



GLOBAL CMA

DIRECT TAX

Paper-7

Syllabus-2016

Answer of Postal test Paper
Set-2

Sol. 1 (a) MCQ

- I. D
- II. D
- III. D
- IV. B
- V. B
- VI. B
- VII. A
- VIII. B
- IX. C
- X. D

Sol. 1 (b) True/False

- (i) True
- (ii) False
- (iii) True
- (iv) True
- (v) True

Sol. 1 (c) Fill up

- (i) 100
- (ii) 3
- (iii) Exchange
- (iv) 15,000
- (v) Nil

Sol. 1 (d) Match the following

Column A

- (i) Section 234B
- (ii) Securities
- (iii) Section 234C
- (iv) Construction Costs
- (v) Section 44AD

Column B

- For non-payment of advance tax
- ICDS VIII
- For deferment of Advance tax Payment
- ICDS III
- Presumptive Income of Eligible Business

Sol. 2 (a)

Computation of total income of A for the assessment year 2017-18 relating to the previous year 2016-17:

Particulars	Resident and ordinarily resident ₹	Resident but not ordinarily resident ₹	Non-resident ₹
Profit on sale of shares in Indian company, sold in India but proceeds received in France	30,000	30,000	30,000
Dividend from a Korean company received in France	50,000	-	-
Rent from property in Sri Lanka deposited in Sri Lanka but latter remitted to India through approved banking channel – Gross (note 1)	70,000	-	-
Dividend from ABC (P) Ltd. [Exempt u/s 10 (34)]	-	-	-
Income from nursery in Gujarat [Agricultural income, exempt us 10(1)]	-	-	-
	1,50,000	30,000	30,000

Sol. 2 (b)

- (a) **Disintegration of single sum into capital and income:** Where a composite sum is received, it should be apportioned and the part which is revenue in nature should be charged to tax.
- (b) **Lump sum and periodic sum:** An income need not be recurring one. Similarly, a capital receipt need not be a single receipt. In a number of cases it has been held that a single or occasional receipt may be an item of income and an annual receipt recurring over a number of years may be capital receipt.
- (c) **Magnitude of receipt:** The magnitude of receipt is not material for deciding its nature.
- (d) **Accounting treatments:** The name given to the transaction by the parties involved or its treatment in the books of account may not alter its character as capital or revenue. For example, if a receipt is a trading receipt, its treatment in the books of account otherwise will not prevent the assessing authority from treating it as trading receipt.
- (e) **Income from wasting assets:** Profits from capital which is consumed and exhausted in the process of realization, e.g. royalties from mines and quarries, is taxable as income regardless of the consumption of capital involved in the process.
- (f) **Receipt from fixed capital:** A receipt is not taxable when it is referable as fixed capital. However, what is capital asset in the hands of one person may be trading asset in the hands of another person and accordingly, the incidence of tax may vary according to the nature of the trade in connection with which it arises.
- (g) **Capital sale and business sale:** While a transaction entered into in the ordinary course of business is revenue receipt, profits accruing from the sale of any assets are capital receipt.
- (h) **Transactions in the ordinary course of business:** A transaction carried out in the ordinary course of business is normally in the nature of trade. However, there can be a situation when transaction in the ordinary course of business may be regarded as capital in nature. For example, when a money-lender takes over a land from his debtor in satisfaction of a debt and subsequently sells it, it may be regarded as sale of capital investment. However, whether a transaction is in the course of business or an isolated transaction, the onus is on the Income-tax Department to prove it.
- (i) **Shares and securities:** The profit or loss on sale of shares held by an ordinary investor would be capital in nature, but when such shares are held as part of the business of the assessee, such profits and losses would be revenue in nature.

Sol. 2 (c)

An assessee is a person by whom any tax or any other sum of money is payable under the Income-tax Act. The term assessee also includes the following:

- (a) every person in respect of whom any proceeding under the Income-tax Act has been initiated for the assessment of his income or assessment of fringe benefits or loss or any amount of refund due to him or for the assessment of income, loss or refund of any other person in respect of which he is assessable.
- (b) every person who is deemed to be an assessee under any provision of the Income-tax Act;
- (c) every person who is deemed to be an assessee in default under any provision of the Income tax Act.

