rate of duty and eligibility to exemptions.
♦ CETA is based on Harmonised System of Nomenclature (HSN).
♦ The First Schedule to CETA specifying rate of CENVAT has Sections which are divided into Chapters. A Chapter is further divided into headings and sub-headings.</td></tr>
<tr><td>Eight digit classification system</td><td colspan="2">♦ Excisable goods are classified by using 8-digit system. Description with eight digits is termed as ‘tariff item’.
♦ First two digits refer to Chapter Number of the Tariff, Next two digits refer to heading of the goods in that Chapter, Next two digits indicate Chapter sub-heading and Last two digits refer to the Chapter sub-sub-heading.</td></tr>
<tr><td>Trade parlance theory</td><td colspan="2">If a product is not adequately classified in CETA, it should be classified according to its popular meaning or meaning attached to it by those dealing with it, i.e., in commercial sense.</td></tr>
<tr><td>Rate of duty</td><td colspan="2">♦ Rate of duty in respect of each tariff entry is specified in CETA.
♦ Effective rate of duty is ascertained by considering the exemption(s) available in respect of a particular item.</td></tr>
<tr><td colspan="3">Valuation of excisable goods</td></tr>
<tr><td rowspan="3">Basis of computing duty payable</td><td>Specific duty</td><td>❖ Duty payable on units like length, weight, volume etc</td></tr>
<tr><td>Compounded levy scheme</td><td>❖ Optional duty payable on the basis of specified factors relevant to production of the goods covered under the scheme at specified rates for specified period.</td></tr>
<tr><td>Duty based on capacity of production</td><td>❖ Mandatory duty payable on notified goods on the basis of production capacity, without any reference to the actual production.
❖ Goods are notified having regard to the nature of the process of manufacture or production of excisable goods of any specified description, the extent of evasion of duty in regard to such goods etc.</td></tr>
</table>

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<table>
<tr><td rowspan="1"></td><td>Duty based on value</td><td>♣ Duty payable on the basis of Tariff Value [Section 3(2) of CEA]
♣ Duty payable on the basis of Retail Sale Price [Section 4A of CEA]
♣ Duty payable on the basis of Transaction Value [Section 4 of CEA]</td></tr>
<tr><td>Tariff value [Section 3(2)]</td><td colspan="2">♦ Central Government fixes/alters tariff values in respect of notified goods. Duty payable is a percentage of such tariff value.
♦ Different tariff values may be fixed for different classes or descriptions of the same excisable goods.
♦ Different tariff values may also be fixed for same class or description of the goods but produced or manufactured by different classes of producers or manufacturers or sold to different classes of buyers.
♦ Tariff values may be fixed on the basis of wholesale price or average price of various manufacturers as the Government may consider appropriate.</td></tr>
<tr><td rowspan="3">Retail sale price (RSP) based valuation [Section 4A]</td><td colspan="2">Applicable in respect of excisable goods
♣ which are notified by Central Government as goods in relation to which duty will be paid on the basis of RSP less abatements, if any; and
♣ declaration of RSP on package of such goods is required under Legal Metrology Act, 2009.</td></tr>
<tr><td colspan="2">Definition of RSP: Retail sale price has been defined to mean the maximum price at which the excisable goods in packaged form may be sold to the ultimate consumer and includes all taxes, local or otherwise, freight, transport charges, commission payable to dealers, and all charges towards advertisement, delivery, packing, forwarding and like, as the case may be, and the price is the sole consideration for such sale.
However, if the provisions of the Act, rules or Legal Metrology Act, 2009 require the retail sale price to exclude any taxes, local or otherwise, the retail sale price shall be construed accordingly.</td></tr>
<tr><td colspan="2">Value = RSP printed on the package – Abatement, if any, notified by the Government</td></tr>
</table>

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	♦ More than one RSP on package of excisable goods - Maximum of such price to be deemed as the RSP. ♦ Different RSPs on different packages meant for sale in different areas - Each such RSP to be the RSP in the relevant area. ♦ RSP increased after clearance from the place of manufacture - Increased RSP to be deemed as the RSP. ♦ RSP declaration is not mandatory on wholesale packages, packaged commodities for institutional/ industrial consumers, agricultural farm produce etc.
Transaction value [Section 4]	♦ **Residual method of valuation** – If goods cannot be valued by any of the methods described above, they are to be valued as per provisions of section 4. ♦ Assessable value of the excisable goods shall be the 'transaction value' if following conditions are satisfied:- ➢ Price is the sole consideration for the sale i.e., assessee must not receive any other sum either by way of money or by way of any other assistance for the manufacture of goods. ➢ Assessee and buyer of the goods are not related persons. ➢ Goods have been sold by assessee for delivery at the time and place of removal.
	Definition of Transaction Value ♣ Transaction value means the price actually paid or payable for the goods, when sold, **and includes** in addition to the amount charged as price, ♣ any amount that the buyer is liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale, whether payable at the time of the sale or at any other time, **including, but not limited to,** ♣ any amount charged for, or to make provision for, advertising or publicity, marketing and selling organization expenses, storage, outward handling, servicing, warranty, commission or any other matter; **but does not include** ♣ the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods.

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	Inclusions in transaction value	**Exclusions from transaction value**
	➢ Outward handling upto place of removal ➢ All forms of packing (special, general, protective, etc.) ➢ Dharmada or charity ➢ Design, development and engineering charges specific to goods produced ➢ Bought out essential items if the same are fitted to the main article at the time of removal. ➢ Consultancy charges relating to design, layout, etc. of final product done upto place of removal ➢ Testing & inspection charges ➢ Pre-delivery inspection charges and after sales service charges **collected by the manufacturer** ➢ Freight from factory to depot if sale is from depot	➢ Durable/reusable packing as it is amortized and included in the cost of product itself ➢ Optional bought out items and accessories ➢ Independent testing done by the buyer himself or through a third party ➢ All forms of discount if actually passed on to the buyers. ➢ Notional interest on deposits, advances unless it can be proved that price has been lowered on account of receipt of such advance from the buyer ➢ Interest on delayed payment of receivables ➢ Bank charges for collection of sale proceeds ➢ Delayed payment charges ➢ Outward freight from factory/depot to place of customer. ➢ Transit insurance
	Price-cum-duty	
What is price-cum-duty?	Price actually paid for the goods sold + Money value of the additional consideration = Price-cum-duty - Sales tax and other taxes actually paid = Price-cum-duty deemed to be inclusive of the duty payable on such goods **Assessable Value** $= \frac{\textbf{Price - cum - duty (exclusive of sales tax/local tax)} \times 100}{\textbf{(100 + Rate of excise duty)}}$	

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	Price charged (exclusive of sales tax/local tax) will be taken as price-cum-duty: ♣ If the assessee has collected less duty from the buyer than what is due; or ♣ If the assessee has not collected any duty from the buyer even though the product is liable to duty; or ♣ If the assessee has paid duty on lesser value due to receipt of additional consideration.
	♦ Amount of duty should be indicated prominently in all the documents/invoice, etc. ♦ Person liable to pay duty should forthwith deposit any sum collected from the buyer in name of excise duty with the Government.
Small scale industry (SSI) exemption	
What is SSI exemption?	♦ Units having turnover upto ₹ 400 lakh in the previous financial year and manufacturing goods specified in the SSI exemption notification are eligible for exemption from duty up to turnover of ₹ 150 lakh in the current financial year. In case of jewellery manufacturers, the SSI exemption would be upto ₹ 600 lakh in a year with an eligibility limit of ₹ 1200 lakh in the preceding year. ♦ A SSI unit can avail CENVAT credit on inputs only after it starts paying duty (means after its turnover crosses ₹ 1.5 crore). However, CENVAT credit of capital goods can be availed (but can be utilized only after the turnover crosses ₹ 150 lakh) even if the same have been received during period of exemption. ♦ SSI exemption is not available in respect of clearances bearing a brand name of another person. However, goods manufactured in rural area, packing material, account books, registers, writing pads etc. are entitled to SSI exemption even though they bear the brand name of other person.

Question 1

Examine whether central excise duty is leviable in the following situations:-

(a) Mohan Builders have constructed an office building for M/s XYZ & Co.

(b) ABC Maintenance Services Ltd. provided maintenance services for refrigerators and air-conditioners.

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Answer

(a) **No.** Excise duty is leviable only when manufacture results in goods that are excisable. For being called goods, items ought to be movable and marketable. Since office building is marketable but not movable, it is not 'goods' but an immovable property. Hence, excise duty is not leviable on construction of office building.

(b) **No**. Excise duty is leviable on manufacture of excisable goods. However, activity of maintenance of refrigerators and air conditioners is not 'manufacture' as it does not result into emergence of a new article having different name, character or use. Thus, since the activity is not 'manufacture', excise duty is not leviable on the same.

Question 2

A trader of steel articles purchases steel bars of 10 meters. He cuts the bars as per requirements of customer and supplies the cut bars to them. He seeks clarification whether he will be liable to pay excise duty on the cut bars sold by him.

Answer

Supreme Court has held that 'manufacture' can be said to have taken place when after a process, a new and different article emerges having a distinctive name, character or use. However, in this case, after cutting, the product continues to be a bar. There is no change in name, character or use. Hence, the activity is not 'manufacture' and excise duty will not be payable.

Question 3

ABC Co. is buying oil in drums of 200 liters. They pack this oil in small tins of one litre each, put their label giving details of contents, volume and MRP. Advise whether ABC Co. are liable to pay excise duty on small tins sold by them.

Answer

Mere repacking from large container to small pack is not 'manufacture' of oil as oil continues to be oil – no new product comes into existence having a distinct name, character or use. Hence, the activity is not 'manufacture' and excise duty is not payable.

However, if such oil is covered under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), the activity of labelling will be 'deemed manufacture' and ABC Co. will be liable to pay excise duty on such containers of one litre each.

Question 4

A purchases cloth and gives it to B, who is a tailor, to stitch a shirt as per measurements and requirements of A. B stitched the shirt and gave it to A. In the given case, who will be treated as manufacturer of the shirt for the purpose of levy of central excise duty?

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Answer

A person who carries out actual manufacturing process is considered as 'manufacturer' for the purpose of levy of central excise duty even if raw material is supplied by someone else and goods are manufactured as per the specifications of such person. In other words, ownership of raw material is not relevant.

Therefore, in this case, B (tailor), being the actual manufacturer, will be treated as 'manufacturer' for purpose of levy of excise duty even though the cloth (raw material) for making shirt is provided by A and the shirt is stitched as per his specifications.

Question 5

Famous Hero Motors Ltd. purchases raw material and supplies it to JBK Engineering Company. JBK Engineering Company manufactures automobile components as per the design supplied by Famous Hero Motors. Such components bear brand name of Famous Hero Motors Ltd. namely, 'Famous Hero'. JBK Engineering Company supplies these components to Famous Hero Motors Ltd., who in turn sells them in market as spare parts of automobiles. Who is liable to pay central excise duty on such components?

Answer

Liability to pay central excise duty falls on actual manufacturer of goods. Therefore, in this case, JBK Engineering Company, being actual manufacturer, will be liable to pay excise duty. This would be so even if raw material does not belong to them and goods manufactured by them bear the brand name of Famous Hero Motors Ltd. as in case of central excise, ownership of goods is not the relevant criterion to determine duty liability.

Question 6

Distinguish between tariff rate of excise duty and effective rate of excise duty.

Answer

Tariff rate of duty is the rate which is given in Central Excise Tariff. However, Government can give partial or complete exemption from payment of excise duty. Thus, the rate at which excise duty is actually payable is termed as 'effective rate of excise duty'. For example, if rate of excise duty given in Central Excise Tariff is 12.5%, the same would be termed as 'tariff rate'. However, if by way of an exemption notification, excise duty payable is reduced to 6%, the effective rate of excise duty would be 6%.

Question 7

Excise duty payable on cane molasses is ₹ 1,000 per ton. Excise duty on cane sugar is 12.5%. A manufacturer cleared 100 tons of cane molasses from his factory. He sold the cane molasses @ ₹ 15,000 per ton. Calculate the excise duty payable.

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Answer

When excise duty is payable on the basis of a specific rate, the rate at which goods are actually sold is immaterial. Therefore, since in this case, excise duty on cane molasses is payable on the basis of tonnage (specific rate), rate at which they are sold is not relevant.

Thus, excise duty payable in this case will be ₹ 1,00,000 [₹ 1,000 x 100 tons].

Question 8

GHI Co. is a manufacturer. It intends to pay ad valorem excise duty on the basis of assessable value computed under section 4 of the Central Excise Act, 1944. However, Excise Department insists that GHI Co. should pay duty under Compounded Levy Scheme as the product manufactured by it is covered under the said scheme.

You are required to examine the situation in the light of the relevant statutory provisions. Will your answer be different if the product manufactured by GHI Co. is notified under production capacity based duty scheme?

Answer

Under Compounded Levy Scheme, assessee has an **option** to pay excise duty on the basis of specified factors relevant to production of goods covered under the scheme (size of equipment employed, number and types of machines used for manufacture etc.) at specified rates. The prescribed duty has to be paid by the assessee for a specified period.

Therefore, since Compounded Levy Scheme is an **optional scheme**, GHI Co. can pay *ad valorem* duty under section 4 even if goods manufactured by it are covered under Compounded Levy Scheme.

However, duty based on production capacity is **mandatory** i.e, duty cannot be paid in any other manner in respect of the goods notified under this scheme. Therefore, if goods manufactured by GHI Co. get notified under production capacity based duty scheme, it will not be able to pay duty under section 4 and will have to compulsorily pay duty based on its production capacity.

Question 9

Decent Footwear is a leading manufacturer of shoes. Legal Metrology Act, 2009 requires declaration of retail sale price on the package of shoes and shoes are also notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions).

Following information has been furnished by Decent Footwear:

Abatement available on shoes	*25% of retail sale price*
MRP marked on the package	*₹ 2,000 per pair of shoes*
Price at which Decent Footwear sells the shoes to their wholesalers	*₹ 1,300 per pair of shoes*
Price at which wholesalers sell the shoes to retail shop owners	*₹ 1,500 per pair*

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Price at which shoes are sold by retailers to final consumers	*₹ 1,900 (₹ 100 offered as discount on printed retail sale price)*
Excise duty	*12.5%*

Calculate excise duty payable on a pair of shoes.

Answer

Since Legal Metrology Act, 2009 requires declaration of retail sale price on the package of shoes and shoes are also notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), excise duty will be payable on the basis of RSP less abatement.

Particulars	**₹**
MRP marked on the package of a pair of shoes	2,000
Less: Abatement @ 25% of RSP [25% of ₹ 2,000]	500
Value for purpose of excise duty	1,500
Excise duty @ 12.5% [12.5% of ₹ 1,500]	187.50
Excise duty payable (rounded off)	**188**

Question 10

Zebra Engineers are manufacturers of specialty articles. Such articles are sold through retail shops.

MRP marked on the package	*₹ 2,000 per piece*
Price at which Zebra Engineers sells articles to their wholesalers	*₹ 1,300 per piece*
Price at which wholesalers sell the articles to retail shop owners	*₹ 1,500 per piece*
Price at which articles are sold by retailers to final consumers	*₹ 1,900 (₹ 100 offered as discount on printed retail sale price)*
Excise duty	*12.5%*

Calculate excise duty payable on an article. Such articles are not covered under section 4A of Central Excise Act, 1944.

Answer

Since the articles are not covered under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), excise duty will be payable on the basis of assessable value under section 4 of Central Excise Act (transaction value). Thus, value for purpose of excise duty will be ₹ 1,300 i.e., the price at which the articles are sold to wholesalers.

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Particulars	₹
Transaction value [price at which Zebra Engineers sells articles to their wholesalers]	1,300
Excise duty @ 12.5% [12.5% of ₹ 1,300]	162.5
Excise duty payable (rounded off)	**163**

Question 11

A manufacturer of machinery sold a special machine. Following details are provided in relation to amounts charged:

S.No.	*Particulars*	₹
(i)	*Price of machinery excluding taxes and duties (before cash discount)*	*6,00,000*
(ii)	*Transit insurance shown separately in the invoice*	*11,000*
(iii)	*Packing charges*	*9,000*
(iv)	*Extra charges for designing the machine*	*20,000*
(v)	*Outward freight beyond place of removal*	*12,000*

Charges mentioned in (ii) to (v) are not included in (i) above. Other information furnished is -

(a) Cash discount @ 2% on price of machinery has been allowed to the customer.

(b) State VAT rate – 5%.

(c) Central excise duty rate – 12.5%.

Calculate excise duty payable on the special machine.

Answer

Computation of excise duty payable

Particulars	₹
Price of machinery	6,00,000
Add: Packing charges [Note 1(i)]	9,000
Extra design charges [Note 1(i)]	20,000
Total	6,29,000
Less : 2% cash discount on price of machinery [₹ 6,00,000 x 2%] [Note 1(iv)])	12,000
Assessable value	6,17,000
Excise duty @ 12.5%	**77,125**

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Notes:-

1. While computing assessable value:-
   (i) packing charges and extra designing charges have been included as such payments are 'in connection with sale'.
   (ii) transit insurance shown separately in the invoice has not been included as it is a part of transportation cost.
   (iii) outward freight has not been included as it is incurred for transporting the goods beyond the place of removal.
   (iv) cash discount has been allowed as deduction as it has been passed on to the buyer.
2. State VAT does not affect excise duty payable.

Question 12

A *manufacturer cleared some goods by charging excise duty. The invoice provided the following details:*

	₹
Price	*10,000*
Excise duty @ 10.30%	*1,030*
Total	*11,030*

However, he came to know later that actual rate of excise duty is 12.5%. How much differential duty is payable by him, if he is not able to recover any extra amount from the customer?

Answer

Since the manufacturer charged only ₹ 11,030 and he is not able to recover any extra amount from customer, this amount is required to be treated as price–cum–duty. Hence, differential duty payable by him will be computed as under:

Particulars	**₹**
Price-cum-duty	11,030
Excise duty @ 12.5% [₹ 11,030 x 12.5/112.5)	1,225.56
Excise duty (rounded off)	1,226
Differential excise duty to be paid [₹ 1,226 – ₹ 1,030 (duty already paid)]	**196**

Question 13

Net value of clearances (excluding taxes and duties) of Gopal Fan Manufacturers was ₹ 345 lakh during the year 2014-15. During the year 2015-16, their net value of clearances

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(excluding taxes and duties) was ₹ 365 lakh. Calculate excise duty payable by Gopal Fan Manufacturers during 2015-16, if excise duty rate is 12.5%.

Answer

Units having turnover upto ₹ 400 lakh in the previous financial year and manufacturing goods specified in the SSI exemption notification are eligible for exemption from duty up to turnover of ₹ 150 lakh in the current financial year.

Therefore, in the give case Gopal Fan Manufacturers can avail SSI exemption of ₹ 150 lakh in 2015-16 as their turnover during 2014-15 was less than ₹ 400 lakh. It is presumed that goods manufactured by them are specified under SSI exemption notification.

Hence, they have to pay excise duty @ 12.5% on balance value i.e. on ₹ 215 lakhs (₹ 365 – ₹ 150). Thus, duty payable will be ₹ 26,87,500.

Question 14

Calculate the assessable value and the excise duty payable from the following particulars:

	₹
(i) Total invoice price (inclusive of taxes)	*55,000*
(ii) State VAT	*5,500*
(iii) Insurance charges for dispatch of final product	*275*
(iv) Packing charges	*1,200*
(v) Outward freight beyond the place of removal	*2,100*

Charges mentioned in (ii) to (v) are included in (i) above. Excise duty rate is 12.5%. An exemption notification grants exemption of 50% of the duty payable on this product.

Answer

Computation of assessable value and excise duty payable

Particulars	**₹**
Total invoice price (inclusive of taxes)	55,000
Less: State VAT (Note 1)	5,500
Insurance charges (Note 2)	275
Outward freight charges (Note 2)	2,100
Price-cum-duty **(a)**	47,125
Less : Excise duty [Rate of excise duty will be 50% of 12.5%, i.e. 6.25%] [₹ 47,125 × 6.25/106.25]	2,772.06
Excise duty (rounded off) (b)	**2,772**
Assessable value (a) – (b)	**44,353**

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Notes:

1. Invoice price includes State VAT. Thus for calculating assessable value, deduction has been allowed for State VAT.
2. Insurance charges for dispatch of final product and outward freight beyond the place of removal are allowed as deduction as the same are incurred after the place of removal.
3. Since packing charges are includible in assessable value, deduction for the same has not been provided.

Question 15

Mittal Brothers are the manufacturers of certain non-excisable goods. They manufactured goods worth ₹ 2,00,000 on 25.06.20XX. These goods were removed from the factory on 20.09.20XX. On 01.09.20XX, these goods were brought within the purview of the Central Excise Tariff and chargeable to excise duty @ 12.5%.

Discuss the leviability of excise duty on the goods manufactured by Mittal Brothers.

Answer

As per charging section 3 of the Central Excise Act, 1944, excise duty is levied on all excisable goods which are produced or manufactured in India. However, as per rule 5 of the Central Excise Rules, 2002, the rate of duty applicable to any excisable goods is the rate in force on the date when such goods are removed from the factory.

In the given case, the goods were non-excisable at the time of manufacture. Hence, excise duty liability will not arise even though such goods have been made excisable by bringing them under Tariff prior to their removal.

Question 16

Grand India Ltd. sold a machine, manufactured by it, to Indian Industries Ltd. (IIL) at a price of ₹ 10,00,000 (excluding taxes and duties). Further, following additional amounts were also charged from IIL:

	₹
Expenses pertaining to installation and erection of the machine at premises of IIL (machine was permanently affixed to earth)	*30,000*
Special packing charges	*12,500*
Design and engineering charges	*40,000*
Dharmada (charged in the invoice and recovered from IIL)	*10,000*

Determine the total amount of central excise duty payable on the machine from the aforesaid information.

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Answer

Computation of central excise duty payable

Particulars	**₹**
Price of machine excluding taxes and duties	10,00,000
Add : Installation and erection expenses [Note 1]	-
Special packing charges [Note 2]	12,500
Design and engineering charges of the machine [Note 2]	40,000
Dharmada charged in the invoice	10,000
Assessable value	10,62,500
Excise duty payable @ 12.5% [rounded off]	**1,32,813**

Notes:

1. Installation and erection expenses have not been included in the assessable value as after the installation and erection, machine has been permanently affixed to earth and thus, it has resulted in an immovable property.
2. Special packing charges and design and engineering charges have been included in the assessable value as such payments are 'in connection with sale'.

Question 17

Safe Kitchen is a leading manufacturer of pressure cookers. Legal Metrology Act, 2009 requires declaration of retail sale price on the package of pressure cookers and pressure cookers are also notified under section 4A of Central Excise Act, 1944 [Retail Sale Price (RSP) based valuation] with notified rate of abatement of 25%.

Calculate excise duty payable on 50 pieces cleared during September, 20XX using the following information furnished by Safe Kitchen assuming the rate of excise duty as 12.5%.

No. of pieces sold	***Particulars***
10	*RSPs printed on the package of pressure cooker are ₹ 4,500 and ₹ 3,800.*
20	*RSP printed on the package of 15 pieces sold in Delhi is ₹ 3,000 per piece* *RSP printed on the package of 5 pieces sold in Haryana is ₹ 2,800 per piece*
20	*RSP printed on the date of removal of package from factory is ₹ 3500 per unit. However, after removal from factory RSP is increased to ₹ 4,100 per piece*

Would the provisions of section 4A of Central Excise Act, 1944 apply had the goods not been notified by Central Government and manufacturer voluntarily affixed RSP on the products?

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Answer

Since Legal Metrology Act, 2009 requires declaration of retail sale price on the package of pressure cooker and pressure cookers are also notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions), excise duty will be payable on the basis of RSP less abatement.

Particulars	₹	₹
RSP of 10 pieces (10 × ₹4,500) (Note-1)	45,000	
Less: Abatement @ 25%	11,250	
Assessable value (A)		33,750
RSP of 15 pieces sold in Delhi (15 × ₹ 3,000) (Note-2)	45,000	
Less: Abatement @ 25%	11,250	
Assessable value (B)		33,750
RSP of 5 pieces sold in Haryana (5 × ₹ 2,800) (Note 2)	14,000	
Less: Abatement @ 25%	3,500	
Assessable value (C)		10,500
RSP of 20 pieces (20 × ₹ 4,100) (Note-3)	82,000	
Less: Abatement @ 25%	20,500	
Assessable value (D)		61,500
Total assessable value (A) +(B)+(C)+(D)		1,39,500
Excise duty @ 12.5% [12.5% of ₹ 1,39,500]		17,437.50
Total excise duty payable (rounded off)		**17,438**

Notes:

1. Where more than one RSP is declared on the package of excisable goods, the maximum of such price will be deemed to be the RSP.
2. If different RSPs on different packages are declared for different areas, each such RSP is deemed to be the RSP.
3. If RSP on the package is increased after removal from factory, increased RSP would be deemed to be the RSP.

All goods on which RSP has been declared will not be covered under the provisions of section 4A. Only when the declaration of RSP on the goods is mandatory under the Legal Metrology Act, 2009 or under any other law and such goods have been notified by the Central Government for the purpose of section 4A, then the goods be valued under section 4A. Thus, provisions of section 4A of Central Excise Act, 1944 would not apply if the goods had not been notified by Central Government and manufacturer voluntarily affixed RSP on the products.

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Question 18

A manufacturer of machinery sold a machine on which excise duty is payable under section 4 of Central Excise Act, 1944. Following information is furnished by him:

		₹
(i)	*Total invoice price (before cash discount)*	*7,50,000*
(ii)	*Erection charges (Erection results in permanent affixation of the machinery to earth)*	*50,000*
(iii)	*Packing charges*	*12,000*
(iv)	*Design charges*	*20,000*
(v)	*Insurance charges (for dispatch to customer's factory)*	*8,000*
(vi)	*Outward freight (from place of removal to customer's factory)*	*17,000*

Charges mentioned in (ii) to (vi) are included in (i) above. Cash discount @ 2% on invoice price has been allowed to the customer. Excise duty rate is 12.5% and State VAT rate is 12.50%.

Calculate assessable value of the machine and excise duty payable thereon.

Answer

Computation of assessable value of the machine and excise duty payable thereon

Particulars	**₹**
Total invoice price (inclusive of VAT and excise duty)	7,50,000
Less: Cash discount @ 2% of invoice price [₹ 7,50,000 × 2%]	15,000
Erection charges [Note 1]	50,000
Insurance charges [Note 2]	8,000
Outward freight charges [Note 2]	17,000
Price-cum-duty	6,60,000
Less : State VAT @ 12.5% [₹ 6,60,000 x 12.5/112.5]	73,333
Price cum duty deemed to be inclusive of duty payable on such goods	5,86,667
***Less*: Excise duty @ 12.5% [₹ 5,86,667 x 12.5/112.5] rounded off**	**65,185**
Assessable value	**5,21,482**

Notes:

1. Erection charges have not been included in the assessable value as the same results in permanent affixation of the machinery to earth, thereby resulting in an immovable property.

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2. Insurance charges and outward freight charges are allowed as deduction as the same are incurred after the place of removal.
3. Packing charges and designing charges are includible in the assessable value and thus, not deducted from the invoice price.
4. Cash discount has been allowed as deduction as it has been passed on to the buyer.

Question 19

Define the term "transaction value" as per Central Excise Act, 1944.

Answer

As per section 4 of the Central Excise Act, 1944, transaction value means the price actually paid or payable for the goods, when sold, and includes in addition to the amount charged as price,--

- any amount that the buyer is liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale, whether payable at the time of the sale or at any other time, including, but not limited to,
- any amount charged for, or to make provision for, advertising or publicity, marketing and selling organization expenses, storage, outward handling, servicing, warranty, commission or any other matter;
- but does not include the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods.

Question 20

Explain the term "price cum duty" as per Central Excise Act, 1944.

Answer

Price cum duty is the sum total of price actually paid for the goods sold and money value of the additional consideration flowing from buyer to seller in connection with sale of such goods. Such price cum duty after excluding sales-tax and other taxes actually paid, is deemed to be inclusive of the excise duty payable on such goods [Section 4(1) of the Central Excise Act, 1944].

Price charged (exclusive of sales tax/local taxes) will be taken as price-cum-duty in the following cases:-

(i) If the assessee has collected less duty from the buyer than what is due; or

(ii) If the assessee has not collected any duty from the buyer even though the product is liable to duty; or

(iii) If the assessee has paid duty on lesser value due to receipt of additional consideration.

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Question 21

Mr. Arnab Ghosh, a manufacturer, furnished the following particulars:

Price of machine excluding tax and duties	*₹ 2,00,000*
Transit insurance shown separately	*₹ 10,000*
Packing charges	*₹ 10,000*
Extra charges for designing the machine	*₹ 25,000*
Outward freight beyond the place of removal	*₹ 15,000*
Cash discount on price of machinery excluding tax and duties allowed to customer for full payment made in advance	*2%*
VAT	*2%*
Excise duty	*12.5%*

Calculate the excise duty payable by Mr. Arnab Ghosh stating the reason for inclusion or exclusion for each of the items.

Note: Price of the machinery does not include any of the additional charges given in the question.

Answer

Computation of excise duty payable

Particulars	₹
Price of the machinery	2,00,000
Add: Packing charges [Note 1]	10,000
Add: Extra design charges [Note 1]	25,000
Total	2,35,000
Less : 2% cash discount on price of machinery [₹ 2,00,000 x 2%] [Note 2]	4,000
Assessable value	2,31,000
Excise duty @ 12.5%	**28,875**

Notes:

1. While computing assessable value, packing charges and extra designing charges have been included as such payments are in connection with sale.
2. Cash discount has been allowed as deduction since discount has been passed on to the buyer.
3. While computing assessable value, outward freight and transit insurance has not been included as they are incurred for transporting the goods beyond the place of removal.
4. State VAT does not affect excise duty payable.

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Question 22

M/s. Packard Industries (not an SSI unit) are in production of corrugated paper cartons. It provides the following details for the month of June, 20XX:

It sold waste and scrap generated in the course of manufacture. Besides, it also manufactured and sold prohibited goods. On the basis of such information, answer the following questions:

(A) Whether excise duty payable on the following items?

(i)	*Waste*	*₹ 1,50,000*
(ii)	*Scrap sale*	*₹ 11,50,000*
(iii)	*Manufacture of prohibited goods*	*₹ 2,50,000*

(B) When and how?

(i) payment of excise duty to be made.

(ii) return of excise duty to be filed.

Answer

Excise duty is leviable on waste and scrap if –

(i) the waste/scrap is 'excisable goods' i.e., they are specified in Central Excise Tariff and are marketable, and

(ii) the waste and scrap is generated in the course of manufacture.

In the given case, waste and scrap is generated in the course of manufacture and is marketable. Therefore, excise duty will be leviable on the waste and scrap if the same are mentioned in the Central Excise Tariff.

Excise duty will also be leviable on manufacture of prohibited goods, if such goods find place in Tariff. Excise duty is leviable on manufacture of excisable goods irrespective of whether such excisable goods are prohibited or not.

Duty will be payable on waste and scrap and prohibited goods at the effective rate of duty mentioned in Central Excise Tariff (after considering exemptions, if any).

M/s. Packard Industries should pay the excise duty by 06.07.20XX. Duty may be paid in cash or by utilizing CENVAT credit or both [Rule 8 of the Central Excise Rules, 2002 (CER)]. Monthly ER-1 return will have to be filed electronically by 10.07.20XX [Rule 12 of CER].

Question 23

Spring Fresh is a leading manufacturer of bottled aerated water. Legal Metrology Act, 2009 requires declaration of retail sale price on the bottles of aerated water.

Following information has been furnished by Spring Fresh:

Particulars	***Amount (₹)***
Abatement available on aerated water - 40% of retail sale price	

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MRP marked on the bottles of aerated water	*₹ 30 per bottle*
Price at which Spring Fresh sells the bottles of aerated water to their wholesalers	*₹ 19 per bottle*
Price at which wholesalers sell the bottles of aerated water to retail shop owners	*₹ 24 per bottle*
Price at which bottles of aerated water are sold by retailers to final consumers	*₹ 28 per bottle (₹ 2 offered as discount on printed MRP)*

Calculate the assessable value for the purpose of excise duty on the bottles of aerated water. Will your answer change, if Spring Fresh declares two MRPs namely, ₹ 30 and ₹ 40 on each bottle of aerated water?

Note: Aerated waters are notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions).

Answer

Since aerated waters are notified under section 4A of Central Excise Act, 1944, excise duty will be payable on the basis of RSP less abatement.

Particulars	**(₹)**
MRP marked on the bottles of aerated water	30
Less: Abatement @ 40% of MRP [40% of ₹ 30]	12
Assessable Value for purpose of excise duty	**18**

When more than one MRP is declared on the package of excisable goods, the maximum of such price will be deemed to be the MRP. Thus, if Spring Fresh declares two MRPs namely, ₹ 30 and ₹ 40 on each bottle of aerated water, then ₹ 40 would be deemed to be the MRP. The assessable value for the purpose of excise duty will be calculated in the following manner:-

Particulars	**(₹)**
MRP marked on the bottles of aerated water	40
Less: Abatement @ 40% of MRP [40% of ₹ 40]	16
Assessable Value for purpose of excise duty	**24**

Question 24

Super Lasting Ltd. sold a machine, manufactured by it, to Goel Steel Ltd. (GSL) at a price ₹ 10,00,000 (excluding taxes and duties). Further, following additional amounts were also charged from GSL:

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Particulars	*(₹)*
Outward handling charges (from factory to GSL's premises)	*5,000*
Protective packing charges	*12,500*
Expenses pertaining to installation and erection of the machine at premises of GSL (machine was permanently affixed to earth)	*26,000*
Testing and inspection charges (testing done by Super Lasting Ltd.)	*40,000*
Delayed payment charges	*3,000*
Dharmada (charged in the invoice and recovered from GSL)	*10,000*

Determine the assessable value and total amount of central excise duty payable on the machine from the aforesaid information assuming that the machinery has been sold at the factory gate.

Answer

Computation of assessable value and excise duty payable

Particulars	**(₹)**
Price of machine excluding taxes and duties	10,00,000
Add: Outward handling charges [Note 1]	-
Protective packing charges [Note 2]	12,500
Installation and erection expenses [Note 3]	-
Testing and inspection charges [Note 2]	40,000
Delayed payment charges [Note 4]	-
Dharmada charged in the invoice [Note 5]	10,000
Assessable value	10,62,500
Excise duty payable @ 12.5% [rounded off]	**1,32,813**

Notes:

1. Outward handling charges are not included in the assessable value as the same are incurred after the place of removal.
2. Protective packing charges and testing and inspection charges have been included in the assessable value as such payments are 'in connection with sale'.
3. Installation and erection expenses have not been included in the assessable value as the same are incurred after the place of removal and after the installation and erection, machine has been permanently affixed to earth and thus, it has resulted in an immovable property.
4. Delayed payment charges are not includible as the same are finance charges and cannot

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be considered as payment by reason of sale.

5. Dharmada charged in the invoice and recovered from the customer is includible in the assessable value.

Exercise

1. *What is an excise duty? Discuss the relevant Constitutional provisions governing the imposition of such levy.*
2. *Explain different types of excise duties.*
3. *Enlist and explain various sources of central excise law.*
4. *What is the taxable event for levy of excise duty? Explain the provisions of charging section 3 of Central Excise Act, 1944?*
5. *Discuss the concept of goods and excisable goods and bring out the difference between the two.*
6. *Explain the concept of manufacture and deemed manufacture by giving two examples in each case.*
7. *Write a short note on dutiability of site-related activities and waste and scarp.*
8. *Who is a manufacturer? Discuss whether a raw material supplier or a brand name owner can be treated as a manufacturer?*
9. *Discuss the provisions governing collection of duty.*
10. *Distinguish between Section and Chapter of Central Excise Tariff.*
11. *What are the different bases of computing excise duty payable?*
12. *When will the transaction value be taken as the assessable value under section 4 of the Central Excise Act, 1944?*
13. *In what circumstances will the price charged be taken as price-cum-duty?*
14. *Write a short note on SSI exemption available under central excise.*

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UNIT – 3 : CUSTOMS DUTY

<table>
<tr><th colspan="3">KEY POINTS</th></tr>
<tr><td>Meaning of customs duty</td><td colspan="2">A duty or tax, which is levied by the Central Government on:-
♦ import of goods into, and
♦ export of goods from, India</td></tr>
<tr><td>Constitutional provisions</td><td colspan="2">Power to levy customs duty is conferred by Entry 83 of the Union List [Duties of customs including export duties]</td></tr>
<tr><td>Sources of customs law</td><td colspan="2">Customs Act, 1962, Customs Tariff Act, 1975, Annual Union Finance Acts, Rules, Notifications, Circulars/ Instructions, Trade Notices/Clarifications and Case Laws</td></tr>
<tr><td colspan="3">LEVY OF CUSTOMS DUTY</td></tr>
<tr><td rowspan="4">Applicability of the Act</td><td colspan="2">♦ The Customs Act, 1962 applies to the whole of India. India includes territorial waters of India.
♦ Besides, the Customs Act, 1962 and Customs Tariff Act, 1975 have been further extended to:-
(i) the notified designated areas in the Continental Shelf of India (CSI) and Exclusive Economic Zone of India (EEZI) and
(ii) whole of EEZI and CSI for the purpose of processing for extraction or production of mineral oils and supply of any goods in connection thereto.</td></tr>
<tr><td>Indian territorial waters</td><td>Indian customs waters</td></tr>
<tr><td>Indian territorial waters extend upto 12 nautical miles (nm) (22 km) into the sea from the appropriate base line.</td><td>Indian customs waters extend upto a total of 24 nm from base line</td></tr>
<tr><td>All the provisions of the Customs Act and rules and regulations thereunder are applicable in Indian territorial waters.</td><td>Certain powers of the customs officers have been extended in the Indian customs waters as well (for example, power to stop and search any vessel, power to arrest a person in Indian customs waters etc.).</td></tr>
</table>

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<table>
<tr><td rowspan="1">Charging section
[Section 12]</td><td colspan="3">♦ Customs duties shall be levied
♦ at such rates as may be specified under the Customs Tariff Act, 1975. [The two schedules of the Tariff specify the rates: First schedule specifies import duty rates and Second schedule specifies export duty rates]
♦ on goods [whether belonging to Government or not]
♦ imported into and exported from India.
Note: A lower preferential rate of duty has been prescribed for the goods imported from preferential areas.</td></tr>
<tr><td rowspan="7">Determination of duty where goods consist of articles liable to different rates of duty</td><td colspan="3">Where goods consist of a set of articles, duty shall be calculated as follows: -</td></tr>
<tr><td colspan="2">Articles which are liable to duty with reference to</td><td>shall be chargeable to</td></tr>
<tr><td colspan="2">quantity</td><td>that duty</td></tr>
<tr><td colspan="2">value and liable to duty at same rate</td><td>duty at that rate</td></tr>
<tr><td colspan="2">value and liable to duty at different rates</td><td>duty at the highest of such rates</td></tr>
<tr><td colspan="2">Articles not liable to duty</td><td>shall be chargeable to duty at the rate at which articles liable to duty with reference to value are liable.</td></tr>
<tr><td colspan="3">♦ Accessories, spare parts or maintenance and repairing implements for any article are chargeable at the same rate of duty as that article.
♦ If the importer produces evidence to the satisfaction of the proper officer or the evidence is available regarding the value of any of the articles liable to different rates of duty, such article shall be chargeable to duty separately at the rate applicable to it.</td></tr>
<tr><td rowspan="2">Taxable event in case of import/export</td><td>Imports</td><td colspan="2">Import commences when goods cross the territorial waters, but continues and is completed when they become part of the mass of goods within the country. Taxable event is reached at the time when the goods reach the customs barriers and bill of entry for home consumption is filed.</td></tr>
<tr><td>Exports</td><td colspan="2">Export of goods is complete when the goods cross the territorial waters of India.</td></tr>
</table>

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<table>
<tr><td>Goods derelict, wreck etc coming into India</td><td>♦ Customs duty is payable on all goods, derelict, jetsam, flotsam and wreck brought or coming into India.
♦ If such goods are entitled to be admitted duty-free, duty would not be levied provided it is shown to the satisfaction of the proper officer that they are so entitled.</td></tr>
<tr><td colspan="2">CUSTOMS DUTY NOT LEVIABLE IN CERTAIN CASES</td></tr>
<tr><td rowspan="3">No duty on pilfered goods</td><td>♦ If any imported goods are pilfered
♦ after the unloading thereof
♦ but before the proper officer has made an order for clearance for home consumption or deposit in a warehouse,
♦ the importer shall not be liable to pay the duty leviable on such goods.</td></tr>
<tr><td>However, where such goods are restored to the importer after pilferage, the importer becomes liable to duty.</td></tr>
<tr><td>Pilfer means “to steal, especially in small quantities; petty theft”. Therefore, the term does not include loss of total package.</td></tr>
<tr><td>Remission of duty on goods lost or destroyed</td><td>♦ Where it is shown to the satisfaction of the Assistant Commissioner/ Deputy Commissioner of Customs that
♦ any imported goods have been lost (otherwise than as a result of pilferage) or destroyed,
♦ at any time before clearance for home consumption,
♦ the Assistant Commissioner of Customs or Deputy Commissioner of Customs shall remit the duty on such goods.</td></tr>
<tr><td rowspan="3">No duty in case of relinquishment of the title to the goods</td><td>♦ The owner of any imported goods may,
♦ at any time before an order for clearance of goods for home consumption or an order for permitting the deposit of goods in a warehouse has been made,
♦ relinquish his title to the goods and thereupon,
♦ he shall not be liable to pay the duty thereon.</td></tr>
<tr><td>Such relinquishment is not allowed in respect of such goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.</td></tr>
<tr><td>“Relinquish” means to give over possession/control of, to leave off.</td></tr>
</table>

