

Paper 16- DIRECT TAX LAWS AND INTERNATIONAL TAXATION

Paper 16- Direct Tax Laws and International Taxation

Full Marks: 100

Time allowed: 3 hours

Section - A

- 1. Multiple Choice Questions with Justification: [10x2=20]**
- (i) As per section 178(3), the _____ of a company has to intimate the tax authority before he parts with any of the assets of the company or the properties in his hands and has to set aside the amount if any intimated to him by the tax authorities.
- (a) Managing Director
(b) Manager
(c) Chartered Accountant
(d) Liquidator
- (ii) Prosecution can be launched and the taxpayer can be punished if he commits wilful failure to produce before the tax authorities the accounts and documents as demanded under section _____.
- (a) 154
(b) 147
(c) 143(1)
(d) 142(1)
- (iii) Any mistake which is apparent from the record in any order passed by the Assessing Officer can be rectified under section _____.
- (a) 154
(b) 147
(c) 143
(d) 254
- (iv) MAT stands for _____
- (a) Minimum Alternate Tax
(b) Minimum Allowed Tax
(c) Minimum Applicable Tax
(d) Minimum Adjustable Tax
- (v) The Commissioner of Income-tax (Appeals) is the _____ appellate authority
- (a) First
(b) Second
(c) Third
(d) Fourth
- (vi) As per section 115QA(3), tax to credit of Government in case of distributed income of domestic company for buy-back of shares shall be deposited within _____ days from date of payment of any consideration to the shareholder on buy-back of shares.
- (a) 7 days
(b) 14 days
(c) 10 days
(d) 30 days

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- (vii) Provisions relating to advance ruling are provided in sections _____.
(a) 80C to 80U
(b) 245A to 245L
(c) 237 to 245
(d) 245N to 245V
- (viii) As per section _____ when any specified domestic transaction is carried out between associated enterprises, the said transaction should be carried out at arm's length price.
(a) 90
(b) 91
(c) 92
(d) 90A
- (ix) Section _____ deals with methods of computation of arm's length price.
(a) 94
(b) 93
(c) 92C
(d) 91
- (x) Arm's length price is to be determined by applying _____.
(a) Resale Price Method
(b) Fair Market Value Method
(c) Stamp Duty Value Method
(d) Indexed Cost of Acquisition Method

Answer:

(i) (d) As per section 178(3), the liquidator of a company has to intimate the tax authority before he parts with any of the assets of the company or the properties in his hands and has to set aside the amount if any intimated to him by the tax authorities

(ii) (d) Section 142(1) deals with the general provisions relating to an inquiry before assessment. U/s 142(1), the Assessing Officer can issue notice asking the taxpayer to file the return of income, if he has not filed the return of income or to produce or cause to be produced such accounts or documents as he may require and to furnish in writing and verified in the prescribed manner information in such form and on such points or matters (including a statement of all assets and liabilities of the taxpayer, whether included in the accounts or not) as he may require. Sec. 276D provides for prosecution in the case of wilful failure by the taxpayer to produce accounts and documents under section 142(1)

(iii) (a) Any mistake which is apparent from the record in an order passed by the Assessing Officer can be rectified u/s 154.

(iv) (a) MAT stands for Minimum Alternate Tax and AMT stands for Alternate Minimum Tax. Initially the concept of MAT was introduced for companies and progressively it has been made applicable to all other taxpayers in the form of AMT.

(v) (a) The Commissioner of Income-tax (Appeals) is the first appellate authority.

(vi) (b) As per section 115QA(3), tax to credit of Government in case of distributed income of domestic company for buy-back of shares shall be deposited within 14 days from date of payment of any consideration to the shareholder on buy-back of shares.

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(vii) (d) Provisions relating to advance ruling are provided in sections 245N to 245V.

(viii) (c) As per section 92, when any specified domestic transaction is carried out between associated enterprises, the said transaction should be carried out at arm's length price. In other words, income arising or allowance of any expenses to an entity resulting from specified domestic transactions with associated enterprise should be computed by having regard to arm's length price of such transaction.

(ix) (c) Section 92C deals with methods of computation of arm's length price.