From the above definition, the following points emerge:

- An assessee is a person who is liable to pay tax on his own income.
- Even if the said person has no income during the year, he may be called an assessee in respect of any loss that he has incurred or in respect of any amount of refund due from the income-tax authorities.
- The said person can be an assessee in respect of income or loss of another person. Examples of this type of assessee are the following:
 - (i) An agent of a non-resident person.
 - (ii) The guardian of a person suffering from incapacity to contract, e.g., a minor, a lunatic or an idiot.
 - (iii) A person responsible for deduction of tax at source.
 - (iv) A trustee.

Sol. 3 (a)

Computation of Profits and gains of business or profession for the assessment year 2017-18 relating to the previous year 2016-17

	₹	₹
Net profit as per P/L Account		60,00,000
Add: Expenses disallowed:		
Depreciation (treated separately)	3,50,000	
Bad debt (Note 1)	Nil	
Proposed dividend	6,00,000	
Machinery discarded (treated separately)	90,000	
Provident fund collection from employees and own contribution not deposited within due date	2,60,000	
Provision for taxation	15,00,000	(+)28,00,000
Less: Incomes wrongly credited:	50,000	
Agricultural income	Nil	
Bank loan credited to capital reserve (Note 2)	3,00,000	
Less: Depreciation as per IT Act (Note 3)		(-)3,50,000
Business income		84,50,000

Note:

- (1) In TRF Ltd. V. CIT it has been held that it is not necessary to establish that the debt has become irrecoverable; it is enough if bad debt is written off as irrecoverable in the accounts of the assessee.
- (2) Recently, the Delhi High Court (High Court) in the case of Logitronics Pvt. Ltd. [Logitronics Pvt. Ltd v. CIT (ITA no. 1623 of 2010) & CIT v. Jubilant Securities Pvt. Ltd. (ITA No. 503 of 2010) it was held that in the context of waiver of loan amount, taxability would depend upon the purpose for which the loan was taken. Waiver of loan taken for acquiring a capital asset would not result in income exigible to tax. However, waiver of loan availed for trading purpose, results in the income taxable under the Income-tax Act, 1961 (the Act).
- (3) Depreciation as per IT Act:

WDV as on 1.4.2106		15,90,000
Add: New machinery purchased	4,10,000	4,10,000
Less: Money received in respect of machinery discarded or demolished	Nil	
WDV as on 31.3.2017		20,00,000
Depreciation @ 15%		3,00,000

Sol. 3 (b)

Computation of tax liability from slump sale of software unit for the assessment year 2017-2018 relating to the previous year 2016-2017

Particulars	₹(lakh)
Sale consideration for slump sale of Software Unit	385
Less: Cost of acquisition being the net worth of Software Unit	185
Long term capital gains arising on slump sale (The capital gains is long-term as the Software Unit is held for more than 36 months)	200
Tax liability on LTCG	40.00
Under section 112 @ 20% on ₹ 200 lakhs	3.00
Add: Surcharge 7.5%	43.00
Add : Education Cess @2% and SHEC @ 1%]	1.29
Tax payable	44.29

Note:

(1) Computation of net worth of the software unit:

	₹ (lakh)
(1) Book value of non-depreciable assets:	
Land (Revaluation not to be considered)	40
Debtors	110
Inventories	35
Written down value of depreciable assets under section 43(6)	90
Aggregate value of total assets	275
Less : Current liabilities of software unit	90
Net worth of software unit	185

Note 2:

For computing net worth, the aggregate value of total assets in the case of depreciable assets shall be the written down value of the block of assets as per section 43(6).

Sol. 4 (a)

Computation of capital gains of R for the assessment year 2017-18 relating to previous year 2016-17:

Particulars	₹	₹
Sale consideration		90,00,000
Less: Indexed cost of acquisition [₹ 3,40,000 x 1125/*426] (Note 1)		8,97,887
Long-term capital gains		81,02,113
Less: Exemption u/s 50EC for REC Bond	30,00,000	
Less: Exemption u/s 54 for construction of new house	51,02,112	81,02,113
Taxable capital gains		Nil

Note 1: Since the property is inherited by R from his father, indexation is done with reference to the FMV as on 1.4.81 or actual cost whichever is higher. However, the indexation benefit is available with reference to the time when R became the owner.