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<table>
<tr><td rowspan="6">**Abatement of duty on damaged or deteriorated goods**</td><td colspan="2">♦ The importer has an option to pay the reduced duty
♦ if it is shown to the satisfaction of the Assistant Commissioner/ Deputy Commissioner of Customs that
♦ the goods are damaged/deteriorated under any of the following circumstances:</td></tr>
<tr><td colspan="2">**In case**</td></tr>
<tr><td colspan="2">any imported goods had been damaged or had deteriorated at any time before or during the unloading of the goods in India</td></tr>
<tr><td>any imported goods, other than warehoused goods, had been damaged on account of any accident, at any time after the unloading thereof in India but before their examination for assessment by the customs authorities</td><td rowspan="2">Provided such accident is not due to any wilful act, negligence or default of the importer, his employee or agent.</td></tr>
<tr><td>any warehoused goods had been damaged on account of any accident at any time before clearance for home consumption</td></tr>
<tr><td colspan="2">$= \frac{\text{Value of damaged/deteriorated goods *}}{\text{Value of goods before damage/deterioration}} \times \text{Duty on goods before damage/ deterioration}$
*Valuation of the damaged or deteriorated goods shall be as follows:-
(a) Value ascertained by the proper officer
or
(b) The proper officer may sell such goods by public auction/tender or if the importer agrees, in any other manner and the gross sale proceeds shall be deemed to be the value of such goods.</td></tr>
<tr><td colspan="3">**EXEMPTION FROM CUSTOMS DUTY**</td></tr>
<tr><td colspan="3">Central Government may grant exemption from customs duty if it is satisfied that it is necessary in the public interest to do so.</td></tr>
<tr><td>**General exemption**</td><td colspan="2">Central Government may, by notification in the Official Gazette, exempt generally either absolutely or subject to specified conditions.</td></tr>
<tr><td>**Special exemption**</td><td colspan="2">Central Government may, by special order, exempt from payment of duty, any goods on which duty is leviable only under circumstances of an exceptional nature to be stated in such order.</td></tr>
<tr><td colspan="3">**CLASSIFICATION OF IMPORTED GOODS**</td></tr>
<tr><td>**Meaning**</td><td colspan="2">To determine the headings or sub-headings of Customs Tariff Act, 1975 (CTA) under which imported/export goods would be covered.</td></tr>
</table>

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<table>
<tr><td>Need</td><td colspan="3">It determines:
(a) rate of applicable duty,
(b) applicability of import controls or restrictions,
(c) applicability of anti-dumping duty, safeguard duty etc.,
(d) benefits of duty exemption notifications.</td></tr>
<tr><td colspan="4">VALUATION OF IMPORTED AND EXPORT GOODS</td></tr>
<tr><td colspan="4">Valuation of imported/ export goods
→ Where custom duty is chargeable on ad valorem basis
  → Transaction Value
  → Tariff Value
→ Where specific duty is charged</td></tr>
<tr><td colspan="3">Transaction value, in case of imported/export goods shall be
♦ the price actually paid or payable for the goods
♦ when sold for export to/from India
♦ for delivery at the time and place of importation/exportation
♦ where the buyer and seller of the goods are not related and
♦ price is the sole consideration for the sale
subject to such other conditions as may be specified in the rules made in this behalf.</td><td>CBEC may fix tariff values for any class of imported books or export goods by notification.
In such a case, duty is chargeable with reference to such tariff values.</td></tr>
<tr><td rowspan="2">Date relevant for determination of rate of exchange</td><td>For imported goods</td><td colspan="2">rate of exchange, notified by CBEC, prevalent on the date of filing bill of entry</td></tr>
<tr><td>For export goods</td><td colspan="2">rate of exchange, notified by CBEC, prevalent on the date of filing shipping bill (in case of export by vessel or aircraft) or bill of export (in case of export by vehicle)</td></tr>
</table>

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DATE FOR DETERMINING THE RATE OF DUTY AND TARIFF VALUATION OF IMPORTED GOODS	
In case of	**the rate of duty and tariff valuation shall be the rate and valuation in force on the**
goods entered for home consumption	date of presentation of bill of entry OR date of entry inwards of the vessel/arrival of the aircraft or vehicle whichever is later.
goods cleared for home consumption from the warehouse	date on which a bill of entry for home consumption in respect of such goods is presented
any other goods	date of payment of duty

DATE FOR DETERMINING THE RATE OF DUTY AND TARIFF VALUATION OF EXPORT GOODS	
In case of	**the rate of duty and tariff valuation shall be the rate and valuation in force on the date**
goods entered for export	on which the proper officer makes an order permitting clearance and loading of the goods for exportation
any other goods	of payment of duty

TYPES OF CUSTOMS DUTIES	
Basic customs duty	♦ Duty levied under the charging section-section 12 of the Customs Act, 1962 ♦ on any imported/export goods ♦ at the rates specified in the First and Second Schedules of the Customs Tariff Act, 1975 ♦ on transaction value under section 14(1) /tariff value determined under section 14(2) of the Customs Act, 1962.
Additional customs duty under section 3(1) of the Customs Tariff Act, 1975 [also known as Countervailing duty (CVD)]	♦ Duty imposed on any imported article ♦ equal to excise duty for the time being in force leviable on a like article if produced or manufactured in India ♦ at the rate of excise duty leviable on a like article if produced or manufactured in India** (except in case of alcoholic liquor for human consumption for which rate of additional duty is notified by the Central Government). ***If a like article is not so produced or manufactured in India, rate of duty is the rate of excise duty which would be leviable on the class/description of articles to which the imported article belongs, and where such duty is leviable at different rates, the highest of such rates of duty.*

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CVD under section 3(3) of the Customs Tariff Act, 1975	♦ Duty levied on any imported article ♦ equal to additional duty[1] representing such portion of the excise duty leviable on such raw materials, components and ingredients [1]*as determined by rules made by the Central Government in this behalf*
Special CVD under section 3(5) of the Customs Tariff Act, 1975	♦ Duty levied on any imported article ♦ to counter-balance the sales tax, VAT, local tax or any other charges for the time being in force leviable on a like article on its sale, purchase or transportation in India** ♦ at the rate as notified by the Central Government, but not exceeding 4%. ***If a like article is not so sold, purchased or transported, rate of duty is the rate at which such taxes/charges would be leviable on the class or description of articles to which the imported article belongs, and where such taxes/ charges are leviable at different rates, the highest of such tax/ such charge.*
Education cess (EC)	♦ Duty levied on imported goods ♦ @ 2% on aggregate of customs duties leviable on such goods.
Secondary and Higher Education cess (SHEC)	♦ Duty levied on imported goods ♦ @ 1% on aggregate of customs duties leviable on such goods.
Protective duties	♦ Duty imposed on imported goods ♦ for the protection of the interests of any industry established in India ♦ on the recommendation of Tariff Commission.
Safeguard duty	♦ Duty levied if the Central Government is satisfied that: (a) any article is imported into India in increased quantities; and (b) such increased importation is causing or threatening to cause serious injury to domestic industry. ♦ Education cess and secondary and higher education cess is not payable on it. ♦ It shall be in force for a period of 4 years from the date of its imposition extendable further by 6 years. ♦ It shall not apply to articles imported by a 100% EOU/unit in a SEZ unless - (i) specifically made applicable; or (ii) the article imported is either cleared as such into DTA or used in the manufacture of any goods that are cleared into DTA.

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Countervailing duty on subsidized articles	♦ It is imposed if:- (a) any country or territory, directly or indirectly, pays or bestows subsidy upon the manufacture or production or exportation of any article. Such subsidy includes subsidy on transportation of such article. (b) such articles are imported into India. (c) the importation may/may not directly be from the country of manufacture/production and (d) the article, may be in the same condition as when exported from the country of manufacture or production or may be changed in condition by manufacture, production or otherwise. ♦ It shall be in force for a period of 5 years from the date of its imposition extendable further by 5 years.
Anti-dumping duty	♦ Where any article is exported by an exporter to India at less than its normal value, then, upon the importation of such article into India, the Central Government may impose an anti-dumping duty not exceeding the margin of dumping in relation to such article. Margin of dumping = Normal Value-Export Price ♦ It shall be in force for a period of 5 years from the date of its imposition extendable further by 5 years. ♦ It shall not be leviable on articles imported by a 100% EOU unless specifically made applicable

Steps for computation of basic customs duty, CVD, special CVD & education cesses:

S.No.	*Particulars*	₹
(1)	*Assessable value for computing basic customs duty [Transaction value under section 14(1)/Tariff value under section 14(2)]*	*xxxx*
(2)	*Add: Basic custom duty [**(1)** × Rate of BCD]*	*xxxx*
(3)	*Total value for computing additional customs duty u/s 3(1) [**(1)+(2)**]*	*xxxx*
(4)	*Additional custom duty u/s 3(1) [**(3)** × Rate of CVD]*	*xxxx*
(5)	*Total duty amount for education cess of customs [**(2)+(4)**]*	*xxxx*
(6)	*Education cess @ 2% of **(5)***	*xx*
(7)	*Secondary and higher education cess @ 1% of **(5)***	*xx*

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(8)	*Total duty payable before additional customs duty u/s 3(5)* ***[(5)+(6)+(7)]***	*xxxx*
(9)	*Total value for computing additional customs duty u/s 3(5) [**(1)+(8)**]*	*xxxx*
(10)	*Additional customs duty u/s 3(5) [**(9)** × Rate of special CVD]*	*xxxx*
(11)	*Total duty payable [**(8)+(10)**]*	*xxxx*

Question 1

Distinguish between Indian territorial waters and Exclusive Economic Zone of India with regard to applicability of the Customs Act, 1962.

Answer

Indian territorial waters extend upto 12 nautical miles inside the sea from normal base line. Sovereignty of India extends upto territorial waters. Hence, all provisions of the Customs Act, 1962 are applicable to area covered under territorial waters.

Area beyond 12 nautical miles and upto 200 nautical miles from normal base line is covered under Exclusive Economic Zone of India. In this area, India has exclusive economic rights. Hence, provisions of customs law do not apply in this area unless any of such provisions has been specifically so made applicable.

Question 2

Answer the following questions:-

(i) ABC Manufacturers Ltd. imported some goods from Japan through a vessel. After the ship entered Indian port, the goods were unloaded and were lying with the custodian. The said goods were pilfered before the proper officer made an order for clearance for home consumption. Is ABC Manufacturers Ltd. liable to pay duty on such goods? Further, what would be the customs duty implication if such goods are restored to ABC Manufactures Ltd.

(ii) Amino Industries imported certain goods from Norway. The said goods were warehoused in a public warehouse for a period of 3 months after which it is cleared for home consumption on payment of applicable customs duty. While transporting the goods from customs warehouse to the factory of the importer, the said goods were damaged. Can duty paid on such goods be remitted to Amino Industries?

Answer

(i) No, ABC Manufacturers Ltd. is not liable to pay duty in the given case. If any goods are pilfered after the unloading thereof but before the proper officer has made an order for clearance for home consumption, the importer shall not be liable to pay duty on such goods.

However, where such goods are restored to the importer after the pilferage, the importer becomes liable to pay duty. Thus, ABC Manufacturers Ltd. will be liable to pay duty if goods are restored to it.

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(ii) No, duty paid on the goods, in the instant case, cannot be remitted as the goods have been damaged after their clearance for home consumption from the warehouse. The duty on the imported goods can be remitted only when such goods are destroyed at any time before clearance for home consumption.

Question 3

Suhana Ltd. imports certain goods from Germany. Since the goods have been imported from outside India and not manufactured in India, excise duty is not leviable on such goods. However, excise duty is charged indirectly by the Government on such imported goods. Do you agree?

Answer

Though excise duty cannot be charged on imported goods, an additional duty of customs also known as countervailing duty (CVD) which is equal to excise duty on similar goods manufactured in India is payable on the imported goods. CVD is payable on assessable value plus basic customs duty. Thus, indirectly, excise duty is levied on imported goods.

Question 4

An importer imports a carton of goods containing 10,000 pieces with assesable value of ₹ 1,00,000 under section 14 of the Customs Act, 1962. On said product, rate of basic customs duty is 10% and rate of excise duty is 12.5% ad valorem. Similar product in India is assessable under section 4A of the Central Excise Act, 1944, after allowing an abatement of 30%. MRP printed on the package at the time of import is ₹ 25 per piece. Calculate the countervailing duty (CVD) under section 3(1) of the Customs Tariff Act, 1975 payable on the imported goods.

Answer

If imported goods are similar to goods covered under section 4A of the Central Excise Act, 1944, CVD is payable on basis of MRP printed on the packing less abatement as permissible.

Particulars	Amount (₹)
Maximum retail price [10,000 pieces × 25]	2,50,000
Less: Abatement @ 30%	75,000
Assessable value	1,75,000
CVD @ 12.5% of ₹ 1,75,000	21,875

Question 5

Sofo Enterprises imported some goods from USA for being used in manufacture of its final product. Determine the exchange rate to be considered for computation of import duty from the following information:-

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Date	*Particulars*	*Rate of exchange notified by CBEC*
21.10.20XX	*Import general manifest was submitted by master of vessel*	*1 US Dollar = ₹ 64.20*
25.10.20XX	*Entry Inwards was granted by the customs officer*	*1 US Dollar = ₹ 64.30*
27.10.20XX	*Sofo Enterprises filed the Bill of Entry*	*1 US Dollar = ₹ 64.50*
31.10.20XX	*Goods were allowed to be cleared from the customs port*	*1 US Dollar = ₹ 64.60.*

Answer

The relevant rate of exchange for the purpose of valuation of imported goods is the rate of exchange as in force on the date on which a bill of entry in relation to imported goods is presented, i.e. 1 US Dollar = ₹ 64.50.

Question 6

Genuine Industries exported some goods to UK in a vessel. You are required to determine the rate of exchange for the purposes of computation of export duty from the following additional information:

Particulars	*Date*	*Exchange rate notified by CBEC*	*Exchange rate notified by RBI*
Date of presentation of shipping bill	*18.06.20XX*	*₹ 89 per UK pound*	*₹ 90 per UK pound*
Date of entry outwards	*20.06.20XX*	*₹ 85 per UK pound*	*₹ 87 per UK pound*

Answer

The exchange rate in the given case will be the rate of exchange notified by CBEC on the date of presentation of shipping bill, i.e. 18.06.20XX. Hence, the rate of exchange for the purposes of computation of export duty will be ₹ 89 per UK pound.

Question 7

Nanak Enterprises imported machinery from USA in an aircraft. The bill of entry was presented on 05.06.20XX and the aircraft arrived in India on 15.06.20XX. The rate of import duty on the respective dates was as follows:-

Particulars	*Date*	*Rate of customs duty*
Date of bill of entry	*05.06.20XX*	*10%*
Date of arrival of aircraft	*15.06.20XX*	*11%*

Determine the rate of import duty applicable in the given case.

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Answer

In case the goods have been imported in an aircraft, the rate of duty shall be the rate in force on:-

(i) the date on which Bill of Entry in respect of such clearance is presented

or

(ii) the date on which arrival of aircraft takes place

whichever is later.

Therefore, the relevant date for determination of the rate of import duty, in the given case, is 15.06.20XX. Hence, the rate of import duty applicable in the given case is 11%.

Question 8

A German manufacturer is exporting magnets to India. He is selling the magnets in Germany @ ₹ 100 per piece, but exports same magnets to India @ ₹ 50 per piece. Due to availability of cheap imported magnets, Indian manufacturers of the magnets are suffering. What action can be taken by the Government in this regard?

Answer

Government can impose anti dumping duty on such imported magnets to protect the domestic producers. The anti-dumping duty is equal to difference between normal value (i.e. his sale price in his country) and export price (price at which he is exporting the goods).

Question 9

ABC Ltd. has imported a machinery to be used for providing a taxable service. The assessable value of imported machinery under customs laws is ₹ 2,00,000. Basic customs duty is payable @ 10%. If the machinery is manufactured in India, excise duty @ 12.5% is leviable on such machinery. Education cess and secondary and higher education cess of customs are as applicable. Special CVD is payable on said machinery @ 4%. You are required to:-

(i) calculate the total customs duty payable.

(ii) examine whether ABC Ltd. can avail any CENVAT credit of the custom duties so paid? If yes, how much?

Answer

Computation of customs duty payable

Particulars	Rate %	Amount (₹)	Amount of Duty (₹)
Assessable value		2,00,000	
Basic customs duty	10	20,000	20,000

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Sub-total for calculating CVD		2,20,000	
CVD (₹ 2,20,000 x excise duty rate)	12.5	27,500	27,500
Sub-total for education cess on customs (₹ 20,000 + ₹ 27,500)		47,500	
Education cess of customs	2	950	950
Secondary and Higher Education cess of customs	1	475	475
Sub-total for special CVD (₹ 2,00,000 + ₹ 20,000 + ₹ 27,500 + ₹ 950 + ₹ 475)		2,48,925	
Special CVD u/s 3(5)	4	9,957	9,957
Total customs duty payable			**58,882**

Since ABC Ltd. is a service provider, it can avail CENVAT credit of only CVD i.e. only of ₹ 27,500 and not of special CVD.

Question 10

Sumar Export House exported some goods to Switzerland. Compute the export duty payable by it from the following information available:

(i) Assessable value ₹ 55,00,000.

(ii) Shipping bill presented electronically on 26.06.20XX.

(iii) Proper officer passed order permitting clearance and loading of goods for export on 04.07.20XX.

(iv) Rates of export duty are as under:

	Rate of export duty
On 26.06.20XX	*10%*
On 04.07.20XX	*8%*

Answer

Computation of export duty

Particulars	**Amount (₹)**
Assessable value of the export goods	55,00,000
Export duty @ 8% [Refer Note below]	4,40,000

Note: In case of goods entered for export, the rate of duty shall be the rate in force on the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation.

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Question 11

Trident Enterprises imported goods from Bangladesh in a vehicle. Determine the rate of import duty to be considered for computation of import duty from the following information:-

Particulars	*Date*	*Rate of customs duty*
Date of filing of Bill of Entry	*15.09.20XX*	*10%*
Date of arrival of vehicle	*20.09.20XX*	*12%*
Date on which goods were allowed to be cleared from the land customs station	*28.09.20XX*	*11%*
Date of payment of the value of the goods imported	*30.09.20XX*	*8%*

Answer

Section 15 of the Customs Act, 1962 provides that in case the goods have been imported in a vehicle, the rate of duty shall be the rate in force on:-

(i) the date on which Bill of Entry is presented

or

(ii) the date on which arrival of vehicle takes place

whichever is later.

Therefore, the relevant date for determination of the rate of import duty, in the given case, is 20.09.20XX. Hence, the rate of import duty applicable in the given case is 12%.

Question 12

Mariam importers imports a carton of goods from Japan on 10.11.20XX containing 5,000 pieces valued at ₹ 1,00,000 (assessable value in terms of section 14 of the Customs Act, 1962). On the said product, customs duty @ 10% and excise duty at 12.5% ad valorem is leviable.

Similar products in India are assessable under section 4A of Central Excise Act 1944, after allowing an abatement of 30%. MRP printed on package at the time of import is ₹ 30 per piece. Special CVD under section 3(5) of Customs Tariff Act, 1975 is also applicable to the product. Determine the total duties payable.

Answer

Computation of customs duty payable

Particulars		₹
Assessable value (A)	(A)	1,00,000.00
Basic customs duty @ 10% of (A)	(B)	10,000.00
CVD [Refer note below]	(C)	13,125.00

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Education cesses of customs @ 3% on (B) + (C)	(D)	693.75
Value for computing special CVD (A) + (B) + (C) + (D)	(E)	1,23,818.75
Special CVD @ 4% on (E) (rounded off)	(F)	4,952.75
Total custom duty payable (B) + (C) + (D) + (F) [Rounded off]		**28,772**

Note: If imported goods are similar to goods covered under section 4A of the Central Excise Act, 1944, CVD is payable on basis of MRP printed on the package less abatement, as permissible. Therefore, CVD is computed as under:

Particulars	₹
Maximum retail price [5,000 pieces × ₹ 30]	1,50,000
Less: Abatement @ 30%	45,000
Assessable value for CVD	1,05,000
CVD @ 12.5% of ₹ 1,05,000	13,125

Question 13

Mahabalipur Enterprises imported some goods in a vessel. The assessable value of the imported goods is ₹ 10,00,000. Compute the customs duty payable from the following additional information:

Date of bill of entry *Date of entry inwards*	*09.10.20XX (Rate of BCD is 8%)* *19.10.20XX (Rate of BCD is 10%)*
CVD is payable @ 12.5% *Special CVD – as applicable*	

Will your answer change if the goods are imported in a vehicle and date of arrival of vehicle is 19.10.20XX?

Answer

Computation of customs duty payable

Particulars	(₹)
Assessable value	10,00,000.00
Add: Basic custom duty @ 10% (Note below)	1,00,000.00
Total	11,00,000.00
Add: CVD @12.5%	1,37,500.00
Add: Education cess @ 2% and Secondary and Higher Eduction Cess @ 1% (3% of custom duty) = 3% of (₹ 1,00,000 + ₹ 1,37,500)	7,125.00
Total for Special CVD [₹ 11,00,000 + ₹ 1,37,500 + ₹ 7,125]	12,44,625.00

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Special CVD @ 4%	49,785.00
Total duty payable (₹ 1,00,000 + ₹ 1,37,500 + ₹ 7,125 + ₹ 49,785)	**2,94,410**

Note: The rate of duty shall be:-

(i) the rate in force on the date of presentation of bill of entry

or

(ii) the rate in force on the date of entry inwards

whichever is later.

No, the answer will not change if the goods are imported in a vehicle. Section 15 of the Customs Act, 1962 provides that the relevant date for determination of rate of duty and tariff valuation for imports through a vehicle would be-

(i) the rate in force on the date of presentation of bill of entry

or

(ii) the rate in force on the date of arrival of vehicle

whichever is later.

Exercise

1. *With reference to the Customs Act, 1962, discuss the following:-*
   - *(a) Special exemption*
   - *(b) General exemption*
2. *Distinguish between clearance of imported goods for home consumption and clearance of imported goods for warehousing.*
3. *Write short note on the following with reference to the Customs Act, 1962:-*
   - *(a) Remission of customs duty on imported goods damaged or destroyed*
   - *(b) Customs duty on pilfered goods*
4. *Distinguish between:-*
   - *(a) Jetsam and flotsam*
   - *(b) Pilferage of goods under section 13 and loss or destruction of goods under section 23(1) of the Customs Act, 1962.*
5. *Define the following terms with reference to the Customs Act, 1962:*
   - *(a) Goods*
   - *(b) Export*

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(c) Export goods

(d) Exporter

6. *Briefly discuss whether the customs duty is liable to be paid on derelict, jetsam, flotsam and wreck brought or coming into India.*
7. *Enumerate the circumstances in which abatement of duty on damaged or deteriorated goods is available.*
8. *List the different types of customs duties.*
9. *How is the customs duty determined where imported goods consist of articles liable to different rates of duty?*
10. *Differentiate between protective duty and safeguard duty.*
11. *Write a brief note on education cess on customs duty.*
12. *Briefly discuss the date for determining the rate of duty and tariff valuation of export goods.*

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UNIT – 4 : CENTRAL SALES TAX

For the sake of brevity, Central Sales Tax has been referred to as CST and the Central Sales Tax Act, 1956 has been referred to as CST Act.

KEY POINTS	
Meaning of inter-State sales and intra-State sales	Sales made within a State are intra-State sales and are liable to sales tax within the State. Sales made from one State to another are inter-State sales and are liable to Central Sales Tax (CST).
Constitutional provisions	Central sales tax is levied by drawing power from Entry 92A of the Union List *[Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce]*
Sources of central sales tax law	Central Sales Tax Act, 1956, Annual Union Finance Acts, Rules, Notifications, Circulars/ Instructions, Trade Notices/Clarifications and Case Laws.
Objects of the CST Act	The objects of the Central Sales Tax Act include: (i) formulation of principles for determining as to:- (a) when a sale or purchase of goods takes place in the course of inter-State trade or commerce, or (b) when a sale or purchase takes place outside a State, or (c) when a sale or purchase takes place in the course of import into or export from India (ii) provision for the levy, collection and distribution of taxes on sales of goods in the course of inter-State trade or commerce (iii) declaration of certain goods to be of special importance in inter-State trade or commerce (iv) State laws to be subjected to the restrictions and conditions in the matter of imposing taxes on the sale or purchase of goods declared by the Central Government to be of special importance.
Levy and collection of CST	♦ CST extends to whole of India. ♦ It is levied by the Government of India. ♦ CST so levied is collected by that State Government from which the movement of the goods is commenced.

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<table>
<tr><td>Charge of CST</td><td>♦ Every dealer
♦ shall be liable to pay tax under CST Act
♦ on sales of all goods, other than electrical energy,
♦ effected by him in the course of inter-State trade or commerce
♦ during any year.</td></tr>
<tr><td colspan="2">IMPORTANT TERMS</td></tr>
<tr><td>Meaning of Goods</td><td>♦ include all materials, articles, commodities and all other kinds of movable property, but
♦ does not include newspapers, actionable claims, stocks, shares and securities.</td></tr>
<tr><td rowspan="2">Meaning of Sale</td><td>Conventional definition
Sale means any transfer of property in goods by one person to another for cash or deferred payment or for any other valuable consideration but does not include a mortgage or hypothecation of or a charge or pledge on goods</td></tr>
<tr><td>Deemed sales
Sale includes:
(i) a transfer, otherwise than in pursuance of a contract, of property in any goods;
(ii) transfer of property in goods involved in works contract;
(iii) a delivery of goods on hire-purchase/any system of payment by instalments;
(iv) a transfer of the right to use any goods;
(v) a supply of goods by any unincorporated association or body of persons to a member;
(vi) a supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating).</td></tr>
<tr><td>Meaning of Dealer</td><td>♦ means any person who carries on the business of buying, selling, supplying or distributing goods, directly or indirectly, for cash, or for deferred payment, or for commission, remuneration or other valuable consideration, and
♦ includes:-
▪ a local authority, a body corporate, a company, any cooperative society or other society, club, firm, Hindu undivided family or other association of persons which carries on such business.</td></tr>
</table>

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	▪ a factor, broker, commission agent, del credere agent, or any other mercantile agent, and ▪ an auctioneer.
	A mercantile agent, agent handling goods/documents of title to goods or an agent for collection of payment, acting on behalf of a dealer residing outside the State, is also a dealer.
	Government is also a dealer except in case of sale of old and discarded stores or waste.
Meaning of Sales tax law	Sales tax law <u>means</u> any law for the time being in force in any State or part thereof, which provides for the levy of taxes on the sale or purchase of goods generally or *on any specified goods expressly mentioned in that behalf* and <u>includes</u> Value Added Tax (VAT) law, and "general sales tax law" <u>means</u> the law for the time being in force in any State or part thereof which provides for the levy of tax on the sale or purchase of goods generally and <u>includes</u> VAT law.
INTER-STATE SALE [SECTION 3]	
Where sale occasions movement of goods from one State to another	♦ Inter-State sale takes place if <u>sale occasions the movement of goods from one State to another</u>. ♦ Where the movement of goods commences and terminates in the same State, it shall not be deemed to be a movement of goods from one State to another.
Where sale is effected by transfer of documents of title to goods during their movement from one State to another	♦ Inter-State sale takes place if the sale or purchase is effected by a transfer of documents of title to the goods *during their movement from one State to another.* ♦ Where goods are delivered to a carrier or other bailee for transmission, the movement of the goods shall be deemed to commence at the time of such delivery and terminate at the time when delivery is taken from such carrier or bailee.
Where gas sold or purchased and transported through a common carrier pipeline involves comingling of gases	♦ Sale or purchase is deemed to be inter-state sale/purchase where gas sold/purchased and transported through a common carrier pipeline becomes co-mingled and fungible with other gas in the pipeline and such gas is introduced in the pipeline in one state and is taken out from the pipeline in another state.

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INTER-STATE STOCK TRANSFER/INTER-STATE CONSIGNMENT TRANSFER	
Not liable to CST	Where the goods are sent by a dealer, outside the State to his other place of business or his agent/principal in other State, such transfer is not liable to CST.
Conditions to be fulfilled	(i) There was no pre-existing agreement with the branch for the sale of the goods so transferred.
	(ii) Dealer must obtain Form F from its branch office and furnish it to the assessing authority.
SALE OUTSIDE THE STATE	
Sale outside a State	When a sale/purchase of goods is determined to take place inside a State, such sale/purchase shall be deemed to have taken place outside all other States.
Sale inside a State	A sale or purchase of goods shall be deemed to take place inside a State if the goods are within the State- (a) in the case of specific or ascertained goods, at the time the contract of sale is made; and (b) in the case of unascertained or future goods, at the time of their appropriation to the contract of sale by the seller or by the buyer, whether assent of the other party is prior or subsequent to such appropriation. Where there is a single contract of sale or purchase of goods situated at more places than one, it shall be deemed that there are separate contracts in respect of the goods at each of such place.
SALE IN COURSE OF IMPORT/EXPORT	
No CST	CST is not leviable on sale in course of export/import.
Sale in the course of export	Following sales shall be deemed to be sale in the course of export:-
	(i) Sale or purchase occasions export involving transhipment of goods from one country to the other and shall be between two parties of two countries.
	(ii) Sale or purchase effected by transfer of documents of title to goods after the goods have crossed customs frontiers of India.

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	(iii) Penultimate sales, i.e. the sale preceding the sale occasioning the export. A sale is considered as penultimate sale if: (i) There is a pre-existing agreement or order in relation to export. (ii) Penultimate sale must be, after the agreement with the foreign buyer, for the purpose of complying with such agreement or order in relation to export. (iii) Same goods which are sold in penultimate sale must be exported, though may not be in the same form. Selling dealer needs to furnish Form H obtained from the exporter to whom the goods are sold. If any designated Indian carrier purchases Aviation Turbine Fuel for the purposes of its international flight, such purchase shall be deemed to take place in the course of the export.
Sale in course of import	Following sales shall be deemed to be sale in the course of import:-
	(i) Sale or purchase occasioning import of goods into India.
	(ii) Sale or purchase effected by a transfer of documents of title to goods before the goods have crossed customs frontiers of India.
Meaning of customs frontier of India	Customs frontier means crossing the limits of the area of a customs station in which imported goods/export goods are ordinarily kept before clearance by customs authorities.
RATES OF TAX ON SALES IN THE COURSE OF INTER-STATE TRADE OR COMMERCE	
Concessional rate of CST	The concessional rate of CST is:- (i) 2% of the turnover of the dealer or (ii) Rate applicable to the sale or purchase of such goods inside the appropriate state under the sales tax law of that State whichever is lower.

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Conditions to be fulfilled for concessional rate of CST	A dealer is liable to pay CST at the concessional rate of CST provided the following conditions are satisfied:- (i) Sale is of goods eligible for concessional rate of CST**, i.e. the goods described in section 8(3). (ii) Sale has been made to a registered dealer. (iii) Selling dealer has obtained a declaration in Form C from the purchasing dealer and furnish it to the prescribed authority.
	****** Following goods as specified in the certificate of registration of the registered purchasing dealer, are eligible for concessional rate of CST:- (a) goods of the class/classes intended for resale by him, for use by him in manufacture or processing of goods for sale, for use in the telecommunications network, for use in mining, or for use in the generation or distribution of electricity or any other form of power.
	(b) containers or other materials intended for being used for the packing of goods for sale. Further, containers or other materials used for the packing of any goods referred to in clause (a) or (b) above are also so eligible [Section 8(3)]
Cases where concessional rate of CST is not applicable	In case any of the three conditions are not fulfilled (as specified above), the rate of CST would be the rate applicable to the sale or purchase of such goods inside the appropriate State under the sales tax law of that State.
DETERMINATION OF TURNOVER FOR CENTRAL SALES TAX	
Meaning of turnover	Turnover means the aggregate of the sale prices received and receivable by him in respect of sales of any goods in the course of inter-State trade or commerce made during any prescribed period and determined in accordance with the provisions of this Act and the rules made thereunder.
Deductions to be made from the aggregate of the sale prices while computing the turnover	(i) Central sales tax payable $\text{Turnover} = \text{Aggregate of sales price} \times \frac{100}{100 + \text{Rate of tax}}$

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<table>
<tr><td rowspan="2"></td><td colspan="2">(ii) Sale price of all goods returned to the dealer by the purchasers of such goods within a period of 6 months from the date of delivery of the goods.
The period of six months for return of goods is not applicable in respect of rejected goods as it is a case of un-fructified sale.</td></tr>
<tr><td colspan="2">(iii) Such other deductions as the Central Government may, having regard to the prevalent market conditions, facility of trade and interests of consumers, prescribe.</td></tr>
<tr><td rowspan="4">Meaning of sale price</td><td colspan="2">Sale price means the amount payable to a dealer as consideration for the sale of any goods subject to following inclusions and exclusions:-</td></tr>
<tr><td>Inclusions</td><td>Any sum charged for anything done by the dealer in respect of the goods at the time of or before the delivery thereof</td></tr>
<tr><td rowspan="2">Exclusions</td><td>Cash discount</td></tr>
<tr><td>Cost of freight/ delivery or cost of installation where such cost is separately charged by the dealer.</td></tr>
</table>

Other Inclusions and Deductions from sale price	
Dharmada	includible because so far as the purchaser is concerned, he has to pay the whole amount for purchasing the goods.
Weighment dues	includible if the services of weighing are in respect of the goods and incidental to their being sold.
Insurance charges	includible if incurred by the assessee prior to the delivery of the goods.
Packing charges	packing charges and cost of packing material are includible.
Indemnity/ Guarantee charges	excluded as it is recovered from the same buyers to incur loss during transit at buyers' request.
Excise duty	includible
Government subsidies	excluded
Design Charges	includible if charged separately in respect of goods manufactured as per design and sold to buyer

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<table>
<tr><td>Deposits for returnable containers</td><td>excluded</td></tr>
<tr><td>Free of cost material supplied by customer</td><td>excluded</td></tr>
<tr><td colspan="2">Sale price in case of works contract: Sale price of goods involved in execution of works contract shall be determined in the prescribed manner (no rules so far notified) by making such deductions from the total consideration for the works contract as may be prescribed and such price shall be deemed to be the sale price.</td></tr>
<tr><td>Collection of tax only by registered dealers</td><td>No person who is not a registered dealer shall collect in respect of any sale made by him of goods in the course of inter-State trade or commerce any amount by way of tax under this Act.</td></tr>
<tr><td>CST payable to be rounded off</td><td>The amount of CST, interest, penalty, fine or any other sum payable, and the amount of refund due, under CST Act shall be rounded off to the nearest rupee while crediting the same to the Government.</td></tr>
<tr><td colspan="2">EXCEPTIONS TO LEVY OF CENTRAL SALES TAX (CST)</td></tr>
<tr><td>No CST on penultimate sales for export</td><td>A dealer shall not be liable to pay CST on the penultimate sales for export.</td></tr>
<tr><td rowspan="2">No CST on subsequent sales</td><td>Conditions to be satisfied for exemption to subsequent inter-State sale of the goods are as follows:</td></tr>
<tr><td>(i) First sale should be an inter-State sale and <u>subsequent sale should be effected by transfer of documents of title</u> to the goods during the movement of such goods in course of inter-State sales.
Note: Exemption to subsequent sales is available even if the first inter-State sale is exempt from CST.</td></tr>
</table>

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	(ii) Subsequent inter-Sate sale is exempt only if:- (a) purchaser is a registered dealer. (b) the goods are of description referred to in section 8(3) (subsequently discussed).
	(iii) The dealer effecting the subsequent sale needs to furnish following certificates/declaration:- (a) Form E-I/Form E-II: obtained from the registered dealer from whom he has purchased the goods, and (b) Form C: obtained from buying dealer if the subsequent sale is made to a registered dealer*.
	*However, it shall not be necessary to furnish Form C in respect of a subsequent sale of goods if: (a) the sale or purchase of such goods is, exempt from tax generally or is subject to tax lower than 3%, under the sales tax law of the appropriate State and (b) the dealer effecting such subsequent sale proves to the satisfaction of the prescribed authority that such sale is of the nature referred herein.
	CST is leviable if any of the three conditions mentioned above are not fulfilled. Levy and collection of CST, in such cases, would be in the following States:- (a) Where such subsequent sale has been effected by a registered dealer: State in which he is registered. (b) Where such subsequent sale has been effected by an unregistered dealer: State from which such subsequent sale has been effected.
No CST on sale to foreign missions or UN etc.	No CST is payable on inter-State sale of any goods to any official or personnel/consular/diplomatic agent of:- (i) any foreign diplomatic mission or consulate in India or (ii) the United Nations or any other similar international body.
	Conditions: (i) Such buyer has purchased such goods for himself or for the purposes of such mission, consulate, United Nations or other body. (ii) The dealer selling such goods furnishes to the prescribed authority Form J obtained from such buyer.

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EXEMPTION FROM CST	
Exemption by notification granted by the State Government	State Government can grant exemption if following conditions are satisfied:- (a) State Government is satisfied that such exemption is necessary in the public interest. (b) Sale is made to a registered dealer. (c) The selling dealer has furnished Form C as obtained from the registered purchasing dealer.
Exemption from CST to a sale to unit/developer in SEZ	A registered dealer in SEZ (unit in SEZ/developer of SEZ) can obtain goods from outside SEZ, for specified purposes, without payment of CST provided:- ♦ Form I has been furnished by the purchasing dealer, and ♦ goods are of such class as specified in registration certificate of the registered dealer
GOODS OF SPECIAL IMPORTANCE/DECLARED GOODS	
Declared goods/Goods of special importance	♦ "Declared goods" means goods declared to be of special importance in inter-State trade or commerce. ♦ An illustrative list of goods of special importance: (i) Cereals (ii) Coal, including coke in all its forms, but excluding charcoal (iii) Cotton, (indigenous or imported) in its unmanufactured state, whether ginned or unginned, baled, pressed or otherwise, but not including cotton waste (iv) Cotton fabrics (v) Cotton yarn, but not including cotton yarn waste.
Restrictions imposed on the tax imposed on the declared goods	♦ The tax payable under the sales tax law of a State in respect of any sale or purchase of such goods inside that State shall not exceed 5% of the sale or purchase price. ♦ If a tax is levied on sales or purchase of any declared goods inside a State and the same commodity is subsequently sold in the course of inter-State trade or commerce and is subjected to CST, the sales tax paid within the State realised previously in respect of the commodity is reimbursed provided:- (a) the tax on the inter-State sale has been actually paid, and (b) the inter-State sale of goods is in the same form.

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Question 1

State the distinctions between the central sales tax and central excise duty.

Answer

Central Sales Tax	Central Excise Duty
Levied under Entry 92A of List I of Seventh Schedule to Constitution of India.	Levied under Entries 84 of List I of Seventh Schedule to Constitution of India.
The levy is on sale of goods.	Levy is on manufacture or production of goods.
Revenue is collected and retained by State Government.	Revenue is collected and retained by the Central Government.
Tax is payable only when goods move from one State to another.	Duty is payable when manufactured goods are removed from the factory.

Question 2

Briefly examine the validity of the following statements with reference to the CST Act:-

(i) Since goods include all materials, articles and all other kinds of movable property, newspapers would also be considered as goods.

(ii) 'Place of business' includes place of business of the agent.

(iii) Profit motive is essential to call an activity a "business".

(iv) CST is leviable on transactions of leasing / hiring of assets for a defined period.

Answer

(i) No, the statement is not valid. Although as per the definition of goods, goods include all materials, articles and all other kinds of movable property, newspapers have been specifically excluded from the said definition. Hence, newspapers cannot be considered as goods.

(ii) Yes, the statement is valid. The definition of place of business specifically includes the place of business of an agent where a dealer carries on business through such agent.

(iii) No, the statement is not valid. Profit motive is not essential to call an activity a 'business' under the CST Act. The definition of "business" clearly specifies that for an activity to be called "business", profits motive is not necessary.

(iv) Yes, the statement is valid. CST is leviable on transactions of leasing / hiring of assets for a defined period. As per the definition of sale, transaction of leasing and hiring of assets for a defined period is deemed to be a sale.

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Question 3

X of Kolkata sells goods to Y of Chennai and hands over the goods to MKS Transport, Kolkata for transporting the same to Chennai. The lorry receipt is sent to Y by post. While goods are in transit, Y sells the goods to Z of Vijayawada, Andhra Pradesh by endorsing the lorry receipt and goods are diverted to Vijayawada. X, Y and Z are registered dealers. Is the second sale between Y and Z chargeable to tax?

Answer

The first sale by X to Y is chargeable to central sales tax. However, sale of goods by Y to Z is exempt as it is a subsequent sale by transfer of documents of title to the goods during their movement provided subsequent sale is made to a registered dealer (in the given case Z is a registered dealer), Form C is furnished by the buying dealer, Z to Y of Chennai and Y has collected Form E1 from X of Kolkata.

Question 4

Examine whether the following amount to inter-State sales under CST:-

(i) X of Chennai sends goods by air to his branch office at London. Subsequently, he transfers the documents of title of such goods to a buyer in Scotland after said goods have crossed the customs frontiers of India.

(ii) M of Mumbai comes to Delhi, purchases certain chemicals from N and transports them in his own name to Mumbai.

(iii) A London based entrepreneur enters into a contract of sale of goods with Pawan of Gujarat and sends the goods to India.