(x) (a) The arm's length price in relation to an international transaction or specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely:

Transaction Based Methods —

1. comparable uncontrolled price method;
2. resale price method;
3. cost plus method;

Profit Based Methods —

4. profit split method;
5. transactional net margin method;
6. such other method as may be prescribed by the Board.

Section-B (Answer any five questions out of seven questions)

2.(a) Calculate interest u/s 234A in the following cases –

Name of the assessee	A	A Ltd.	B
Due date of furnishing return	31 st July	30 th September	31 st July
Date of filing return	4 th December	30 th January	Not filed
Date of completion of assessment	1 st March	15 th April	15 th February
Income as per return	₹ 5,80,000	₹ 5,00,000	--
Assessed Income	₹ 6,10,000	₹ 5,50,000	₹ 12,00,000
Advance tax paid	₹ 10,000	₹ 25,000	₹ 80,000
Tax deducted at source	₹ 10,000	₹ 15,000	₹ 80,000
Tax paid along with return	₹ 6,000	₹ 1,50,000	--

Ignore interest under any other section.

[8]

(b) What are the objectives of tax planning?

[8]

Answer:

(a) Computation of interest u/s 234A

Particulars	Code	A	A Ltd.	B
Period of default	A#	5 months	4 months	7 months
		(Aug. to Dec.)	(Oct. to Jan.)	(Aug. to Feb.)

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Assessed Income	B	6,10,000	5,50,000	12,00,000
Tax rate	C	Slab-rate	30%	Slab rate
Tax liability before surcharge	$D=B \times C$	34,500	1,65,000	1,72,500
Rate of Surcharge	E	Nil	Nil	Nil
Surcharge	$F=D \times E$	Nil	Nil	Nil
Tax and surcharge payable	$G=D+F$	34,500	1,65,000	1,72,500
Education cess & SHEC	$H=G \times 3\%$	1,035	4,950	5,175
Tax liability on assessed income	$I=G+H$	35,535	1,69,950	1,77,675
Less: Advance tax paid & tax deducted at source	J	20,000	40,000	1,60,000
Shortfall	$K=I-J$	15,535	1,29,950	17,675
Rounded off	L	15,500	1,29,900	17,600
Interest (1% * A * L)		775	5,196	1,232
Note: Tax paid along with return shall not be reduced while computing interest u/s 234A				

(b) Tax planning is an exercise undertaken to minimize tax liability through the best use of all available allowances, deductions, exclusions, exemptions, etc. The objectives of tax planning cannot be regarded as offending any concept of the taxation laws and subjected to reprehension of reducing the inflow of revenue to the Government's coffer, so long as the measures are in conformity with the statute laws and the judicial expositions thereof. The basic objectives of tax planning are:

1. Reduction of Tax liability

Tax law provides multiple choices and options to taxpayers. This necessary offer of options within tax legislation creates the opportunity for choice on the part of the tax payer. However, due to lack of awareness of legal requirements, in many a cases, a taxpayer may suffer heavy taxation. Through proper tax planning and awareness, a tax payer may reduce such heavy tax burden.

2. Minimisation of litigation

In the matter of taxation, the tax payers will try to pay the least tax and on the other hand, the tax administrator will attempt to extract the maximum. This conflict behaviour may results into litigations. However, where proper tax planning is adopted by the tax payer in conformity with the provisions of the taxation laws, the incidence of litigation can be minimised. This saves him from the hardships and inconveniences caused by the unnecessary litigations.

3. Productive investment

A tax payer may reduce heavy tax burden through proper tax planning. Such reduction results into reduction in cash-outflow. In the days of credit squeeze and dear money conditions, even a rupee of tax decently saved may be taken as an interest-free loan from the Government, which perhaps, an assessee need not repay. Such retained cash can be utilised in other productive venture which also provide additional earning to the taxpayer. That means, proper tax planning is a measure of proper utilisation of available resources which in turn maximise the cash-inflow and minimise the tax burden.

4. Healthy growth of economy

The growth of a nation's economy is synonymous with the growth and prosperity of its citizens. In this context, a saving of earnings by legally sanctioned devices fosters the growth of both, because savings by dubious means lead to generation of black money, the evils of which are obvious. Conversely, tax-planning measures are aimed at generating white money having a free flow and generation without reservations for the overall progress of the nation. Tax planning assumes a great significance in this context.