However, if the judgment of the Bombay High Court in CIT v. Manjula J Shah (2012) is adopted, the indexation benefit shall be available with reference to the year in which the previous owner first became the owner (Here with reference to 1.4.1981. In accordance with this judgment the answer would be as under:

Particulars	₹	₹
Sale consideration		90,00,000
Less: Indexed cost of acquisition [₹ 3,40,000 x 1125/*100] (Note 1)		38,25,000
Long-term capital gains		51,75,000
Less: Exemption u/s 50EC for REC Bond	30,00,000	
Less: Exemption u/s 54 for construction of new house	21,75,000	51,75,000
Taxable capital gains		Nil

Note 2: Amount forfeited after 1.4.2014 shall be taxable as income from other sources. It will no longer be deducted from cost of acquisition.

Sol. 4 (b)

(a) Since Mr. and Mrs. X together hold 20% share in the concern, the clubbing provisions as mentioned in section 64(1) will be applicable here. The salary shall be clubbed with the total income of the husband or wife, whose total income, excluding the remuneration, is greater. In the present case total income (excluding salary from Z & Co.) of Mrs. X is more than the total income of Mr. X (See note 1). Accordingly, salary of Mr. X from Z & Co. shall be clubbed with the income of Mrs. X and the total income of Mr. and Mrs. X will be as under:

	Mr. X (₹)	Ms. X (₹)
Income from own business	1,20,000	90,000
Interest from Z & Co.	20,000	4,10,000
Income from other sources (as given)	2,10,000	1,10,000
Salary from Z & Co.:		
Mr. X (Clubbed u/s 64(1))	-	96,000
Mrs. X		84,000
Gross total income	3,50,000	7,90,000
Less: Deduction u/s 80C-80U	Nil	Nil
Total income	3,50,000	7,90,000

(b) If the combined shares of Mr. X and Mrs. X are less than 20%, the clubbing provision will not be applicable. In that case, salary income of Mr. X will not be added with the income of Mrs. X.

Note 1: Total income of Mr. X and Mrs. X:

	Mr. X	Mrs. X
Income from own business	1,20,000	90,000
Income from other sources	2,10,000	1,10,000
Interest from Z & Co.	20,000	4,10,000
Add salary	3,50,000	6,10,000
Total		

Sol. 5 (a)

Computation of total income and tax liability of X for the assessment year 2017-2018 relating to the previous year 2016-2017.

	₹	₹
• Profits and gains of business or profession:		
Net income from manufacturing business	1,30,000	
Share of profit from a partnership concern [Exempt u/s 10(2A)]	Nil	
Share of income from 11UF in which X is a member [Exempt u/s 10(2)]	Nil	1,30,000
• Capital gains :		
Short-term capital gains on sale of land	24,000	
Long-term capital gain on sale of house property	1,20,000	1,44,000
• Income from other sources :		
Interest on Post Office Savings Bank Account [Exempt u/s 10(15)]	Nil	
Interest on bank deposit in own name	4,000	
Interest on bank deposit in the name of minor child [Exempt u/s 10(32)]	Nil	
Winning from camel race	10,000	14,000
Gross total income		2,88,000
Less : Deductions u/ss 80C - 80U :		
(i) u/s 80DD for medical treatment of dependent with disability [Fixed]	75,000	
(ii) u/s 80E for repayment of education loan [4,000 x 1/8 (Note 1)]	500	
(iii) u/s 80C for donation (Note 2)	20,000	95,500
Total income		1,92,500

Notes:

- (1) With effect from the assessment year 2006-07, deduction under Section 80E is allowed on account of interest for loan taken to pursue any higher education (part-time or full-time course) in India or abroad. The deduction shall be allowed over eight assessment years.
- (2) 100% of donation to the Prime Minister's National Relief Fund is eligible for deduction u/s 80G.