Answer

(i) Since in the given case, sale is effected by transfer of documents of title to the goods after the goods have crossed the customs frontiers of India, it is not an inter-State sale, but a sale in the course of export.

(ii) The sale is completed at Delhi itself. Therefore, the sale does not occasion the movement of goods from one State to another. Hence, sale of goods by N to M is not an inter-State sale.

(iii) Since in this case, the sale has occasioned the import of the goods into the territory of India, it is not an inter-State sale, but a sale in the course of import.

Question 5

Examine whether CST is leviable on the following transactions:-

(i) Inter-State sale of the electrical energy.

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(ii) Samar is a dealer of textiles in Vapi, Gujarat. Madhav of Lucknow approached him and purchased goods worth ₹ 1,00,000. However, instead of taking the delivery of the goods in Vapi, he directed Samar to deliver said goods in his factory located at Surat, Gujarat.

Answer

(i) Although electrical energy is goods, CST is not leviable on it as the charging Section 6(1) specifically excludes it from the purview of levy of CST.

(ii) CST is not leviable on the goods dispatched by Samar to Madhav's factory in Surat as there is no inter-State movement of goods. Goods have merely moved from one city of Gujarat to another.

Question 6

Discuss the validity of the following statements with reference to computation of tax liability under CST Act:

(i) Cost of freight, separately charged in the invoice, shall be deducted from sale price.

(ii) Subsidy given by Government to manufacturers (selling the product at controlled price) to compensate cost of production will form part of sale price.

(iii) Charity or dharmada collected by dealer will not form part of sale price.

(iv) Free of cost material supplied by the customer will be added to the sale price.

Answer

(i) The statement is valid. The cost of freight is excluded from the sale price where such cost is separately charged by the dealer in the invoice.

(ii) The statement is not valid. Where a product is 'controlled' and has to be sold at 'controlled price', subsidies are granted by the Government to manufacturers to compensate the cost of production, which is usually higher than the 'controlled price'. Such subsidy will not form part of sale price.

(iii) The statement is not valid. Charity / Dharmada collected by dealer will form part of sale price because so far as the purchaser is concerned, he has to pay the whole amount for purchasing the goods.

(iv) The statement is not valid. Under CST Act, free of cost material supplied by buyer is not required to be added.

Question 7

Mr. Mohandas, a first stage dealer of a machine in the State of Maharashtra, furnishes the following data:

S.No.	*Particulars*	*₹*
(i)	*Total inter-State sales during current financial year (CST not shown separately)*	*93,87,000*

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(ii)	*Above sales include:*	
	Dharmada	*9,00,000*
	Freight (₹ 1,20,000 is not shown separately in invoices)	*3,20,000*
	Cost of corrugated boxes specially designed for packing of the machinery	*56,000*
	Installation and commissioning charges shown separately	*52,000*

Determine CST payable assuming that all transactions were covered by valid 'C' Forms and sales tax rate within the State is 5%.

Answer

Computation of Mr. Mohandas's CST payable

Particulars	₹	₹
Total inter-State sales		93,87,000
Less: Freight shown separately in the invoices [Note-2]	2,00,000	
Installation and commissioning charges shown separately [Note-3]	52,000	2,52,000
Turnover including CST		91,35,000
CST payable = $91,35,000 \times \frac{2}{102}$ (B) [Note-4]		1,79,118

Notes:

1. Dharmada and cost of packing material are includible while calculating turnover.
2. Freight charges of ₹ 1,20,000 are not deductible while calculating the turnover as they are not shown separately in invoices. Remaining amount of freight, shown separately in the invoices, is deductible.
3. Installation and commissioning charges are deductible while calculating the turnover since shown separately in the invoices.
4. The CST on transactions covered by valid 'C' Form is 2% or the sales tax rate within the State, whichever is lower. Since, in this case, the State sales-tax rate is higher than 2%, the rate of CST is taken as 2%.

Question 8

Solaris India Pvt. Ltd.'s total inter-State sales @ 4 % CST for the current financial year is ₹ 1,50,00,000 (CST not shown separately). In this regard, following additional information is available:

(i) *Goods sold to Mr. A for ₹ 1,50,000, on 16.07.20XX were returned by him on 12.12.20XX.*

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(ii) *A buyer, Mr. B, to whom goods worth ₹ 55,000 were dispatched on 16.04.20XX, rejected such goods. The said goods were received back on 15.11.20XX.*

(iii) *Goods sold to Mr. C for ₹ 5,00,000, on 16.04.20XX were returned by him on 12.12.20XX.*

Determine the amount of sale price under CST Act.

Answer

Computation of Sale Price of Solaris India Pvt. Ltd. under CST Act

Particulars	₹
Total sales	1,50,00,000
Less: Goods returned by Mr. A	1,50,000
(deductible as returned within 6 months)	
Goods returned by Mr. C	Nil
(not deductible since returned after six months)	
Goods rejected by Mr. B after six months (Refer note below)	55,000
Sale price under CST Act	1,47,95,000

Note: The period of six months for return of goods is not applicable in respect of rejected goods as it is a case of un-fructified sale.

Question 9

Mr. Y of Mumbai purchased declared goods (goods of special importance) from Nagpur by paying sales tax at @ 5%. Subsequently, the commodity is sold to a dealer at Chennai. The dealer Y while collecting and remitting tax on the inter-State sale, wants refund of tax paid on sale within State (i.e. purchase from Nagpur). Is he correct?

Answer

If a tax has been levied on sale or purchase of any declared goods inside a State and the same goods are subsequently sold in the course of inter-state trade or commerce and is subjected to tax under the CST Act, sales tax paid has to be reimbursed to the dealer. However, sales tax paid within the state can be reimbursed only when the CST has been paid subsequently and not otherwise.

Hence, in this case, Mr. Y can claim refund of tax paid within the State after payment of central sales tax in respect of such declared goods.

Question 10

Mr. Mani reported inter-State sales of ₹ 45,00,000 (inclusive of central sales tax) for the current financial year. In this regard following additional information is available:

(i) *Freight ₹ 2,30,000 (₹ 80,000 is not shown separately on invoices)*

(ii) *Goods sold to Mr. X for ₹ 45,000 on 15.05.20XX were returned on 18.10.20XX.*

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(iii) Mr. Z, a buyer to whom goods worth ₹ 30,000 were dispatched on 17.04.20XX, rejected such goods. The said goods were received back on 18.11.20XX.

Determine the taxable turnover and CST payable, assuming that all the transactions were covered by valid "C" forms and sales tax rate within the State is 5%.

Answer

Computation of Mr. Mani's taxable turnover and CST payable

Particulars	**₹**	**₹**
Total inter-State sales		45,00,000
Less: Freight shown separately in the invoices [Freight not shown separately in invoices is not deductible]	1,50,000	
Goods returned by Mr. X [deductible as returned within 6 months]	45,000	
Goods rejected by Mr. Z after 6 months [deductible although returned after 6 months, as it is a case of an un-fructified sale]	30,000	2,25,000
Turnover (including CST)		42,75,000
Taxable turnover (rounded off) [₹ 42,75,000 × 100/102]		**41,91,176**
CST @ 2% [₹ 42,75,000 × 2/102]		
Since transactions are covered by valid 'C' Form, CST is 2% or sales tax rate within the State (5%), whichever is lower, i.e., 2%		
CST payable (rounded off)		**83,824**

Question 11

Briefly examine the validity of the following statements with reference to the Central Sales Tax Act, 1956:-

(i) Sale includes a mortgage or hypothecation of or a charge or pledge on goods.

(ii) Central sales tax is leviable on the inter-State sale of goods by any unincorporated association or body of persons to a member.

(iii) Penultimate sales for exports is not liable to central sales tax.

Answer

(i) No, the statement is not valid. The definition of sales clearly excludes a mortgage or hypothecation of or a charge or pledge on goods.

(ii) Yes, the statement is valid. Central sales tax is leviable on sales of all goods, other than electrical energy, in course of inter-state trade/ commerce. As per the definition of

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sale under Central Sales Tax Act, 1956, sale of goods by any unincorporated association or body of persons to a member is deemed to be a sale. Hence, Central sales tax is leviable on the sale of goods by any unincorporated association or body of persons to a member.

(iii) Yes, the statement is valid. Since penultimate sale for exports is deemed to be the sale in the course of exports, it would not be liable to central sales tax.

Question 12

The total CST sales of 'X' Ltd. for the current financial year is ₹ 75 lakhs. Company provides the following additional information:

(i) Goods sold to Mr. A for ₹ 1,00,000 on 16.04.20XX, were returned by him on 10.07.20XX.

(ii) A buyer Mr. B, to whom goods worth ₹ 50,000 were dispatched on 12.05.20XX, rejected such goods. The said goods were received back on 15.11.20XX.

(iii) Goods sold to Mr. C for ₹ 5,00,000 on 16.05.20XX were returned by him on 12.12.20XX.

(iv) The total turnover of the year includes Dharmada ₹ 30,000.

(v) All the amounts mentioned are inclusive of tax.

Determine the amount of sale price under CST Act.

Answer

Computation of sale price under CST Act

Particulars	₹
Total sales	75,00,000
Less: Goods returned by Mr. A	1,00,000
(deductible since such goods are returned within 6 months)	
Goods rejected by Mr. B after six months	50,000
(deductible since the period of 6 months for return of goods is not applicable in respect of rejected goods being a case of un-fructified sale)	
Goods returned by Mr. C	Nil
(not deductible since such goods are returned after six months)	
Dharmada (includible while computing turnover)	Nil
Sale Price under CST Act	**73,50,000**

Question 13

Briefly explain whether central sales tax will be applicable:-

(i) when goods are sent by dealer outside the State to his other place of business.

(ii) if at the time of stock transfer outside the State, dealer has an order for such sale in hand.

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Answer

(i) When the goods are sent by dealer outside the State to his other place of business, such movement of goods is an inter-State stock transfer and is not liable to central sales tax. The burden to prove that the inter-State movement of goods is stock transfer, lies on the dealer and not on the Department. For this purpose, the dealer has to submit a declaration obtained from his other place of business in Form F.

(ii) If at the time of stock transfer outside the State, the dealer has an order for such sale in hand; movement of such goods shall be deemed to have been occasioned as a result of sale. Therefore, such inter-State sale of goods will be liable to central sales tax.

Question 14

Mr. Harish is a registered dealer in Delhi. You are required to compute the central sales-tax payable by him from the details furnished below:-

Particulars	***₹***
Total inter-State sales (including CST)	*16,00,000*
(i) Weighment dues (Weighing is incidental to the goods being sold)	*48,000*
(ii) Deposits for returnable container	*25,000*
(iii) Excise duty	*80,000*
(iv) Freight charges recovered separately in the invoice	*60,000*
(v) Goods returned by dealers within six months of sale, but after the end of the financial year	*40,000*
Amounts given in points (i) to (v) above are included in total inter-State sales of ₹ 16,00,000	
Buyers have issued 'C' forms for all purchases	
Sales tax rate within the State is 1%.	

Answer

Computation of central sales tax payable

	₹	**₹**
Sales as per bill (including CST)		16,00,000
Less: Weighment dues (Note-1)	-	
Deposits for returnable container (Note-2)	25,000	
Excise duty (Note-3)	-	
Freight charges (Note-4)	60,000	
Goods returned within 6 months of sale	40,000	1,25,000
Turnover including CST		14,75,000

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Central sales tax @ 1% $\left(₹\,14,75,000 \times \frac{1}{101}\right)$ (Note-5)		14,603.96
CST payable (rounded off)		**14,604.00**

Notes:

1. If the service of weighing is in respect of goods and incidental to their being sold, it forms part of sale price.
2. Deposits for returnable container are not includible in the sales price.
3. Excise duty is a part of sales price.
4. When freight charges are separately charged by dealer, they should be deducted from the sales price.
5. CST on transactions covered by valid 'C' forms is 2% or the sales-tax rate within the State, whichever is lower. Since, in this case, the State sales-tax rate is lower than 2%, the rate of CST is taken as 1%.

Exercise

1. *State the objects of the CST Act, 1956.*
2. *To what extent the Constitution (46th Amendment) Act, 1982 has widened the scope of making levy both in the case of Central Governments as well as State Governments.*
3. *Write short note on Appropriate State.*
4. *Write short note on business and place of business with reference to CST, 1956.*
5. *Write short note on:*
   (i) *Crossing the customs frontier of India.*
   (ii) *Prescribed period.*
6. *A branch outside the State cannot be considered as a place of business. Discuss the correctness of the said proposition.*
7. *Discuss the term 'dealer' under the CST Act, 1956.*
8. *Write short note on deemed dealer.*
9. *When can a Government be treated as a dealer?*
10. *Explain the term "declared goods". Furnish any eight items of such declared goods under the CST Act, 1956.*
11. *Explain the term "sale in course of export".*
12. *What is sale in course of import?*
13. *When does the liability to pay tax on inter-State sales arise?*
14. *Is a subsequent inter-State sale of goods exempt from central sales tax?*

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UNIT – 5 : VALUE ADDED TAX

<table>
<tr><th colspan="3">KEY POINTS</th></tr>
<tr><td>Value Added Tax (VAT)</td><td colspan="2">VAT is a tax on the value added to the commodity at each stage in production and distribution chain.
When tax is levied on tax i.e, tax leviable at each stage is chargeable on a value which includes the tax paid at earlier stage; it leads to cascading of taxes.
Under VAT, tax is not levied on tax paid at earlier stage; it is levied only on the value added as credit of tax paid at earlier stages is allowed to be set off against the tax payable at the next stage. Thus, VAT helps in eliminating cascading of taxes.</td></tr>
<tr><td rowspan="3">Variants of VAT</td><td>Gross Product Variant</td><td>Tax is levied on all sales and deduction for tax paid on inputs excluding capital goods is allowed.</td></tr>
<tr><td>Income Variant</td><td>Tax is levied on all sales and deduction for tax paid on inputs and only depreciation on capital goods is allowed.</td></tr>
<tr><td>Consumption Variant</td><td>Tax is levied on all sales and deduction for tax paid on all business inputs (including capital goods) is allowed. Consumption variant of VAT is the most widely used variant of the VAT.</td></tr>
<tr><td rowspan="2">Methods of computation of VAT</td><td>Addition Method</td><td>❖ All factor payments (excluding value of materials) including profits aggregated to arrive at the total value addition on which tax rate is applied to calculate the tax.
❖ Mainly used with income variant of VAT.</td></tr>
<tr><td>Invoice Method</td><td>❖ Tax is imposed at each stage of sales on entire sale value and tax paid at the earlier stage (on purchases) is allowed as set-off.
❖ Also called as 'Tax Credit Method' or 'Voucher Method'.
❖ Most common and popular method for computing VAT liability.
❖ Mainly used with consumption variant of VAT.</td></tr>
</table>

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<table>
<tr><td></td><td>Subtraction Method</td><td>❖ Tax is charged only on value added at each stage of sale of goods i.e., difference between sales and purchases.
❖ Applied where tax is not charged separately.
❖ Suitable for gross product variant of VAT.</td></tr>
<tr><td rowspan="2">Merits and Demerits of VAT</td><td>Merits</td><td>Demerits</td></tr>
<tr><td>➢ Reduced tax evasion
➢ Increased tax compliance
➢ Certainty
➢ Transparency
➢ Cheaper exports
➢ Better accounting systems
➢ Neutrality</td><td>➢ Distortions in case of exemptions/ concessions
➢ Increased compliance cost
➢ Increased working capital requirements
➢ Consumption favoured over production
➢ Tax evasion through bogus invoices
➢ Regressive tax</td></tr>
<tr><td rowspan="3">VAT in Indian context</td><td>Central Level</td><td>❖ CENVAT on manufacture of goods & services</td></tr>
<tr><td>State Level VAT</td><td>❖ State VAT on intra-State sale of goods (replacing erstwhile sales tax regime)
❖ White Paper on State-Level VAT in India provided the broad framework of State-Level VAT to be adopted in India.</td></tr>
<tr><td>Proposed dual GST</td><td>❖ GST would create a common domestic market, remove multiplicity of taxes, eliminate cascading effect of tax on tax, make prices of the Indian products competitive and, above all, benefit the end consumers.
❖ Dual model GST has been proposed in India so that both Central and State Governments can collect taxes on goods and services.
❖ GST will subsume most of the indirect taxes being levied in India including central sales tax (CST).</td></tr>
</table>

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<table>
<tr><td rowspan="3">Constitutional provisions</td><td colspan="2">♦ Entry 54 of State List provides for 'Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of entry 92A of Union List'.
♦ Clause (29A) of the Article 366 of the Constitution provides an inclusive definition of "tax on sale or purchase of goods" which lays down six specific instances of deemed sale i.e., cases which are not sale in traditional sense but have been deemed to be sale for the purpose of leviability of CST/VAT.
♦ Deemed sale encompass elements of both goods as well as services - goods portion is chargeable to CST/VAT and services portion to service tax.</td></tr>
<tr><td colspan="2">Sale means-
♣ any transfer of property in goods by one person to another for cash or deferred payment or for any other valuable consideration; and
♣ includes "deemed sales" transactions under Article 366(29A) of the Constitution of India; but
♣ does not include a mortgage or hypothecation of, or a charge or pledge on, goods.</td></tr>
<tr><td colspan="2"><u>Goods</u>
♦ Broadly the definition of goods adopted by various States is on the lines of definition of goods provided under CST Act.
♦ Goods may be tangible (like computer, pen, pencil etc.) as well as intangible (like patent, copyright).
♦ Goods include all kinds of movable property, but not newspapers, actionable claims, stocks, shares and securities.
♦ Plant and machinery erected at site, being immovable property, is not goods.
♦ Electricity is goods but lottery ticket, being actionable claim, is not goods.
♦ Software (branded as well as unbranded) is goods.</td></tr>
<tr><td rowspan="2">VAT rates</td><td>0%</td><td>❖ Natural and unprocessed products in unorganised sector - Items which are legally barred from taxation and items which have social implications</td></tr>
<tr><td>1%</td><td>❖ Precious stones, bullion, gold and silver ornaments etc.</td></tr>
<tr><td></td><td></td><td>❖ Rate of declared goods has also been increased to 5% by many States after amendment of CST Act w.e.f. 08.04.2011.</td></tr>
</table>

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	5%	❖ Items of basic necessities like medicines and drugs, all agricultural and industrial inputs, declared goods & capital goods. Originally White Paper had proposed 4% rate on such goods but many States have subsequently increased this rate to 5%.
	12.5/ 13.5%	❖ All other goods not chargeable to any of the above rates. Originally White Paper had proposed 12.5% rate as the revenue neutral rate but most of the States have subsequently increased this rate to 13.5%.
Coverage of goods under VAT	❖ Generally, all the goods, including declared goods are covered under VAT (benefit of input tax credit allowed). ❖ Liquor, lottery tickets, petrol, diesel, aviation turbine fuel and other motor spirit are not covered under VAT. ❖ Though sale of liquor, petrol, diesel and aviation turbine fuel (ATF) is charged to tax under VAT laws in many States, taxes paid on them are not allowed as credit to the buyer. Thus, they are outside the VAT chain.	
Input tax and Output tax	♦ Input tax is the tax paid or payable in the course of business on purchases of any goods (inputs, capital goods and other goods) from a registered dealer OF THE STATE. ♦ Output tax is the tax charged or chargeable under the Act, by a registered dealer on the sale of goods in the course of business.	
Input Tax Credit (ITC)		
Basic principles	♦ ITC in relation to any period means setting off the amount of input tax by a registered dealer against the amount of his output tax. ♦ CST paid on purchases made from outside the State cannot be claimed as ITC but ITC can be used for paying CST arising on inter-State sale. ♦ ITC can be availed by both manufacturers and traders in respect of input tax paid on purchase of inputs and capital goods within the State from a registered dealer for being sold within the State as well as in other States, irrespective of when these will be utilized/sold. ♦ There is a negative list of capital goods (on the basis of principles already decided by the Empowered Committee) not eligible for input tax credit. ♦ As per White Paper, input tax credit on capital goods can be adjusted over a maximum of 36 equal monthly installments.	

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Purchases eligible for ITC	Taxable goods should be purchased for any one of the following purposes- ➢ for intra-State or inter-State sale/resale; ➢ for being used in the manufacture of taxable goods or in the packing of such manufactured goods intended for intra-State or inter-State sale or exports ; ➢ for being used in the execution of a works contract; ➢ for being used as capital goods required for the purpose of manufacture or resale of taxable goods; ➢ for making zero-rated sales other than exports
Purchases not eligible for ITC	ITC may not be allowed in respect of following purchases- ➢ purchases from unregistered dealers; ➢ purchases from registered dealer who opts for composition scheme; ➢ invoice less purchases; ➢ purchase where invoice does not show amount of tax separately; ➢ purchases for being utilized in the manufacture of exempted goods or purchase of goods when sales are exempt; ➢ purchase of goods for personal use/consumption or to be provided free of charge as gifts, free samples; ➢ imports and inter-State purchases
Some special aspects	♦ VAT does not require bill to bill co-relation between input and output. ♦ Proportionate ITC is available when inputs are used both for taxable and exempt output. Credit relating to exempt output has to be reversed. ♦ In case of stock transfer, input tax paid in excess of 2% is allowed as ITC. ♦ Whereas for zero rated sales ITC can be availed, it cannot be availed in respect of exempt sale. ♦ After utilizing ITC for payment of VAT and CST, excess credit, if any, can be carried forward. ♦ As per White Paper, if goods are exported, input tax paid is to be refunded within a period of 3 months from the end of the period in which export took place.

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	♦ As per White Paper, SEZ units and EOU are granted either exemption from payment of input tax or refund of input tax paid within three months. ♦ Special CVD paid on imported goods can be refunded if VAT is charged on further sale of such imported goods and VAT invoice mentions that buyer will not be able to avail CENVAT credit of such duty.
VAT Liability	
What is VAT liability?	♦ VAT liability of the dealer is calculated by deducting input tax credit from output tax payable i.e., tax chargeable on sales during the payment period (say, a month). ♦ **Net tax payable = Output tax – Input tax**
Composition Scheme	
Scheme	♦ White Paper provides a optional composition scheme for small registered dealers where tax is paid at a small percentage (composition rate) of the gross turnover. Composition rate can be reduced to as low as 0.25%. ♦ Input tax credit is not allowed under the scheme and dealer opting for the scheme is not authorized to issue VAT-able invoices.
Eligible and Non-eligible dealers	**Eligible dealer:** ❖ A registered dealer who is liable to pay VAT and whose turnover does not exceed ₹ 50 lakh in preceding financial year and whose purchases and sales are within the State, can opt for Composition Scheme. **Non-eligible dealer:** ❖ Dealer making inter-state purchases/sales; ❖ Dealer importing/exporting goods for sale in/outside India; ❖ Dealer stock transferring goods outside the State; ❖ Dealer desirous of issuing VAT-able invoice.
Exercising of option	♦ On the day of exercising the option, dealer should not have any stock of goods which are brought from outside the State and not claim input tax credit on the inventory available on that day. ♦ He should also not use any goods brought from outside the State after such date.

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<table>
<tr><td rowspan="2">Advantages and Disadvantages</td><td colspan="2">Advantages</td><td>Disadvantages</td></tr>
<tr><td colspan="2">➢ Minimum records
➢ Simple tax calculation
➢ Simple return</td><td>➢ Non-availability of input tax credit
➢ VAT chain gets broken</td></tr>
<tr><td colspan="4">VAT & Sales Tax Incentives</td></tr>
<tr><td rowspan="4"></td><td colspan="3">Any exemption from tax is against the principles of VAT as it breaks the VAT chain. State Governments, therefore, stopped giving incentives to new industries after January, 2000 and incentives already given to industries set up prior to January, 2000 were continued under VAT regime by converting them to deferral schemes so that such industries could pass on the benefit of VAT to their buyers.
By and large sales tax incentives were given in three modes as described below:</td></tr>
<tr><td>Exemption from tax</td><td colspan="2">❖ Neither tax charged nor tax collected by eligible industry.
❖ Input tax also not payable on purchases of raw materials.
❖ Exemption ceases either with the expiry of exemption period or the exemption amount, whichever occurs first.</td></tr>
<tr><td>Deferment of tax liability</td><td colspan="2">❖ Tax collected from buyers but payment thereof to the Government deferred.
❖ After expiry of prescribed period, liability to be paid in specified installments.</td></tr>
<tr><td>Remission of tax</td><td colspan="2">❖ Tax collected from buyers but payment thereof remitted.
❖ Input tax paid on purchases by the unit to be refunded.</td></tr>
<tr><td colspan="4">VAT and Works Contract</td></tr>
<tr><td>Basic principles</td><td colspan="3">♦ Works contract is a deemed sale (composite contract of goods and services) and is thus, liable to VAT.
♦ While VAT is leviable on goods involved in the execution of works contract, service tax is levied on value of services.
Where labour and other service charges are quantifiable, taxable turnover would be contract price less labour and other service charges.</td></tr>
</table>

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	♦ Where labour and other service charges are not quantifiable- ▪ taxable turnover can be cost of goods plus cost of transfer/conversion and profit margin; or ▪ Standard rate of deduction provided in State VAT laws can be used for deducting labour and other like charges in the contract to arrive at the taxable turnover.
Tax rates	♦ **Schedule rate** if value of each item of material transferred in the course of execution of a works contract is identifiable. Tax is charged on value of individual items of materials as provided under the schedules to the concerned State VAT legislation. ♦ **Revenue neutral rate** if values of individual goods are not identifiable. Contractor can pay tax at Revenue Neutral Rate (RNR - generally 12.5%/13.5%) after deducting the value attributable towards labour and other like charges.
Composition scheme	♦ VAT legislations provide for an optional Composition Scheme to collect tax on works contracts in a simple manner so as to minimize the inconvenience caused to the assessees. ♦ Tax is paid at a composite rate on the gross contract value. Tax rate is generally lower in such scheme. ♦ Input tax credit is not allowed under the scheme. However, in some States (e.g. Maharashtra) partial input tax credit is granted.
VAT and Lease Transactions	
Lease	Under a lease, a party owning the asset (called the 'lessor') provides that asset for use over a certain period of time to another party (called the 'lessee') for consideration (called 'rentals'). Legal ownership of the asset remains with the lessor, but the lessee retains the possession and uses the asset over the period of the lease.
	♦ Lease is a deemed sale and is thus, liable to VAT. ♦ If complete possession and control is not handed over in respect of an asset given on rent, transaction is not a deemed sale (as it is not a transfer of right to use) but a service and is thus, liable to service tax. ♦ Sub-lease of an asset too can be taxed, unless the State Value Added Tax law has provided for the levy of tax only at one stage. ♦ Taxable event is transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration.

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<table>
<tr><td></td><td>

- Taxable turnover is the amount of valuable consideration paid or payable for any sale during the given period. Certain States provide deduction of interest or financial charges for determining taxable turnover.
- Input tax credit is allowed to lessor on purchase of the asset which is to be leased. Since these assets are generally capitalized in the books of lessor, provisions relating to input tax credit on capital goods apply in this case also.
- Maintenance of the leased asset involving supply of consumables by the lessor is not a works contract (as there is no transfer of property in such materials to the lessee) and is thus, not liable to VAT. It is a service contract liable to service tax.
  - If parts are also supplied during maintenance, such contract becomes a works contract liable to VAT.
- Sale of a leased asset after the lease period is over is taxable in the same manner in which normal sale of such asset would have been taxed.

</td></tr>
<tr><td colspan="2">VAT and Hire Purchase</td></tr>
<tr><td rowspan="2">Hire Purchase (HP)</td><td>Whereas under HP, hirer acquires the goods immediately on signing the hire-purchase agreement but ownership or title of the same is transferred only when last installment is paid, under installment payment system, buyer gets ownership of the goods with the payment of first installment.</td></tr>
<tr><td>

- Since HP transactions are deemed sales, they are liable to VAT.
- Transactions which are purely of a financial nature between the financier and the hirer (hire-purchase finance) are not liable to VAT.
- Taxable event is the actual or physical delivery of goods on hire purchase or under any system of payment by installments.
- Some States provide for deduction of interest or finance charges included in the installment in arriving at the taxable turnover while some do not provide any such deduction.
- Provisions relating to input tax credit in case of a normal sale apply in case of HP also. However, some States provide for *pro rata* credit.
- Tax may not be payable when transaction fructifies into a concluded sale as tax has already been paid on installments. However, other view is that tax is payable again on fructified sale on depreciated value of the asset or on its market value but if no consideration is payable on fructified sale, then tax is not attracted.

</td></tr>
</table>

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	♦ Goods returned are treated as normal sales return and thus refund of tax can be claimed as per the provisions of respective State VAT laws if goods are returned within the prescribed period. ♦ When transaction of hire purchase fails, vendor takes possession of the goods and normally installment received for the intervening period gets forfeited.
VAT and Sale of Food Articles	
	♦ Sale of food in a hotel is a deemed sale liable to VAT. Service portion involved in such a sale is declared to be a service liable to service tax.
Deficiencies in State-Level VAT	
	❖ Non-uniformity in VAT rates across the country, ❖ Non-uniformity in provisions of VAT laws across the country, ❖ CST is non-Vatable, ❖ Double taxation - No clear distinction between goods and services which leads to double taxation i.e., both service tax and VAT are levied on the same transaction. ❖ Hurdles in movement of inter-state goods.

Question 1

Briefly answer the following questions:-

(a) *Which is the most popular and common method for computing VAT liability and at what stage is the tax imposed under this method?*

(b) *Can VAT be said to be non-beneficial as compared to single stage-last point system?*

(c) *What are the items aggregated in the addition method to calculate the VAT payable? When is this method mainly used?*

(d) *Does White Paper on VAT allow only a manufacturer to avail set off of input tax credit on capital goods and not a trader?*

Answer

(a) Invoice method is the most common and popular method for computing the tax liability under the VAT system. Under this method, tax is imposed at each and every stage of sale on the entire sale value, and the tax paid at the earlier stage is allowed as set-off.

(b) VAT system has many advantages like reduced tax evasion, transparency, certainty, reduction in cascading effect of taxes etc. which are not there in the single stage-last point system. However, since VAT is imposed or paid at various stages and not at last stage, it increases the working capital requirements and the interest burden on the same. To this extent, it may be considered to be non-beneficial as compared to the single stage-last point taxation system though to a large extent, this rigour is brought down through input tax credits on purchases.

(c) Under addition method, all factor payments (excluding value of material) and profit are added to arrive at the value addition on which VAT rate is applied to compute the VAT payable. This method is mainly used with income variant of VAT.

(d) No. As per the White Paper on VAT, set off of input tax credit on capital goods is available to both manufacturers and traders.

Question 2

Briefly explain whether following purchases are eligible for availing input tax credit:

(a) Rohan purchased goods from a registered dealer. He claims to have paid VAT on the said goods but the invoice pertaining to said purchase has been lost on account of negligence of a clerk in his office.

(b) Jain & Co. purchased goods from Tide Enterprises. Tide Enterprises is an unregistered dealer.

(c) Ankit purchased some capital goods. The final product manufactured by Ankit using these capital goods is exported.

(d) Mohan purchased goods for being used in execution of a works contract.

(e) Singla & Co. purchased goods from Malhotra Enterprises, a registered dealer. Malhotra Enterprises has opted for composition scheme under the provisions of respective State VAT Act.

(f) Sahil purchased goods from Ganesh. Ganesh has not shown VAT charged on the purchase value, separately in the invoice.

Answer

(a) Input tax credit cannot be claimed on purchase made by Rohan as the purchase invoice is not available with him.

(b) Purchases made by Jain & Co. from Tide Enterprises are not eligible for input tax credit as Tide Enterprises is not a registered dealer.

(c) Capital goods used for manufacturing/packing goods to be sold in the course of export out of the territory of India are eligible for claiming input tax credit. Thus, Ankit can claim input tax credit on capital goods purchased by him.

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(d) Mohan can claim input tax credit as purchase of goods for being used in execution of a works contract are eligible for input tax credit.

(e) Purchases made by Singla & Co. from Malhotra Enterprises are not eligible for input tax credit as purchases from registered dealer who opts for composition scheme under the provisions of respective State VAT Act are not eligible for Input Tax Credit.

(f) Purchases made by Sahil are not eligible for input tax credit as the invoice issued by Ganesh does not show VAT charged on the purchase value separately in the invoice.

Question 3

Mr. Goenka is a trader selling raw materials to manufacturers of finished products. He procures his stock in trade from other States as well as purchases the same from the local markets. Following transactions pertain to a sale made by Mr. Goenka to a manufacturer for the year ended 20XX:-

S.No.	*Particulars*	*₹*
(1)	*Cost of materials procured from other States excluding tax*	*1,00,000*
(2)	*Cost of local materials including VAT*	*2,25,000*
(3)	*Other expenditure including storage, transport, interest and loading and unloading and profit earned by him*	*87,500*

Calculate the invoice value charged by Mr. Goenka to the manufacturer. Assume VAT rate to be 12.50% and central sales tax to be 2%.

Answer

Computation of invoice value

Particulars		**₹**
Cost of materials procured from other States		1,00,000
[Since input tax credit cannot be availed in respect of CST, it will be included in the cost of inputs]		2,000
Add: Cost of local materials	2,25,000	
Less: VAT @12.5%	25,000	2,00,000
[Since, input tax credit of ₹ 25,000 would be available, it will not be included in cost of inputs]		
Add: Other expenses and profit		87,500
Sales Price of goods		3,89,500
Add: VAT on the above @12.5% (rounded off)		48,688
Invoice value charged by Mr. Goenka to the manufacturer		**4,38,188**

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Question 4

Mr. Rajesh, a registered dealer, sells his products to dealers in his State and in other States. Profit margin is 15% of cost of production and VAT rate is 12.5% of sales. Following further information is provided by Mr. Rajesh:

(i) Intra-State purchases of raw material ₹ 2,50,000/- (excluding VAT @ 4%)

(ii) Purchases of raw materials from an unregistered dealer ₹ 80,000/-.

(iii) High seas purchases of raw materials are ₹ 1,85,000/- (excluding custom duty @ 10%).

(iv) Purchases of raw materials from other States (excluding CST @ 2%) ₹ 50,000/-.

(v) Transportation charges, wages and other manufacturing expenses excluding tax ₹ 1,45,000/-

(vi) Interest paid on bank loan ₹ 70,000/-. Loan is taken to acquire a land for building a factory.

All the afore-mentioned purchases have been sold by Mr. Rajesh. You are required to compute net tax liability and total sales value (invoice value) under value added tax.

Answer

Computation of net VAT liability and total sales value

Particulars	**₹**
Intra-State purchases of raw material (excluding VAT ₹ 10,000)	2,50,000
Purchases of raw materials from unregistered dealer *[Refer Note 1]*	80,000
High seas purchases of raw materials *[Refer Note 2]*	2,03,500
Purchase of raw materials from other States *[Refer Note 3]*	51,000
Transportation charges, wages and manufacturing expenses	1,45,000
Cost of production	7,29,500
Add : Profit margin 15%	1,09,425
	8,38,925
Add: VAT @ 12.5%	1,04,866
Total sales value (invoice value)	**9,43,791**

Computation of Net VAT liability

	₹
VAT on above sales price @ 12.5%	1,04,866
Less: Input tax credit on intra-State purchases *[Refer Note 4]*	10,000
Net VAT payable	**94,866**

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Notes:

1. Input tax credit is not available on the purchases of raw materials from unregistered dealer.
2. Duty paid on high seas purchases i.e., imports is not a State VAT, so input tax credit is not available in respect of the same and it is a part of cost of production.
3. Input tax credit in respect of tax paid on inter-state purchases is not allowed.
4. Tax on intra-State purchases is ₹ 10,000. As credit of the same will be available, it is not included in the cost of production.
5. Interest on loan has been excluded for calculating the cost of production as the loan is availed for purposes other than working capital.

Question 5

Following are the details of purchases, sales, etc. effected by Vasudha & Co., a registered dealer, for the year ended 31.3.2016:

Particulars	*(₹)*
Purchase of raw materials within State (1000 units) inclusive of VAT levy at 12.5%	*2,70,000*
Inter-State purchases of raw materials, inclusive of CST at 2%	*2,04,000*
Import of raw materials, inclusive of customs duty of ₹ 35,000	*4,35,000*
Capital goods purchased on 1.5.2015, inclusive of VAT levy at 10% (input credit to be spread over 2 financial years)	*3,30,000*
Other manufacturing expenses	*1,50,000*
Sale of taxable goods within State, inclusive of VAT levy at 4%	*7,28,000*
Sale of goods within State, exempt from levy of VAT (Goods were manufactured from the Inter-State purchase of raw materials)	*1,20,000*
Closing stock as on 31.3.2016 was 100 units of raw materials purchased within the State	

Compute net VAT liability of the dealer for the year ended 31.3.2016.

Answer

Computation of Net VAT liability of Vasudha & Co. for the year ended 31.3.2016

Particulars	**(₹)**
Input tax credit:	
Intra-State purchases of 1000 units raw materials *[Refer Note 1]*	30,000
Inter-State purchases of raw materials *[Refer Note 2]*	-

Import of raw materials *[Refer Note 3]*	
Purchase of Capital Goods *[Refer Note 4]*	15,000
Other manufacturing expenses *[Refer Note 5]*	-
Total input tax credit available (A)	45,000
Output VAT payable:	
Sale of taxable goods within State [(₹ 7,28,000 x 4)/104]	28,000
Sale of exempted goods within State *[Refer Note 6]*	-
Total VAT payable (B)	28,000
Net VAT liability [VAT credit to be carried forward) [(B)-(A)]	**(17000)**

Notes:-

1. VAT paid on intra-State purchases is eligible for input tax credit $\left[\frac{2,70,000 \times 12.5}{112.5}\right]$.
2. CST paid on intra-State purchases is not eligible for input tax credit.
3. Customs duty is not eligible for input tax credit.
4. VAT paid on purchase of capital goods is eligible for input tax credit. However, the same has to be spread over a period of two years $\left[\frac{3,30,000 \times 10}{110 \times 2}\right]$.
5. No input tax credit can be availed on expenses incurred on manufacturing.
6. No VAT will be payable on sale of goods exempted from levy of VAT. Further, since these goods were manufactured from the inter-State purchases of raw materials (non-vattable inputs), input tax credit is not affected.
7. VAT system allows credit in respect of purchases made during a period to be set-off against the taxable sales during that period, irrespective of when the supplies/inputs purchased are utilized/sold. Therefore, input tax credit in respect of closing stock of raw materials need not be reduced from total input tax credit available.

Question 6

Ashok, purchased raw material 'A' for ₹ 30,00,000 plus VAT @ 4%. Out of such raw material 60% was used for manufacture of taxable goods and the remaining for manufacture of goods which are exempt from VAT.

Another raw material 'B' was purchased for ₹ 15,00,000 on which VAT was paid at 1%. Entire raw material' 'B' was used for manufacture of taxable goods only.

The entire taxable goods were sold for ₹ 50,00,000 plus VAT @ 12.5%.

Compute net VAT liability of Ashok on the assumption that there was no opening or closing inventory.

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Answer

Computation of Net VAT liability of Ashok

Particulars	₹	₹
Output VAT (50,00,000 × 12.5%) [A]		6,25,000
Input VAT [B]		
Raw material 'A' (30,00,000 × 60% × 4%) [Refer Note]	72,000	
Raw material 'B' (15,00,000 × 1%)	15,000	87,000
Net VAT payable by Ashok [A] – [B]		**5,38,000**

Note : Input tax credit is allowed only in respect of the raw material used in manufacture of taxable goods and hence, the same has been restricted to the extent of 60%.

Question 7

Determine net VAT liability of X for the month of December, 20XX using invoice method of computation from the following data:

Purchase price of goods acquired from local market (including VAT)	*₹ 52 lakhs*
VAT rate on input	*4%*
Transportation, insurance, warehousing and handling cost incurred by X	*₹ 20,000*
Goods sold at a profit margin (% of cost of production)	*14%*
VAT rate on sales	*12.50%*

Answer

Computation of Net VAT liability

Particulars	₹
Purchase price of goods acquired from local market excluding VAT (input tax credit does not form part of cost of production) ₹ $\left[52{,}00{,}000 \times \frac{100}{104}\right]$	50,00,000
Transportation, insurance etc.	20,000
Cost of production	50,20,000
Profit @ 14% on cost of production	7,02,800
Total Sales	57,22,800
Output VAT payable @ 12.5%	7,15,350
Less: Input tax credit [VAT paid on goods acquired from local market is eligible for input tax credit]	2,00,000
Net VAT payable	**5,15,350**

Question 8

The particulars regarding sale, purchase etc. of Shubham Udyog for the last quarter of a financial year are as under:

	Particulars	*₹*
1.	*Purchases of raw material within the State*	
	(i) taxable @ 1%	*40,00,000*
	(ii) taxable @ 4% (Inputs were used in the manufacture of goods meant for intra-State sale, exempted sale and inter-State sale in the ratio of 2:1:1)	*60,00,000*
	(iii) taxable @ 12.5%	*10,00,000*
2.	*Sale of goods manufactured from raw material purchased @ 4% tax rate*	
	(i) Sale within the State (tax rate 4%)	*20,00,000*
	(ii) Exempted sale within the State	*10,00,000*
	(iii) Sale in the course of Inter-State trade or commerce (CST rate 2%)	*10,00,000*
3.	*Sale of raw material purchased @ 1% tax rate*	*44,00,000*
4.	*Goods manufactured from the raw material purchased @ 12.5% tax rate were given on lease. The deemed sale price of such goods is ₹ 12,00,000, taxable @ 12.5%.*	

You may assume that input tax credit of tax paid on raw material used in manufacture of leased goods is available immediately. Compute the amount of net Value Added Tax (VAT) payable by M/s Shubham Udyog for the relevant quarter. There was no opening or closing inventory. All figures of purchases and sales given above are exclusive of taxes.