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5. Economic stability

Tax planning results in economic stability by way of:

- (i) productive investments by the tax payers; and
- (ii) harnessing of resources for national projects aimed at general prosperity of the national economy and reaping of benefits even by those not liable to pay tax on their incomes.

3. Compute gross total income of Minakshi Ltd. under the head Profits & gains of business or profession for the assessment year 2018-19

Profit & Loss A/c for the year ended 31/3/2018

Particulars	Amount	Particulars	Amount
To Opening stock	4,00,000	By Sales	17,80,000
To Purchases of raw material	5,00,000	By Closing Stock	5,00,000
To Conversion cost	4,00,000	By Interest on debenture	10,000
To Customs duty	1,70,000	By Bad debt recovery	25,000
To Salary and wages	80,000	(Previously allowed)	
To Bonus to employee	15,000	By Interest on income tax Refund	6,000
To Carriage inward	20,000	By Rent from house property	40,000
To Advertisement	30,000		
To Interest	2,000		
To Carriage outward	38,000		
To Depreciation	50,000		
To Provision for income tax	20,000		
To Compensation paid to director	1,00,000		
To Provision for bad debt	10,000		
To Audit fees	20,000		
To Bad debt	30,000		
To Traveling expenses	25,000		
To Municipal tax	5,000		
To Net profit	4,46,000		
	23,61,000		23,61,000

Additional information:

- (a) Minakshi, holder of 21% share, sold goods to the company for ₹ 40,000 though market value is lower by ₹ 10,000. Payment to her made by way of bearer cheque.
- (b) Advertisement expenses relate to purchase of a machinery for advertisement. Depreciation allowed on such machinery is ₹ 2,250.
- (c) Ritu, holder of 21% share, purchased goods from the company for ₹ 30,000 though market value is ₹ 35,000. She made payment by way of bearer cheque.
- (d) Purav, who supplies more than 25% of goods, sold goods to company for ₹ 10,000 however, market value of such goods was ₹ 8,000.
- (e) Outstanding salary ₹ 20,000 is paid on 30-12-2018.
- (f) Bonus is not paid till due date of furnishing return.
- (g) Provision for bad debts is in excess of ₹ 1,000.
- (h) Salary paid in excess of requirement to non-relative ₹ 2,000 and to relative of director ₹ 6,000.
- (i) Traveling expenses is on traveling of Minakshi for 10 days out of which she used 8 days for acquiring a new machine from Jaipur for company and 2 days for meeting her relative. However, Minakshi agreed to refund proportionate cost.
- (j) On 31-7-2017, company purchased a machine from Jaipur costing ₹ 5,00,000.

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- (k) Customs duty paid on 30-11-2018. However, company paid ₹ 5,000 on 30-7-2017 outstanding customs duty of earlier year
- (l) Company incurred capital expenditure of ₹ 1,00,000 for promoting family planning among its workers.
- (m) Carriage inward shows the expenditure incurred for acquiring machine from Jaipur.
- (n) Interest paid is related to loan taken for purchasing debenture.
- (o) As on 1-4-2017, company holds following assets –

Assets	Rate	Value
Plant & Machinery	15%	6,00,000
Furniture	10%	1,00,000

Compute gross total income for assessment year 2018-19. Ignore provision of sec. 115JB.

[16]

Answer:

Computation of gross total income of Minakshi Ltd. for the A.Y. 2018-19

Particulars	Notes	Details	Amount	Amount
Income from house property				
Gross Annual value (Rent received)			40,000	
Less: Municipal tax			5,000	
Net annual value (NAV)			35,000	
Less: Standard deduction u/s 24(a) [30% of NAV]			10,500	24,500
Profits & gains of business or profession				
Net profit as per Profit and Loss A/c			4,46,000	
Add: Expenditure disallowed but debited in P/L A/c				
Depreciation	1	50,000		
Provision for income tax	2	20,000		
Provision for bad debt	3	10,000		
Municipal tax	4	5,000		
Excessive payment to Minakshi	5	10,000		
Cash payment to Minakshi in excess of ₹ 10,000	6	30,000		
Advertisement expenditure	7	30,000		
Bonus	8	15,000		
Excess payment of salary to relative of director	9	6,000		
Travelling expenses	10	25,000		
Customs duty	11	1,70,000		
Carriage inward	10	20,000		
Interest	12	2,000	3,93,000	
			8,39,000	
Less: Expenditure allowed but not debited to P/L A/c				
Customs duty of earlier years	11	5,000		
Expenditure on promoting family planning among employees	13	20,000		
Depreciation u/s 32	1	2,91,250		
Less: Income taxable under other head but credited in P/L A/c				
Rent from house property	14	40,000		
Interest on debenture	14	10,000		
Interest on refund of income tax	14	6,000	3,72,250	4,66,750

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Income from other sources				
Interest on debenture		10,000		
Less: Interest on borrowed capital	12	2,000	8,000	
Interest on refund of income tax			6,000	14,000
Gross Total Income				5,05,250

Notes —

1. Depreciation is allowed as per Income tax Act being calculated as under -

Particulars	Details	Amount										
Block 1: Plant and Machinery @ 15%												
W.D.V. as on 1/4/2017	6,00,000											
Add: Purchase during the year	5,40,000 [#]											
	11,40,000											
Less: Sale during the year	-											
	11,40,000											
Depreciation @ 15% [₹ 11,40,000 x 15%]	1,71,000											
Additional depreciation @ 20% [₹ 5,40,000 x 20%]	1,08,000	2,79,000										
Block 2: Furniture @ 10%												
W.D.V. as on 1/4/2017	1,00,000											
Add: Purchase during the year	-											
	1,00,000											
Less: Sale during the year	-											
	1,00,000											
Depreciation @ 10% [₹ 1,00,000 x 10%]		10,000										
On machinery for advertisement		2,250										
Depreciation allowed u/s 32		2,91,250										
[#] Computation of actual cost of machinery purchased during the year - <table style="width: 100%; margin-top: 5px;"> <thead> <tr> <th style="width: 60%;">Particulars</th> <th style="width: 40%;">Amount</th> </tr> </thead> <tbody> <tr> <td>Purchase cost</td> <td style="text-align: center;">5,00,000</td> </tr> <tr> <td>Carriage inward</td> <td style="text-align: center;">20,000</td> </tr> <tr> <td>Traveling cost *</td> <td style="text-align: center;">20,000</td> </tr> <tr> <td>Actual cost of purchased machinery</td> <td style="text-align: center;">5,40,000</td> </tr> </tbody> </table> <p>* Since traveling cost for 10 days was ₹ 25,000. Hence cost for 8 days (used for acquiring the new machine) is ₹ 20,000.</p>			Particulars	Amount	Purchase cost	5,00,000	Carriage inward	20,000	Traveling cost *	20,000	Actual cost of purchased machinery	5,40,000
Particulars	Amount											
Purchase cost	5,00,000											
Carriage inward	20,000											
Traveling cost *	20,000											
Actual cost of purchased machinery	5,40,000											

2. Income tax is not allowed u/s 40(a).
3. Any anticipatory loss is not allowed.
4. Municipal tax is not allowed as deduction from business income but allowed from Income from house property.
5. Since Minakshi has a substantial interest in the company, hence, excessive payment is disallowed u/s 40A(2).
6. Payment of allowed expenditure otherwise than by account payee cheque or demand draft in excess of ₹ 10,000 shall be disallowed u/s 40A(3).
7. Any capital expenditure is not allowed.
8. By virtue of sec. 43B, bonus to employees is allowed as deduction on payment basis.
9. Excessive payment to relative of director is disallowed [Sec. 40A(2)].
10. Since traveling expenditure and carriage inward is related to acquisition of machine, hence the same should be added with the cost of machine. Further, personal expenditure of Minakshi being refundable shall not be treated as expenditure.
11. By virtue of sec. 43B, customs duty is allowed as deduction on payment basis.