Sol. 5 (b)

Computation of total income and tax liability of Mr. C, for the assessment year 2017-18 relating to the previous year 2016-17

		₹
Salaries:		
Basic salary [₹ 24,000 x 12]		2,88,000
Encashment of leave while in service (fully taxable)		10,000
D.A.		1,20,000
Perquisites:		
Rent free accommodation [Note]		62,700
Reimbursement of medical expenses	32,000	
Less: Exemption (non-recognized hospital)	15,000	17,000
Children education allowance	13,200	
Less: Exempt u/s 10(14) [@ ₹100 p.m.]	1,200	12,000
Income-tax paid by employer		15,000
Professional tax paid by the employer		2,400
Gross salary		5,27,100
less: Professional tax u/s 16(iii)		2,400
Net salary		5,24,700
Capital Gains (Long-term capital gains)	10,000	
Less: Short-term capital loss	8,000	2,000
Total income		5,26,700

Tax Liability

Tax on long term capital gains (₹2,000 @ 20%)	400
Tax on other incomes of ₹5,24,700 at normal rates	29,940
	30,340
Add: Education Cess and Higher Education cess 3% (2% + 1%)	910
Total Tax Liability	31,250

Working Note:1.

Rent- free accommodation being lower of the following:	
A. Rent paid by employer	₹ 72,000
B. 15% of salary (basic salary, leave encashment and D.A. i.e., (2,88,000+10,000+1,20,000 = ₹ 4,18,000)	₹ 62,700

Note 2: Loss from speculation business is to be set off against income from speculation business income only.

Sol. 6 (a)

Computation of total income of H for the assessment year 2017-2018, relating to the previous year 2016-2017

• Profits and gains of business or profession :		₹	₹	₹
Net profit as per Profit and Loss Account			36,000	
Add :	Expenses disallowed:			
	Interest on capital	1,200		
	Remuneration to self	2,400		
	Rent of self-owned godown	1,500		
	Excess depreciation	2,500		
	Donation to National Defence Fund	4,000	11,600	
			47,600	
Add :	Goods withdrawn by owner below cost price (₹ 8,000 – ₹ 6,000)	2,000		
Add:	Net adjustment for undervaluation of stocks [₹ (7,200 - 4,500) x 1/9]	300	2,300	
			49,900	
Less:	Incomes not taxable under this head:			
	Bank interests	2,500		

	Dividend from Indian company	5,000	7,500	42,400
• Income from other sources:				
	Bank interest		2,500	
	Dividend from Indian companies			
	[Exempt u/s 10(34)]		-	2,500
	Gross total income			44,900
Less :	Deductions u/ss 80C to 80U :			
	Deduction u/s 80G in respect of			
	donation to National Defence Fund			4,000
Total	income			40,900

Sol. 6 (b)

Computation of Income from house property of S for the assessment year 2017-18 relating to the previous year 2016-17

		₹	₹
Ground floor (Self-occupied):			
	Gross Annual Value	Nil	
	Less: Municipal tax	Nil	
	Net Annual Value	Nil	
	Less: Deduction u/s 24(b) for interest on borrowed capital	86,250	(-)86,250
First floor (let out):			
	Gross annual value for 9 months:		
	Step 1: Reasonable expected rent being higher of :	60,000	
	(a) Municipal value for 9 months: [80,000 x 9/12]	90,000	90,000
	(b) Fair rent for 9 months [₹ 1,20,000 x 9/12]	1,80,00	
	Step 2: Annual rent [20,000 x 9]	40,000	1,40,000
	Less: Loss for vacancy [2 months x 20,000]		1,40,000
	Gross annual value being higher of Step 1 and Step 2		5,000
	Less : Municipal tax paid		1,35,000
	Net Annual Value	40,500	
	Less: Deduction u/s 24:	86,250	1,26,750
	(a) Standard deduction u/s 24(a)		
	(b) Interest on borrowed capital u/s 24(b)		8,250
	Income from house property (loss)		(-) 78,000

Note: Interest on borrowed capital:

(a) Interest for pre-construction period [1.7.2015 to 31.3.16 = 9months @10%] = 1,12,500

1/5th of the interest for pre-construction period

₹ 22,500

Add: Interest for the current year :