How can he utilize the balance of input tax credit available, if any?

Answer

Computation of Net VAT payable for the last quarter of a financial year

	Particulars	₹
(A)	Output VAT payable	
(i)	On sale of taxable finished goods within the state (₹ 20,00,000 × 4%)	80,000
(ii)	On raw material (₹ 44,00,000 × 1 %)	44,000
(iii)	On leased goods (₹ 12,00,000 × 12.5%) (Deemed sale)	1,50,000
	Total (A)	2,74,000
(B)	Input tax credit available	
(i)	On raw material purchased @ 1% (₹ 40,00,000 × 1%)	40,000

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(ii)	On raw material purchased @ 4% (₹ 60,00,000 × 4%) × 3/4 (Note-1)	1,80,000
(iii)	On raw material purchased @ 12.5% (₹ 10,00,000 × 12.5%)	1,25,000
	Total (B)	3,45,000
	Net VAT payable = (A)-(B)	**(71,000)**
	CST payable on inter-state sale adjusted (₹ 10,00,000 × 2%)(Note-2)	20,000
	Excess input tax credit can be carried forward to next quarter (₹ 71,000 – ₹ 20,000)	**51,000**

Notes :

1. If goods manufactured from raw material are exempt from tax, no input tax credit is available on such raw material. Thus, out of total sales of ₹ 40,00,000 of goods manufactured from raw material purchased @ 4%, credit will not be allowed on 1/4th of the inputs used in manufacture of exempted goods. In other words, input tax credit will be allowed in respect of 3/4th of the inputs.
2. If finished goods are sold in the course of inter-state trade and commerce, input tax credit can be set off against the output tax liability.

Question 9

From the following information provided by M/s RA Ltd., registered under VAT law of Gujarat as dealer in consumer goods, compute the amount of net VAT payable for the month of July, 20XX and VAT credit to be transferred, if any:

Purchase of raw material (within the State)

Item	*(₹)*	*Rate of VAT*
Goods 'X'	*7,50,000*	*Exempt*
Goods 'Y'	*25,00,000*	*1%*
Goods 'Z'	*35,00,000*	*12.5%*

Sales

Particulars of finished goods sold	***State in which goods are sold***	***Value ₹***	***VAT/CST Rate %***
(i) Produced from goods 'X'	*Gujarat*	*5,00,000*	*12.5% VAT*
	Inter-State sales to Maharashtra	*6,00,000*	*2% CST*
(ii) Produced from goods 'Y'	*Gujarat*	*30,00,000*	*Exempt*
(iii) Produced from goods 'Z'	*Gujarat*	*40,00,000*	*4% VAT*

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Raw materials valued at ₹ 5 lakh of goods 'Z' have been transferred to the branch in Madhya Pradesh during the month. All figures of purchases and sales given above are exclusive of taxes.

Make assumptions where required and provide suitable explanations.

Answer

Computation of Net VAT payable by M/s. RA Ltd. for the month of July, 20XX

	Particulars	₹
(A)	Output VAT payable	
	(i) On sale of finished goods produced from Goods 'X' within Gujarat (₹ 5,00,000 × 12.5%)	62,500
	(ii) On sale of finished goods produced from Goods 'Z' within Gujarat (₹ 40,00,000 × 4 %)	1,60,000
	Total (A)	2,22,500
(B)	Input tax credit available	
	(i) Goods 'X' (Exempt)	Nil
	(ii) Goods 'Y' (Note-2)	Nil
	(iii) Goods 'Z' transferred to branch (₹ 5,00,000×10.5%) (Note-3)	52,500
	(iv) Remaining Goods 'Z' after transfer to the branch [₹ (35,00,000- 5,00,000)×12.5%]	3,75,000
	Total (B)	4,27,500
	Net VAT payable = (A)-(B)	(2,05,000)
	CST payable (₹ 6,00,000 × 2% = ₹ 12,000) on inter-state sale of goods produced from Goods 'X' adjusted (Note-4)	12,000
	Excess input tax credit carried forward to next month	**1,93,000**

Notes:

1. It is assumed that there is no opening and closing inventory. Hence, entire purchases of the raw materials have been used to manufacture the respective finished goods.
2. Goods utilized in the manufacture of exempted goods are not eligible for input tax credit. Hence, no input tax credit is available in respect of VAT paid on purchase of Goods 'Y' as they have been used to produce goods which are exempt from VAT.
3. In case of stock transfer, input tax paid in excess of 2% can be claimed as input tax credit.
4. Input tax credit can be used to set off the central sales tax payable on the inter-state sales.

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Question 10

The following particulars are provided by Mr. Purohit of Calcutta, who has purchased raw materials and other materials for manufacturing PVC Cans and PVC Pipes. The applicable State VAT rate and CST rate for raw materials and other materials is 12.5% and 2% respectively.

S. No.	*Particulars*	₹
1.	*Purchase of raw materials [exclusive of tax]*	*1,00,000*
2.	*Purchase of other materials [exclusive of taxes]*	
	-- Local	*20,000*
	-- Inter-State purchases	*40,000*
3.	*Manufacturing expenses*	*39,200*
4.	*Profit margin (on Sale Value)*	*20%*

Mr. Purohit manufactured 75% of production as PVC cans and 25% of production as PVC pipes. While PVC cans are subject to 12.5% VAT, PVC pipes are exempt. All materials were used in production and there was no closing stock of raw materials and other materials.

What would be the invoice value of sales charged by Mr. Purohit if all the manufactured goods were sold within the State? What would be his net liability to VAT?

Answer

Computation of invoice value of sales charged by Mr. Purohit

Particulars	**PVC Cans (12.5% VAT)**	**PVC Pipes (Exempt)**
	₹	**₹**
	(75%)	(25%)
Raw materials	75000	25000
VAT paid on the same [₹ 1,00,000 x 12.5% = ₹ 12,500]	NIL	3125
	(Refer Note 2)	(Refer Note 3)
Other materials - Local	15000	5000
VAT paid on the same [₹ 20,000 x 12.5% = ₹ 2,500]	NIL	625
	(Refer Note 2)	(Refer Note 3)
Other materials – Inter-State purchases	30000	10000
CST paid on the same [₹ 40,000 x 2% = ₹ 800] (Refer Note 4)	600	200
Manufacturing expenses	29400	9800

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Cost of goods sold	150000	53750
Add : Profit is 20% on sales (i.e., 25% of cost)	37500	13438
Sale price	187500	67188
Add : VAT payable (rounded off to nearest rupee)	23438	NIL
Invoice value	**210938**	**67188**

Computation of Net VAT liability for PVC Cans

Particulars	₹
Output VAT	23438
Less : Input VAT = [(12500 × 75%)+(2500×75%)] (Refer Note 5)	11250
Net VAT liability	**12188**

Notes:-

1. All the expenses have been apportioned in the ratio of 3:1 on *pro-rata* basis.
2. Since PVC Cans are taxable goods, VAT paid on raw materials is allowed as input tax credit and thus, the same will not form part of total cost.
3. Since PVC pipes are exempt goods, VAT paid on raw materials will not be allowed as input tax credit and thus, the same will form part of total cost.
4. Input tax credit is not available on CST. Therefore it will form part of total cost.
5. Input tax credit to the extent (75%) used in the production of taxable PVC Cans is allowed.

Question 11

Raj and Co., a manufacturer of product 'X', sold its goods to a distributor at ₹ 11,250. The distributor sold the goods to wholesaler for ₹ 13,500. The wholesaler sold the goods to a retailer for ₹ 16,875. The retailer sold the goods to consumer at ₹ 22,500. All the sales were inclusive of VAT @ 12.5%.

Compute total VAT payable under the subtraction method.

Answer

Computation of VAT payable by Raj & Co. under subtraction method

Particulars	Value added (₹)	VAT (₹)
Sale by manufacturer to distributor	11,250	$\left\lfloor 11,250 \times \frac{12.5}{112.5} \right\rfloor$ = 1,250
Sale by distributor to wholesaler	13,500 - 11,250 = 2,250	$\left\lfloor 2,250 \times \frac{12.5}{112.5} \right\rfloor$ = 250

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Sale by wholesaler to retailer	16,875 - 13,500 = 3,375	$\left[3{,}375 \times \frac{12.5}{112.5}\right]$ = 375
Sale by retailer to consumer	22,500 - 16,875 = 5,625	$\left[5{,}625 \times \frac{12.5}{112.5}\right]$ = 625
Total VAT payable		**2,500**

Question 12

Sidharth Enterprises, a dealer in Gujarat, purchased raw material worth ₹ 80,00,000 (excluding VAT) and manufactured finished goods worth ₹ 1,50,00,000 from such raw material in the month of August, 20XX. It transferred these finished goods to its branch in Mumbai on September 15, 20XX so that the goods can be sold from there. Thereafter, it received an order from Mr. X for the said finished goods in Mumbai on September 20, 20XX and hence sold the said goods to Mr. X from Mumbai branch. Compute:

(i) Amount of input tax credit available for the month of September, 20XX

(ii) Net VAT payable for the month of September, 20XX, and

(iii) Balance input tax credit carried forward to next month, if any.

Input VAT rate is 12.5% and output VAT rate is 4%.

Answer

Computation of VAT payable and input tax credit for September, 20XX

Particulars	**₹**
Output VAT payable (Note-1)	Nil
***Less*: Input tax credit** $\left[80{,}00{,}000 \times \frac{(12.5-2)}{100}\right]$ (Note-2)	**8,40,000**
Net VAT payable	**Nil**
Balance input tax credit carried forward to next month	**8,40,000**

Notes:

1. Inter-State stock transfers do not involve sale and, therefore they are not subject to VAT. Further, CST is not payable as there was no pre-existing agreement for the sale of the goods so transferred.
2. In case of stock transfer of finished goods, input tax paid (on inputs used in manufacture of such finished goods) in excess of 2% is available as input tax credit.

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Question 13

Lee Traders, a registered dealer having stock of goods worth ₹ 30,000, purchased from outside the State, wishes to opt for Composition Scheme. Advise the dealer whether it is possible.

Answer

If a dealer wishes to opt for Composition Scheme, he should not have any stock of goods which are brought from outside the State on the day he exercises the option to pay tax by way of composition. Hence, it is not possible for Lee Traders to opt for Composition Scheme as it has goods worth ₹ 30,000 purchased from outside the State on the day it wishes to opt for the Composition Scheme.

Question 14

Strong Constructions undertakes works contracts and maintains sufficient records to quantify the labour and other service charges. From the details given below, calculate the taxable turnover, input tax credit and net VAT payable under the State VAT Law:

	Particulars	*(₹)*
(i)	*Total contract price (excluding VAT)*	*1,80,00,000*
(ii)	*Materials purchased and used for the contract taxable at 12.5% VAT (inclusive of VAT)*	*33,75,000*
(iii)	*Labour charges paid for execution of the contract*	*40,00,000*
(iv)	*Other service charges paid for the execution of the contract*	*20,00,000*
(v)	*Cost of consumables used not involving transfer of property in goods*	*10,00,000*

Strong Constructions also purchased a plant for use in the contract for ₹ 20,80,000 (inclusive of VAT). In the VAT invoice relating to the same, VAT was charged at 4% separately. Assume 100% input tax credit is available on capital goods immediately and output VAT is leviable at 12.5%. Make suitable assumptions where required and show the workings.

Answer

Under works contract, VAT is imposed on the sale price of the goods in which there is a transfer of property. Labour and other charges incurred for such execution are deductible.

Computation of the taxable turnover, input tax credit and net VAT payable

Particulars	**₹**	**₹**
Total contract price		1,80,00,000
Less : Deductions admissible		
Labour charges paid for executing the contract	40,00,000	
Service charges paid for execution of contract	20,00,000	

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Cost of consumables not involving transfer of property in goods	10,00,000	70,00,000
Taxable turnover		**1,10,00,000**
Output VAT payable @ 12.5%		13,75,000
Less : Input tax credit admissible		
On the material purchased ₹ $\left[33,75,000 \times \frac{12.5}{112.5}\right]$	3,75,000	
On the plant purchased ₹ $\left[20,80,000 \times \frac{4}{104}\right]$	80,000	
Total input tax credit		**4,55,000**
Net VAT payable		**9,20,000**

Question 15

State with reasons in brief whether the following statements are correct or incorrect with reference to the provisions of value added tax laws:

(i) It is permitted to issue 'tax invoice' inclusive of VAT i.e., aggregate of sale price & VAT.

(ii) VAT laws of different States require a registered dealer to compulsorily get his books of accounts audited irrespective of the quantum of his turnover.

(iii) Taxpayer's Identification Number (TIN) is a 10 digit alpha numeral.

Answer

(i) Incorrect. One of the requirements under the contents of the tax invoice is that rate and amount of tax charged in respect of taxable goods should be distinctly shown in the 'tax invoice', in order to claim input tax credit.

(ii) Incorrect. Different States have prescribed different turnover limits for VAT audit and only if the turnover of the registered dealer crosses such limit, he is required to get his books of accounts audited under VAT laws.

(iii) Incorrect. Taxpayer's Identification Number (TIN) is a 11 digit numeral. The first two characters represent the State Code as used by the Union Ministry of Home Affairs and the next nine characters are different in different states.

Question 16

Vivitha & Co., a registered dealer in Ludhiana, furnishes the following details of purchases and sales pertaining to the month of May, 20XX:

	₹ (in lakh)
Opening balance in VAT input credit brought forward	*0.20*
Purchases of raw materials within the State (final invoice value)	
From registered dealers	*26.00*

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From dealers opting for Composition Scheme	*5.20*
Purchases from outside the State (final invoice value)	*10.20*
Sales within State of finished goods, excluding VAT	*40.00*
Input VAT rate for raw materials is 4%	
Output VAT rate is 10%.	

Determine the VAT liability of the dealer.

Answer

Computation of Net VAT liability of Vivitha & Co. for the month of May, 20XX

Particulars		₹ (in lakh)
Input VAT:		
Opening balance of input VAT credit		0.20
VAT paid on purchases of raw materials within the State from registered dealers [₹ 26 lakh × 4/104]		1.00
VAT paid on purchases of raw materials within the State from dealers opting for composition scheme [Note 1]		Nil
CST paid on purchases from outside the State [Note 2]		Nil
Total input tax credit available	**(A)**	1.20
Output VAT:		
VAT @ 10% on sale of finished goods within the State		
[₹ 40 lakh × 10/100]	**(B)**	4.00
Net VAT liability [(B)-(A)]		**2.80**

Notes:

1. Purchases of raw materials within the State from dealers opting for composition scheme are not eligible for input tax credit.

2. Inter-State purchases are not eligible for input tax credit.

Question 17

Compute net VAT payable by Rainbow & Co. from the following details furnished by it for the month of July, 20XX:-

Inputs procured		*(₹)*
(i)	*Raw material at Nil rate of VAT*	*5,00,000*
(ii)	*Raw material at 4% VAT*	*20,00,000*
(iii)	*Raw material at 12% VAT*	*10,00,000*

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Output		*(₹)*
(i)	*Intra-State sale of finished goods at 4% VAT (these goods were produced entirely from raw material procured at Nil VAT)*	*8,00,000*
(ii)	*Exempted sales (60% of the raw material procured at 4% VAT was used in producing these goods)*	*10,00,000*
(iii)	*Intra-State sale of finished goods at 12% VAT*	*10,00,000*
(iv)	*Intra-State sale of raw material purchased at 4% VAT*	*5,00,000*
(v)	*50% of the raw material produced at 12% VAT has been utilised to produce capital goods for the manufacturing process in Rainbow & Co's factory (Market Value is ₹ 7,50,000)*	

There was no opening and closing stock of goods.

Answer

Computation of Net VAT payable by Rainbow & Co.:-

Particulars	**₹**
Output VAT payable:	
Sale of goods at 4% VAT (₹ 8,00,000 × 4%)	32,000
(manufactured out of exempted material)	
Sale of finished goods at 12% VAT (₹ 10,00,000 × 12%)	1,20,000
Sale of raw materials purchased at 4% VAT (₹ 5,00,000 × 4%)	20,000
Total (A)	1,72,000
Input tax credit available:	
Purchase of raw material @ 4% VAT	32,000
40% of (₹ 20,00,000 × 4%) [Note – 1]	
Purchase of raw material @ 12% VAT including purchases used for manufacturing capital goods produced (12% of ₹ 10,00,000) [Note – 2]	1,20,000
Total (B)	1,52,000
Net VAT payable (A) – (B)	20,000

Notes:

1. Input tax credit in respect of goods used to produce exempted goods is not allowed. Hence, 60% of the input tax credit has been disallowed on goods purchased at 4% VAT which are utilized to produce exempted goods.
2. Input tax credit on raw materials is allowed even if the same has been consumed to produce capital goods. Hence, full input tax credit on goods purchased at 12% VAT has been allowed.

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Question 18

Compute net VAT liability of Tirupati from the following information:-

Particulars	*₹*	*₹*
Raw materials from foreign market		*1,20,000*
(including duty paid on imports @ 20%)		
Raw material purchased from local market		
Cost of raw material	*2,50,000*	
Add: Excise duty @ 12.5%	*31,250*	
	2,81,250	
Add: VAT @ 4%	*11,250*	*2,92,500*
Raw material purchased from neighbouring State (including CST @ 2%)		*51,000*
Storage and transportation cost		*10,000*
Manufacturing expenses		*21,000*

Tirupati sold goods to Suresh and earned profit @ 12% on the cost of production. VAT rate on sale of such goods is 4%.

Answer

Computation of VAT liability of Tirupati

Particulars	₹	₹
Raw materials purchased from foreign market (including duty paid on imports @ 20%) [Customs duty forms part of cost of production, input tax credit of customs duty paid is not available]		1,20,000
Raw material purchased from local market:-		
Cost of raw material	2,50,000	
Add: Excise duty @ 12.5%	31,250	2,81,250
[Input tax credit of excise duty is not available]		
Raw material purchased from neighbouring State (including CST @ 2%) [Input tax credit of CST is not available]		51,000
Storage and transportation cost		10,000
Manufacturing expenses		21,000
Cost of production		4,83,250
Add: Profit @ 12% of cost of production		57,990
Sale Price		5,41,240

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VAT @ 4% on ₹ 5,41,240		21,649.6
Net VAT liability of Tirupati:-		
VAT on sale price (rounded off)		21,650
Less: Input tax credit		
Duty paid on imports	Nil	
CST paid on inter-State purchases	Nil	
VAT paid on local purchases	11,250	11,250
Net VAT payable by Tirupati		10,400

Question 19

Mr. Mahesh of Kolkata purchased goods from Mr. Suresh of Kolkata amounting to ₹ 8,55,000 including VAT @ 12.50% in the month of January, 20XX. He incurred ₹ 2,50,000 as manufacturing & other expenses and added @ 25% profit on cost.

Mr. Mahesh sold 80% of the goods to Mr. Nayan of Kolkata and charged VAT @ 12.50% on 02-02-20XX. Remaining 20% of the goods were transferred to his branch in Manipur on 05-02-20XX.

Compute the net VAT payable and input tax credit, if any, for the month of February, 20XX by assuming input output ratio to be 1: 1.

Answer

Computation of Net VAT payable and input tax credit

Particulars	₹	₹
Purchases of raw material [excluding VAT of ₹ 95,000 (₹ 8,55,000 × 12.5/112.5)]		7,60,000
Manufacturing and other expenses		2,50,000
Cost of production		10,10,000
Cost of goods sold [80% of ₹10,10,000]		8,08,000
Add: Profit @ 25% on the cost of goods sold		2,02,000
Sale price		10,10,000
Output VAT payable @ 12.5% (A)		1,26,250
Input tax credit on raw materials used in manufacture of finished goods that are sold [₹ 95,000 x 80%]	76,000	
Add: Input tax credit on raw materials used in manufacture of finished goods that are stock transferred to Manipur [₹ 7,60,000 x 20% x (12.5 – 2)%] (In case of inter-State stock transfer of finished goods, input tax paid on inputs used in manufacture of such finished	15,960	

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goods in excess of 2% is available as input tax credit.)		
Total input tax credit (B)		**91,960**
Net VAT payable (A) – (B)		**34,290**

Question 20

Justify the following statements with reference to the provisions of VAT:

(i) Sub-lease can be taxed.

(ii) Central sales tax is not vatable.

(iii) Sale of food in hotel is a deemed sales liable to VAT.

(iv) Refund can be claimed for goods returned under hire purchase transactions.

Answer

(i) Transfer of the right to use goods does not require that the goods should be owned by the person effecting such transfer. Accordingly, sub-lease of an asset too can be taxed, unless the State Value Added Tax law provides for the levy of tax only at one stage.

(ii) Under VAT, tax paid on inputs can be set-off against the tax paid on outputs. This can happen only when both the input tax and output tax are paid to one authority. Since, central sales tax (CST) is paid on purchases made from outside the State; credit thereof cannot be allowed by the State where sale is to be made. Thus, CST is not vatable.

(iii) Tax on sale/ purchase includes a tax on supply, by way of/ as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating) where such supply/ service is for cash, deferred payment or other valuable consideration. Thus, sale of food in hotel is a deemed sale liable to VAT.

(iv) Under hire purchase, VAT is payable on the date of delivery of the goods. If, for any reason the goods are returned, then refund of tax can be claimed as per the provisions of respective State VAT laws because in substance, this is a sales return. Refund can be claimed if the goods are returned within the specified period, if any, prescribed by the State VAT laws in this regard.

Question 21

Sparsh Enterprises, a dealer in consumer goods, submits the following information pertaining to the month of December, 20XX:

(i) Exempt goods 'P' purchased for ₹ 1,75,000 and sold for ₹ 3,50,000.

(ii) Goods 'Q' purchased for ₹ 2,25,000 (including VAT) and sold at a margin of 20% profit on purchases (VAT rate for purchases and sales 12.5%)

(iii) Goods 'R' purchased for ₹ 2,00,000 (excluding VAT) and sold for ₹ 2,50,000 (VAT rate for purchases and sales 4%);

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(iv) *His unutilized balance of input VAT credit on 1.12.20XX was ₹ 3,000.*

Compute the turnover, Input VAT, Output VAT and Net VAT payable by Sparsh Enterprises.

Answer

Computation of Turnover, Input VAT and Output VAT

Goods	Purchases [A]	Input VAT rate [B]	Input VAT credit [C] = [A] x [B]	Sales (Turnover) [D]	Output VAT rate [E]	Output VAT [F] = [D] x [E]
	₹	%	₹	₹	%	₹
P	1,75,000	-	-	3,50,000	-	-
Q (See Note)	2,00,000	12.5	25,000	2,40,000	12.5	30,000
R	2,00,000	4	8,000	2,50,000	4	10,000
Total	5,75,000		**33,000**	**8,40,000**		**40,000**

Computation of Net VAT payable by Sparsh Enterprises

	(₹)
Opening balance of input VAT credit	3,000
Add: Input VAT credit for December, 20XX **[C]**	33,000
Total Input VAT credit available	36,000
Less: Output VAT payable on taxable turnover **[F]**	40,000
Net VAT payable	**4,000**

Note:

	(₹)
Purchase value of goods Q (including VAT)	2,25,000
Less: VAT included in above $2,25,000 \times \frac{12.5}{112.5}$	25,000
Purchase price excluding VAT	2,00,000

Question 22

Mr. Naveen is a registered dealer of goods in Bihar. He sells his products to dealers in his State and in other States. Following additional information is provided by Mr. Naveen:

(i) *Raw material purchased in Bihar worth ₹ 80,000 (excluding VAT @ 12.5%)*

(ii) *High seas purchases of raw materials are ₹ 1,85,000 (excluding custom duty @ 10%).*

(iii) *Purchases of raw materials from West Bengal (excluding CST @ 2%) worth ₹ 50,000*

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(iv) *Transportation charges, wages and other manufacturing expenses are ₹ 3,50,000*

(v) *Interest paid on bank loan is ₹ 55,000. Loan is taken to acquire a land for building a factory.*

Mr. Naveen has sold all the manufactured goods after adding a profit margin of 10% of cost of production. VAT rate on sales is 12.5%. You are required to compute net VAT liability and total sales value (invoice value). There is no opening or closing inventory of both raw materials and manufactured goods.

Answer

Computation of total sales value

Particulars	₹
Intra-State purchases of raw material [excluding VAT of ₹ 10,000 (80,000 x 12.5%)]	80,000
High seas purchases of raw materials [Note 1]	2,03,500
Purchase of raw materials from West Bengal [Note 2]	51,000
Transportation charges, wages and manufacturing expenses	3,50,000
Cost of production	6,84,500
Add: Profit margin 10%	68,450
Sale price (exclusive of VAT)	7,52,950
Add: VAT @ 12.5% (rounded off)	94,119
Total sales value (invoice value)	**8,47,069**

Computation of net VAT liability

	₹
VAT paid on sales @ 12.5%	94,119
Less: Input tax credit on intra-State purchases [Note 3]	10,000
Net VAT payable	**84,119**

Notes:

1. Duty paid on high seas purchases i.e., imports is not a State VAT, so input tax credit is not available in respect of the same and it is a part of cost of production.
2. Input tax credit in respect of tax paid on inter-State purchases is not allowed and it is a part of cost of production.
3. Tax on intra-State purchases is ₹ 10,000. As credit of the same will be available, it is not included in the cost of production.

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4. Interest on loan has been excluded while calculating the cost of production as the loan is availed for purposes other than working capital.

Exercise

1. *Discuss the merits and demerits of VAT system.*
2. *Write a note on different methods of computation of VAT.*
3. *What are the different tax rates under VAT system?*
4. *Differentiate between input tax and output tax.*
5. *List the purchases which are not eligible for input tax credit.*
6. *Discuss the tax consequences of inter-State stock transfer under the VAT scheme.*
7. *Enumerate the eligible purchases in respect of which input tax credit can be availed.*
8. *State the benefits and drawbacks for a dealer who opts for Composition Scheme under VAT as per White Paper.*
9. *Who are not eligible for Composition Scheme under the VAT regime? Discuss briefly.*
10. *Briefly explain the different modes in which VAT incentives are given.*
11. *Explain the concept of Hire-purchase transactions. Comment upon their leviability to VAT.*
12. *Write a note to explain the impact of VAT on lease transactions.*
13. *Explain briefly whether VAT is leviable on following lease transactions:-*
    - *(a) Inter-State leasing*
    - *(b) Sale of leased asset after lease period*
    - *(c) Maintenance of leased asset*
14. *State the importance of VAT invoice in administering VAT.*
15. *Briefly list out the contents of VAT invoice.*

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2 Basic Concepts of Service Tax

Question 1

Briefly explain as to how and when the amendments made in Finance Bill, in respect of service tax matters come into force?

Answer

Amendments made by the Finance Bill, in respect of service tax matters, come into force from the date of enactment of the Finance Bill i.e., the date on which the Finance Bill receives the assent of the President of India. However, wherever it is specifically provided so in the Finance Bill, certain amendments become effective from a date to be notified after the enactment of the Finance Bill.

Question 2

With reference to the provision of Finance Act, 1994, examine whether service tax is leviable in the following situations:

(i) Services provided in a vessel stationed at a distance of 10 nautical miles from the Indian land mass.

(ii) Services provided in a vessel stationed at a distance of 54 nautical miles from Indian land mass in Exclusive Economic Zone (EEZ) of India for carrying out fishing operations.

(iii) Services provided in a vessel stationed at a distance of 54 nautical miles from Indian land mass in Exclusive Economic Zone (EEZ) of India for extraction of mineral oil.

Answer

(i) Yes. Levy of service tax extends to whole of India except Jammu and Kashmir and India means, *inter alia,* its territorial waters which extend upto 12 nautical miles from Indian land mass. Therefore, services provided in the vessel stationed at a distance of 10 nautical miles from the Indian land mass i.e., in Indian territorial waters will be liable to service tax.

(ii) No. Levy of service tax extends to whole of India except Jammu and Kashmir and India means, *inter alia,* the vessels located in the continental shelf of India and the exclusive economic zone of India, for the purposes of prospecting or extraction or production of mineral oil and natural gas and supply thereof. Therefore, though the vessel is stationed at a distance of 54 nautical miles from Indian land mass in Exclusive Economic Zone

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(EEZ) of India, services provided thereat will not be liable to service tax as the vessel is used for carrying out fishing operations.

(iii) **Yes.** In this case, since the vessel is used for one of the designated purposes i.e., for extraction of mineral oil, services provided thereat will be liable to service tax.

Question 3

With reference to service tax law as contained in Finance Act, 1994, discuss whether any 'consideration' is involved in following cases:

(i) Donations given to political parties.

(ii) Gifts received from friends at the time of wedding.

(iii) Grant given to a researcher to carry out a research in a particular field.

(iv) Grant given to a researcher to carry out any research of his choice. However, the researcher will have to provide IPR rights of the outcome of such research activity.

Answer

'Consideration' means everything received or recoverable in return for a provision of service. It includes monetary payment and any consideration of non- monetary nature or deferred consideration as well as recharges between establishments located in a non-taxable territory and taxable territory. In the backdrop of this definition, given situations are examined hereunder:

(i) **No,** as the donation is not given in return for provision of any service.

(ii) **No,** as in this case also gifts are given out of free will and not in lieu of any provision of service.

(iii) **Yes,** as there is a direction to carry out a specific activity, i.e., a research in a particular field in this case.

(iv) **Yes.** Though grants given for a research where the researcher is under no obligation to carry out a particular research is not a consideration, grant given with counter obligation on the researcher **to provide IPR rights** on the outcome of research undertaken with the help of such grants is a consideration for the provision of service of research.

Question 4

With reference to service tax law as contained in Finance Act, 1994, discuss whether any 'consideration' is involved in following cases:

(i) Donations given to a charitable trust with the condition that such trust would display the name of the donor in a fair organized by it.

(ii) Fine imposed by Traffic Police on over speeding vehicles on an expressway.

(iii) Services are provided by A to B. However, payment for the services is made by C, a debtor of B, on the instructions of B.

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Answer

'Consideration' means everything received or recoverable in return for a provision of service. It includes monetary payment and any consideration of non- monetary nature or deferred consideration as well as recharges between establishments located in a non-taxable territory and taxable territory. In the backdrop of this definition, given situations are examined hereunder:

(i) **Yes.** Donations to a charitable organization are not consideration unless charity is obligated to provide something in return. Since in this case, donations are given to the charitable trust with the condition that such trust would display the name of the donor in a fair organized by it, the donations would amount to consideration.

(ii) **No.** Since fines and penalties are legal consequences of a person's actions and not a consideration for any activity, fine imposed by Traffic Police on over speeding vehicles on an expressway is not a consideration.

(iii) **Yes.** The consideration for a service may be provided by a person other than the person receiving the benefit of service as long as there is a link between the provision of service and the consideration. Since in the given case, payment for the service is made by C, a debtor of service receiver B, on the instructions of B, the payment will be treated as consideration of service provided by A to B.

Question 5

XYZ & Co. is a consultancy firm based in New Delhi. It has two branch offices at Mumbai and Singapore. Services are provided by Mumbai branch to Head Office at New Delhi and by Head Office at New Delhi to Singapore branch. Explain which of the activities will constitute 'service' under service tax law.

Answer

As per section 65B(44) of Finance Act, 1994, a service is an activity carried out by one person for another person in lieu of a consideration. Further, Explanation 3 to section 65B(44) provides *inter alia* that an establishment of a person located in taxable territory and another establishment of such person located in non-taxable territory are treated as establishments of distinct persons. Also, as per explanation 4 to the said section, a person carrying on a business through a branch in any territory is treated as having an establishment in that territory.

Therefore, services provided by Mumbai branch to Head Office at New Delhi will not be 'service' in terms of section 65B(44) since both the establishments namely, Branch office and Head office are located in the taxable territory and are thus, one and the same person. However, when services are provided by Head Office at New Delhi to Singapore branch (located in non-taxable territory), the two establishments are treated as establishments of distinct persons and thus, the services provided in this case will constitute 'service' under service tax law.

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Question 6

Pragyan has received a sum of ₹ 5,00,000 from his employer on premature termination of his contract of employment. Pragyan needs your advice as to whether such receipts are liable to service tax.

Answer

No, Pragyan need not pay any service tax on such amount. Amounts paid by the employer to the employee for premature termination of a contract of employment are treated as amounts paid in relation to services provided by the employee to the employer in the course of employment. Hence, amounts so paid would not be chargeable to service tax.

Question 7

Mr. A boarded Rajdhani Express (fully AC train) from Kanpur on July 5, 20XX and disembarked at New Delhi. He hired a car from a local cab operator for the whole day on a lumpsum consideration and visited Delhi's historical monuments. In the night, he took the Metro to International Airport and boarded a flight to Mumbai. At Mumbai Airport, he used a radio taxi for going to his Hotel. Mr. A returned to Kanpur from a different train, Pushpak Express in sleeper class.

With reference to the provisions of Finance Act, 1994, examine the leviability of service tax on the various modes of travel undertaken by Mr. A.

Answer

As per section 66D of Finance Act, 1994, service of transportation of passengers, with or without accompanied belongings, by *inter alia*-

(i) railways in a class other than an air conditioned coach;

(ii) metro, monorail or tramway;

(iii) metered cabs or auto rickshaws.

are included in the negative list of services.

Therefore in the given case, service tax leviability on the various passenger transportation services used by Mr. A will be determined as under:

(i) Rail travel in AC train – Not covered under negative list and thus, liable to service tax.

(ii) Travel in a car rented for the whole day on a lumpsum consideration – Since travel by only metered cabs is covered in negative list, travel in a car rented for the whole day on a lumpsum consideration will be liable to service tax.

(iii) Metro travel – Covered in negative list and hence, not taxable.

(iv) Air travel – Not covered under negative list and thus, liable to service tax.

(v) Radio taxi travel – Not covered in negative list and thus, liable to service tax.

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(vi) Rail travel in sleeper class - Covered in negative list and hence, not taxable.

Question 8

With reference to the provisions of Finance Act, 1994, examine the validity of following statements:

(i) Services provided to and by Reserve Bank of India are covered in negative list of services.

(ii) Pisciculture (breeding of fish) is not liable to service tax as the same is covered under negative list of services.

Answer

(i) Invalid. Only services provided by Reserve bank of India, and not to Reserve Bank of India are covered in negative list of services.

(ii) Valid. Services relating to agriculture are covered in negative list of services. Agriculture means the cultivation of plants and rearing of all **life-forms of animals**, except the rearing of horses, for food, fibre, fuel, raw material or other similar products. Therefore, breeding of fish, being agriculture, would be covered under negative list of services and thus, be not liable to service tax.

Question 9

(i) "Not all the services provided by an employee to the employers are outside the ambit of service". Explain the statement with reference to service tax law.

(ii) Discuss whether the following services are liable to service tax:

(1) Services provided on contract basis by a person to another.

(2) Services provided by a casual worker to employer who gives wages on daily basis to the workers.

Answer

(i) "Not all the services provided by an employee to the employer are outside the ambit of services". The significance of this statement is that services that are provided by the employee to the employer in the course of employment are only outside the ambit of definition of service as per section 65B(44) of the Finance Act, 1994. Services provided outside the ambit of employment for a consideration would be a service.

(ii) (1) As per section 65B(44) of the Finance Act, 1994, service does not include a provision of service by an employee to the employer in the course of or in relation to his employment. Service provided on contract basis by a person to another are not provided in the course of employment and hence, is a service in terms of section 65B(44) of the Finance Act, 1994. Therefore, such services would be liable to tax.

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(2) Services provided by a casual worker to employer who gives wages on daily basis to the workers are services provided by the worker in the course of employment which comes under the exclusions of definition of service under section 65B(44) of the Finance Act, 1994. Hence, such services are not liable to service tax.

Question 10

BTR Association, an unincorporated body of individuals, provided warehousing services to Mr. Raman for ₹ 7,50,000. BTR Association is of the view that since it is not a natural person, warehousing service provided by it will not be a 'service' in terms of section 65B(44) of the Finance Act, 1994.

Examine whether the view taken by BTR Association is valid in law.

Answer

The view taken by BTR Association is not valid in law. As per section 65B(44) of the Finance Act, 1994, service means, *inter alia*, any activity for consideration carried out by a person for another. The term 'person' is not restricted to a natural person. The definition of person under section 65B(37), includes, *inter alia*, body of individuals, whether incorporated or not.

Thus, BTR Association is a person as it is a body of individuals and services provided by it would come under purview of definition of 'service' under section 65B(44) of the Finance Act, 1994.

Question 11

Shyam has given his tempos on hire to Mohan Brothers for transportation of food stuff for ₹ 14,00,000. He has also transferred the right to use such tempos to Mohan Brothers. Shyam has not paid any service tax on the consideration so received. Discuss whether Shyam is liable to pay service tax on the said transaction.

Answer

No, Shyam is not liable to pay service tax on the transaction entered into by him with Mohan Brothers. The transfer of tempos by way of hiring along with right to use is a deemed sales as per article 366(29A) of the Constitution of India. Charging section 66B of the Finance Act, 1994 stipulates that service tax is leviable on the value of all 'services' provided by one person to another. However, transfer, delivery or supply of any goods which is deemed to be a sale within the meaning of article 366(29A) of the Constitution is specifically excluded from the definition of 'service' under section 65B(44) of the Finance Act, 1994.

Therefore, the transaction entered into by Shyam with Mohan Brothers is not chargeable to service tax. Instead, VAT is leviable on the same.

Question 12

State whether the following services are covered in negative list of services under section 66D of Finance Act, 1994:

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(i) Service provided by way of supply of farm labour relating to agriculture.

(ii) Services by way of renting of residential dwellings for use as residence.

(iii) Services of funeral, burial, crematorium or mortuary and transportation of the deceased.

(iv) Service of transportation of passengers with or without accompanied belongings, by Railways in an air conditioned coach.

(v) Services by way of transportation of goods by road by a goods transportation agency.

(vi) Selling of space or time slots for advertisement broadcast by FM Radio.

Answer

(i) Yes. Service provided by way of supply of farm labour relating to agriculture is covered in the negative list of services.

(ii) Yes. Services by way of renting of residential dwellings for use as residence are covered in the negative list of services.

(iii) Yes. Services of funeral, burial, crematorium or mortuary and transportation of the deceased are covered in the negative list of services.

(iv) No. Service of transportation of passengers with or without accompanied belongings, by Railways in a class other than first class; or an air conditioned coach is covered in the negative list of services. Thus, service of transportation of passengers with or without accompanied belongings, by Railways in an air conditioned coach is not covered in the negative list of services.

(v) No. Services by way of transportation of goods by road, except the services of a goods transportation agency or a courier agency are covered in the negative list of services. Thus, services by way of transportation of goods by road by a goods transportation agency are not covered in the negative list of services.

(vi) No. Only selling of space for advertisements in print media is covered in the negative list of services. Thus, selling of space or time slots for advertisement broadcast by FM Radio will not be covered in the negative list of services.

Question 13

With reference to the provisions of service tax law, briefly examine the service tax implications in the following independent cases:-

(a) Miss Chaitali is working as an Assistant Manager in Success Software Limited (SSL) since 01.04.2014. One of the clause of her employment contract provides that she would be given one month notice by SSL in the event of termination of her services by SSL. However, she has been terminated all of a sudden on 31.3.2016 on account of her poor performance. She was paid termination compensation of ₹ 1,25,0000.

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(b) Mr. Deepak Jindal has entered into a contract with High Technologies Ltd. for rendering legal consultancy services for one year on a lumpsum fee of ₹ 1,25,000 per month.

Answer

(a) The compensation for termination of employment will not attract service tax as it is under the terms of employment. Such amount paid by the employer to the employee for premature termination of contract of employment is treatable as amounts paid in relation to services provided by the employee to the employer in the course of employment. Hence, amount so paid would not be chargeable to service tax.

(b) As per section 65B(44) of the Finance Act, 1994, only services provided by an employee to the employer are outside the ambit of services under service tax law; services provided outside the ambit of employment for a consideration would be a taxable service liable to service tax. In the present case, Mr. Deepak Jindal is hired as a legal consultant, and hence Mr. Deepak Jindal is liable to pay service tax.

Further, Mr. Deepak Jindal has to register under service tax law, make quarterly payment of service tax (since he is an individual) and file half yearly returns for the half year ending on 30th September and 31st March.

Exercise

1. *Write a brief note on Constitutional provisions relating to service tax.*
2. *Enlist the sources of service tax law and explain each one of them.*
3. *What do you mean by selective and comprehensive coverage of services for the purpose of service tax? Which system is being adopted in India?*
4. *Write a note on administration of service tax.*
5. *Write a short note on the nature of professional services that can be rendered by a Chartered Accountant in the field of service tax.*
6. *What is the extent and application of the provisions of Finance Act, 1994 relating to service tax?*
7. *Define service and explain the salient features of the definition.*
8. *Explain the significance of charging section 66B of Finance Act, 1994.*
9. *What is negative list of services? Explain any five of the services covered therein.*

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3 Point of Taxation

For the sake of brevity, Point of Taxation and Point of Taxation Rules, 2011 have been referred to as POT and POTR respectively.

Key Points		
Meaning	Point of taxation means the point in time when a service shall be deemed to have been provided. Point of Taxation Rules, 2011 determine the point of taxation. These rules have been outlined as under:	
Determination of point of taxation-General Rule [Rule 3]	**In case**	**Point of taxation would be**
	the invoice is issued within the prescribed period of 30 days* from the date of completion of provision of service	(a) Date of invoice or (b) Date of payment whichever is earlier
	the invoice is not issued within the prescribed period of 30 days* from the date of completion of provision of service	(a) Date of completion of service or (b) Date of payment whichever is earlier
	*45 days in case of banking and other financial institutions including NBFCs.	
	Point of taxation in case of advance received by service provider is the date of receipt of each such advance.	
	POT for payment received, in excess of the invoice amount, upto ₹ 1,000 will be determined on the basis of invoice or completion of service at the option of taxable service provider, as the case may be, rather than payment.	
	Date of completion of provision of service in case of continuous supply of service: In case of continuous supply of service, the date of completion of each event which requires the service receiver to make any payment to service provider, as specified in the contract shall be deemed to be the date of completion of provision of service.	