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12. Interest on loan taken for acquisition of debenture is deductible from income from debenture.
13. Any capital expenditure on promoting family planning among employees by a company is allowed in 5 equal installments [Sec. 36(1)(ix)].
14. Rent from house property is taxable under the head Income from house property, whereas interest income (including interest on income tax refund) is taxable under the head Income from other sources.
15. Any excessive payment received from a person who has substantial interest is not governed by sec. 40A(2).
16. A person supplying 25% of raw material is not treated as person who holds substantial interest. Hence excessive payment to Purav is allowed.
17. Compensation paid to director shall be allowed u/s 37(1).
18. Sec. 43B covers bonus and commission paid to employee but does not cover salary paid to employee.

4.(a) A is an association governed by the provisions of sec. 44A of the Income-tax act. The subscription receipts for the year ended 31st March, 2018 were ₹ 60,000. The expenditure in the normal course of its activities was ₹ 85,000. Its other income taxable under the Act works out to ₹ 75,000. On these facts, you are consulted as to:

- A. How A's taxable income will be determined for assessment year 2018-2019.**
- B. In case the association did not have the other income taxable will there be any difference in the computation of its income? [8]**

(b) Bright Ltd. incurred ₹ 52.75 lakhs during the period April, 2017 to June, 2017 on advertisement, professional fees, administration cost, etc. for the purpose of public issue of ₹ 55 crore in July, 2017 and had, therefore, accounted all such expenses under the head 'share issue expenses'. However, the clearance for the public issue was not given by SEBI. The company in its return of income filed for the year ended 31st March, 2018 had claimed such expenses as revenue expenses which were disallowed by the Assessing Officer. The company seeks your opinion. Advise. [8]

Answer:

(a) Computation of total income

Particulars	Amount
Other Income	75,000
Less: Deficiency (Note 1)	25,000
Total Income	50,000

Note 1: Calculation of deficiency

Particulars	Amount
Subscription received	60,000
Less: Expenditure	85,000
Deficiency	25,000
Maximum deficiency can be set off against other income is lower of the following:	
a. Actual Deficiency i.e. ₹ 25,000	
b. 50% of other income i.e., ₹ 37,500 being 50% of ₹ 75,000	

In case, association do not have any other taxable income, then the total income shall be nil and the deficiency of ₹ 25,000 shall not be carried forward.

(b) Allowability of the expenses in similar facts has been examined by the Hon'ble Bombay High Court in the case of M/s Nimbus Communications Ltd. Hon'ble Bombay High Court has held that the assessee has incurred the expenditure and that on account of the aborted public issue offer, no new asset has come into existence and consequently there is no question of the assessee getting any enduring benefit. With the approval of SEBI, the assessee was to increase the share capital and thereby promote its business activity. However, the same got aborted due to reasons beyond its control. In these circumstances, the aborted share issue expenditure should be allowed u/s 37.

Earlier, similar view has also been taken by the Hon'ble Bombay High Court in CIT -vs.- Essar Oil Limited.

5.(a) Critically comment with the help of a case law:

“Tips collected by hotel from customers and paid to employees couldn't be taxable as salary and hence TDS u/s 192 is not applicable”. **[8]**

(b) Write brief note on ICDS – II. **[8]**

Answer:

(a) The assessees are engaged in the business of owning, operating, and managing hotels. Surveys conducted at the business premises of the assessees allegedly revealed that the assessees had been paying tips to its employees but not deducting taxes thereon. The Assessing Officer treated the receipt of the tips as income under the head “salary” in the hands of the various employees and held that the assessees were liable to deduct tax at source from such payments u/s 192. The assessees were treated by the Assessing Officers as assessee-in-default u/s 201(1). The Assessing Officers in various assessment orders worked out the different amounts of tax to be paid by all the aforesaid assessees u/s 201(1), as also interest. The CIT (Appeals) allowed the various appeals of the assessees holding that the assessees could not be treated as assessee-in-default u/s 201(1) for non-deduction of tax on tips collected by them and distributed to their employees. Appeals filed by the Revenue to the Income Tax Appellate Tribunal (ITAT) came to be dismissed by the Tribunal. Against the said orders of the Tribunal, appeals were preferred by the Revenue to the High Court.