₹ 1,50,000

Total Interest allowable

₹ 1,72,500

Share of each floor (₹ 1,72,500/2)

₹ 86,250

Sol. 7 (a)

The due dates for submission of return are as under:

Assessee	Due date of submission of return
*A company	30 th September of the assessment year
Where the assessee is a person (other than a company whose accounts are required to be audited under any law)	30 th September of the assessment year
Where the assessee is a working partner of a firm, whose accounts are required to be audited under any law	30 th September of the assessment year

Any other assessee	31st July of the assessment year
*In the case of a company which has entered into an international agreement and is required to furnish u/s 92E a report from an accountant	30th November of the assessment year

Sol. 7 (b)

To identify the direct tax issues in relation to e-commerce transactions and suggest an approach to deal with these issues, a Committee on Taxation of e-commerce was constituted by the Central Board of Direct Taxes to examine the business models for e-commerce. The Report of the Committee was received by the Government and taken into consideration in the preparation of Finance Bill, 2016. This Report provides the view of the Committee on issues related to taxation of e-commerce and recent international developments in this area.

The Committee took cognizance of the Report on Action 1 of Base Erosion & Profit Shifting (BEPS) Project, wherein very significant work has been undertaken for identifying the tax challenges arising from digital economy, the possible options to address them and constraints likely to be faced.

The Committee also notes that this report has been accepted by G-20 countries, including India and OECD, thereby providing a broad consensus view on these issues. The Committee took note of the work done in this field by other experts, as well as the lack of uniformly accepted standards in taxation of royalty and fee for technical services, and the resultant tax disputes.

The BEPS Report on Action 1 clearly highlights the need for modifying existing international taxation rules, and identifies three options, i.e. a new nexus based on significant economic presence, a withholding tax on digital transactions, and Equalization Levy. The Report elaborates in detail the characteristics of these options and their possible tax design.

After examining the three options identified in the report, the Committee notes that compared to the first two options, i.e. a new nexus based on significant economic presence and the withholding tax on digital transactions, which would require changes in a number of tax treaties, the third option of 'Equalization Levy' provides a simpler option that can be adopted under domestic laws without needing amendment of a large number of tax treaties.

Accordingly, the Committee recommends the adoption of this option to address the tax challenges of digital economy and provide greater certainty and predictability in its taxation. The Equalization Levy imposed on the payment for digital transactions, would not be a tax on income, and hence would not be covered by tax treaties. As Equalization Levy is not proposed as tax on income, it would need to be imposed outside the Income-tax Act, 1961.

Sol. 7 (c)

This Income Computation and Disclosure Standard deals with treatment of borrowing costs. This Standard does not deal with the actual or imputed cost of owners' equity and preference share capital.

• **Definitions:** The following definitions have been used:

(a) —**Borrowing costs** has been defined as interest and other costs incurred by a person in connection with the borrowing of funds and include:

- (i) commitment charges on borrowings;
- (ii) amortised amount of discounts or premiums relating to borrowings;
- (iii) amortised amount of ancillary costs incurred in connection with the arrangement of borrowings;
- (iv) finance charges in respect of assets acquired under finance leases or under other similar arrangements.

(b) —**Qualifying asset** has been defined to mean:

- (i) land, building, machinery, plant or furniture, being tangible assets;
- (ii) know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets;
- (iii) inventories that require a period of twelve months or more to bring them to a saleable condition.

• **Recognition:**

(a) Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset shall be capitalised as part of the cost of that asset. The amount of borrowing costs eligible for capitalisation shall be determined in accordance with this Income Computation and Disclosure Standard. Other borrowing costs shall be recognised in accordance with the provisions of the Act.

• **Borrowing Costs Eligible for Capitalisation:** To the extent the funds are borrowed specifically for the purposes of acquisition, construction or production of a qualifying asset, the amount of borrowing costs to be capitalised on that asset shall be the actual borrowing costs incurred during the period on the funds so borrowed.

• **Disclosure:** The following disclosure shall be made in respect of borrowing costs:

- (a) the accounting policy adopted for borrowing costs; and
- (b) the amount of borrowing costs capitalised during the previous year.