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Determination of POT in case of change in effective rate of tax [Rule 4]	**In case taxable service is provided BEFORE the change in effective rate of tax**		
	Invoice has been issued	**Payment received for the invoice**	**Point of taxation shall be**
	AFTER the change in effective rate of tax	AFTER the change in effective rate of tax	(a) date of issuance of invoice or (b) date of receipt of payment whichever is earlier
	PRIOR to the change in effective rate of tax	AFTER the change in effective rate of tax	date of issuance of invoice
	AFTER the change in effective rate of tax	PRIOR to the change in effective rate of tax	date of receipt of payment
	In case taxable service is provided AFTER the change in effective rate of tax		
	Invoice has been issued	**Payment received for the invoice**	**Point of taxation shall be**
	PRIOR to the change in effective rate of tax	AFTER the change in effective rate of tax	date of receipt of payment
	PRIOR to the change in effective rate of tax	PRIOR to the change in effective rate of tax	(a) date of issuance of invoice or (b) date of receipt of payment whichever is earlier
	AFTER the change in effective rate of tax	PRIOR to the change in effective rate of tax	date of issuance of invoice

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<table>
<tr>
<td>Determination of POT in case of payment of tax in case of new services [Rule 5]</td>
<td>❖ Where a service is taxed for the first time, then,—
(a) no tax shall be payable to the extent the invoice has been issued and the payment received against such invoice before such service became taxable;
(b) no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within 14 days of the date when the service is taxed for the first time.
❖ Rule 5 is applicable in case of new levy on services also.
❖ New levy or tax shall be payable on all the cases other than the two situations specified above.</td>
</tr>
<tr>
<td rowspan="3">Determination of POT in case where service receiver is liable to pay service tax under reverse charge or in case of associated enterprises
[Rule 7]</td>
<td>In respect of the persons required to pay tax as recipients under the rules made in this regard in respect of services notified under section 68(2) of the Finance Act, 1994, POT is:
(a) date of making payment to service provider
or
(b) first day that occurs immediately after a period of three months from the date of invoice
whichever is earlier.</td>
</tr>
<tr>
<td>In case of “associated enterprises”, where the person providing the service is located outside India, the POT is
(a) date of debit in the books of service receiver
or
(b) the date of making payment,
whichever is earlier.
“Associated Enterprises” have the same meaning as assigned to it in section 92A of the Income-tax Act, 1961.</td>
</tr>
<tr>
<td>When there is a change in the service tax liability or extent of liability of the service recipient, date of issuance of invoice to be the POT if service has been provided and the invoice issued before date of such change, but payment has not been made as on such date</td>
</tr>
</table>

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	In case of services provided by the Government or local authority to any business entity, the POT will be, - (a) any payment, part or full, in respect of such service becomes due; or (b) payment for such services is made. whichever is earlier.
Determination of POT in case of copyrights etc. [Rule 8]	This rule applies in case of royalties and payments pertaining to copyrights, trademarks, designs or patents provided: (a) whole consideration is not ascertainable at the time of performance of service, and (b) subsequently the use or the benefit of these services by a person other than the provider gives rise to any payment of consideration.
	POT is: (a) date of receipt of consideration or (b) date of invoice, whichever is earlier.
Determination of POT in other cases [Rule 8A] Best Judgment	➢ If POT cannot be determined as per these rules for the reason that date of invoice or date of payment or both are not available ➢ Central Excise Officer may require the concerned person to produce such accounts, documents or other evidence as he may deem necessary ➢ and after taking into account such material and the effective rate of tax prevalent at different points of time ➢ shall by a written order determine the POT to the best of his judgment after giving an opportunity of being heard to the concerned person.

Question 1

Determine the point of taxation in the following cases with reference to POTR:-

(i) Mugdha Private Limited is engaged in providing taxable services. It receives advances of ₹ 1,00,000 from clients on 23rd June, 20XX for the service to be rendered in the month of July, 20XX.

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(ii) Rohan Ltd. provided management consultancy services to M/s Bhatia & Sons on 5th June, 20XX and billed it for ₹ 1,20,000 on 10th July, 20XX. It received the payment for the same on 14th July, 20XX.

Answer

(i) As per rule 3 of the POTR, advances received are taxable at the time when such advances are received. Thus, point of taxation is 23rd June, 20XX.

(ii) Rule 3 of the POTR provides that in case invoice has not been issued within 30 days of completion of service, point of taxation is date of completion of service or date of receipt of payment, whichever is earlier. Thus, point of taxation is 5th June, 20XX.

Question 2

Determine the point of taxation in the following cases with reference to POTR:-

(i) Rahu Ltd. received advance of ₹ 1,15,000 from a client on 30.06.20XX, for providing advertising services in the month of July, 20XX. However, due to some unavoidable reasons, said services could not be provided and the advance money (including service tax) was returned to the client on 12.08.20XX.

(ii) Suraksha Security Services Ltd. provided security services to M/s KP & Sons for the month of July, 20XX. It completed providing said services on 31st July, 20XX and billed it for ₹ 1,20,000 on 10th August, 20XX. However, it had received the payment for the same on 4th August, 20XX itself.

Answer

(i) As per rule 3 of the POTR, advances received are taxable at the time of receipt of such advances. Thus, the point of taxation of the advance received by Rahu Ltd. from the client is 30.06.20XX. It is immaterial that services have not been provided subsequently and the money was returned on 12.08.20XX.

Further, the amount of service tax included in the amount refunded $\left(1{,}15{,}000 \times \frac{15}{115} = ₹\,15{,}000\right)$ in August, 20XX would be adjusted against service tax liability of subsequent periods.

(ii) Rule 3 of the POTR provides that in case invoice has been issued within 30 days of completion of service, point of taxation is date of invoice or date of receipt of payment whichever is earlier. In this case, provision of services has been completed on 31.07.20XX and invoice has been issued on 10.08.20XX (within 30 days of completion of service). Thus, point of taxation, in the given case, is date of invoice (10.08.20XX) or date of receipt of payment (04.08.20XX) whichever is earlier, i.e., 4th August, 20XX.

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Question 3

Henna Services Ltd. entered into an agreement on 28th June, 20XX for continuous supply of services for a period of four months to Mirage Hotel for an agreed consideration of ₹ 8,00,000. The provision of service started on 1st July, 20XX. As per the terms of the contract, Mirage Hotel made the payment of ₹ 3,00,000 in advance on 28th June, 20XX and paid the balance amount in two equal installments each on 26th August, 20XX and 1st November, 20XX on completion of 50% and 100% of the service on 15th August, 20XX and 31st October, 20XX respectively. The invoices raised by Henna Services Ltd. were as follows:-

Date of invoice	*₹*
28th June, 20XX	*3,00,000*
20th August, 20XX	*2,50,000*
3rd December, 20XX	*2,50,000*

Determine the point of taxation in each of the above cases.

Answer

Since, in the given case, the service has been provided on a continuous basis under a contract, for a period exceeding three months with the obligation for payment from time to time, it is a continuous supply of service. In case of continuous supply of service where the provision of the whole or part of the service is determined periodically on the completion of an event in terms of a contract, which requires the receiver of service to make any payment to service provider, the date of completion of each such event as specified in the contract shall be deemed to be the date of completion of provision of service.

The point of taxation for a continuous supply of service shall be determined as per rule 3 of the POTR in the following manner:-

Date of completion of the event	Date of invoice	Date of receipt of payment	Point of taxation as per rule 3 of the POTR
28th June, 20XX	28th June, 20XX	28th June, 20XX	28th June, 20XX as advance received is taxable at the time when such advance is received.
15th August, 20XX	20th August, 20XX	26th August, 20XX	20th August, 20XX. Since invoice has been issued within 30 days of completion of service, point of taxation will be date of invoice or payment, whichever is earlier.

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31st October, 20XX	3rd December, 20XX	1st November, 20XX	31st October, 20XX. Since invoice has not been issued within 30 days of completion of service, point of taxation will be date of completion of service or payment, whichever is earlier.

Question 4

Determine the point of taxation in each of following independent cases in accordance with the POTR:

S. No.	*Date of completion of service*	*Date of invoice*	*Date on which payment is received*
1.	*16.07.20XX*	*11.08.20XX*	*26.08.20XX*
2.	*16.07.20XX*	*11.08.20XX*	*01.08.20XX*
3.	*16.07.20XX*	*11.08.20XX*	*01.08.20XX (part) and 26.08.20XX (remaining)*
4.	*16.07.20XX*	*11.08.20XX*	*12.07.20XX (part) and 15.07.20XX (remaining)*

Answer

As per rule 3 of the POTR, in case the invoice is issued within the prescribed period of 30 days from the date of completion of provision of service, point of taxation is:-

(i) date of invoice

or

(ii) date of payment

whichever is earlier.

However, in case the invoice is not issued within 30 days of the completion of the provision of the service, point of taxation is:-

(i) date of completion of service

or

(ii) date of payment

whichever is earlier.

Further, advances received are taxable at the time when such advances are received.

Accordingly, the point of taxation in each of the given cases is as follows:

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S. No.	Date of completion of service	Date of invoice	Date on which payment is received	Point of taxation
1.	16.07.20XX	11.08.20XX	26.08.20XX	11.08.20XX
2.	16.07.20XX	11.08.20XX	01.08.20XX	01.08.20XX
3.	16.07.20XX	11.08.20XX	Part payment on 01.08.20XX and remaining on 26.08.20XX	01.08.20XX for the part payment and 11.08.20XX for the remaining amount
4.	16.07.20XX	11.08.20XX	Part payment on 12.07.20XX and remaining on 15.07.20XX	12.07.20XX for the part payment and 15.07.20XX for the remaining amount

Question 5

Mihir Ltd. of Assam received some taxable services from Freddie Enterprises of U.K. on 05.10.2015 for which an invoice was raised on 08.10.2015. Determine the point of taxation in accordance with POTR if Mihir Ltd. makes the payment for the said services on:-

Case I: 27.12.2015

Case II: 13.01.2016

Answer

In respect of any taxable services provided or agreed to be provided by any person who is located in a non-taxable territory and received by any person located in the taxable territory, person liable to pay service tax is the recipient of such service, i.e. service tax has to be paid under reverse charge mechanism. Hence, in the given case, service tax is to be paid by Mihir Ltd. of Assam.

Further, rule 7 of the POTR *inter alia* provides that the point of taxation in respect of the persons required to pay tax under reverse charge mechanism, shall be the date on which payment is made provided payment for the same is made within a period of 3 months of the date of invoice, otherwise the point of taxation will be the date immediately following the said period of three months.

In the light of the aforesaid provisions, point of taxation will be as follows:-

Case-I: Since the payment has been made within 3 months from the date of invoice, point of taxation shall be the date of payment i.e. 27.12.2015.

Case-II: Since the payment has not been made within a period of 3 months from the date of invoice, point of taxation will be the date immediately following the said period of 3 months i.e. 09.01.2016.

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Question 6

Sambhav Industries Ltd. (SIL) is an Indian Company. It has received taxable services from a UK based company-George Ltd. on 01.06.20XX. George Ltd. raised on SIL an invoice of £ 45,000 on 27.06.20XX. SIL debited its books of accounts on 07.07.20XX and made the payment on 25.08.20XX.

Assuming that George Ltd. and SIL are associated enterprises, determine the point of taxation using aforesaid details.

Answer

In case of "associated enterprises", where the person providing the service is located outside India, the point of taxation shall be:-

(a) the date of debit in the books of account of the person receiving the service

or

(b) date of making the payment

whichever is earlier.

Hence, in the given case, the point of taxation shall be earlier of the following two dates:-

(a) the date of debit in the books of account of SIL i.e. 07.07.20XX

or

(b) date of making the payment i.e. 25.08.20XX

Thus, the point of taxation is 07.07.20XX.

Question 7

Pranav Desai is a well known author of a book on management. Hindustan Publishing House enters into an agreement with him and obtains the copyright of the said book on 20.04.2013 at a consideration fixed @ ₹15/- per book sold by Hindustan Publishing House. The no. of books sold by Hindustan Publishing House during different financial years as well as other relevant details are:

Relevant Year	***No. of books sold***	***Date of issuance of invoice by Pranav Desai***	***Date of receipt of payment from Hindustan Publishing House***
2013-14	*5,00,000*	*29.07. 2014*	*16.08. 2014*
2014-15	*8,00,000*	*03.06. 2015*	*23.05. 2015*
2015-16	*2,00,000*	*16.06. 2016*	*16.06. 2016*

Determine the point of taxation in each of the above financial years.

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Answer

Since in the given case, whole amount of the consideration for the provision of service is not ascertainable at the time when service was performed and subsequently, the use of these services by a person other than the provider gives right to any payment of consideration, both the conditions specified in rule 8 of POTR get satisfied. The point of taxation for various financial years, determined as per rule 8, is as under:

Financial Year	Point of taxation	Reason
2013-14	29.07.2014	Date of issuance of invoice [29.07.2014] falls before date of payment [16.08.2014]
2014-15	23.05.2015	Date of payment [23.05.2015] precedes date of issuance of invoice [03.06.2015]
2015-16	16.06.2016	Date of issuance of invoice [16.06.2016] as well as date of receipt of payment [16.06.2016] is same.

Question 8

Mr. Vineet rendered a taxable service on 05.06.20XX. The date of issue of invoice was 01.07.20XX. He had received the payment for the same on 20.08.20XX. The aggregate value of services provided by Mr. Vineet in the preceding financial year was ₹ 60 lakh.

Determine the point of taxation in the above case.

Will your answer be different if the aggregate value of services provided by Mr. Vineet in the preceding financial year was ₹ 40 lakh?

Answer

As per rule 6 of the Service Tax Rules, 1994, in case of individuals and partnership firms whose aggregate value of taxable services provided from one or more premises is ₹ 50 lakh or less in the previous financial year, the service provider has the option to pay tax on taxable services provided or agreed to be provided by him upto a total of ₹ 50 lakh in the current financial year on receipt basis. Since in the present case, aggregate value of services provided by Mr. Vineet in the preceding financial year was ₹ 60 lakh, he cannot exercise the said option.

Resultantly, he is required to pay service tax in accordance with Point of Taxation Rules, 2011. As per rule 3 of the POTR, if the invoice is issued within 30 days of the completion of the provision of the service, point of taxation is:-

(i) date of invoice (01.07.20XX), or

(ii) date of receipt of payment (20.08.20XX),

whichever is earlier.

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Thus, point of taxation, in the given case, is date of invoice, i.e., 01.07.20XX.

However, if the aggregate value of services provided by Mr. Vineet in the preceding financial year was ₹ 40 lakh, he has the option to pay tax on taxable services provided or agreed to be provided by him upto a total of ₹ 50 lakh in the current financial year on receipt basis. In that case, point of taxation will be 20.08.20XX.

Question 9

Sunidhi Ltd. provided business support services to Bansi on 10th August, 20XX for ₹ 50,000. The invoice for the same was issued on 20th August, 20XX. Sunidhi Ltd. received the payment against the said invoice on 15th August, 20XX vide cheque dated 12th August, 20XX. The entry for the receipt of payment was made in the books of accounts on 15th August, 20XX itself. However, the amount was credited in the bank A/c on 25th August, 20XX.

Determine the point of taxation in the given case.

Answer

In the given case, since the invoice is issued within the prescribed period of 30 days from the date of completion of provision of service, the point of taxation, as per rule 3 of the POTR, shall be the:

(a) date of invoice (i.e. 20.08.20XX)

or

(b) date of receipt of payment (i.e. 15.08.20XX) [Refer note below]

whichever is earlier, i.e. 15.08.20XX.

Note: Date of payment is:-

(1) date on which the payment is entered in the books of account (i.e. 15.08.20XX)

or

(2) date on which the payment is credited to the bank account of the person liable to pay tax (i.e. 25.08.20XX)

whichever is earlier, i.e. 15.08.20XX [Rule 2A of the POTR].

Question 10

With reference to the POTR, explain what will be the point of taxation in case of continuous supply of services?

Answer

In case of continuous supply of service, the date of completion of each event which requires the service receiver to make any payment to service provider, as specified in the contract is deemed to be the date of completion of provision of service.

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The point of taxation will, then, be determined accordingly in terms of provisions of rule 3 of the POTR.

As per rule 3 of the POTR, if the invoice is issued within 30 days of the completion of the provision of the service, point of taxation is:-

(i) date of invoice

or

(ii) date of payment,

whichever is earlier.

However, if the invoice is not issued within 30 days of the completion of the provision of the service, point of taxation is:-

(i) date of completion of service

or

(ii) date of payment,

whichever is earlier.

Question 11

Mr. Atmaram, who was the recipient of services, which are notified under section 68(2) of the Finance Act, 1994 provides the following data. He requests you to explain the (i) point of taxation and (ii) due date of payment of service tax as per the service tax law and procedures.

Dates of invoice	***Dates of payment***
(i) 15-10-2015	*10-11-2015*
(ii) 20-10-2015	*15-02-2016*

Note: Invoice has been issued within 30 days of completion of service in each of the two above cases.

Answer

Point of taxation and due date of payment of service tax

S. No	Date of invoice	Date of payment	Point of taxation	Due date of payment
(i)	15-10-2015	10-11-2015	**10-11-2015** (Note 1)	**06-01-2016** (Note 2)
(ii)	20-10-2015	15-02-2016	**21-01-2016** (Note 1)	**31-03-2016** (Note 2)

Notes:

1. Rule 7 of POTR *inter alia* provides that in respect of services taxed on reverse charge basis, point of taxation is the date of making payment or the first day occurring immediately after 3 months from the date of invoice, whichever is earlier.

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2. All assesses are mandatorily required to pay service tax electronically. In case of an individual assessee, due date for e-payment of service tax for a quarter in which service is deemed to be provided is the 6th day of the month immediately following said quarter. However, in case service is deemed to be provided in the quarter ending in March, the due date is 31st March [Rule 6 of the Service Tax Rules, 1994].

Question 12

With reference to POTR, determine the point of taxation in respect of following independent transactions:

(a) MNO Ltd. paid directors' fee of ₹ 1,00,000 to one of its director for attending a Board Meeting held in the month of December. The meeting was held for approving accounts of the company. Though the journal entry for the transaction was passed on the same day, actual payment was made to the director by the end of April of the next year.

(b) PQR Ltd. paid consultancy fees of ₹ 50,000 to its associated enterprises located in Dubai. Dubai firm raised the invoice on 27.01.20XX and the same was received by PQR Ltd. on 06.02.20XX. Though the journal entry was passed on 07.02.20XX in the books of PQR Ltd., actual payment to Dubai firm was made on 25.02.20XX.

Answer

(a) In case of taxable service provided by a director of a company to said company, service recipient is liable to pay service tax under reverse charge mechanism.

Further, rule 7 of Point of Taxation Rules, 2011 *inter alia* provides that in respect of persons liable to pay service tax under reverse charge mechanism, the point of taxation shall be the date on which payment is made subject to the condition that payment is made within a period of three months of the date of invoice.

However, if payment is not made within a period of 3 months of date of invoice, point of taxation will be first day that occurs immediately after expiry of said 3 months.

Since, in the present case, payment is made in April end, which is beyond 3 months of the date of invoice (invoice is issued in December), the point of taxation would be the first day that occurs immediately after expiry of said 3 months.

(b) Point of taxation in case of import of service by "associated enterprises" where the person providing the service is located outside India is-

(i) date of debit in the books of account of the person receiving the service

OR

(ii) date of making the payment

whichever is earlier

Here, date of debit in PQR Ltd.'s books of accounts is 07.02.20XX and date of payment to Dubai firm is 25.02.20XX. Therefore, point of taxation is 07.02.20XX.

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Question 13

Softec Industries Ltd. (SIL) is an Indian Company. It has received management consultancy services from a UK based company-Mitchell Ltd. on 15.07.20XX. Assuming that Mitchell Ltd. and SIL are associated enterprises, determine the point of taxation using following details:

Particulars	***Date***
Mitchell Ltd. raised on SIL an invoice of £ 58,000	*27.07.20XX*
SIL debited its books of accounts	*05.08.20XX*
Date of payment by SIL	*24.09.20XX*

Answer

In case of "associated enterprises", where the person providing the service is located outside India, the point of taxation shall be:-

(a) the date of debit in the books of account of the person receiving the service

or

(b) date of making the payment

whichever is earlier.

Hence, in the given case, the point of taxation shall be earlier of the following two dates:-

(a) the date of debit in the books of account of SIL i.e., 05.08.20XX

or

(b) date of making the payment i.e., 24.09.20XX

Thus, the point of taxation will be 05.08.20XX.

Exercise

1. *Where a service provider maintains books of accounts on cash basis relating to taxable services provided by him, will service tax be payable on accrual basis?*
2. *Determine the point of taxation in each of the following independent cases:-*

Date of completion of service	*Date of invoice*	*Date of payment*
10.05.20XX	*15.06.20XX*	*12.06.20XX*
12.04.20XX	*15.06.20XX*	*10.04.20XX*
31.05.20XX	*04.06.20XX*	*15.06.20XX*
15.06.20XX	*30.06.20XX*	*20.06.20XX*
20.04.20XX	*21.05.20XX*	*25.05.20XX*
27.04.20XX	*15.06.20XX*	*20.05.20XX*

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3. *Define the term continuous supply of service.*
4. *What will be the point of taxation where services have been received from "associated enterprises" located outside India?*
5. *How is the point of taxation determined in case where a person is liable to pay service tax under reverse charge mechanism and payment for the service rendered has been made within 3 months of the date of invoice?*
6. *Briefly explain how will the point of taxation be determined in case where payment of ₹ 100 has been received in excess of the invoice amount.*
7. *Nikhil Ltd. provides management consultancy services to its client Aggarwal Properties Ltd. for agreed consideration of ₹ 1,50,000. Aggarwal Properties Ltd. makes the payment on 25th April, 20XX. However, the date of completion of service is 15th April, 20XX. The relevant invoice for ₹ 1,50,000 is raised by Nikhil Ltd. as per following table:*

   Case I: 30th April, 20XX

   Case II: 16th May, 20XX

   Case III: 20th April, 20XX

   Determine point of taxation in each of the above three cases.

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4 Valuation of Taxable Service

For the sake of brevity, Service Tax (Determination of Value) Rules, 2006 has been referred to as ST Valuation Rules and Swachh Bharat Cess and Krishi Kalyan Cess have been referred to as SBC and KKC respectively.

<table>
<tr><th colspan="3">KEY POINTS</th></tr>
<tr><th colspan="3">Valuation of taxable services for charging service tax [Section 67]</th></tr>
<tr><td rowspan="6">Broad Scheme</td><td colspan="2">Service is valued on the basis of mode of receipt of consideration-</td></tr>
<tr><td>Consideration</td><td>Value of Taxable Service</td></tr>
<tr><td>Consideration in terms of money</td><td>Gross amount charged by the service provider.</td></tr>
<tr><td>Consideration not wholly or partly in terms of money</td><td>Such amount in money which with the addition of service tax charged is the consideration</td></tr>
<tr><td>Consideration not ascertainable</td><td>Value is determined in the prescribed manner.</td></tr>
<tr><td>Gross amount charged is inclusive of service tax payable</td><td>Such amount as, with the addition of tax payable, is equal to the gross amount charged.</td></tr>
<tr><td>Gross amount charged</td><td colspan="2">Gross amount charged for the taxable service includes any amount received towards the taxable service before, during or after provision of such service.
It includes
• payment by cheque/credit card
• deduction from account and any form of payment by issue of credit notes/debit notes and book adjustment
• amount credited/debited to any account (including suspense account), in the books of account of a person liable to pay service tax, where the transaction of taxable service is with any associated enterprise.</td></tr>
</table>

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<table>
<tr><td>Consideration</td><td colspan="2">Consideration includes
• amount payable for the taxable services provided or to be provided
• reimbursable expenditure/cost incurred by service provider and charged in the course of providing taxable service, except in certain specified circumstances
• amount retained by the lottery distributor/selling agent from gross sale amount of lottery ticket [in addition to the fee or commission]
Or
discount received [face value of lottery ticket - Price at which the distributor/ selling agent gets such ticket].</td></tr>
<tr><td colspan="3">Service Tax (Determination of Value) Rules, 2006</td></tr>
<tr><td rowspan="4">Special provisions for valuation of money changing service [Rule 2B]</td><td>Situation</td><td>Value of Taxable Service</td></tr>
<tr><td>When a currency is exchanged from, or to, Indian Rupees (INR)</td><td>(Buying Rate/Selling Rate - RBI reference rate at that time) x Total units of currency</td></tr>
<tr><td>Where RBI reference rate for a currency is not available</td><td>1% of the gross amount of Indian Rupees provided or received by the money changer.</td></tr>
<tr><td>Where neither of the currencies exchanged is Indian Rupee</td><td>1% of the lesser of the two amounts the money changer would have received by converting any of two currencies into Indian rupees on that day (at the RBI reference rate)</td></tr>
<tr><td>Manner of determination of value when the value is not ascertainable [Rule 3]</td><td colspan="2">When value is not ascertainable, it will either be
• value of similar services in the ordinary course of trade; or
• the service provider will determine the equivalent money value of such consideration which should not be less than cost of provision of such service, when value of similar services cannot be ascertained.</td></tr>
<tr><td>Rejection of value by Central Excise Officer and its determination</td><td colspan="2">• Central Excise Officer (CEO) is empowered to verify the value adopted by the service provider if there are adequate reasons warranting verification of the value adopted by the service provider.</td></tr>
</table>

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thereon [Rule 4]	• If the Central Excise Officer is satisfied that the value determined by the service provider is not in accordance with the provisions of the Act or these rules, he will issue a show cause notice (SCN) to the service provider. • SCN will specify the value of taxable service fixed by the service provider. • After providing a reasonable opportunity of being heard to the service provider, the Central Excise Officer will determine the value of such taxable service.
Inclusion in or exclusion from value of certain expenditure or costs [Rule 5]	**Inclusions: Expenditure or costs incurred** • Expenditure or costs incurred by the service provider in the course of providing taxable service should be included in the value for the purpose of charging service tax irrespective of whether they are separately indicated in the invoice issued by the service provider or not. • Value of the telecommunication service is the gross amount paid by the person to whom telecommunication service is actually provided.
	Exclusions: Amount paid as pure agent Amounts paid to the third party by the service provider as a **"pure agent"** of the client are not to be included in the taxable value, if all the following eight conditions are satisfied: (i) the service provider acts as a pure agent of the recipient of service when he makes payment to third party for the goods or services procured; (ii) the recipient of service receives and uses the goods or services so procured by the service provider in his capacity as pure agent of the recipient of service; (iii) the recipient of service is liable to make payment to the third party; (iv) the recipient of service authorises the service provider to make payment on his behalf; (v) the recipient of service knows that the goods and services for which payment has been made by the service provider shall be provided by the third party;

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	(vi) the payment made by the service provider on behalf of the recipient of service has been separately indicated in the invoice issued by the service provider to the recipient of service; (vii) the service provider recovers from the recipient of service only such amount as has been paid by him to the third party; and (viii) the goods or services procured by the service provider from the third party as a pure agent of the recipient of service are in addition to the services he provides on his own account.
	Pure Agent: Pure agent means a person who- (a) enters into contractual agreement with the recipient of service to act as his pure agent to incur expenditure or costs in the course of providing taxable service; (b) neither intends to hold nor holds any title to the goods or services so procured or provided as pure agent of the recipient of service; (c) does not use such goods or services so procured; and (d) receives only the actual amount incurred to procure such goods or services. incur costs.
Cases in which the commission, costs, etc., will be included or excluded [Rule 6]	**Inclusions:** (i) Commission/ brokerage charged by a broker on the sale or purchase of securities including the commission/ brokerage paid by stock-broker to any sub- broker; (ii) Adjustments made by the telegraph authority from initial deposits made by the subscriber at the time of application for telephone connection/pager/facsimile etc. (iii) Premium charged by the insurer from the policy holder; (iv) Commission received by the air travel agent from the airline; (v) Commission etc. received by an actuary/intermediary/insurance intermediary/insurance agent from the insurer; (vi) Reimbursement received by the authorised service station from manufacturer for carrying out any service of any motor car/ light motor vehicle/two wheeled motor

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	vehicle manufactured by such manufacturer; (vii) Commission etc. received by the rail travel agent from the Railways or the customer; (viii) Remuneration/ commission paid to such agent by the client engaging such agent for the services provided by a clearing and forwarding agent to a client rendering services of clearing and forwarding operations in any manner (ix) Commission etc. paid to such agent by the insurer appointing such agent in relation to insurance auxiliary services provided by an insurance agent; and (x) Demurrage for the provision of a service beyond the period originally contracted or in any other manner relatable to the provision of service.
	Exclusions: (i) Initial deposit made by the subscriber at the time of application for telephone connection/ pager/facsimile etc. (ii) Airfare collected by air travel agent in respect of service provided by him; (iii) Rail fare collected by rail travel agent in respect of service provided by him; (iv) Interest on delayed payment of any consideration for the provision of services or sale of property, whether moveable or immoveable and However, the above clause will not apply to any service provided by Government or a local authority to a business entity where payment for such service is allowed to be deferred on payment of interest or any other consideration. (v) Taxes levied by any Government (including foreign Governments, where a passenger disembarks) on any passenger travelling by air, if shown separately on the ticket, or the invoice for such ticket, issued to the passenger. (vi) Accidental damages due to unforeseen actions not relatable to the provision of service. (vii) Subsidies and grants disbursed by the Government, not directly affecting the value of service.

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Question 1

ABC Architects entered into a contract with BTC Group of Hotels to design the architecture of one of its hotels at an agreed consideration of ₹ 20 lakh. Out of the total consideration, it asked BTC Group of Hotels to pay ₹ 12,50,000 to its material supplier-Khanna Manufacturers. Will the payment of part of consideration by the service receiver to a third party on behalf of the service provider be included in the value of taxable services?

Answer

Service tax chargeable on any taxable service is on the basis of gross amount charged by service provider for such service provided or to be provided by him. It is not necessary that the service receiver should pay the consideration only to the service provider; any money paid to the third party is also includible. Hence, payment made to Khanna Manufacturers would be includible in the value of taxable services.

Question 2

Rohit, an advocate, rendered professional advice to its client XY Ltd. on the matters relating to tax optimization. As a consideration for the said services, XY Ltd. gave a souvenier to Rohit. The said souvenier was an artifact especially designed and made by the craftsmen as per the specifications suggested by XY Ltd.

Rohit contends that he need not pay service tax on the services provided by him as value of thereof could not be ascertained. Is Rohit's contention correct? Critically examine the case.

Assume that Rohit is not entitled to the exemption available to small service providers.

Answer

No, Rohit's contention is not correct. He should value the service in the manner provided by rule 3 of the Service Tax (Determination of Value) Rules, 2006 and pay service tax. Accordingly, he should value the service provided by him on the basis of similar services and if that is not possible, he should value the service on the basis of equivalent money value of consideration and pay service tax on the same.

However, such value should, in no case, be less than the cost of provision of such taxable service.

Question 3

The value of taxable services determined by the person responsible to pay service tax cannot be rejected by the Department. Examine the validity of the statement.

Answer

No, the statement is not valid. As per rule 4 of the Service Tax (Determination of Value) Rules, 2006, the value determined by the person responsible to pay service tax can be rejected by the Central Excise Officer if he is of the opinion that the value determined by such service provider is not in accordance with the provisions of the Finance Act, 1994 or these rules.

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In such a situation, the Central Excise Officer shall issue a show cause notice and the service provider would then be required to show cause why the value of taxable service should not be fixed at the amount specified in such notice.

The Central Excise Officer, after giving such service provider an opportunity of being heard, will determine the value of such taxable service in accordance with the provisions of the Finance Act, 1994 and these rules.

Question 4

Mugdha Private Limited is engaged in providing taxable services. It received following amounts in the month of July, 20XX:

Receipts	***₹***
Advances received from clients for which no service has been rendered so far	*8,00,000*
Demurrage charges recovered for use of the services beyond the agreed period	*50,000*
Security deposits forfeited for damages done by service receiver owing to his negligence in the course of receiving a service	*5,00,000*

Besides the above receipts, one of the clients (ABC Ltd.) made a payment of ₹ 1,50,000 (out of which ₹ 25,000 were paid extra by mistake). However, Mugdha Private Limited refused to return the excess payment received.

Compute the value of taxable service and the service tax payable by Mugdha Private Limited.

Note: Mugdha Private Limited is not eligible for small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.

Answer

Computation of the value of taxable service and the service tax payable

Particulars	**₹**
Advances received from clients for which no service has been rendered so far (Note-1)	8,00,000
Demurrage charges recovered for use of the services beyond the agreed period [Note-2(a)]	50,000
Security deposits forfeited for damages done by service receiver owing to his negligence in the course of receiving a service [Note-2(b)]	5,00,000
Payment received from ABC Ltd. (Note-3)	1,50,000
Total	15,00,000
Value of taxable service [₹ 15,00,000 × $\frac{100}{115}$] (rounded off)	**13,04,348**

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Service tax payable [₹ 15,00,000× $\frac{15}{115}$] (including SBC and KKC) (rounded off)	**1,95,652**

Notes:

1. Advances received in July, 20XX shall be taxable in the month of receipt of advance. [Rule 3 of the Point of Taxation Rules, 2011].
2. As per rule 6 of the Service Tax Valuation (Determination of Value) Rules, 2006,
   (a) Demurrage charges recovered for use of the services beyond the period agreed upon are includible in the value of taxable service.
   (b) Accidental damages are excluded from the value of taxable services provided such damages are due to unforeseen actions and are not related to provision of services. However since in the given case, damages are due to negligence of the service receiver in the course of receiving the service, forfeited security deposits relating to such damages shall be includible in the value of taxable service.
3. Excess payment made as a result of a mistake, if not returned, but retained by the service provider, becomes a part of the taxable value of services. Hence, entire ₹ 1,50,000 would form part of value of taxable services.

Question 5

Compute the service tax liability of Mr. A, an air travel agent, for the quarter ended September 30, 20XX using the following details:-

Particulars	***₹***
Basic air fare collected for domestic booking of tickets	*50,00,000*
Basic air fare collected for international booking of tickets	*80,00,000*
Commission received from the airlines on the sale of domestic and international tickets	*5,00,000*

In the above case, would the service tax liability of Mr. A be reduced if he opts for the special provision for payment of service tax as provided under rule 6 of the Service Tax Rules, 1994 instead of paying service tax at normal rates ?

Note:

1. *Mr. A is not eligible for the small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.*
2. *Service tax and cesses have been charged separately.*

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Answer

As per rule 6 of the Service Tax (Determination of Value) Rules, 2006, only the commission received by the air travel agent from the airlines is included in the value of taxable service. The air fare collected by the air travel agent in respect of the service provided by him does not form part of the value of taxable service. Accordingly, the service tax liability of Mr. A would be computed as under:

Particulars	₹
Basic air fare collected for domestic booking of tickets	Nil
Basic air fare collected for international booking of tickets	Nil
Commission received from the airlines on the sale of domestic and international tickets	5,00,000
Value of taxable service	5,00,000
Service tax @ 14%	70,000
Add: SBC @ 0.5% (₹ 5,00,000 x 0.5%)	2,500
KKC @ 0.5% (₹ 5,00,000 x 0.5%)	2,500
Service tax payable (including SBC & KKC)	**75,000**

However, if Mr. A opts for the special provision for payment of service tax as provided under rule 6 of the Service Tax Rules, 1994, service tax liability would be computed as under:

Particulars	₹
0.7% of the basic air fare collected for domestic booking of tickets	35,000
[₹ 50,00,000 × 0.7%]	
1.4% of the basic air fare collected for international booking of tickets	
[₹ 80,00,000× 1.4%]	1,12,000
Service tax	1,47,000
Add: SBC @ 0.5% (₹ 1,47,000 x $\frac{0.5}{14}$)	5,250
KKC @ 0.5% (₹ 1,47,000 x $\frac{0.5}{14}$)	5,250
Service tax payable (including SBC & KKC)	**1,57,500**

Therefore, as can be seen from the above two computations of service tax, the service tax liability of Mr. A would not be reduced in the aforesaid option.

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Question 6

Royal Security Agency Ltd. entered into a contract on August 1, 20XX for providing security services to BB Jewellers for a jewellery exhibition held between August 15, 20XX and August 26, 20XX.

At the time of signing the contract for providing the said service, it received ₹ 2,00,000 by an account payee cheque. Thereafter, it received ₹ 5,00,000 by credit card and ₹ 4,00,000 by a pay order in the same month.

Determine the value of taxable service and the service tax payable by Royal Security Agency Ltd. for the month of August, 20XX.

Note:

1. *Royal Security Agency Ltd. is not eligible for the small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.*
2. *Service tax and cesses have been charged separately.*

Answer

Computation of taxable service and service tax liability of Royal Security Agency

Particulars	**₹**
Advance received by an account payee cheque (Note 1)	2,00,000
Amount received through credit card (Note 1)	5,00,000
Amount received by a pay order (Note 2)	4,00,000
Value of taxable service	**11,00,000**
Service tax payable @ 14% on ₹ 11,00,000	1,54,000
Add: SBC @ 0.5% (₹ 11,00,000 x 0.5%)	5,500
KKC @ 0.5%(₹ 11,00,000 x 0.5%)	5,500
Service tax payable (including SBC & KKC)	**1,65,000**

Notes:

1. Gross amount charged, *inter*-alia, includes payment by cheque and through credit card.
2. Money, *inter alia,* means pay order.

Question 7

Guru Coaching Classes Ltd. is a coaching centre. During the year ended 31.3.20XX, it has collected a sum of ₹ 10.2 lakh as service tax, out of which ₹ 70,000 was paid by utilizing the CENVAT credit and balance was paid in cash on the respective due dates. The details pertaining to the month of July, 20XX are as under:

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Particulars	*₹*
Free coaching rendered to a batch of 100 students *(Value of similar services is ₹ 20,000)*	
Coaching fees collected from students for the classes to be held in August, 20XX	*14,50,000*
Advance received on 31.07.20XX from ABC College for teaching their students. However, due to some unavoidable reasons, no coaching was conducted and the advance money was returned on 12.08.20XX.	*3,42,000*

Determine the service tax liability for the month of July, 20XX.

Note: Service tax and cesses have not been charged separately.

Answer

Computation of service tax liability of Guru Coaching Classes Ltd. for the month of July, 20XX

Particulars	₹
Free coaching rendered (Note-1)	Nil
Coaching fees collected from students (Note 2)	14,50,000
Advance received from ABC college (Note 2 & 3)	3,42,000
Value of taxable services including service tax	17,92,000
Service tax liability $\left(\frac{17{,}92{,}000 \times 15}{115}\right)$ **(including SBC & KKC) (rounded off)**	**2,33,739**

Notes:

1. Service is an activity carried out *inter alia* for a consideration. Therefore, since no consideration is involved in case of free services, service tax is not payable thereon.
2. Since, services agreed to be provided are also chargeable to service tax, advance received will also be liable to service tax.

   Advanced received is taxable at the time when such advance is received [Rule 3 of the Point of Taxation Rules, 2011].
3. Advance received from ABC College for teaching their students will also be chargeable to service tax. It is immaterial that no coaching was conducted and the money was returned on 12.08.20XX.

   Service tax of ₹ 44,609 (rounded off) [₹ 3,42,000 x $\frac{15}{115}$] included in the amount so refunded would be adjusted against service tax liability of subsequent periods.

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4. Since the service tax collected in preceding financial year is ₹ 10.2 lakh, the aggregate value of taxable services must have exceeded ₹ 10 lakh in said FY. Thus, Guru Coaching Classes Ltd. is not eligible for SSP exemption in the current financial year.

Question 8

Mr. Ram who has entered into a roll over contract approached NDBC Bank for selling US $ 35,000 at the rate of ₹ 60 per US $. RBI reference rate for US $ is ₹ 60.50 per US $ at that time. However, rate of exchange declared by CBEC for the day is ₹ 61.50 per US$. Calculate the value of taxable service.

Answer

Rule 2B of the Service Tax (Determination of Value) Rules, 2006 provides the manner of determination of the value of taxable service so far as it pertains to purchase or sale of foreign currency, including money changing. The value of service for a currency, when exchanged from, or to, Indian Rupees (INR), shall be equal to the difference in the buying rate or the selling rate, as the case may be, and the Reserve Bank of India (RBI) reference rate for that currency at that time, multiplied by the total units of currency.

Hence, the value of taxable service= (RBI reference rate for $ – Selling rate for $) × Total units

= ₹ (60.50 - 60) × 35,000

= ₹ 0.50 × 35,000

The taxable value shall be ₹ 17,500.

Question 9

Siddhi Ltd. exported some goods to Samson Inc. of USA. It received US $ 9,000 as consideration for the same and sold the foreign currency @ ₹ 61 per US dollar. Compute the value of taxable service under rule 2B of the Service Tax (Determination of Value) Rules, 2006 in the following cases:-

(a) RBI reference rate for US dollar at that time is ₹ 62 per US dollar.

(b) RBI reference rate for US dollars is not available.

What would be the value of taxable service if US $ 9,000 are converted into UK £ 4,500. RBI reference rate at that time for US $ is ₹ 63 per US dollar and for UK £ is ₹ 101 per UK Pound.

Answer

(a) For a currency, when exchanged from, or to, Indian Rupees (INR), the value shall be equal to the difference in the buying rate or the selling rate, as the case may be, and the Reserve Bank of India (RBI) reference rate for that currency at that time, multiplied by the total units of currency.

Hence, in the given case, value of taxable service would be as follows:-

(RBI reference rate for $ – Selling rate for $) × Total units of US $

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=₹ (62-61) × 9,000

=₹ 9,000

(b) If the RBI reference rate for a currency is not available, the value shall be 1% of the gross amount of Indian Rupees provided or received, by the person changing the money.

Hence, in the given case, value of taxable service would be as follows:-

1% of ₹ (61 × 9,000)

=₹ 5,490

In case neither of the currencies exchanged is Indian Rupee:

The value shall be equal to 1% of the lesser of the two amounts the person changing the money would have received by converting any of the two currencies into Indian Rupee on that day at the reference rate provided by RBI.

Hence, in the given case, value of taxable service would be 1% of the lower of the following:-

(a) US dollar converted into Indian rupees = $ 9,000 × ₹ 63 = ₹ 5,67,000

(b) UK pound converted into Indian rupees = £ 4,500× ₹ 101 = ₹ 4,54,500

Value of taxable service = 1% of ₹ 4,54,500 = ₹ 4,545

Question 10

Euro Bank Ltd. furnishes the following information relating to services provided by it:

Particulars	***₹***
Interest on overdraft	*5,00,000*
Interest on loans with a collateral security	*6,00,000*
Interest on corporate deposits	*10,00,000*
Administrative charges (over and above interest) on loans, advances and deposits	*6,00,000*
Service charges relating to sale of foreign exchange to general public [Computed in terms of rule 2B of Service Tax (Determination of Value) Rules, 2006]	*15,00,000*
Service charges relating to issuance of Certificates of Deposit (CDs)	*20,00,000*

Compute the value of taxable service and the service tax liability of Euro Bank Ltd. assuming that it is not eligible for small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012. Service tax and cesses have been charged separately, wherever applicable.

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Answer

Computation of value of taxable service and service tax liability of Euro Bank Ltd.

Particulars	₹
Interest on overdraft (Note-1)	Nil
Interest on loans with a collateral security (Note-1)	Nil
Interest on corporate deposits (Note-1)	Nil
Administrative charges (over and above interest) on loans, advances and deposits (Note-2)	6,00,000
Service charges relating to sale of foreign exchange to general public (Note-3)	15,00,000
Service charges relating to issuance of CD (Note-4)	20,00,000
Value of taxable service	**41,00,000**
Service tax @ 14% [₹ 41,00,000×14%]	5,74,000
Add: SBC @ 0.5% [₹ 41,00,000x0.5%]	20,500
KKC @ 0.5% [₹ 41,00,000x0.5%]	20,500
Service tax liability (including SBC & KKC)	**6,15,000**

Notes:

1. Following services provided are included in the negative list so far as the consideration is represented by way of interest and hence are not taxable:-
   - Overdraft facility.
   - Loans with a collateral security.
   - Corporate deposits.
2. Administrative charges or amounts collected over and above the interest or discount amounts would not be part of the negative list and thus would represent taxable consideration.
3. Services by way of sale of foreign exchange between banks or by banks to authorized dealers of foreign exchange is included in the negative list. However, services provided by banks by way of sale of foreign exchange to general public is not so covered and hence taxable.
4. Since CDs are in the nature of promissory notes, transactions in CDs shall be considered as transaction in money. However, a related activity, for which a separate consideration is charged would not be treated as a transaction of money and would be taxable. Hence, service charges relating to issuance of CDs shall be chargeable to service tax.

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Question 11

Rishabh Professionals Ltd., engaged in providing services which became taxable with effect from July 01, 20XX, furnishes you the following information for the month of July, 20XX:

Particulars	*₹*
Advance received for the services to be rendered in October, 20XX	*9,00,000*
Free services rendered to the friends (Value of similar services is ₹ 20,000)	
Services received from its associated enterprise located in UK	*5,00,000*
(Books of accounts were debited on July 14, 20XX, but payment has not yet been made)	
Other services rendered during the month	*8,00,000*
(Invoices raised for the same in July, 20XX)	

Note: The amounts given above are inclusive of service tax and cesses, wherever applicable.

Compute the service tax liability of Rishabh Professionals Ltd. for the month of July, 20XX.

Answer

Computation of service tax liability of Rishabh Professionals Ltd.

Particulars	₹
Service tax payable on taxable services provided:	
Advance received for the services to be rendered in October, 20XX (Note-1)	9,00,000
Value of free services rendered to the friends (Note-2)	Nil
Other services rendered during the month	8,00,000
Total	17,00,000
Less: Exemption available to small service providers (Note-3)	10,00,000
Value of taxable services including service tax and cesses	7,00,000
Service tax payable = ₹$[7,00,000 \times \frac{15}{115}]$ **(A)** (including SBC and KKC)(rounded off)	91,304
Service tax payable under reverse charge on taxable services received:	
Services received from its associated enterprise located in UK (Note-4)	5,00,000
Service tax payable on services received =(₹ 5,00,000×15/115) (including SBC and KKC) **(B)** (rounded off)	65,217
Total Service tax liability (including SBC & KKC) (A) + (B)	**1,56,521**

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Notes:-

1. Advance received in July, 20XX is taxable in the month of receipt of advance [Rule 3 of Point of Taxation Rules, 2011]
2. Service is an activity carried out, *inter alia,* for a consideration. Therefore, since no consideration is involved in case of free services, service tax is not payable thereon.
3. Since, services provided by Rishabh Professional Ltd. became taxable on July 01, 20XX, aggregate value of taxable services rendered in preceding financial year is Nil. Hence, Rishabh Professional Ltd. is eligible for small service provider's exemption.
4. In case where the taxable services are provided by any person which is located in a non taxable territory and received by any person located in the taxable territory, entire service tax is payable by service receiver. Small service providers' exemption is not available in respect of services taxed under reverse charge mechanism.

   Further, in case of "associated enterprises", where the person providing the service is located outside India, point of taxation is date of debit in the books of account of the person receiving the service or date of making the payment whichever is earlier. [Rule 7 of Point of Taxation Rules, 2011]

Question 12

Ms. Kohana has provided you the following details in respect of various services received/availed by her during December, 20XX:-

(i) Deposited ₹ 1,00,000 in her Savings Bank A/c. Interest of ₹ 5,000 was credited in her account on 31.12.20XX.

(ii) Availed services of a mobile network operator and received a monthly bill for ₹ 2,000.

(iii) Visited an Orthopaedician (MBBS, MS) as she had severe backache and paid consultancy fee of ₹ 1,000.

(iv) Availed beauty treatment services from a salon for ₹ 6,000.

Notes:

1. *All the amounts given above, are exclusive of service tax and cesses, wherever applicable.*
2. *All the service providers who have provided services to Ms. Kohana are not eligible for small service provider's exemption, wherever service tax is applicable.*
3. *Wherever applicable, service tax is to be recovered from the service receiver.*

Compute the amount of service tax payable on services availed/received by Ms. Kohana.

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Answer

Computation of service tax payable on services received/availed by Ms. Kohana

Particulars	Value of services received (₹)	Service tax @ 15% (including SBC & KKC) (₹)
Amount deposited in the saving bank account and interest earned (Note-1)	-	-
Services of mobile network operator (Note-2)	2,000	300
Visit to an orthopaedician on complaint of severe backache (Note-3)	-	-
Beauty treatment services (Note-2)	6,000	900
Service tax payable on services availed/received (including SBC & KKC)		**1200**

Notes:

1. Amount of ₹ 1,00,000 deposited in Savings Bank Account is a transaction in money which is specifically excluded from the definition of service under section 65B(44) of the Finance Act, 1994. Further, ₹ 5,000 received by Ms. Kohana as interest on deposits will not be liable to service tax as services by way of extending deposits in so far as the consideration is represented by way of interest are covered in the negative list of services [Section 66D of the Finance Act, 1994].
2. Service tax is leviable on services of a mobile network operator and beauty treatment services received from a beauty salon as such services are neither covered under negative list of services nor under any exemption notification.
3. Health care service provided, *inter alia,* by an authorized medical practitioner is exempt vide mega exemption *Notification No. 25/2012 ST dated 20.06.2012*. Health care service means any service by way of diagnosis or treatment or care for *inter alia* any illness in any recognized system of medicines in India. Allopathy is a recognized system of medicine in India and a MBBS, MS doctor is an authorized medical practitioner. So, visit to an orthopaedician on complaint of severe backache is not taxable.

Question 13

Compute the service tax payable on the services provided in each of the following independent cases:-

Services	*₹*
Sale of space for advertisement in a leading newspaper	*55,000*

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Services related to preparation of advertisement	*65,000*
Sale of space for advertisements on internet websites	*50,000*
Sale of time for advertisement to be broadcast on TV Channel	*1,00,000*
Advertising in business directories	*25,000*
Advertising on film screen in theatres	*90,000*

Note: All the amounts stated above are exclusive of service tax and cesses. Ignore exemption available to small service providers.

Answer

As per section 66D(g) of the Finance Act, 1994, selling of space for advertisements in print media is included in the negative list of services. In other words, advertisement in all media except print media is liable to service tax. Therefore, sale of space for advertisements on internet websites, sale of time for advertisement to be broadcast on TV Channel and advertising on film screen in theatres are liable to service tax.

Further, definition of print media specifically excludes business directories. Therefore, advertising in business directories attracts service tax.

Services related to preparation of advertisement are liable to service tax as they are not included in the negative list.

Computation of service tax payable

Services	**Value of service ₹**	**Service tax @ 15% (including SBC & KKC) (₹)**
Sale of space for advertisement in a leading newspaper	55,000	Nil
Services related to preparation of advertisement	65,000	9,750
Sale of space for advertisements on internet websites	50,000	7,500
Sale of time for advertisement to be broadcast on TV Channel	1,00,000	15,000
Advertising in business directories	25,000	3,750
Advertising on film screen in theatres	90,000	13,500

Question 14

Rahul & Co. is a firm engaged in the business of recruitment and supply of manpower. It furnishes the following details pertaining to the quarter ended 30.09.20XX:

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	Particulars	*₹*
(i)	*Amount collected from clients for recruitment of*	
	Permanent staff	*5,00,000*
	Temporary staff	*3,00,000*
(ii)	*Amounts collected from clients for pre-recruitment screening*	*2,50,000*
(iii)	*Domestic helps arranged for friends & relative (Value of similar services when provided to other customers is ₹ 45,000)*	*-*
(iv)	*Amount collected from a warehouse of agricultural produce for labour provided for loading and unloading*	*1,75,000*
(v)	*Advance received from prospective employers for conducting campus interviews in colleges to be held in November, 20XX*	*2,00,000*
	(Such campus interviews could not be conducted due to student's strike in those colleges. Hence, the advance received was later on returned to the employers.)	

None of the clients of Rahul & Co. was a body corporate during the relevant quarter. Compute the value of taxable services rendered and the total service tax payable for the relevant quarter assuming that Rahul & Co. is not eligible for the small service provider's exemption. All above amounts are inclusive of service tax and cesses, wherever applicable.

Answer

Computation of value of taxable service and service tax payable by Rahul & Co. for the quarter ended 30.09.20XX

Particulars	₹
Amount collected from clients for recruitment of	
Permanent staff	5,00,000
Temporary staff	3,00,000
Amounts collected from clients for pre-recruitment screening	2,50,000
Domestic helps arranged for friends & relative for free [Note-1]	Nil
Amount collected from a warehouse of agricultural produce for labour provided for loading and unloading [Note-2]	1,75,000
Advances received from prospective employers for conducting campus interviews in colleges to be held in November, 20XX [Note-3]	2,00,000
Value of taxable service including service tax and cesses	14,25,000
Value of taxable service (₹ 14,25,000 × 100/115) (rounded off)	**12,39,130**
Service tax (₹ 12,39,130 × 14/100) [rounded off]	1,73,478
Add: SBC @ 0.5% (₹12,39,130 x 0.5%) (rounded off)	6,196
KKC @ 0.5% (₹12,39,130 x 0.5%) (rounded off)	6,196
Service tax liability (including SBC & KKC)	**1,85,870**

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Notes:

1. Free services are not liable to service tax as there is no consideration involved.
2. Since labour supplied to a warehouse for loading and unloading of agricultural produce can neither be considered as supply of farm labour nor loading, unloading of agricultural produce, such service is not covered in the negative list of services and hence, is taxable [Section 66D of the Finance Act, 1994].
3. Since services agreed to be provided are also chargeable to service tax, advance received will also be liable to service tax. Such advance received from prospective employers will be taxable at the time when it is received irrespective of the fact that no campus interviews were subsequently conducted and advances received were returned to employers.
4. Since none of the clients of Rahul & Co. was a body corporate in the relevant quarter, reverse charge provisions will not be applicable.

Question 15

D & Company is engaged in the sale of space/time for advertisements in different medias. It furnishes the following information for the quarter ending 30.09.20XX:

		Amount (₹)
(i)	*Sale of time for advertisement on Zee TV*	*25,00,000*
(ii)	*Sale of space for advertisement in various websites*	*12,00,000*
(iii)	*Sale of space for advertisement in DNA Newspaper*	*5,50,000*
(iv)	*Sale of space for advertisement in various multiplexes*	*32,00,000*

D & Company also assist it's clients in the preparation of advertisement for which it earned ₹ 8,50,000 during the said quarter.

Compute the service tax liability for the quarter ending 30.09.20XX assuming the above mentioned amounts as exclusive of service tax and cesses. D & Co. is not entitled for small service provider's exemption.

Note: Invoices for all aforesaid services were issued within 30 days of completion of service in the quarter July-September, 20XX and the payment was received in the month of October, 20XX.

Answer

Computation of service tax liability of D & Co. for the quarter ending on 30.09.20XX

Particulars	**₹**
Sale of time for advertisement on Zee TV [Note 1]	25,00,000
Sale of space for advertisement in various websites [Note 1]	12,00,000

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Sale of space for advertisement in DNA Newspaper [Note 1]	Nil
Sale of time/space for advertisement in various multiplexes [Note 1]	32,00,000
Services related to preparation of advertisement [Note 2]	8,50,000
Value of taxable service	**77,50,000**
Service tax (₹ 77,50,000 × 14/100) [rounded off]	10,85,000
Add: SBC @ 0.5% (₹77,50,000 x 0.5%) (rounded off)	38,750
KKC @ 0.5% (₹77,50,000 x 0.5%) (rounded off)	38,750
Service tax liability (including SBC & KKC)	**11,62,500**

Notes:

1. It has been stated that invoices have been issued (within 30 days of the completion of service) in the quarter July-September,20XX. Since invoices have been issued in the quarter July-September 20XX, which is earlier than receipt of payment (October, 20XX), point of taxation will fall in the quarter ending on 30.09.20XX [Rule 3 of Point of Taxation Rules, 2011].
2. As per section 66D(g) of the Finance Act, 1994, selling of space for advertisements in only print media is included in the negative list of services. Therefore, sale of space/time for advertisements on TV channels, websites and multiplexes would be liable to service tax.
3. Services related to preparation of advertisement are liable to service tax as they are not included in the negative list [Section 66D(g) of the Finance Act, 1994].

Question 16

Krishna, an interior decorator, designed the interiors of Mr. P's newly set up office in Navi Mumbai. As a consideration for the said services, Mr. P gave a souvenir to Krishna. The said souvenir was an artifact especially designed and made by the craftsmen as per the specifications suggested by Mr. P.

Krishna did not pay service tax on the services provided by him contending that value thereof could not be ascertained. Is Krishna's contention correct? Critically examine the case assuming that Krishna is not entitled to avail small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.

Answer

No, Krishna's contention is not correct as non-payment of service tax is not permissible under service tax law on the plea that value of a taxable service cannot be ascertained.

Rule 3 of Service Tax (Determination of Value) Rules, 2006 provides that where the value of a taxable service is not ascertainable, the same shall be determined by the service provider in the following manner:-

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(a) The value of such taxable service would be equivalent to the gross amount charged by the service provider to provide similar service to any other person subject to fulfillment of the conditions below:

1. Such service is in the ordinary course of trade.
2. The gross amount charged is the sole consideration.

(b) Where the value cannot be determined in accordance with clause (a), the service provider will determine the equivalent money value of such consideration. However, such value should, in no case be less than the cost of provision of such taxable service.

Therefore, Krishna should also value the service provided by him in the manner provided by rule 3 of Service Tax (Determination of Value) Rules, 2006 and pay service tax. Accordingly, he should value the service provided by him on the basis of similar services and if that is not possible, he should value the service on the basis of equivalent money value of consideration and pay service tax on the same.

Question 17

BIE Academy, registered as a company, is engaged in providing online coaching classes to students of Class XI and XII. During the year ended 31.03.20XX, it paid a sum of ₹ 15.6 lakh as service tax, out of which ₹ 7,00,000 was paid by utilizing the CENVAT credit and balance was paid in cash on the respective due dates. The details pertaining to the month of July, 20XX are as under:

Particulars	*₹*
Free online access for coaching provided to a batch of 100 students	
(Value of similar services is ₹ 52,000)	
Advance fees collected from students for online coaching sessions to be held in August, 20XX	*12,00,000*
Advance received on 31.07.20XX from ABC School for conducting online classes specially designed for their students, in November, 20XX. However, due to some internal disagreement, ABC School cancelled the agreement on 12.08.20XX. The advance received was forfeited by BIE Academy.	*5,92,000*

Determine the service tax liability of BIE Academy for the month of July, 20XX.

Note: Wherever applicable, service tax and cesses have not been charged separately.

Answer

Computation of service tax liability of BIE Academy for the month of July, 20XX

Particulars	₹
Free online access for coaching (Note 1)	Nil
Advance fees collected from students for online coaching sessions	12,00,000

(Note 2)	
Advance received from ABC School (Note 2 & 3)	5,92,000
Value of taxable services including service tax	17,92,000
Service tax liability $\left(\frac{17,92,000 \times 15}{115}\right)$ **(including SBC & KKC) (rounded off)**	**2,33,739**

Notes:

1. Service is an activity carried out, *inter alia,* for a consideration. Therefore, since no consideration is involved in case of free services, service tax is not payable thereon.
2. Since, services agreed to be provided are also chargeable to service tax, advance received will be liable to service tax [Section 66B].

   Advanced received is taxable at the time when such advance is received [Rule 3 of the Point of Taxation Rules, 2011].
3. Since service becomes taxable on an agreement to provide a service, deposits forfeited (on cancellation of agreement) would represent consideration for the agreement that was entered into for provision of service. Further, had the advance deposit alongwith service tax been returned to ABC School on cancellation of agreement, credit of such service tax would have been available.
4. Since the service tax paid in preceding financial year is ₹ 15.6 lakh, the aggregate value of taxable services must have exceeded ₹ 10 lakh in said financial year. Thus, BIE Academy is not eligible for small service provider exemption in the current financial year.

Exercise

1. *Answer the following questions:*

   (a) *Can it be said that if the taxable service is not capable of ascertainment, the same cannot form part of value of taxable services?*

   (b) *How is the value of taxable services determined when the consideration against taxable services is received in other than monetary terms?*
2. *How will a taxable service be valued when the consideration thereof is not wholly or partly in terms of money?*
3. *Briefly provide the manner of determination of the value of taxable service relating to purchase or sale of foreign currency, including money changing.*
4. *Explain the meaning of the expression 'pure agent' in the context of service tax.*

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5. *Sambhav Private Limited is engaged in providing the services liable to service tax. Compute the service tax payable by it for the month of September, 20XX from the information furnished below:-*

Particulars	***Amount(₹)***
Services rendered to poor people free of cost (Value of the services computed on comparative basis is ₹ 40,000)	
Advances received in September, 20XX from clients for which no service has been rendered so far	*50,000*
Renting of agro machinery for agricultural purpose	*5,00,000*
Amount received for the services rendered in July, 20XX (Bills for the same were issued on July 29, 20XX)	*60,000*

Note: *Sambhav Private Limited is not eligible for small service providers' exemption in the current financial year.*

6. *How will a taxable service be valued when the gross amount charged for it includes service tax payable?*

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5 Exemptions and Abatements

For the sake of brevity, Swachh Bharat Cess and Krishi Kalyan Cess have been referred to as SBC and KKC respectively.

Question 1

Good Health Medical Centre, a clinical establishment, offers following services:

(i) Reiki healing treatments. Such therapy is not a recognized system of medicine in terms of section 2(h) of Clinical Establishments Act, 2010.

(ii) Plastic surgeries. One such surgery was conducted to repair cleft lip of a new born baby.

(iii) Air ambulance services to transport critically ill patients from distant locations to the Medical Centre.

(iv) Palliative care for terminally ill patients. On request, such care is also provided to patients at their homes. (Palliative care is given to improve the quality of life of patients who have a serious or life-threatening disease but the goal of such care is not to cure the disease).

(v) Alternative medical treatments by way of yoga.

Good Health Medical Centre also operates a cord blood bank which provides services in relation to preservation of stem cells.

Good Health Medical Centre is of the view that since it is a clinical establishment, all the service provided ***by*** *it as well as all the services provided* ***to*** *it are exempt from payment of service tax.*

You are required to examine the situation in the light of relevant statutory provisions.

Answer

Health care services provided by, *inter alia,* a clinical establishment in any recognized system of medicines in India is exempt from service tax vide *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012*. In light of the said provision, eligibility to exemption in respect of each service offered by Good Health Medical Centre is examined below:

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(i) **Not Exempt.** Since reiki healing is not a recognized system of medicine in terms of section 2(h) of Clinical Establishments Act, 2010, it would not be exempt under mega exemption notification and thus, service tax would be payable thereon.

(ii) Health care service **does not include *inter alia* cosmetic or plastic surgery**, except when undertaken to restore or to reconstruct anatomy or functions of body affected due to congenital defects, developmental abnormalities, injury or trauma.

Therefore, plastic surgeries will not be entitled to the said exemption and thus, service tax would be payable thereon. However, plastic surgery conducted to repair a cleft lip will be eligible for exemption under the said notification as it reconstructs anatomy or functions of body affected due to congenital defects (cleft lip).

(iii) **Exempt.** Health care service includes services by way of transportation of the patient to and from a clinical establishment. Thus, air ambulance service to transport critically ill patients to Good Health Medical Centre would be eligible for exemption under the said notification.

(iv) **Exempt.** Health care service means any service by way of diagnosis or treatment **or care** for illness, injury, deformity, abnormality or pregnancy in any recognized system of medicines in India. It is immaterial whether such service is provided at the clinical establishment or at the home of the patient or at any other place.

(v) **Exempt.** Since Yoga is a recognized system of medicine in terms of section 2(h) of Clinical Establishments Act, 2010, the same would be eligible for exemption under the said notification.

Further, services provided by cord blood banks by way of preservation of stem cells or any other service in relation to such preservation are exempt from service tax. Therefore, services provided in relation to preservation of stem cells by the cord blood bank operated by Good Health Medical Centre will be exempt from service tax.

It is important to note that Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* grants exemption to health care services provided **BY** a clinical establishment and not to services provided **TO** a clinical establishment. Only services provided by common bio-medical waste treatment facility operates to clinical establishments by way of treatment or disposal of bio medical waste or the processes incidental thereto are exempt from payment of service tax. Therefore, Good Health Medical Centre's contention that since it is a clinical establishment, all the services provided **to** it are also exempt from service tax is not correct in law.

Question 2

An individual acts as a referee in a football match organized by Sports Authority of India. He has also acted as a referee in another charity football match organized by a local sports club, in lieu of a lump sum payment. Discuss whether he is required to pay any service tax.

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Answer

Services provided to a recognized sports body by an individual *inter alia* as a referee in a sporting event organized by a recognized sports body is exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012.*

Since in the first case, the football match is organized by Sports Authority of India, which is a recognized sports body, services provided by the individual as a referee in such football match will be exempt under the said notification. However, when he acts as a referee in a charity football match organized by a local sports club, he would not be entitled to afore-mentioned exemption as a local sports club is not a recognized sports body and thus, service tax will be payable in this case.

Question 3

RXL Pvt. Ltd. manufactures beauty soap with the brand name 'Forever Young'. RXL Pvt. Ltd. has organized a concert to promote its brand. Ms. Ahana Kapoor, its brand ambassador, who is a leading film actress, has given a classical dance performance in the said concert. The proceeds of the concert will be donated to a charitable organization.

Explain whether Ms. Ahana Kapoor will be required to pay any service tax.

Answer

Services by an artist by way of a performance in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre are exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012*, if the consideration charged for such performance is not more than ₹ 1,50,000. However, such exemption is not available in respect of service provided by such artist as a brand ambassador.

Since Ms. Ahana Kapoor is the brand ambassador of 'Forever Young' soap manufactured by RXL Pvt. Ltd., the services rendered by her by way of a classical dance performance in the concert organized by RXL Pvt. Ltd. to promote its brand will not be eligible for the above-mentioned exemption and thus, be liable to service tax. The fact that the proceeds of the concert will be donated to a charitable organization will not have any bearing on the eligibility or otherwise to the above-mentioned exemption.

Question 4

High Alps Cable Car Co. runs a cable car to transport pilgrims uphill to a mountain top where a holy shrine is situated. Examine whether High Alps Cable Car Co. is required to pay any service tax.

Answer

With effect from 01.04.2016, the exemption available to transportation of passengers, with or without accompanied belongings by, *inter alia,* a ropeway, cable car or aerial tramway vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* has been withdrawn.

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Therefore, service tax is payable in case of transporting of pilgrims by cable car to the holy shrine situated at the mountain top. It may be noted that service tax is payable irrespective of the purpose of transport of the passengers i.e., religious or otherwise.

Question 5

ABC Ltd., a carrying and forwarding agency, started its operations on August 1, 20XX. It utilized the services of Big Carriers, a goods transport agency, in the month of September, 20XX. Big Carriers have communicated to ABC Ltd. that service tax on the services provided by them is required to be paid by ABC Ltd. under reverse charge. However, ABC Ltd. has communicated to Big Carriers that it is eligible for small service provider (SSP) exemption in the current financial year. Consequently, it will not pay service tax under reverse charge also.

You are required to critically examine each stand of the two parties and arrive at the final conclusion.

Answer

Stand taken by Big Carriers: Entire service tax payable on services provided by a goods transport agency is liable to be paid by service receiver if the person who pays freight is, *inter alia,* a body corporate. Thus, the stand taken by Big Carriers is correct in law.

Stands taken by ABC Ltd.: *Notification No. 33/2012 ST dated 20.06.2012* exempts taxable services of aggregate value not exceeding ₹ 10 lakh in any financial year from service tax, if the aggregate value of taxable services rendered by service provider, from one or more premises, does not exceed ₹ 10 lakh in the preceding financial year. This exemption is called as small service provider (SSP) exemption.

Since, ABC Ltd. has started its operations in the current financial year, it will be eligible for SSP exemption in the said financial year as the turnover of services in the previous year would be nil (less than 10 lakh). Thus, stand of ABC Ltd. to the extent that it is eligible for SSP exemption is correct in law.

However, it is to be noted here that such exemption is in respect of services provided and not services received. Further, liability of service provider and service recipient are different and independent of each other. Thus, whereas ABC Ltd. can enjoy the benefit of SSP exemption in respect of services provided by it, it cannot avail the same benefit in respect of services received by it. Hence, ABC Ltd.'s contention that since it enjoys SSP exemption, it is not required to pay service tax under reverse charge also, is not correct. It shall have to pay service tax on goods transport agency's services received by it from Big Carriers under reverse charge.

Question 6

D & Co. has been providing taxable services for past few years. Value of taxable services provided by it during financial year 2013-14 and 2014-15 is ₹ 12 lakh and ₹ 8.75 lakh respectively. During financial year 2015-16, it provided services having value of ₹ 13 lakh. Calculate the service tax liability of D & Co. for financial year 2015-16.

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Answer

Small service providers who provide taxable services of aggregate value not exceeding ₹ 10,00,000 in the preceding financial year are exempt from payment of service tax on taxable services of aggregate value not exceeding ₹ 10,00,000 in the current financial year.

Since in FY 2014-15, value of taxable services provided by D & Co is ₹ 8.75 lakh, it will be eligible for small service provider exemption in FY 2015-16.

Computation of service tax payable by D & Co. for the FY 2015-16

Particulars	**(₹)**
Value of taxable services	13,00,000
Less: Exemption for small services provider	10,00,000
Value of taxable services on which service tax is payable	3,00,000
Service Tax @ 14%	42,000
Add: SBC @ 0.5% (₹ 3,00,000 x 0.5%)	1,500
KKC @ 0.5% (₹ 3,00,000 x 0.5%)	1,500
Service tax payable (including SBC & KKC)	**45,000**

Question 7

Mr. Sinha has travelled by air from Delhi to Mumbai in economy class. The Airlines has charged ₹ 1,470 as service tax from Mr. Sinha. The Airlines does not avail CENVAT credit on inputs and capital goods used for providing the taxable service.

Compute the value of taxable service provided by the airlines.

Answer

Notification No. 26/2012 ST dated 20.06.2012 provides that transport of passengers by air in economy class, with or without accompanied belongings is eligible for 60% abatement of the value of taxable service if CENVAT credit on inputs and capital goods, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004. In other words, service tax is payable on 40% of the value of taxable service in this case, thus making the effective rate of service tax as 6% [40 x 15%].

Since in the given case, the Airlines complies with the requisite condition for availing abatement, effective rate of service tax charged by it would be 6%. Thus, value of taxable service rendered by the Airlines is ₹ 24,500 [₹ 1,470 /6 x 100].

Question 8

Determine the applicability of service tax in each of the following independent cases:

(i) External asset management services received by Reserve Bank of India from overseas financial institutions.

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(ii) Service provided by an Indian tour operator to Mr. B, a Japanese National, for a tour conducted in Europe.

(iii) Services provided to a Higher Secondary School affiliated to CBSE Board by an IT company in relation to development of a software to be used for enhancing the quality of classroom teaching.

Answer

(i) Exempt. Services received by Reserve Bank of India from outside India in relation to management of foreign exchange reserves are exempt from service tax vide *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012*. External asset management services received by Reserve Bank of India from overseas financial institutions is a specialized financial service in the course of management of foreign exchange reserves.

(ii) Exempt. Services provided by an Indian tour operator to a foreign tourist in relation to a tour wholly conducted outside India are exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012.*

(iii) Taxable. Only the following specific services provided **TO** an educational institution are exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012*:

(a) transportation of students, faculty and staff;

(b) catering, including any mid-day meals scheme sponsored by the Government;

(c) security or cleaning or house-keeping services performed in such educational institution;

(d) services relating to admission to, or conduct of examination by, such institution.

Further, an educational institution inter alia means an institution providing services by way of education up to higher secondary or equivalent. However, the services of a development of software provided to an educational institution are not covered under any of the specific services given above. Thus, service tax will be payable in this case.

Question 9

Mr. Kapur has taken a tour for Australia from Great Tours, a tour operator for booking accommodation and air tickets. Great Tours has raised a bill of ₹ 2,50,000 for the said tour. The bill indicates that it is inclusive of service charges of Great Tours for arranging the said tour and amount charged in the bill is the gross amount charged for such a tour.

Mr. Kapur intends to visit New Zealand after vacationing in Australia. However, he wants to explore New Zealand without any fixed itinerary and thus has asked Great Tours to arrange only for his accommodation in New Zealand. Great Tours has raised a bill of ₹ 1,00,000 for

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the said accommodation. The bill indicates that it includes the cost of such accommodation as well as the service charges of Great Tours for arranging the said accommodation.

Great Tours does not avail CENVAT credit on inputs, capital goods and input services used for providing taxable service. Compute the total amount of service tax charged by Great Tours from Mr. Kapur.

Answer

Notification No. 26/2012 ST dated 20.06.2012 provides that services by a tour operator in relation to a tour other than a tour, only for the purpose of arranging or booking accommodation for any person is eligible for 70% abatement of the value of taxable service if-

(i) CENVAT credit on inputs, capital goods and input services (other than the input service of a tour operator), used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004.

(ii) The bill issued for this purpose indicates that it is inclusive of charges for such a tour and the amount charged in the bill is the gross amount charged for such a tour.

In other words, service tax is leviable on 30% of the value of taxable service in this case, thus making the effective rate of service tax as 4.5% [30 x 15%].

Since in the given case, Great Tours provides a tour for both accommodation as well as air tickets and complies with the requisite conditions for availing abatement, effective rate of service tax charged by it would be 4.5%. Thus, service tax charged by Great Tours from Mr. Kapur on tour to Australia is ₹ 11,250 [₹ 2,50,000 x 4.5%].

Further, the above-mentioned notification also provides that if the tour operator is providing services only for the purpose of arranging or booking accommodation for any person in relation to a tour, the eligible abatement is 90% of the value of taxable service if the following conditions are fulfilled:

(i) CENVAT credit on inputs, capital goods and input services (other than the input service of a tour operator), used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004.

(ii) The invoice, bill or challan issued indicates that it is towards the charges for such accommodation.

Furthermore, this abatement is not available if the invoice, bill or challan issued by the tour operator, in relation to a tour, only includes the service charges for arranging or booking accommodation for any person and does not include the cost of such accommodation.

In other words, service tax is leviable on 10% of the value of taxable service in this case, thus making the effective rate of service tax as 1.5% [10 x 15%].

Since in case of New Zealand tour, Great Tours has only booked the accommodation (not provided any other service) and also the requisite conditions for availing the abatement are fulfilled, effective rate of service tax charged by it would be 1.5%. Thus, service tax charged

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by Great Tours from Mr. Kapur for booking accommodation in respect of New Zealand tour is ₹ 1,500 [₹ 1,00,000 x 1.5%].

Therefore, total amount of service tax charged by Great Tours from Mr. Kapur is ₹ 12,750.

Question 10

Well-Being Hospital has received the following amounts in the month of June, 20XX in lieu of various services rendered by it in the same month. You are required to determine its service tax liability for June, 20XX from the details furnished below:-

S. No.	*Particulars*	*₹ (in lakh)*
(i)	*Services provided by cord blood bank unit of the nursing home by way of preservation of stem cells*	*24*
(ii)	*Hair transplant services*	*100*
(iii)	*Naturopathy treatments. Such treatment is a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010*	*80*
(iv)	*Plastic surgery to restore anatomy of a child affected due to an accident.*	*30*
(v)	*Pranic healing treatments. Such treatment is not a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010*	*120*
(vi)	*Mortuary services*	*10*

Well-Being Hospital does not have its own ambulances so it avails ambulance services from Life Savers, an ambulance service provider, to transport critically ill patients from various locations to the Hospital. Examine whether Life Savers would be charging any service tax from Well Being Hospital on the services provided by them.

***Note**: All the amounts given above are exclusive of service tax and cesses. Further, Well-Being Hospital is not eligible for the small service provider's exemption under Notification No. 33/2012-ST dated 20.06.2012. Point of taxation for the services rendered by Well-Being Hospital in the month of June, 20XX fall in the month of June itself.*

Answer

Computation of service tax liability of Well-Being Hospital for the month of June, 20XX

Particulars	**₹ (in lakh)**
Services provided by cord blood bank by way of preservation of stem cells [Note-2]	-

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Hair transplant services [Note-1(a)]	1,00
Naturopathy treatments [Note-1(b)]	-
Plastic surgery to restore anatomy of a child affected due to an accident [Note-1(c)]	-
Pranic healing treatments [Note-1(d)]	1,20
Mortuary services [Note 3]	-
Value of taxable service	2,20
Service tax @ 14% [₹ 2,20,00,000 × 14%]	30.8
Add: SBC @ 0.5% (₹ 2,20,00,000 x 0.5%)	1.1
KKC @ 0.5% (₹ 2,20,00,000 x 0.5%)	1.1
Service tax liability (including SBC & KKC)	**33**

Notes:

(1) Health care services provided by, inter alia, a clinical establishment in any recognized system of medicines in India is exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012*.

(a) Hair transplant services are specifically excluded from the health care services, and thus are not eligible for exemption.

(b) Since naturopathy is a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010, it would be eligible for exemption.

(c) Health care service does not include *inter alia* cosmetic or plastic surgery, except when undertaken to restore or to reconstruct anatomy or functions of body affected due to congenital defects, developmental abnormalities, injury or trauma. Hence, plastic surgery to restore anatomy of a child affected due to an accident will be eligible for exemption.

(d) Since pranic healing treatment is not a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010, it would not be eligible for exemption.

(2) Services provided by cord blood banks by way of preservation of stem cells or any other service in relation to such preservation are also exempt from service tax vide Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012*.

(3) Mortuary services are covered under negative list of services under section 66D of the Finance Act, 1994. Hence, the same are not liable to service tax.

Services by way of transportation of the patient to and from a clinical establishment are specifically included in the definition of health care services. Thus, ambulance services to transport critically ill patients from various locations to Well Being Hospital are eligible for

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exemption. Furthermore, ambulance services provided by an entity which is not a clinical establishment or an authorised medical practitioner or paramedics are also exempt from service tax vide a separate entry in the Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012.* Therefore, ambulance services provided by Life Savers will also be exempt from service tax. Thus, Life Savers will not charge any service tax from Well Being Hospital on the ambulance services rendered by them.

Question 11

Examine the validity of following statements with reference to service tax law:

(i) Consultancy services provided to Government in relation to slum improvement and upgradation is exempt from service tax.

(ii) The transport of goods in a vessel from Mumbai Port to Goa Port attracts service tax at 40% of the gross amount charged.

(iii) Both service providers and service receivers need to satisfy the condition of non-availment of CENVAT credit for claiming abatement in case of GTA service.

Answer

(i) The said statement is not valid. Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012*, provides that services provided, *inter alia*, to Government by way of water supply, public health, sanitation conservancy, solid waste management or slum improvement and up-gradation are exempt but the exemption is not extendable to other services such as consultancy, designing, etc., not directly connected with these specified services.

(ii) The said statement is not valid. Abatement *Notification No. 26/2012 ST dated 20.06.2012* provides an abatement of 70% in respect of transport of goods in a vessel. Thus, transport of goods in a vessel from Mumbai Port to Goa Port would attract service tax at 30% of the value of taxable service provided CENVAT on inputs and capital goods has not been taken.

(iii) The said statement is not valid. Abatement *Notification No. 26/2012 ST dated 20.06.2012* provides that the condition for non-availment of CENVAT credit is required to be satisfied by the service providers only.

Question 12

Discuss whether the following services are chargeable to service tax or not:

(i) Paddy milled into rice on job work basis.

(ii) A hockey player gets fees from Indian Hockey Federation for participating in an international event.

(iii) Sonakshi Sinha, a brand ambassador of Colgate Palmolive Ltd., gets ₹ 15,00,000 for advertising its products.

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Answer

(i) Carrying out an intermediate production process as job work in relation to agriculture is exempt from service tax *vide Mega Exemption Notification No. 25/2012 ST dated 20.06.2012*. Paddy milled into rice, on job work basis is exempt from service tax since such milling of paddy is an intermediate production process in relation to agriculture.

(ii) Services provided to a recognized sports body by, *inter alia,* an individual as a player for participation in a sporting event organized by a recognized sports body are exempt from service tax vide *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012*. If, the international event is organized by a recognized sports body (since Indian Hockey Federation is a national sports federation, it is a recognized sports body), the fee received by the hockey player towards the sports service provided by him will be exempt from service tax.

(iii) Services provided by brand ambassadors do not enjoy any exemption and are liable to service tax vide *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012*. Therefore, service tax will be payable on ₹ 15,00,000 received by Sonakshi Sinha, the brand ambassador for Colgate Palmolive Ltd., for advertising the products of the company.

Question 13

Armaan travelled by air in business class on 15.04.20XX, by Origin Airlines. He booked the ticket on the same day. The airfare charges (value on which service tax was payable) was ₹ 1,00,000. Determine the amount of service tax payable on the service received by Armaan assuming that:

(a) Origin Airlines opted for abatement under Notification No. 26/2012 ST dated 20.06.2012 and did not avail CENVAT credit on inputs and capital goods used for providing such service,

(b) Origin Airlines is not eligible for small service provider's exemption under Notification No. 33/2012 ST dated 20.06.2012.

Answer

Notification No. 26/2012 ST dated 20.06.2012 provides that service of transport of passengers by air, with or without accompanied belongings in other than economy class is eligible for 40% abatement of the value of taxable service on the condition of non-availment of CENVAT credit on inputs and capital goods used for providing the taxable service. Therefore, service tax will be payable on 60% of the value of airfare charges in such higher classes. Hence, in the given case, service tax will be payable on 60% of the value of airfare charges paid by Armaan on 15.04.20XX in the following manner:

Service tax = (₹ 1,00,000 × 60%) × 15%(inclusive of SBC and KKC)

= ₹ 9,000.

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Question 14

Examine the following independent services provided in the month of August, 20XX and determine the amount of service tax payable, if any, in each of these cases:

S. No.	*Particulars*	*(₹)*
1.	*Services by way of waxing of apples to provide it an artificial sheen for increasing its marketability*	*1,00,000*
2.	*Admission to a Railway Museum*	*50,000*
3.	*Transportation of patients to ABC Nursing Home and Bheem Multispecialty Hospital, in an ambulance owned by XYZ Ltd.*	*1,20,000*
4.	*Admission to a Telly Award Function* *[Value per ticket per person is ₹ 510]*	*5,10,000*
5.	*Transportation of milk by a goods transport agency*	*1,50,000*

Note: Ignore small service providers' exemption. Wherever applicable, service tax and cesses have been charged separately.