Sol. 8 (a)

This section applies when the assessee claims identical question law is pending before High Court or the Supreme Court. Accordingly, where an assessee claims that any question of law arising in his case for an assessment year which is pending before the Assessing Officer or any appellate authority is identical with a question of law arising in his case for another assessment year which is pending before the High Court on a reference under section 256 or before the Supreme Court on a reference under section 257

or in appeal under section 260A before the High Court or in appeal under section 261 before the Supreme Court, he may furnish to the Assessing Officer or the appellate authority, as the case may be, a declaration in the prescribed form and verified in the prescribed manner, that if the Assessing Officer or the appellate authority, as the case may be, agrees to apply in the relevant case the final decision on the question of law in the other case, he shall not raise such question of law in the relevant case in appeal before any appellate authority or in appeal before the High Court under section 260A or in appeal before the Supreme Court under section 261.

Sol. 8(b)

With a view to rectifying any mistake, which is apparent from the record, an income-tax authority referred to in Section 116 may do the following:

- (a) amend an order passed by it under the provisions of this Act;
- (b) amend any intimation or deemed intimation under Section 143(1) or Section 200A
- (c) amend any intimation under Section 200A (1).
- (d) in relation to an order, where any matter has been considered and decided in any proceeding by way of appeal or revision, it cannot be rectified under Section 154. However, the matter which has not been considered and decided in the appeal or revision may be rectified under Section 154.
- (e) Rectification under Section 154 shall be made by:
 - (i) the income-tax authority on its own motion.
 - (ii) the income-tax authority, if it is brought to its notice by the assessee or the deductor or collector;
 - (iii) the commissioner (Appeals), if the mistake is brought to its notice by the Assessing Officer.

• **Order of rectification:**

An order of rectification is subject to the following conditions:

- (a) Where an amendment is made under this section and if such an amendment has the effect of enhancing or reducing a refund or otherwise increasing the liability of the assessee, a notice specifying the intention to do so is necessary. The assessee shall also be allowed reasonable opportunity of being heard [Section 154(3)].
- (b) In the above case, the Assessing Officer shall serve on the assessee a notice of demand in the prescribed form specifying the sum payable. Such a notice of demand shall be deemed to be notice under Section 156 and the provisions of Section 156 and the provisions of the Act shall apply in this case [Section 154(6)].
- (c) An order shall be passed in writing by the income-tax authority concerned [Section 154(4)].

(d) Where any such amendment has the effect of reducing the assessment, the Assessing Officer shall make any refund which may be due to the assessee or the deductor or the collector [Section 154(5)].

(e) Where any such amendment has the effect of enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee or the deductor or the collector, the Assessing Officer shall serve on the assessee or the deductor, as the case may be, a notice of demand in the prescribed form specifying the sum payable, and such notice of demand shall be deemed to be issued under Section 156 and the provisions of this Act shall apply accordingly [Section 154(6)].

(f) Except for cases coming under Sections 155 or 186(4), rectification of an order can be made only within four years from the end of the financial year in which the order sought to be amended was passed [Section 154(7)].

However, where a application for amendment under Section 154 is made by the assessee on an income-tax authority, the authority shall pass an order (either making the amendment or refusing it) within a period of six months from the end of the month in which the application is received by it [Section 154(8)].

Sol. 8 (c)

A person wishing to carry forward and set off of losses under the following heads must file return within the due date prescribed under Section 139(1):

- (i) loss under the head —Profits and gains of business or professionll [u/s 72(1)];
- (ii) (ii) any loss computed in respect of speculation business. [u/s 73(2)] ;
- (iii) (iii) any loss in respect of a business specified in Section 35AD which has not been fully set off [Section 73A (2)];
- (iv) 73A (2);
- (v) (iv) losses under the head —Capital gainsll [u/s 74(1)];
- (vi) (v) loss on maintaining race horses [u/s 74A (3)];
- (vii) Except in the case of a company and cases covered under the first proviso to Section 139(1), it is not
- (viii) necessary to furnish return if the total income is below the taxable limit. But in the case of losses
- (ix) mentioned above, the right of the assessee to carry forward losses shall be lost unless return is furnished
- (x) within the due date prescribed in Explanation 2 to Section 139(1).



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