Answer

Computation of service tax payable

S. No.	Particulars	Value of taxable services (₹)	Service tax liability (including SBC & KKC) (₹)
1.	Services by way of waxing of apples to provide it an artificial sheen for increasing its marketability [Note 1]	Nil	
2.	Admission to a Railway Museum [Note 2]	Nil	
3.	Transportation of patients to ABC Nursing Home and Bheem Multispecialty Hospital, in an ambulance owned by XYZ Ltd. [Note 3]	Nil	
4.	Admission to a Telly Award Function [Note 4]	5,10,000	5,10,000 ×15% = 76,500
5.	Transportation of milk by a goods transport agency [Note 5]	Nil	

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Notes:

As per mega exemption *Notification No. 25/2012 ST dated 20.06.2012:*

1. services by way of waxing of fruits which do not change/alter the essential characteristics of the said fruits are exempt from service tax.
2. services provided by way of admission to a museum are exempt from service tax.
3. ambulance services provided by an entity which is not a clinical establishment or an authorised medical practitioner or paramedics are also exempt from service tax.
4. service by way of admission to award functions is exempt from service tax if the amount charged is upto ₹ 500 per person for right to admission to such event. In case the amount charged per person exceeds ₹ 500, entire consideration would be liable to service tax.
5. services of transportation of milk, salt and food grain including flours, pulses and rice by a goods carriage are exempt from service tax.

Question 15

Kesar Maharaj, a renowned classical dancer gave a classical dance performance in an auditorium. The consideration charged for the said performance is ₹ 98,500. Is Kesar Maharaj liable to pay service tax on the consideration received for the said performance if such performance is not for promotion of any product/services? If yes, determine his service tax liability. Will your answer be different if:

(i) consideration charged by Kesar Maharaj for the said performance is ₹ 1,60,000?

(ii) Kesar Maharaj is a brand ambassador of a food product and aforesaid performance is for the promotion of such food product?

(iii) Kesar Maharaj gives a contemporary Bollywood style dance performance?

Note: Ignore small service providers' exemption. Wherever applicable, service tax and cesses have been charged separately.

Answer

Mega exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts services by an artist by way of a performance in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, if the consideration charged for such performance is not more than ₹ 1,50,000. However, exemption will not apply to service provided by such artist as a brand ambassador.

In view of the aforesaid provisions, services provided by Kesar Maharaj are exempt from service tax as consideration for the classical dance performance has not exceeded ₹ 1,50,000. Therefore, his service tax liability is nil.

(i) If the consideration charged for the said performance by Kesar Maharaj is ₹ 1,60,000, he will be liable to pay service tax on the same as although the performance is by way of

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classical art form of dance, consideration charged for such performance has exceeded ₹ 1,50,000. His service tax liability would, therefore, be ₹ 24,000 (₹ 1,60,000 × 15%).

(ii) If Kesar Maharaj is a brand ambassador of a food product and aforesaid performance is for the promotion of such food product, he will be liable to pay service tax as aforesaid exemption is not applicable to service provided by an artist as a brand ambassador. His service tax liability (including SBC & KKC) would, therefore, be ₹ 14,775 (₹ 98,500 × 15%).

(iii) If Kesar Maharaj gives a contemporary Bollywood style dance performance, such performance will not be eligible for aforesaid exemption. The reason for the same is that although the consideration charged does not exceed ₹ 1,50,000, said performance is not in folk or classical art forms of dance. Hence, service tax would be payable on the same. His service tax liability (including SBC & KKC) would, therefore, be ₹ 14,775 (₹ 98,500 × 15%).

Question 16

With reference to the provisions of Finance Act, 1994, whether service tax is payable in the following independent cases:-

(a) Sarvshiksha, an Educational Trust, runs a play school, 'Tiny Tots' for providing pre-school education.

(b) 'Pinnacle Academy' provides educational services upto higher secondary school.

(c) "Mahajan Classes", a coaching centre provides coaching for IIT JEE entrance examinations to meritorious students of economically weak background.

(d) "Global Point", an institution provides coaching classes for examinations of Certified Public Accountant, USA.

Answer

Mega exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts services provided inter alia by an **educational institution** to its students, faculty and staff. Further, an "Educational Institution" means an institution providing services by way of *inter alia* —

(i) pre-school education and education up to higher secondary school or equivalent;

(ii) education as a part of a curriculum for obtaining a qualification recognised by any law for the time being in force.

(a) Service tax will not be payable on education services rendered by the play school (pre-school), 'Tiny Tots' as "Sarvshiksha" comes under the definition of educational institution and services provided by it are exempt from service tax.

(b) Service tax will not be payable in this case as 'Pinnacle Academy' is covered under the definition of educational institution and services provided by it are exempt from service tax.

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(c) Service tax will be payable by coaching centre providing coaching for IIT JEE entrance examination as coaching given by private coaching institutes/centres is not a part of a curriculum for obtaining recognized qualification, the same is not covered under the definition of educational institution. Also, it is immaterial that coaching is given to economically weak students or for a national level entrance examination.

(d) Service tax will be payable by Global Point as coaching given by private coaching institutes/centres is not a part of a curriculum for obtaining recognized qualification, the same is not covered under the definition of educational institution. Only services provided inter alia by an **educational institution** to its students, faculty and staff are exempt from service tax.

Question 17

Industrial Training Institute (ITI), Manikpuri offers a short term Modular Employable Skill Course in the Information & Communication Technology Sector. The said course is approved by the National Council of Vocational Training (NCVT). ITI, Manikpuri is registered with the Directorate General of Training, Ministry of Skill Development and Entrepreneurship. Revenue raised a demand for service tax on the services provided by ITI Manikpuri.

Examine whether the demand raised by Revenue is correct in law.

Answer

Mega exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts services provided inter alia by an **educational institution** to its students, faculty and staff. Further, an "Educational Institution" means an institution providing services by way of *inter alia* education as a part of an approved vocational education course.

A Modular Employable Skill Course, approved by the National Council of Vocational Training, run by a person registered with the Directorate General of Training, Ministry of Skill Development and Entrepreneurship is, *inter alia,* an approved vocational education course.

Since, ITI Manikpuri falls under the definition of educational institution as the course offered by it is covered under the definition of approved vocational education course, the services provided by ITI Manikpuri will be exempted from service tax.

Therefore, the demand raised by Revenue is not correct in law.

Question 18

With reference to the provisions of service tax law, briefly examine the service tax implications in the following independent cases:-

(a) AB Pvt. Ltd. manufactures alcoholic liquor for human consumption on job-work basis.

(b) Splash and Splutter is a water park. It charges ₹ 500 per person as entry fee.

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Answer

(a) Services by way of carrying out any process amounting to manufacture or production of goods excluding alcoholic liquor for human consumption are covered in the Negative List of services under section 66D of the Finance Act, 1994.

Further, Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* provides exemption for carrying out an intermediate production process as job work in relation to any goods excluding alcoholic liquor for human consumption on which appropriate duty is payable by the principal manufacturer.

Consequently, service tax would be leviable on manufacture of alcoholic liquor for human consumption on job-work basis by AB Pvt. Ltd.

(b) Entry fee to Splash and Splutter water park (being an entry to amusement facility) will be chargeable to service tax as this is neither covered under negative list of services under section 66D of the Finance Act, 1994 nor under Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012.*

Exercise

1. *Briefly explain any five exemptions given vide mega exemption notification.*
2. *What do you understand by small service providers' exemption? Explain the conditions for availing the said exemption.*
3. *Briefly discuss the provisions governing refund of service tax paid by an exporter under reverse charge.*
4. *Write a short note on exemption provided to services received by a developer/unit of SEZ.*
5. *Enlist five abatements granted to taxable services vide Notification No. 26/2012 ST dated 20.06.2012 and explain the conditions which are required to be fulfilled for availing the said abatements.*

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6 Service Tax Procedures

For the sake of brevity, Swachh Bharat Cess and Krishi Kalyan Cess have been referred to as SBC and KKC respectively.

Question 1

Pinnacle Academy, an IIT JEE coaching institution, has its centres in various cities across the country from where coaching is provided to students. Its Head Office is located at New Delhi. Pinnacle Academy wants to apply for service tax registration. In what ways can Pinnacle Academy obtain registration? Explain.

Answer

As per rule 4 of Service Tax Rules, 1994, where a person, liable for paying service tax on a taxable service provides such service from more than one premises or offices and has centralised billing/accounting system in respect of such service, and such centralised billing/accounting systems are located in one or more premises, he may, at his option, register such premises or offices from where centralised billing/accounting systems are located.

However, if such assessee does not have any centralized billing/accounting systems, he shall make separate applications for registration in respect of each of such premises or offices to the jurisdictional Superintendent of Central Excise. The registration for a single premises shall be applied by making an online application at ACES website of CBEC.

Therefore, since Pinnacle Academy provides coaching from different centres spread across the country, it can opt for centralized registration if it has centralized billing/accounting system located at one or more of its centres. However, if it does not have any centralized billing/accounting systems, it shall have to obtain separate registration for each of its centres.

Question 2

X is a consulting engineer. He has obtained service tax registration on April 3, 20XX. X has entered into a contract with Y for provision of consulting services on April 4, 20XX. X provides the services on April 15, 20XX but Y has communicated that he will be able to pay the consideration only after six months owing to his poor financial condition.

X has not issued any invoice or bill for the said service as he is not sure of the requirements of an invoice issued by a registered service tax provider. You are required to guide X with regard to content and time of issuance of an invoice.

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Answer

Rule 4A of Service Tax Rules, 1994 contains the provisions in respect of invoices to be issued by every person providing taxable service.

In terms of that rule, X has to issue an invoice or a bill, or a challan signed by him or a person authorized by him in respect of taxable service provided by him. The invoice, bill or challan should contain the following details and be serially numbered:

(i) Name, address and the registration number of X;

(ii) Name and address of Y (person receiving taxable service);

(iii) Description of taxable service provided or agreed to be provided;

(iv) Value of taxable service provided or agreed to be provided and

(v) Service tax payable thereon.

Such an invoice has to be issued within 30 days from the date of completion of such taxable service or receipt of any payment towards the value of such taxable service, whichever is earlier. Since X will receive the payment for the services only after six months, he should issue the invoice latest by May 15, 20XX i.e., within 30 days from April 15, 20XX (date of completion of such taxable service).

Question 3

MBM Caretakers, a service tax assessee, provides the services of repair and maintenance of electrical appliances. On April 1, 2016, it has entered into an annual maintenance contract with P for its Air Conditioner and Washing Machine. As per the terms of contract, maintenance services will be provided in the first week of each quarter of the financial year 2016-17 and payment for the same will also be charged quarterly after completion of such services in each quarter. Services were provided during the year 2016-17 on April 4, July 2, October 3, and January 3. When should MBM Caretakers issue the invoice for the services rendered?

Answer

Continuous supply of service means *inter alia* any service which is provided, or agreed to be provided continuously or on recurrent basis, under a contract, for a period exceeding three months with the obligation for payment periodically or from time to time.

Therefore, the above situation is a case of continuous supply of service as repair and maintenance services provided by MBM Caretakers have been provided on a quarterly basis, under a contract, for a period of one year with the obligation for quarterly payment.

In terms of rule 4A of Service Tax Rules, 1994, in case of continuous supply of service, every person providing such taxable service has to issue an invoice, bill or challan, as the case may

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be, within 30 days of the date when each event specified in the contract, which requires the service receiver to make any payment to service provider, is completed.

Therefore, since the contract requires P to make payment on completion of services provided in each quarter, MBM Caretakers should issue quarterly invoices latest by May 4, August 1, November 2 and February 2 (within 30 days of April 4, July 2, October 3, and January 3).

Question 4

Mr. A sponsored a dance competition organized by 'Taal Academy', a dance school run by an individual. The dance competition was named as 'Mr. A's Dance Show' by 'Taal Academy'. Who is liable to pay service tax in this case? Will your answer be different if 'Taal Academy' is run by a partnership firm?

Answer

In case of taxable service provided or agreed to be provided by way of sponsorship to any body corporate or partnership firm located in the taxable territory, person liable to pay service tax is the person receiving such service.

However, since in the given case sponsorship service is provided to an individual (Mr. A), the person liable to pay service tax will be service provider i.e., 'Taal Academy'. Further, since the status of service receiver is relevant for determining as to who would pay service tax, status of service provider is immaterial. Therefore, as long as sponsorship service is rendered to an individual, service tax will be payable by service provider i.e., 'Taal Academy' irrespective of whether the same is run by an individual or a partnership firm.

Question 5

Answer the following questions:

(i) Mr. T, an architect, hires a cab from Mr. S, who is engaged in the business of renting of motor cabs. Value of services provided by Mr. S is ₹ 3,000. Mr. S avails CENVAT credit on inputs and capital goods. Who is liable to pay service tax in this case?

Will your answer be different if RST Ltd., a manufacturing company, hires the cab from Mr. S?

Also, compute the amount of service tax payable assuming that Mr. S is not eligible for small service providers' exemption.

Note: Mr. T, Mr. S and RST Ltd. are located in Mumbai and wherever applicable, service tax and cesses have been charged separately.

(ii) PQR Ltd., a manufacturing company, hires a cab from Mr. M, who is engaged in the business of renting of motor cabs. Value of services provided by Mr. M is ₹ 3,000 and service tax payable thereon is ₹ 180. Who is liable to pay service tax in this case?

Note: PQR Ltd and Mr. M are located in New Delhi and wherever applicable, service tax and cesses are charged separately.

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Answer

(i) In case of renting of motor cabs, abatement of 60% from gross amount charged is available if CENVAT credit on inputs, capital goods and input services, other than input service of renting of motorcab, is not availed. Therefore, since in the given case, Mr. S avails CENVAT credit on inputs and capital goods, it cannot pay service tax on abated value.

In case of taxable services provided by way of renting of a motor vehicle designed to carry passengers on **non abated** value to any person who is not engaged in the similar line of business by any individual/HUF/partnership firm (whether registered or not) including association of persons, located in the taxable territory to a business entity registered as body corporate, located in the taxable territory; both service provider and service receiver are liable to pay service tax. 50% of tax is to be paid by service provider and 50% by service receiver.

Since in the given case, service by way of renting of motor cabs is provided by an individual (Mr. S) to another individual (Mr. T) and not to any body corporate, reverse charge provisions will not apply and entire service tax will be payable by service provider (Mr. S). Thus, service tax of ₹ 450 (15% of ₹ 3,000) is liable to be paid by Mr. S.

However, when motor cab is taken on rent by RST Ltd. (a company), reverse charge provisions will apply and 50% of tax will be paid by Mr. S (service provider) and 50% by RST Ltd. (service receiver). Thus, Mr. S will pay ₹ 225 and RST Ltd. will pay ₹ 225.

(ii) In case of renting of motor cabs, abatement of 60% is available from gross amount charged on fulfillment of certain conditions. In other words, effective rate of service tax in case of renting of motor cabs provided on abated value is 6% [15% of 40%]. Since in the given case service tax payable is 6% of the value of taxable service [(₹ 180 / ₹ 3000) x 100 = 6%], service tax is payable on abated value.

In case of taxable services provided by way of renting of a motor vehicle designed to carry passengers on **abated** value to any person who is not engaged in the similar line of business by any individual/HUF/partnership firm (whether registered or not) including association of persons, located in the taxable territory to a business entity registered as body corporate, located in the taxable territory; entire service tax is liable to be paid by service receiver.

Since in the given case, renting of motor cab service is provided to a company (PQR Ltd.), reverse charge provisions will apply and entire service tax will be payable by service receiver (PQR Ltd.). Thus, service tax of ₹ 180 (6% of ₹ 3,000) is liable to be paid by PQR Ltd.

Question 6

A tour operator booked a tour for a client. He billed the client for his services, but did not charge any service tax though he is liable to pay service tax under the relevant provisions. It

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is the contention of the operator that since he has not collected any service tax from the client, he will not deposit the same with the Government. On the basis of said information, answer the following questions:

(i) Do you think the contention of the tour operator is correct in law? Explain.

(ii) In case the tour operator is liable to pay service tax, how will the service tax liability be determined?

Answer

(i) Section 68 of Finance Act, 1994 casts the liability to pay service tax upon the service provider. This liability is not contingent upon the service provider realizing or charging service tax at the prevailing rate. Statutory liability does not get extinguished if service provider fails to realize or charge service tax from service receiver.

Therefore, action taken by tour operator is not correct in law. He will have to deposit service tax even if he has not collected the same from his client.

(ii) The amount received by the tour operator from the service receiver will be taken to be inclusive of service tax. Accordingly, service tax payable by the tour operator shall be ascertained by making back calculations in the following manner:-

$$\text{Service tax payable (including cesses)} = \frac{\text{Amount billed} \times \text{Service tax rate (including cesses)}}{\left(100 + \text{Service tax rate including cesses}\right)}$$

Question 7

'Service tax cannot be paid provisionally'. Examine the correctness of the statement.

Answer

The statement is not correct. If an assessee is, for any reason, unable to correctly estimate, at the time of the deposit, the actual amount payable for any month or quarter, he may make a written request to Assistant/Deputy Commissioner of Central Excise giving reasons for payment of service tax on provisional basis. On receipt of such request, the Assistant/Deputy Commissioner of Central Excise may allow payment of service tax on provisional basis on such value of taxable service as may be specified by the assessee for making payment of service tax on provisional basis. Provisions of Central Excise Rules, 2002 relating to provisional assessment apply in case of provisional payment of service tax also, except the provisions relating to execution of bond.

Question 8

Mr. Saravanan, a service provider, has collected a sum of ₹ 15,000 as service tax from a client mistakenly, even though no service tax was chargeable on the service rendered by him.

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Mr. Saravanan has not refunded such amount to the client. Should the amount so collected be remitted to the credit of the Central Government? Explain.

Answer

Section 73A of the Finance Act, 1994 casts an obligation on every person who has collected any amount, which is not required to be collected, from any other person, in any manner as representing service tax, to forthwith remit the same to the credit of the Central Government.

Hence, Mr. Saravanan has to remit the amount collected mistakenly as service tax to the credit of the Central Government.

Question 9

Mr. Vasudevan has conducted a market survey for Mr. Subramanian. However, Mr. Vasudevan has not charged any fee for such services as Mr. Subramanian happens to be his best friend. Is service tax payable on such free service? Explain.

Answer

Section 67 and Service Tax (Determination of Value) Rules, 2006 make provisions for valuation even when consideration is not ascertainable. However, these provisions apply only when there is consideration. If there is no consideration i.e., in case of free service, section 67 and Service Tax (Determination of Value) Rules, 2006 cannot apply.

Thus, no service tax is payable when value of service is zero. In other words, if the value is zero, the tax will also be zero even though the service may be taxable. However, this principle applies only when there is really a 'free service' and not when its cost is recovered through other means.

Therefore, service tax is not payable on service rendered by Mr. Vasudevan to Mr. Subramanian as Mr. Vasudevan has not charged any fee from Mr. Subramanian.

Question 10

Mr. M is a money changer. He is finding it difficult to charge service tax at the rate specified in section 66B of the Finance Act, 1994 on the value of services provided by him. Can he pay service tax at a different rate? Explain.

Answer

Person liable to pay service tax in relation to purchase or sale of foreign currency, including money changing, has an option to pay an amount at the following rates instead of paying service tax at the rate specified in section 66B of the Finance Act, 1994:-

For an amount	Service tax shall be calculated at the rate of
Upto ₹ 1,00,000	0.14 % of the gross amount of currency exchanged or ₹ 35

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	whichever is higher
Exceeding ₹ 1,00,000 and upto ₹ 10,00,000	₹ 140 + 0.07 % of the (gross amount of currency exchanged - ₹ 1,00,000)
Exceeding ₹ 10,00,000	₹ 770 + 0.014 % of the (gross amount of currency exchanged - ₹ 10,00,000) or ₹ 7,000 whichever is lower

On the service tax so calculated (as given in the above table), Swachh Bharat Cess will be levied by multiplying the service tax so calculated by (0.5/14). Similarly Krishi Kalyan Cess will also be levied by multiplying the service tax so calculated by (0.5/14).

However, the person providing the service shall exercise such option for a financial year and such option shall not be withdrawn during the remaining part of that financial year.

Therefore, Mr. M, being a money changer, has an option to pay service tax at the aforementioned rates.

Question 11

Mr. Rajesh Singla is a service tax assessee. His service tax liability for the quarter April - June was ₹ 35,000. However, on account of a clerical error, he paid ₹ 3,50,000 as service tax for the said quarter. Now Mr. Rajesh Singla wants to adjust the excess payment of ₹ 3,15,000 against his service tax liability for the succeeding quarter. Can he do so? What is the condition to be satisfied for it?

Answer

Where an assessee has paid to the credit of Central Government any amount in excess of the amount required to be paid towards service tax liability for a month/quarter, the assessee may adjust such excess amount paid by him against his service tax liability for the succeeding month/quarter. Such adjustment is subject to the condition that the excess amount paid is on account of reasons not involving interpretation of law, taxability, valuation or applicability of any exemption notification.

Since Mr. Rajesh Singla has paid the excess amount on account of a clerical error, he can adjust the excess payment of ₹ 3,15,000 against his service tax liability for the succeeding quarter.

Question 12

S Ltd. is liable to pay service tax of ₹ 10,000 for the month of September, 20XX. It had discharged its service tax liability for the preceding financial year by paying ₹ 70,000 in cash and utilizing CENVAT credit of ₹ 20,000. Is it required to deposit service tax for the month of September, 20XX electronically?

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Answer

Service Tax Rules, 1994 provide that e-payment of service tax is compulsory for all assesses irrespective of the quantum of service tax paid in the previous financial year. Hence, S Ltd. will be required to deposit service tax for the month of September, 20XX electronically.

Question 13

Mr. U is an air travel agent, who discharges his service tax liability at special rates provided under rule 6(7) of the Service Tax Rules, 1994. Compute his service tax liability for the quarter July – September, 20XX with the help of following particulars furnished by him:

Particulars	*Basic fare as per rule 6(7) of Service Tax Rules, 1994 (₹)*	*Other charges and fee (₹)*	*Taxes (₹)*	*Total value of tickets (₹)*
Domestic Bookings	*1,00,900*	*9,510*	*4,990*	*1,15,400*
International Bookings	*3,16,880*	*20,930*	*15,670*	*3,53,480*

Mr. U wants to pay service tax at the general rate of 15% (including cesses) in respect of bookings done by him during the quarter October-December, 20XX. Can he do so? Explain.

Answer

Computation of service tax liability of Mr. U for the quarter July-September, 20XX

Particulars	**₹**
Basic fare in case of domestic bookings	1,00,900
Service tax @ 0.7% **[A]** Refer Note 1	706.30
Basic fare in case of international bookings	3,16,880
Service tax @ 1.4% **[B]** Refer Note 1	4,436.32
Service tax payable [A] + [B] (rounded off)	5,143
Add: SBC @ 0.5% (₹ 5,143 x 0.5/14) (rounded off)	184
KKC @ 0.5% (₹ 5,143 x 0.5/14) (rounded off)	184
Service tax payable (including SBC & KKC)	**5,511**

Notes:

1. Rule 6(7) of Service Tax Rules, 1994 provides an option to an air travel agent to pay service tax at special rates of 0.7% and 1.4% of 'basic fare' in case of domestic and international bookings for air travel respectively.
2. Since the given basic fare is in terms of rule 6(7) of Service Tax rules, 1994, service tax has been computed as a percentage of such basic fare only and other charges, fee and taxes have been ignored.

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The option once exercised, applies uniformly in respect of all the bookings for air travel made by the air travel agent and cannot be changed during a financial year under any circumstances. Therefore, Mr. U cannot pay service tax @ 15% (including cesses) for the quarter October-December, 20XX and will have to discharge his service tax liability for the said quarter by paying service tax at the special rates mentioned above. However, he can change the option and pay service tax @ 15% (including cesses) from the next financial year.

Question 14

SBM Ltd. provides multiple taxable services. It wants to use a single challan for payment of service tax on various services rendered by it. Please offer your views if SBM Ltd. is permitted to do so under service tax law.

Answer

A multiple service provider (a service provider rendering more than one taxable service) can use single GAR-7 challan for payment of service tax on different services. However, amounts attributable to each such service along with concerned accounting codes should be mentioned clearly in the column provided for this purpose in the GAR-7 challan.

Thus, SBM Ltd. can use a single challan for payment of service tax on various services rendered by it.

Question 15

Determine the interest payable under section 75 of Finance Act, 1994 on delayed payment of service tax from the following particulars:

Service tax payable	*₹ 60,500*
Due date of payment	*06.06.2016*
Date of payment	*06.12.2016*

Note: Turnover of services in the preceding financial year was ₹ 80 lakh. Service tax of ₹ 60,500 has been collected from clients before 06.06.2016.

Answer

Section 75 of Finance Act, 1994 levies simple interest on failure to pay service tax by the prescribed due date for the period by which such crediting of tax or any part thereof is delayed. Section 75 of Finance Act, 1994 read with *Notification No. 13/2016 ST dated 01.03.2016* provides that in case of collection of any amount as service tax but failing to pay the amount so collected to the credit of the Central Government on or before the date on which such payment becomes due, the simple interest @ 24% p.a. is payable. However, in all other cases, 15% simple interest p.a. is payable. Interest payable under section 75 will be computed as under:

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Computation of interest payable under section 75

Particulars	Rate of interest per annum	Interest (₹)
Period of delay [07.06.2016 - 06.12.2016]	24%	₹ 60,500 × 24% x 6/12
Interest payable		**7,260**

Since the turnover of the services in the preceding financial year is more than ₹ 60 lakh, concession of 3% on applicable rate of interest cannot be availed.

Question 16

Compute the interest payable on delayed payment of service tax by service provider where service tax has not been collected from service receivers in following cases:

Name of the service provider	*PQR Ltd.*	*Mr. Manik*
Service tax liability	*₹ 1,23,600*	*₹ 2,16,000*
Delay in payment of service tax	*20 days*	*25 days*

Aggregate value of taxable services rendered in preceding financial year by PQR Ltd. was ₹ 40,00,000 and by Mr. Manik was ₹ 62,00,000.

Answer

Computation of interest on delayed payment of service tax

Name of the service provider	PQR Ltd.	Mr. Manik
Service tax liability	₹ 1,23,600	₹ 2,16,000
Delay in payment of service tax	20 days	25 days
Value of taxable services in previous financial year	₹ 40,00,000	₹ 62,00,000
Rate of interest	12% per annum	15% per annum
Interest (rounded off)	[₹ 1,23,600 x (12/100) x (20/365)] =₹ 813 (rounded off)	[₹ 2,16,000 x (15/100) x (25/365)] =₹ 2,219 (rounded off)

Note: As per section 75 of Finance Act, 1994 read with *Notification No. 13/2016 ST dated 01.03.2016* in case of collection of any amount as service tax but failing to pay the amount so collected to the credit of the Central Government on or before the date on which such payment becomes due, the simple interest @ 24% p.a. is payable. However, in all other cases, 15% simple interest p.a. is payable. Since in the above case, service tax has not been collected, so simple interest @ 15% p.a. is payable. However, the applicable rate gets reduced by 3% for

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service providers whose turnover of services does not exceed ₹ 60 lakh in the preceding financial year.

Question 17

Black and White Consulting Group (BWCG), a management consultancy firm, has to file its first service tax return. The firm wants to know if any other information is also required to be furnished by it at the time of filing its first return. You are required to provide the necessary guidance to the firm.

Answer

BWCG will be required to furnish to the Superintendent of Central Excise, at the time of filing the return for the first time, a list of following documents in duplicate:

(a) all the records prepared or maintained by the assessee for accounting of transactions in regard to

(i) providing of any service;

(ii) receipt or procurement of input services and payment for them;

(iii) receipt, purchase, manufacture, storage, sale or delivery, as the case may be, in regard to inputs and capital goods;

(iv) other activities such as manufacture and sale of goods, if any.

(b) all other financial records maintained by him in the normal course of business.

Question 18

Mr. M is a service provider and is registered under service tax. He wants to know when and at what intervals he should file a service tax return. You are required to provide the necessary advice to Mr. M.

Answer

Service tax return should be filed on half yearly basis by 25th of the month following the particular half-year. The due dates on this basis are:

Half year	Due date
1st April to 30th September	25th October
1st October to 31st March	25th April

If due date of filing the return falls on a public holiday, assessee can file the return on immediately succeeding working day.

Further, every assessee will submit an annual return for the financial year to which the return relates by the 30th day of November of the succeeding financial year.

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Question 19

Mr. Raju is a multiple service provider and files only a single half yearly return for all the services. State with reasons whether he can do so.

Answer

Yes, Mr. Raju can file single half yearly return for all the services even though he is a multiple service provider. He has to furnish the details in each of the columns of the Form ST-3 separately for each of the taxable services rendered by him. Thus, instead of showing a lumpsum figure for all the services together, service-wise details should be provided in the return.

Question 20

A service provider has not been able to file the half yearly service tax return by the prescribed due date. He is worried and does not know what recourse is available to him in this situation. He seeks your help on the issue. What advice will you offer him?

Answer

Service tax law provides for delayed filing of returns. A half-yearly return can be filed after the due date with prescribed late fee. The prescribed late fee is given hereunder:

Period of delay	Late fee
15 days from the date prescribed for submission of the return	₹ 500
Beyond 15 days but not later than 30 days from the date prescribed for submission of the return.	₹ 1,000
Beyond 30 days from the date prescribed for submission of the return	An amount of ₹ 1,000 plus ₹ 100 for every day from the 31st day till the date of furnishing the said return.

However, such late fee cannot exceed ₹ 20,000. Further, if the gross amount of service tax payable is nil, such late fee may be reduced/waived by the Central Excise Officer on being satisfied that there was sufficient cause for the delay.

Question 21

Mr. Z is a service provider rendering multiple services. After having filed the half yearly service tax return, Mr. Z noticed an inadvertent error in the return so filed. Mr. Z has approached you for advice on this issue. Examine the situation with reference to relevant statutory provisions.

Answer

Under service tax law, an assessee can submit a revised half yearly return, in Form ST-3, in triplicate, to correct a mistake or omission. Therefore, Mr. Z can submit a revised half yearly

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return to correct the inadvertent error. The half yearly return can be revised within a period of 90 days from the date of submission of the original return.

Question 22

Mr. Lavi, a taxable service provider, submitted the return for the half year April – September on 5th October. However, he desires to submit a revised return for the said half year on 20th January of next year to correct a mistake. Examine whether he can do so.

Answer

No, Mr. Lavi cannot file the revised service tax return for the half year April – September on 20th January of next year.

Under service tax law, an assessee can submit a revised half yearly return, to correct a mistake or omission, within a period of 90 days from the date of submission of the original return.

Since, Mr. Lavi has submitted the half-yearly return on 5th October, he cannot file the revised return after 3rd January of the next year. The period of 90 days starts from the date of submission of the original return (5th October) and not from the due date of filing the return (25th October).

Question 23

Prasad & Co. wants to file a revised half yearly service tax return. However, the original half yearly return was filed belatedly. You are required to advice Prasad & Co. if it is valid to do so. Your answer must be supported with reasons.

Answer

Yes, Prasad & Co. can file a revised half yearly return. Revised half yearly service tax returns may be filed within 90 days from the date of filing original half yearly return. Thus, even if the original half yearly return is filed belatedly, the same could be revised by filing a revised return.

Question 24

Mr. Abhi, a service provider, wants to furnish consolidated details of lumpsum amounts pertaining to the half year relating to value of taxable service charged, amount realised against the same and service tax payable, in his half-yearly service tax return. Explain whether he can do so.

Answer

A service tax return must indicate *inter alia*, **monthwise:**

(i) the value of taxable services charged/billed;

(ii) the value of taxable service realised;

(iii) the amount of service tax payable/paid etc.

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Therefore, Mr. Abhi cannot furnish consolidated details relating to value of taxable service charged, amount realised against the same and service tax payable in his half-yearly service tax return.

Question 25

Mr. Amarnath, a registered service provider, did not render any taxable services during the half year October - March. Is he required to file any half yearly service tax return?

Answer

Every assessee has to file a half yearly return. Even if no service is provided during a half year, and no service tax is payable; a NIL return has to be filed. Therefore, Mr. Amarnath is required to file a half yearly service tax return even if he did not render any taxable services during the half year October - March.

Question 26

PS Ltd. has paid service tax of ₹ 9 lakh during the preceding financial year. You are required to examine whether it is required to file service tax return electronically for the half year ended September 30, 20XX.

Answer

Service Tax Rules, 1994 provide that every assessee has to submit half-yearly service tax return electronically, irrespective of the amount of service tax paid by him in the preceding financial year. Hence, PS Ltd. has to file service tax return electronically for the half year ended September 30, 20XX.

Question 27

Ashok, a taxable service provider, outsourced a part of work by engaging Suresh, a subcontractor. Service tax is charged and paid by Ashok for the total work. Whether Suresh, the sub contractor, is liable to charge and pay any service tax?

Answer

Yes, Suresh, the sub-contractor is liable to charge and pay service tax.

The fact that services provided by such sub-contractors are used by the main service provider for completion of his work does not in any way alter the fact of provision of taxable service by the sub-contractor.

In essence, Suresh, the sub-contractor has to be treated like any other service provider and service tax liability has to be determined accordingly.

The fact that Ashok, the main contractor has paid the service tax on the total work, will not absolve Suresh from his exigibility or liability to pay service tax. Suresh has to charge and pay service tax in respect of the taxable services rendered by him to Ashok.

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Question 28

Mohan, a service provider, had received ₹ 2,50,000 in advance from Rakesh. Mohan had deposited service tax on such amount in the relevant half year. He finally rendered services valuing to ₹ 2,20,000 only and refunded balance amount to Rakesh. Mohan want to adjust service tax on ₹ 30,000 refunded by him against his current dues of service tax. Advise him.

Answer

Where an assessee has received any payment against a service to be provided which is not so provided by him either wholly or partially for any reason, the assessee may take the credit of such excess service tax paid by him, if the assessee has refunded the payment or part thereof, so received for the service not provided to the person from whom it was received [Rule 6 of the Service Tax Rules, 1994].

Since, in the given case, service provider Mohan has refunded the payment relatable to the value of services not provided (₹ 30,000) to service receiver Rakesh, he can take the credit of excess service tax paid by him on the said amount and adjust the same against his current service tax dues.

Question 29

Compute service tax liability of Mr. Dominic, a selling agent of lottery for the month of July, 20XX, using the following details.

(i)	*Lucky Star - a Jackpot organized for Kerala Government where guaranteed prize payout is*	*> 80%*
	Aggregate face value of lottery tickets sold	*₹ 37,00,000*
(ii)	*Magic Winner - another Jackpot organized for Kerala Government where guaranteed prize payout is*	*< 80%*
	Aggregate face value of lottery tickets sold	*₹ 55,00,000*
(iii)	*Commission received from the sale of above tickets, was 10% of aggregate face value of lottery tickets sold.*	

Will there be any difference in the service tax liability of Mr. Dominic if he opts for special provision for payment of service tax as provided under rule 6 of Service Tax Rules, 1994 instead of paying service tax at 15% (including cesses)?

Note: Mr. Dominic is not eligible for SSP exemption and the lottery tickets sold by him are the lottery tickets printed by the Kerala Government.

Answer

Computation of service tax liability of Mr. Dominic for the month of July, 20XX:

Particulars	₹
Commission received from sale of lottery tickets	9,20,000

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[10% of ₹ 92,00,000 (₹ 37,00,000 + ₹ 55,00,000)] Value of taxable service = ₹ $\left(9{,}20{,}000 \times \frac{100}{115}\right)$ (rounded off)	8,00,000
Service tax (₹ 8,00,000 x 14%)	1,12,000
Add: SBC @ 0.5% (₹ 8,00,000 x 0.5%)	4,000
KKC @ 0.5% (₹ 8,00,000 x 0.5%)	4,000
Service tax payable (including SBC & KKC)	**1,20,000**

If Mr. Dominic opts for the special provision for payment of service tax as provided under rule 6 of the Service Tax Rules, 1994, service tax liability would as under:

Particulars	₹
Amount payable as service tax where the guaranteed lottery prize payout is > 80% [Note 1]	32,800
Amount payable as service tax where the guaranteed lottery prize payout is < 80% [Note 2]	76,800
Service tax	1,09,600
Add: SBC @ 0.5% (₹ 1,09,600 x 0.5/14) (rounded off)	3,914
KKC @ 0.5% (₹ 1,09,600 x 0.5/14) (rounded off)	3,914
Service tax payable (including SBC & KKC)	1,17,428

Notes:

1. Where the guaranteed lottery prize payout is > 80%, ₹ 8,200 /- on every ₹ 10 Lakh (or part of ₹ 10 Lakh) of aggregate face value of lottery tickets can be paid instead of paying service tax @ 15% (including cesses) viz. ₹ 32,800 [4 × ₹ 8,200].
2. Where the guaranteed lottery prize payout is < 80%, ₹ 12,800/- on every ₹ 10 Lakh (or part of ₹ 10 Lakh) of aggregate face value of lottery tickets can be paid instead of paying service tax @ 15% (including cesses) viz. ₹ 76,800 [6 × ₹ 12,800].

If Mr. Dominic opts for payment of service tax in accordance with special provisions provided under rule 6 of Service Tax Rules, 1994, his service tax liability would be reduced by ₹ 2,572.

Question 30

Mr. X, a Delhi resident, submits a cab request to Speed Cabs for travelling from Delhi to Gurgaon. Speed Cabs is a mobile application owned and managed by Speed Technologies Ltd. located in India. The application facilitates a potential customer to connect with persons providing cab service under the brand name of Speed Cabs. After Mr. X pays the cab charges using his debit card, he gets details of the driver, Mr. Y and the cab's registration number.

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With reference to the Service Tax Rules, 1994, discuss who is liable to pay service tax in this case. Will your answer be different, if Speed Technologies Ltd. is located in New York and does not have a representative in India?

Answer

Aggregator means a person, who owns and manages a web based software application, and by means of the application and a communication device, enables a potential customer to connect with persons providing service of a particular kind under the brand name or trade name of the aggregator. In relation to service provided by a person involving an aggregator in any manner, the aggregator of the service is the person liable for paying service tax.

Since in the given case, Speed Technologies Ltd. fulfills all the conditions of being an aggregator, it will be liable to pay service tax under reverse charge.

However, where the aggregator neither has a physical presence nor does it have a representative for any purpose in the taxable territory, it will have to appoint a person in the taxable territory for the purpose of paying service tax and such person will be the person liable for paying service tax. Therefore, Speed Technologies Ltd. will have to appoint a person in India for the purpose of paying service tax if Speed Technologies Ltd. is located in New York and does not have a representative in India.

Question 31

Mr. Paritosh is an air travel agent. He is finding it difficult to charge service tax at the rate specified in section 66B of the Finance Act, 1994 on the value of services provided by him. Can Mr. Paritosh pay service tax at any alternative rate? Explain.

Whether such option of payment of service tax at alternative rates is available in respect of any other service? If yes, mention such service(s).

Answer

Person liable for paying the service tax in relation to the services of booking of tickets for travel by air provided by an air travel agent, has an option to pay following amounts instead of paying service tax at the rate specified in section 66B of the Finance Act, 1994:-

In the case of	Option to pay an amount calculated at the rate of
Domestic bookings of passage for travel by air	0.7% of the basic fare
International bookings of passage for travel by air	1.4% of the basic fare

Here, basic fare means that part of the air fare on which commission is normally paid to the air travel agent by the airline.

Therefore, Mr. Paritosh can pay service tax at the above-mentioned alternative rates instead of paying service tax at the rate specified in section 66B of the Finance Act, 1994. On the service tax so calculated (as given in the above table), Swachh Bharat Cess will be levied by

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multiplying the service tax so calculated by (0.5/14). Similarly Krishi Kalyan Cess will also be levied by multiplying the service tax so calculated by (0.5/14).

However, he should keep in mind that if he exercises such an option, the same will apply uniformly in respect of all the bookings of passage for travel by air made by him and cannot be changed during a financial year under any circumstances.

Yes, the option of payment of service tax at alternative rates is available in respect of three other services namely, life insurance service, purchase or sale of foreign currency including money changing and promotion, marketing or organising/assisting in organising lottery.

Question 32

Fitness Ltd. is engaged in providing taxable services for the half year ended on 30th September, 2016. The company filed its half yearly service tax return on:

Case I: 9th November, 2016

Case II: 23rd November, 2016

Case III: 25th January, 2017

Determine the amount of late fee payable, if any, by Fitness Ltd. in each of the above independent cases.

Answer

Computation of the amount of late fee payable by Fitness Ltd.

Case	Particulars	Late fee as per rule 7C of Service Tax Rules, 1994
Due date for filing half yearly return – 25.10.2016		
I.	If period of delay is 15 days from the date prescribed for submission of the return	₹ 500
	In the present case, return has been filed with a delay of 15 (6+9) days from the date prescribed for submission of the return	₹500
II.	If period of delay is beyond 15 days but not later than 30 days from the date prescribed for submission of the return.	₹ 1,000
	In the present case, return has been filed with a delay of 29 (i.e. 6+23) days from the date prescribed for submission of the return	₹ 1,000
III.	Beyond 30 days from the date prescribed for submission of the return	An amount of ₹ 1,000 plus ₹ 100 for every day from the 31st day till the date of furnishing the said return However, total late fee for delayed submission of return shall not exceed

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		₹ 20,000.
	In the present case, return has been filed with a delay of 92 (i.e. 6+30+31+25) days from the date prescribed for submission of the return	Lower of the following two amounts: (i) ₹ 1,000+ ₹ 6,200 (₹ 100 × 62 days) = ₹ 7,200 (ii) ₹ 20,000 Thus, late fee leviable is ₹ 7,200

Exercise

1. *Explain the basic provisions relating to service tax registration.*
2. *Write a brief note on centralised registration.*
3. *Enlist the contents of an invoice issued under service tax provisions. Also, mention the exceptions to the general rule, if any.*
4. *Explain what is reverse charge mechanism under service tax.*
5. *Explain whether a service provider is allowed to pay service tax on a provisional basis.*
6. *Whether life insurer carrying on life insurance business has option to calculate service tax at different rate?*
7. *How can an assessee adjust the excess payment of service tax against his liability of service tax for subsequent periods? What is the basic condition for the same?*
8. *Explain optional composition scheme under service tax for distributor or selling agents of lotteries.*
9. *Write a short note on Service Tax Code Number and the objective sought to be achieved by the same.*
10. *What is EASIEST scheme and state the benefits in the context of service tax?*
11. *State the service tax provisions regarding adjustment of service tax paid when service was not provided either wholly or partly.*
12. *Briefly explain the important points to be kept in mind while paying service tax.*
13. *Briefly explain the provisions relating to advance payment of service tax.*
14. *Explain the treatment for excess amount of service tax collected from the recipient under service tax.*
15. *What are the consequences of non-payment or delayed payment of service tax?*
16. *When should the return be filed, if the due date happens to be a public holiday?*
17. *'X', an individual, has not provided any services in the half year April to September. Should he file any return for this period? Give your opinion.*

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7 CENVAT Credit

For the sake of brevity, CENVAT Credit Rules, 2004, Swachh Bharat Cess and Krishi Kalyan Cess have been referred to as CCR 2004, SBC and KKC respectively in this Chapter.

Question 1

Examine the validity of the following statements:-

(i) The provisions of the CCR, 2004 in relation to availment and utilization of credit of service tax apply to whole of India including Jammu and Kashmir.

(ii) Dumpers used in the factory of a manufacturer for carrying bulk raw material, are eligible capital goods for the purposes of claiming the CENVAT credit.

Answer

(i) The statement is not valid. The provisions of the CCR, 2004 in relation to availment and utilization of credit of service tax apply to whole of India except Jammu and Kashmir. The said provisions do not apply to Jammu and Kashmir as service tax law is not applicable to the State of Jammu & Kashmir.

(ii) The statement is valid. As per the definition of the capital goods, dumpers used in the factory of the manufacturer of the final product are eligible as capital goods for the purposes of claiming the CENVAT credit.

Question 2

Briefly discuss, whether the following purchases are eligible for CENVAT credit as capital goods under rule 2(a) of the CCR, 2004:-

(i) Cool Cab Services Ltd., engaged in providing the passenger transportation service, purchased 10 cabs (not registered in the name of Cool Cab Services Ltd.) for the purpose of providing said service.

(ii) Samar Manufacturers, engaged in the manufacture of excisable goods, purchased two special purpose motor vehicles, falling under tariff heading 8705, for use in its factory.

(iii) Safe Cabs Limited, engaged in providing passenger carriage service, purchased 3 new cars (in the name of its associate and registered as such) for their business.

Answer

(i) The cabs purchased by Cool Cab Services Ltd. are not eligible as capital goods as such cabs are not registered in the name of the service provider i.e. Cool Cab Services Ltd.

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(ii) The special purpose motor vehicles, falling under tariff heading 8705, are eligible as capital goods. As per the definition of capital goods, motor vehicles other than those falling under tariff headings 8702, 8703, 8704 and 8711 used in the factory of the manufacturer of the final products are eligible capital goods.

(iii) Motor vehicle designed to carry passengers is eligible capital goods when used for providing output service of transportation of passengers provided such motor vehicle is registered in the name of service provider. Since in the given case, cars purchased by Safe Cabs Limited are not registered in the name of service provider viz., Safe Cabs Limited, such cars are not eligible as capital goods.

Question 3

ABC Co. Ltd. is engaged in the manufacture of excisable goods. It procured the following items during the month of July, 20XX. Determine the amount of CENVAT credit available by giving necessary explanations for treatment of various items.

Items	***Excise duty paid (₹)***
Electrical transformers falling under Chapter 85 of the Excise Tariff	*52,000*
Moulds and dies	*1,00,000*
Pollution control equipment	*30,000*
Trucks used for the transport of raw material falling under tariff heading 8704	*10,000*
Office equipment used in an office within the factory	*20,000*
Capital goods used outside the factory for generation of electricity for captive use within the factory	*10,000*
Refractories	*5,000*

Answer

Computation of CENVAT credit available to ABC Co. Ltd.

Particulars	**₹**
Electrical transformers falling under Chapter 85 of Excise Tariff (Note-1)	52,000
Moulds and dies (Note-1)	1,00,000
Pollution control equipment (Note-1)	30,000
Trucks used for the transport of raw material falling under tariff heading 8704 (Note-2)	Nil
Office equipment used in an office within the factory (Note-3)	20,000
Capital goods used outside the factory for generation of electricity for captive use within the factory (Note-1)	10,000

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Refractories (Note-1)	5,000
Total excise duty paid on the eligible capital goods	2,17,000
CENVAT credit available = 50% of excise duty paid on capital goods (Note-4)	**1,08,500**

Notes:

1. As per the definition of capital goods following goods are, *inter alia,* eligible capital goods for the purposes of claiming CENVAT credit:-
   (a) all goods falling under Chapter 85,
   (b) moulds and dies,
   (c) pollution control equipment,
   (d) refractories
   (e) capital goods used outside the factory of the manufacturer of the final products for generation of electricity for captive use within the factory.
2. Motor vehicles used in the factory of the manufacturer are eligible as capital goods provided they do not fall under tariff headings 8702, 8703, 8704 and 8711. Therefore, the trucks used for the transport of raw material falling under tariff heading 8704 are not eligible capital goods.
3. CENVAT credit is allowed on equipment or appliance which are used in an office located within the factory and not outside the factory.
4. CENVAT credit of only upto 50% of the excise duty paid is available in respect of the eligible capital goods in the year of purchase.

Question 4

Briefly examine whether the following goods can be termed as exempted goods in accordance with rule 2(d) of the CCR, 2004:-

(a) Goods in respect of which the benefit of exemption under Notification No. 1/2011 CE dated 01.03.2011 is availed and excise duty @ 2% is paid.

(b) Goods which are not liable to excise duty as they are not mentioned in the Central Excise Tariff.

Answer

(a) As per the definition of exempted goods, such goods, *inter alia,* include the goods in respect of which the benefit of exemption under *Notification No. 1/2011-CE dated 01.03.2011* is availed. Thus, even though a duty @ 2% is paid on such goods, such goods are exempted goods.

(b) As per the definition of exempted goods under rule 2(d), only excisable goods can be termed as exempted goods. Since the goods which are not mentioned in the Central

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Excise Tariff are not excisable, such goods are not exempted goods. However, Explanation 1 to rule 6(1) clarifies that for the purposes of rule 6, exempted goods or final products as defined in clauses (d) and (h) of rule 2 will include non-excisable goods cleared for a consideration from the factory. In other words, now inputs and input services used in the manufacture of non-excisable goods will also attract the reversal provisions under rule 6. However, it is to be noted that the said explanation is applicable only for the purposes of rule 6.

Question 5

Briefly examine whether the following services can be termed as exempted services in accordance with rule 2(e) of the CCR, 2004:-

(a) *Services provided to United Nations.*

(b) *Services of transport of passengers by air in economy class in respect of which an abatement of 60% of the gross amount has been availed after complying with all the necessary conditions for availing abatement.*

(c) *Services of transport of passengers by a radio taxi in respect of which an abatement of 60% of the gross amount has been availed after complying with all the necessary conditions for availing abatement.*

Answer

(a) The taxable services which are exempt from whole of the service tax leviable thereon are exempted services. Accordingly, since services provided to United Nations are exempt from service tax *vide* Mega Exemption *Notification No. 25/2012-ST dated 20.06.2012,* such services are exempted services.

(b) Exempted services, *inter alia*, means a taxable service whose part of value is exempted on the condition that no credit of **inputs AND input services**, used for providing such taxable service, shall be taken. The condition for availing abatement in respect of services of transport of passengers by air in economy class is that CENVAT credit on **inputs and capital goods** has not been taken. However, there is no restriction on taking credit of the input services used for providing such services. Consequently, such services are not exempted services.

(c) Exempted services, *inter alia*, means a taxable service whose part of value is exempted on the condition that no credit of **inputs AND input services**, used for providing such taxable service, shall be taken. The condition for availing abatement in respect of services of transport of passengers by a radio taxi is that CENVAT credit on **inputs, capital goods and input services** has not been taken. Consequently, such services are exempted services.

Question 6

PQR Ltd., an iron rods manufacturer, used abrasives for the purpose of polishing such iron rods. The abrasives were consumed during the manufacturing process and were not present

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in the manufactured final product. You are required to advice PQR Ltd. whether it can avail CENVAT credit of excise duty paid on such consumables.

Answer

As per the definition of inputs, all goods used in the factory by the manufacturer of the final product and which have some relationship with the manufacture of a final product, are eligible inputs. There is no requirement that the inputs should be present in the final product. Hence, PQR Ltd. can avail CENVAT credit of excise duty paid on abrasives.

Question 7

P & T Manufacturers has a canteen for the workers in its factory, as per requirement of the Factories Act, 1948. It purchases a cooking gas range for use in the canteen. Supplier of cooking gas range has charged excise duty of ₹ 5,000. Can P & T Manufacturers avail the CENVAT credit of the excise duty paid on cooking gas range?

Answer

As per the definition of the inputs, the cooking gas range in the canteen - which has no relation with manufacture of the final product - cannot be termed as inputs. Further, any goods which are used primarily for personal use or consumption of any employee are not eligible as inputs for the purposes of CENVAT credit. Hence, P & T Manufacturers cannot avail CENVAT credit of the excise duty paid on the cooking gas range used in the canteen.

Question 8

Mahavir Motors Ltd. (MML) was engaged in the manufacture of cars. It provided seat covers, music system, hand tool kit, safety alarm and floor mats as accessories to the cars and included the value of such accessories in the value of the car. MML availed the CENVAT credit of the central excise duty paid on such accessories. Department disallowed the CENVAT credit on the accessories (as claimed by MML) on the ground that such accessories cannot be termed as inputs to the car.

Examine whether the action of the Department is justified in law.

Answer

No, the action of the Department is not justified in law. As per the definition of inputs, accessories cleared along with the final product are eligible inputs provided the value of such accessories is included in the value of the final products. Since in the given case, the value of the accessories is included in the value of the car, MML is entitled to claim the CENVAT credit of the excise duty paid on such accessories.

Question 9

Determine the amount of CENVAT credit available with Arihant Manufacturing Ltd. in respect of the following items procured by them in the month of September, 20XX:

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S.No.	***Item***	***Excise duty paid (₹)***
(i)	*Raw materials used in the factory of Arihant Manufacturing Ltd.*	*72,000*
(ii)	*Goods used in the guest house primarily for the temporary stay of the newly recruited employee.*	*40,000*
(iii)	*Inputs used for making structures for support of capital goods*	*1,25,000*
(iv)	*Capital goods used as parts and components in the manufacture of final product*	*40,000*

Answer

Computation of CENVAT credit available with Arihant Manufacturing Ltd.

Particulars	**₹**
Raw materials used in the factory of Arihant Manufacturing Ltd.	72,000
Goods used in the guest house primarily for the temporary stay of the newly recruited employees. [Note 1]	Nil
Inputs used for making structures for support of capital goods [Note 1]	Nil
Capital goods used as parts and components in the manufacture of final product [Note 2]	40,000
Total CENVAT credit available	**1,12,000**

Notes:

1. As per the definition of inputs, there is specific exclusion with regard to the following:-
   (i) goods used in a guest house when the same are used primarily for personal use or consumption of any employee.
   (ii) goods used for making of structures for support of capital goods.

   Thus, CENVAT credit cannot be claimed in respect of the above goods.
2. Though definition of inputs specifically excludes capital goods, capital goods used as parts or components in the manufacture of a final product are included therein. Thus, CENVAT credit will be available on the same.

Question 10

ABC India Ltd. is engaged in the manufacture of some dutiable goods. It purchased the following goods in the month of July, 20XX:-

S.No.	***Item***	***Excise duty paid (₹)***
(i)	*Raw material used for the production of the final product*	*1,00,000*

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(ii)	*Goods used for generation of electricity for captive consumption*	*20,000*
(iii)	*Goods used for providing free warranty – Value of such free warranty provided by ABC India Ltd. is included in the price of the final product and is not charged separately from the customers*	*10,000*
(iv)	*Light diesel oil*	*5,000*

Compute the amount of CENVAT credit available with ABC India Ltd.

Answer

Computation of CENVAT credit available with ABC India Ltd.

Particulars	₹
Raw material used for the production of the final product	1,00,000
Goods used for generation of electricity for captive consumption [Note 1]	20,000
Goods used for providing free warranty [Note 2]	10,000
Light diesel oil [Note 3]	Nil
Total CENVAT credit available	**1,30,000**

Notes:

1. As per the definition of inputs, goods used for generation of electricity for captive consumption are eligible inputs.
2. Since the value of the free warranty provided by ABC India Ltd. is included in the price of the final product and is not charged separately from the customer, the goods used for providing such free warranty will be inputs eligible for the CENVAT credit.
3. As per the definition of inputs, there is specific exclusion with regard to light diesel oil. Thus, CENVAT credit cannot be claimed in respect of the said goods.

Question 11

Solo Tyres India Ltd., a manufacturer procured raw material from Ram Rahim Manufacturers. It paid service tax and cesses on the freight charged, under reverse charge mechanism, for bringing the goods from the factory of Ram Rahim Manufacturers to its manufacturing unit. You are required to advise Solo Tyres India Ltd. whether it is eligible for claiming CENVAT credit of the service tax and cesses paid by it.

Answer

As per the definition of input services, inward transportation of inputs or capital goods are eligible input services for a manufacturer. Thus, service tax paid on freight by Solo Tyres India Ltd. under reverse charge can be availed as CENVAT credit because such transportation service has been used for inward transportation of inputs. It may be noted that since Solo

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Tyres India Ltd. is a manufacturer, credit of KKC will not be available. SBC as such, is also not CENVATable.

Question 12

Compute the CENVAT credit available with Krishna Motors Ltd., a manufacturer of cars, in respect of the following services availed by it in the month of July, 20XX:-

S.No.	***Services availed***	***Service tax paid (including SBC & KKC)(₹)***
(i)	*Sales promotion services*	*1,50,000*
(ii)	*Market research for the new car launched by Krishna Motors Ltd.*	*3,00,000*
(iii)	*Quality control services*	*1,50,000*
(iv)	*Routine maintenance of the cars manufactured by Krishna Motors Ltd.*	*75,000*
(v)	*Insurance of the cars manufactured*	*1,05,000*
(vi)	*Outdoor catering services provided to its employees*	*1,50,000*

Answer

Computation of CENVAT credit available with Krishna Motors Ltd.:

Particulars	**Service tax @ 14% (₹)**
Sales promotion services [Note 1]	1,40,000
Market research for the new car launched by Krishna Motors Ltd. [Note 1]	2,80,000
Quality control services [Note 1]	1,40,000
Routine maintenance of the cars manufactured by Krishna Motors Ltd. [Note 2]	70,000
Insurance of the cars manufactured [Note 2]	98,000
Outdoor catering services provided to its employees [Note 3]	Nil
Total CENVAT credit available	**7,28,000**

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Notes:

1. As per the definition of the input services, there is a specific inclusion with regard to the following services:-

   (a) Sales promotion services

   (b) Market research services

   (c) Quality control services

   Hence, the CENVAT credit of the service tax paid on the aforesaid services is available.

2. Service of general insurance business and repair and maintenance, in so far as they relate to a motor vehicle which is not a capital goods, is excluded from the definition of the input service except when used by a manufacturer of a motor vehicle in respect of a motor vehicle manufactured by such person.

   Thus, credit of the service tax paid on the insurance and maintenance of cars manufactured by Krishna Motors Ltd. is available.

3. Outdoor catering services to the employees are specifically excluded from the definition of the input services. Hence, CENVAT credit of service tax paid on such services is not available.

4. Credit of SBC is not available since it is not CENVATable. Further, since Krishna Motors Ltd. is a manufacturer, credit of KKC will also not be available. So, credit of only service tax @ 14% is allowed.

Question 13

Compute the CENVAT credit available with Ram Services Ltd., an output service provider in respect of the following services availed by it in the month of August, 20XX:-

S.No.	***Services availed***	***Service tax paid (including SBC & KKC) (₹)***
(i)	*Accounting and auditing services*	*15,00,000*
(ii)	*Legal services*	*7,50,000*
(iii)	*Security services*	*75,000*
(iv)	*Motor vehicles taken on rent* *(Such motor vehicles are not eligible capital goods for the purposes of claiming CENVAT credit)*	*1,50,000*

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Answer

Computation of CENVAT credit available with Ram Services Ltd.:

Particulars	Service tax @ 14%(₹)	KKC (₹)
Accounting and auditing services [Note 1]	14,00,000	50,000
Legal services [Note 1]	7,00,000	25,000
Security services [Note 1]	70,000	2,500
Motor vehicles taken on rent [Note 2]	Nil	Nil
Total CENVAT credit available	**21,70,000**	**77,500**

Notes:

1. As per the definition of the input services, there is a specific inclusion with regard to the following services:-
   (a) Accounting and auditing services
   (b) Legal services
   (c) Security services

   Hence, the CENVAT credit of the service tax paid on the aforesaid services is available.
2. The definition of input services specifically excludes the services of renting of motor vehicles which are not eligible capital goods.
3. Credit of SBC is not available since it is not CENVATable. Further, since Ram Services Ltd. is an output service provider, credit of KKC is available.

Question 14

Discuss briefly the validity of the following statements with reference to rule 3 of the CCR, 2004:

(i) A manufacturer can sell the inputs on which CENVAT credit has already been availed of, as such, provided he pays the amount equal to the credit availed.

(ii) CENVAT credit can be utilised for payment of any duty of excise on goods in respect of which the benefit of an exemption under Notification No. 1/2011-C.E. dated 01.03.2011 is availed.

(iii) CENVAT credit can be utilised for payment of the Clean Energy Cess leviable under section 83 of the Finance Act, 2010.

(iv) Credit of duty paid @ 2% on inputs in pursuance of Notification No. 1/2011 C.E. dated 01.03.2011 is available to the manufacturer as well as service provider who buys them.

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Answer

(i) Correct. A manufacturer of the final products can remove inputs on which CENVAT credit has been taken, as such, from the factory if he pays an amount equal to the credit availed in respect of such inputs and such removal is made under the cover of CENVATable invoice. However, such payment would not be required to be made where inputs are removed outside the factory for providing free warranty for final products.

(ii) Incorrect. Rule 3 specifically provides that CENVAT credit cannot be utilised for payment of any duty of excise on goods in respect of which the benefit of an exemption under *Notification No. 1/2011-C.E. dated 01.03.2011* is availed. In simple words, excise duty liability on goods in respect of which the benefit of an exemption under *Notification No. 1/2011-C.E. dated 01.03.2011* is availed has to be discharged in cash/ by cheque/ e-payment only.

(iii) Incorrect. CENVAT credit of any duty specified under rule 3 of the said rules cannot be utilised for payment of the Clean Energy Cess leviable under section 83 of the Finance Act, 2010.

(iv) Incorrect. CENVAT credit of excise duty paid on goods cleared by availing the exemption under *Notification No. 1/2011 C.E. dated the 1st March, 2011,* is not allowed.

Question 15

PQR Ltd., a manufacturer of excisable goods, purchased in the month of April, 20XX inputs worth ₹ 1,00,000/- on which it paid excise duty of ₹ 12,500/-. The company utilized the aforementioned CENVAT of ₹ 12,500/- while discharging its excise duty liability for the month of April, 20XX. In June, 20XX before the said inputs are put into use, the company has written off ₹ 20,000 out of the total inputs. The balance inputs of ₹ 80,000 were not written off.

What economic consequences the company has to face for writing off of ₹ 20,000/-. However, subsequently, in the month of September, 20XX, the company put to use the entire inputs of ₹ 1,00,000/-. Can the company get some economic benefit now?

Answer

As per rule 3 of the CCR, 2004, a manufacturer is required to pay an amount equivalent to the CENVAT credit taken in respect of inputs when the value of such inputs is written off fully or partially before being put to use.

Thus, PQR Ltd. will have to pay an amount equivalent to the CENVAT credit taken on inputs valuing ₹ 20,000 (inputs written off) which is ₹ 2,500 $\left(12{,}500 \times \frac{20{,}000}{1{,}00{,}000}\right)$.

However, if said inputs is subsequently used in the manufacture of final products, manufacturer shall be entitled to take credit of the amount equivalent to the CENVAT credit paid earlier subject to the other provisions of CCR, 2004. Thus, in present case, by virtue of

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aforesaid provision, when in September, 20XX, company puts to use entire inputs of ₹ 1,00,000; the company will be entitled to take credit of amount equivalent to the CENVAT credit paid earlier i.e. ₹ 2,500/-.

Question 16

The goods manufactured by a company have been destroyed in a fire. The payment of duty has been ordered to be remitted. Is the company required to reverse the CENVAT credit taken on input services used in manufacture of such destroyed goods?

Answer

Where on any goods manufactured by an assessee, the payment of duty is ordered to be remitted under rule 21 of the Central Excise Rules 2002, the CENVAT credit taken on input services used in or in relation to manufacture or production of said goods has to be reversed.

Question 17

RSL Pvt. Ltd. purchased a pollution control equipment on 20.06.2011 for ₹ 15,00,000 (including excise duty of ₹ 1,85,400); and took the CENVAT credit of 50% of the excise duty paid in the financial year 2011-12 and balance credit of 50% in the financial year 2012-13.

After using such equipment, RSL Pvt. Ltd. sold it as scrap for ₹ 50,000 excluding excise duty, on 31st July, 2016. Examine whether:

(i) RSL Pvt. Ltd. was correct in availing the CENVAT credit on the said equipment in financial years 2011-12 and 2012-13 ?

(ii) on selling of above equipment in the financial year 2016-17, RSL Pvt. Ltd. needs to pay the amount of excise duty earlier availed as CENVAT credit?

Note: *RSL Pvt. Ltd is not eligible for SSI exemption available under Notification No. 8/2003 CE dated 01.03.2003.*

Answer

(i) As per the definition of capital goods under rule 2(a) of the CENVAT Credit Rules, 2004, pollution control equipment is eligible capital goods. Further, as per rule 4 of CCR, CENVAT credit of only upto 50% of the excise duty paid is available in respect of the eligible capital goods in the year of purchase.

Thus, RSL Pvt. Ltd. is justified in taking 50% of the CENVAT credit of duty paid on the pollution control equipment in FY 2011-12 and balance in FY 2012-13.

(ii) Since the pollution control equipment is sold as scrap, RSL Pvt. Ltd. is required to pay an 'amount' equal to excise duty leviable on transaction value of scrap, i.e. 12.5% of ₹ 50,000 in terms of rule 3 of CCR.

Thus, RSL Pvt. Ltd. is required to pay an 'amount' of ₹ 6,250 and not the amount of excise duty earlier availed as CENVAT credit.

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Question 18

A manufacturer had purchased raw material for use in manufacturing process, on which excise duty paid was ₹ 1,00,000. The manufacturer took CENVAT credit of ₹ 1,00,000. Due to change in production schedule, the raw material was not used for two years. In compliance with Accounting Standards, the manufacturer made a provision in the books of accounts to fully write off the value of the raw material. However, the raw material is in stock in the store room and the manufacturer is hopeful that he will be able to utilize the material some day.

Is he required to take any action in respect of CENVAT credit? What would happen if subsequently, he actually uses the material in manufacture?

Answer

As per rule 3 of the CCR, 2004, where in respect of the value of any inputs before being put to use, on which CENVAT credit has been taken, any provision to write off fully or partially has been made in the books of account, then the manufacturer shall pay an amount equivalent to the CENVAT credit taken in respect of the said inputs. Further, if the said input is subsequently used in the manufacture of final products, the manufacturer shall be entitled to take the credit of the amount equivalent to the CENVAT credit paid earlier.

Thus, in the instant case, the manufacturer is required to reverse the CENVAT credit of ₹ 1,00,000. However, if at a later stage, he utilizes the raw material in manufacture, he can take CENVAT credit of ₹ 1,00,000.

Question 19

Ram, a manufacturer of excisable goods, imported some inputs which were received by him in July 20XX. Bill of Entry in respect of said imported goods was duly filed and basic customs duty of ₹ 1,000, countervailing duty under section 3(1) of Customs Tariff Act, 1975 of ₹ 1,375, Education cess of ₹ 47.50, Secondary and Higher Education cess of ₹ 23.75, Special CVD under section 3(5) of Customs Tariff Act, 1975 of ₹ 497.85 was paid by him.

You are required to determine:-

(i) how much CENVAT credit can Ram avail?

(ii) in case Ram is an output service provider and not a manufacturer, how much CENVAT credit can he avail?

Answer

(i) Rule 3 of the CCR, 2004 allows the credit of additional duty of customs leviable under section 3(1) and 3(5) of the Customs Tariff Act, 1975. However, the credit of basic custom duty and education cess and secondary and higher education cess of customs is not allowed. Therefore, the amount of CENVAT credit that can be availed by Ram is as follows:-

Particulars	₹
Countervailing duty under section 3(1) of Customs Tariff Act, 1975	1,375.00

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Special CVD under section 3(5) of Customs Tariff Act, 1975	497.85
CENVAT credit available	**1,872.85**

(ii) If Ram is a service provider, it will not make any difference with respect to availment of credit of CVD of ₹ 1,375 as credit for the same can be availed both by the manufacturers and the service providers alike. However, it will not be entitled to the CENVAT credit of ₹ 497.85 as a service provider is not entitled to avail the credit of special CVD.

Question 20

Sabhytaa Manufacturers received some inputs on 05.04.20XX and immediately availed CENVAT credit of the excise duty of ₹ 1,00,000 paid on those inputs. It sent the inputs to a job worker outside its factory for further processing on 30.04.20XX. The job worker carried out the processing and returned the inputs to Sabhytaa Manufacturers on 21.12.20XX. Discuss whether Sabhytaa Manufacturers is required to take any further action with respect to the CENVAT credit availed by it.

Answer

If any inputs are sent to a job worker for further processing and are received back in the factory within 180 days of their being sent to a job worker, CENVAT credit in respect of such inputs is allowed to the manufacturer. However, if the inputs are not received back within 180 days, the manufacturer shall pay an amount equivalent to the CENVAT credit attributable to the inputs by debiting the CENVAT credit or otherwise, but the manufacturer can take the CENVAT credit again when the inputs are received back in his factory.

In the given case, the goods sent on 30.04.20XX should have been received back latest by 27.10.20XX (May – 31, June – 30, July – 31, August - 31, September – 30, October – 27 = 180 days). However, since the inputs have not been received back from the job worker within 180 days, Sabhytaa Manufacturers is required to reverse CENVAT credit of ₹ 1,00,000.

Further, when it receives the inputs after processing on 21.12.20XX, it can again take the CENVAT credit of ₹ 1,00,000.

Question 21

Mahavir Traders purchases 10 tons of steel bars from a manufacturer of steel bars. The manufacturer has charged excise duty of ₹ 1,00,000 on the steel bars. Mahavir Traders sells 2 tons of steel bars to XYZ Fasteners Ltd., a manufacturer who uses the steel bars in his factory for the manufacture of the final product. XYZ Fasteners Ltd. wishes to avail the CENVAT credit of excise duty on the steel bars.

You are required to advise XYZ Fasteners Ltd. whether it can claim the CENVAT credit of excise duty paid on the steel bars. How much CENVAT credit it can avail, if allowable?

Answer

XYZ Fasteners Ltd. can avail CENVAT credit if Mahavir Traders is a first stage dealer and issues an invoice to XYZ Fasteners Ltd. indicating that the original manufacturer had paid

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excise duty of ₹ 20,000 on the steel bars (on proportionate basis). On the basis of such an invoice of Mahavir Traders, XYZ Fasteners Ltd. can avail CENVAT credit of ₹ 20,000.

Question 22

Raghav Motor Driving School has purchased a motor vehicle (registered in its name) for training its students in current Financial Year. The excise duty paid on the motor vehicle is ₹ 60,000. It is availing small service provider's exemption in the said financial year under Notification No. 33/2012 ST dated 20.06.2012 as the aggregate value of services provided by it in the preceding financial year is less than ₹ 10 lakh.

Can Raghav Motor Driving School avail CENVAT credit of the excise duty that has been paid on the motor vehicle, in current Financial Year?

Answer

As per the definition of capital goods, motor vehicles designed to carry passengers, registered in the name of the service provider, are eligible capital goods when same are used for providing output service of imparting motor driving skills. Hence, the motor vehicle purchased by Raghav Motor Driving School is eligible capital goods.

However, *Notification No. 33/2012 ST dated 20.06.2012* provides that a service provider shall not avail the CENVAT credit on capital goods received, during the period in which the service provider avails small service provider's exemption. Hence, Raghav Motor Driving School cannot avail CENVAT credit of the excise duty that has been paid on the said motor vehicle, in current Financial Year.

Question 23

LMN (Pvt.) Ltd., an output service provider, is engaged in providing taxable services to its clients. Its service tax liability for the month of May, 20XX is ₹ 3,50,000. LMN (Pvt.) Ltd. has to make e-payment of service tax on the due date i.e., on 06.06.20XX.

Break-up of CENVAT credit available with LMN Ltd. as on 01.05.20XX is given below:

Particulars	***Service tax/ Excise duty (₹)***	***KKC (₹)***	***Total (₹)***
Inputs	*50,000*		*50,000*
Capital goods	*1,00,000*		*1,00,000*
Input services	*14,000*	*500*	*14,500*

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LMN (Pvt.) Ltd. has provided the following further details:

Particulars	***Excise duty***		***Service tax (including SBC & KKC) [Input services] (₹)***
	Inputs (₹)	***Capital goods (₹)***	
Inputs received on 10.05.20XX (Invoice dated 15.05.20XX)	*30,000*		
Inputs received on 15.05.20XX (Invoice dated 17.05.20XX)	*50,000*		
Capital goods received on 20.05.20XX (Invoice dated 21.05.20XX)		*70,000*	
Invoice (for input services) dated 23.05.20XX received on same day			*45,000*
Invoice (for input services) dated 02.06.20XX received on same day			*45,000*
Inputs received on 04.06.20XX (Invoice dated 04.06.20XX)	*45,000*		

Out of total duty of ₹ 50,000 paid on inputs received on 15.05.20XX, ₹ 15,000 represented National Calamity Contingent Duty.

You are required to determine the service tax payable by LMN (Pvt.) Ltd. in cash, if any.

***Note**: LMN (Pvt.) Ltd. is not eligible for the small service provider exemption under Notification No. 33/2012 ST dated 20.06.2012.*

Answer

As per rule 3(4) of CCR, while paying excise duty or service tax, CENVAT credit can be utilized only to the extent such credit is available on the last day of the month or quarter for payment of duty or tax relating to that month or the quarter. Thus, CENVAT credit available as on 31.05.20XX can only be utilized by LMN (Pvt.) Ltd. to discharge service tax liability of the month of May.

Further, as per rule 3(7), credit of NCCD can be utilized towards payment of NCCD only. Therefore, CENVAT credit of ₹ 15,000 relating to NCCD cannot be utilized by LMN (Pvt.) Ltd. towards payment of its service tax liability.

In view of the above provisions, CENVAT credit available with LMN (Pvt.) Ltd. as on 31.05.20XX will be computed as under:

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Particulars		CENVAT credit			
	Excise duty		Service tax [Input services] (₹)	KKC [Input services] (₹)	Total (₹)
	Inputs (₹)	Capital goods (₹)			
Balance as on 01.05.20XX	50,000	1,00,000	14,000	500	1,64,500
Inputs received on 10.05.20XX	30,000				30,000
Inputs received on 15.05.20XX	50,000				50,000
Capital goods received on 20.05.20XX [Upto 50% of the excise duty paid can be availed as CENVAT credit in respect of capital goods in the year of purchase.]		35,000			35,000
Invoice (for input services) dated 23.05.20XX received same day			42,000	1,500	43,500
Balance as on 31.05.20XX	**1,30,000**	**1,35,000**	**56,000**	**2,000**	**3,23,000**

Computation of service tax payable in cash by LMN (Pvt.) Ltd.

Particulars	₹
Service tax liability for the month of May, 20XX	3,50,000
Less: CENVAT credit available as on 31.05.20XX [(₹3,23,000 - ₹15,000) as credit of NCCD cannot be utilized to pay service tax]	3,08,000
Service tax to be paid in cash	**42,000**

Note:

Credit of SBC is not available since it is not CENVATable. Further, since LMN Pvt. Ltd. is an output service provider, credit of KKC is available.

Question 24

Mr. Govinda, a manufacturer, is engaged in the manufacture of excisable goods. While Mr. Govinda avails CENVAT credit of excise duty paid on the inputs, he does not avail

CENVAT credit of service tax paid on input services as he thinks that being a manufacturer, he cannot do so. However, his Tax Consultant has advised him that as per the provisions of the CENVAT Credit Rules, 2004, he can also avail CENVAT credit of service tax paid on input services used for manufacture of final products.

Having come to know of his entitlement, Mr. Govinda wants to avail CENVAT credit of service tax paid on input services used by him for manufacture of final products.

You are required to examine whether Mr. Govinda can take CENVAT credit of service tax paid on input services on the basis of following invoices:

Bill No.	***Date of issue of invoice***
701	*02.03.20XX*
705	*14.03.20XX*
803	*15.04.20XX*

Mr. Govinda wants to avail CENVAT credit on 12th March of next year.

Answer

As per rule 3 of the CCR, a manufacturer of final product can take CENVAT credit of service tax paid on any input service received by it and used for the manufacture of final product. Thus, Mr. Govinda being a manufacturer of final product is eligible to avail CENVAT credit of service tax paid on input services received. However, rule 4(7) of CCR, stipulates that the manufacturer or the provider of output service shall not take CENVAT credit after one year of the date of issue of invoice. Further, credit will not be available of SBC and KKC paid on value of input services. Since Mr. Govinda is a manufacturer, credit of KKC is not available. Credit of SBC is also not available as it is not CENVATable.

In view of the said provisions, Mr. Govinda can avail CENVAT credit with respect to Bill No. 705 and 803 and not with respect to Bill No. 701 as period of one year has expired from the date of issuance of invoice.

Question 25

Seethe Granites Ltd. purchased a machine for ₹ 20,00,000 (excluding excise duty) on 01-03-2015. The excise duty rate charged on the said machine was 12.5%. It was sold on 15-03-2016 for ₹ 10,00,000 (excluding excise duty), as second hand machine at the same rate of excise duty.

Calculate the amount of CENVAT to be reversed at the time of disposal of the machinery in the year 2015-16 towards 100% CENVAT credit utilized and exhausted by the month of April, 2015.

Note: *Seethe Granites Ltd. is not eligible for SSI exemption available under Notification No. 8/2003 CE dated 01.03.2003.*

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Answer

Computation of amount payable towards CENVAT credit on disposal of machinery

Particulars		₹	₹
Price of the machinery			20,00,000
Excise duty @ 12.5%			2,50,000
CENVAT credit allowable on the machinery			
FY 2014-15	[Upto 50% of excise duty paid can be taken as credit in the financial year in which the capital goods is received. Balance credit can be taken in any subsequent financial year (Rule 4 of the CENVAT Credit Rules, 2004)]		1,25,000
FY 2015-16			1,25,000
Total CENVAT credit availed			2,50,000
Less:			
(i) First 50% credit = [₹ 1,25,000 × 2.5%] × 5 quarters (credit availed on 01.03.2015)		15,625	
(ii) Next 50% credit = [₹ 1,25,000 × 2.5%] × 4 quarters (credit availed on 01.04.2015)		12,500	28,125
Amount - I			2,21,875
Amount -II			1,25,000
Duty leviable on transaction value (₹ 10,00,000 × 12.5%)			
Amount payable towards CENVAT credit on disposal of machinery is higher of *Amount I* or *Amount II* in terms of rule 3(5A) of CENVAT Credit Rules, 2004			**2,21,875**

Question 26

Explain the provisions with regard to filling of CENVAT credit returns as explained in sub-rules (7) to (11) of rule 9 of CENVAT Credit Rules, 2004.

Answer

CENVAT credit returns are required to be filed electronically in the manner described below:

(i) A manufacturer has to submit a monthly return within 10 days from the close of each month.

However, in case of SSI units, a quarterly return has to be filed within 10 days after the close of the quarter to which the return relates.

(ii) A first stage/second stage dealer or registered importer has to submit a return within 15 days from the close of each quarter of a year.

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(iii) An output service provider availing CENVAT credit has to submit a half yearly return by the end of the month following the particular quarter/half year.

An input service distributor has to submit a half yearly return, giving the details of credit received and distributed during the said half year, by the end of the month following the half year period.

(iv) An output service provider or input service distributor can file revised return to rectify mistakes or omissions within 60 days from the date of filing of original return.

Question 27

Briefly answer the following questions with reference to the provisions of CENVAT Credit Rules, 2004:-

(i) Mr. Q, a manufacturer, receives an invoice dated 05.03.2016 for inputs purchased by it. Mr. Q has been advised by his consultant that CENVAT credit on said inputs cannot be taken after one year of the date of invoice. You are required to offer your comments, if any.

(ii) Mr. P, an output service provider, receives some capital goods within his premises and immediately sends them to a job worker for reconditioning on 22.03.2016. Mr. P has been informed by his consultant that for the purpose of availing CENVAT credit, he should get back the capital goods in his premises within 180 days of their being sent from his premises.

Answer

(i) The time limit for availment of CENVAT credit on inputs is one year of the date of the issue of invoice/bill/challan etc. Thus, in case of the invoice dated 05.03.2016, Mr. Q can take CENVAT credit on inputs only upto one year of the date of such invoice. Therefore, the advice of Mr. Q's consultant is correct.

(ii) For the purpose of availing CENVAT credit, the time limit for receiving back the capital goods from job worker to premises of the output service provider is 2 years. Thus, the time limit for return of capital goods sent to a job worker on 22.03.2016 for the purpose of availing CENVAT credit is not 180 days, but two years. Therefore, information of Mr. P's consultant is not correct.

Question 28

LT Pvt. Ltd. manufactures rubber slippers. Compute the CENVAT credit available with LT Pvt. Ltd. in respect of the following goods/services procured by it:

S. No.	*Particulars*	*Excise duty paid (₹)*	*Service tax paid (including SBC & KKC)(₹)*
(i)	*Machine for manufacture of rubber soles*	*10,00,000*	
(ii)	*Rubber sheets for manufacture of slippers*	*5,00,000*	

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(iii)	*Adhesives*	*50,000*	
(iv)	*Club Membership fee of employees*		*1,00,000*
(v)	*Expenses incurred on advertising the slippers on television*		*6,00,000*

Note: LT Pvt. Ltd. is not entitled to SSI exemption under Notification No. 8/2003 CE dated 01.03.2003.

Answer

Computation of CENVAT credit available with LT Pvt. Ltd.

Particulars	₹
Machine for manufacture of rubber soles [Note 1]	5,00,000
Rubber sheets for manufacture of slippers [Note 2]	5,00,000
Adhesives [Note 2]	50,000
Club membership fee of employees [Note 3]	Nil
Expenses incurred on advertising the slippers on television [Note 4]	5,60,000
Total CENVAT credit available	**16,10,000**

Notes:

1. Since LT Pvt. Ltd. is not a SSI unit, CENVAT credit of only upto 50% of the excise duty paid is available in respect of the eligible capital goods, in the year of purchase [Rule 4 of CCR].
2. Raw material (rubber sheets) and consumables (adhesives) are eligible inputs.
3. Services used primarily for personal use or consumption of any employee are excluded from the definition of input service.
4. Advertising service is an eligible input service. Credit of SBC is not available since it is not CENVATable. Further, since LT Pvt. Ltd. is a manufacturer, credit of KKC is also not available. So, credit of only service tax @ 14% is allowed.

Exercise

1. *Briefly explain the term "capital goods" with reference to the CCR, 2004.*
2. *When will accessories be eligible as "inputs" under the CCR, 2004?*
3. *Examine whether the following purchases are eligible as inputs under rule 2(k) of the CCR, 2004:*
   - *(a) High Speed oil*
   - *(b) Goods used for generation of electricity or steam for captive use.*
   - *(c) Motor vehicles*

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(d) *Any goods which have no relationship whatsoever with the manufacture of a final product.*

4. *Discuss the term "first stage dealer" with reference to the CCR, 2004.*

5. *Examine whether the following purchases are eligible as input services under rule 2(l) of the CCR, 2004:*

   (a) *Services used in relation to modernisation, renovation or repairs of the premises of provider of output service.*

   (b) *Inward transportation of inputs or capital goods.*

   (c) *Services provided by way of renting of a motor vehicle, in so far as they relate to a motor vehicle which is not a capital goods.*

   (d) *Beauty treatment services for the employees.*

6. *Capital goods, on which CENVAT credit has been taken, are removed as such from the factory. You are required to answer, with reference to rule 3 of the CCR, 2004, whether any action is required by the manufacturer of the final products.*

7. *The CENVAT credit in respect of inputs may be taken immediately on receipt of the inputs in the premises of the provider of output service. Critically evaluate the statement.*

8. *Briefly discuss the provisions relating to refund of the CENVAT credit under the CCR, 2004.*

9. *Enumerate the duties in respect of which CENVAT credit can be availed under the CCR, 2004.*

10. *The provider of output service shall not take CENVAT credit after one year of the date of issue of invoice. Examine the validity of the statement.*

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