The High Court held, after considering Sections 15, 17 and 192 of the Income Tax Act, that tips would amount to ‘profit in addition to salary or wages’ and would fall under Section 15(b) read with Section 17(1)(iv) and 17(3)(ii). Even so, the High Court held that when tips are received by employees directly in cash, the employer has no role to play and would therefore be outside the purview of Section 192 of the Act. However, the moment a tip is included and paid by way of a credit card by a customer, since such tip goes into the account of the employer after which it is distributed to the employees, the receipt of such money from the employer would, according to the High Court, amount to “salary” within the extended definition contained in Section 17 of the Act.

The Apex Court held that first and foremost, under sec. 192(1) thereof, “any person responsible” for paying any income chargeable under the head “salaries” is alone brought into the dragnet of deduction of tax at source. The person responsible for paying an employee an amount which is to be regarded as the employee's income is only the employer. In the facts of the present case, the person who is responsible for paying the employee is not the employer at all, but a third person – namely, the customer.

Also, if an employee receives income chargeable under a head other than the head “salaries”, then Section 192 does not get attracted at all. Income from tips would be

chargeable in the hands of the employees as income from other sources, such tips being received from customers and not from the employer, Section 192 would not get attracted at all on the facts of the present case.

Further, there should be a vested right in an employee to claim any salary from an employer or former employer, whether due or not if paid; or paid or allowed, though not due. There is no vested right in the employee to claim any amount of tip from his employer. Tips being purely voluntary amounts that may or may not be paid by customers for services rendered to them would not, therefore, fall within Section 15(b) at all.

Section 15(b) necessarily has reference to the contract of employment between employer and employee, and salary paid or allowed must therefore have reference to such contract of employment. The amount of tip paid by the employer to the employees has no reference to the contract of employment at all. Tips are received by the employer in a fiduciary capacity as trustee for payments that are received from customers which they disburse to their employees for service rendered to the customer. There is, therefore, no reference to the contract of employment when these amounts are paid by the employer to the employee.

(b) ICDS II: Valuation of Inventories:

Scope:

- ⊗ This Standard shall be applied for valuation of inventories, except
 - i. Work-in-progress arising under 'construction contract'
 - ii. Work-in-progress which is dealt with by other Standard
 - iii. Shares, debentures and other financial instruments held as stock-in-trade¹
 - iv. Producers' inventories of livestock, agriculture and forest products, mineral oils, ores and gases to the extent that they are measured at net realisable value
 - v. Machinery spares, which can be used only in connection with a tangible fixed asset and their use is expected to be irregular²

Measurement:

- ⊗ Inventories shall be valued at cost, or net realisable value, whichever is lower.
 - Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Cost of Inventories:

- ⊗ Cost of inventories shall comprise of all costs of purchase, costs of services, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.
 - The costs of purchase shall consist of purchase price including duties and taxes, freight inwards and other expenditure directly attributable to the acquisition. Trade discounts, rebates and other similar items shall be deducted in determining the costs of purchase
 - The costs of services shall consist of labour and other costs of personnel directly engaged in providing the service including supervisory personnel and attributable overheads.
 - The costs of conversion of inventories shall include costs directly related to the units of production and a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods.

¹ Refer ICDS on Securities

² Refer ICDS on Tangible Fixed Assets

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- Other costs shall be included in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.
- Interest and other borrowing costs shall not be included in the costs of inventories, unless they meet the criteria for recognition of interest as a component of the cost as specified in the Income Computation and Disclosure Standard on borrowing costs.
- In determining the cost of inventories, the following costs shall be excluded
 - a. Abnormal amounts of wasted materials, labour, or other production costs;
 - b. Storage costs, unless those costs are necessary in the production process prior to a further production stage;
 - c. Administrative overheads that do not contribute to bringing the inventories to their present location and condition;
 - d. Selling costs.

Cost Formulae:

- ⊗ The standard recognizes 3 cost formulae viz. (i) Specific Identification Method; (ii) First-in-First-Out Method (FIFO); (iii) Weighted Average Method

Change of Method of Valuation of Inventory:

- ⊗ The method of valuation of inventories once adopted by a person in any previous year shall not be changed without reasonable cause

Disclosure:

- ⊗ Following shall be disclosed:
 - a. the accounting policies adopted in measuring inventories including the cost formulae used; and
 - b. the total carrying amount of inventories and its classification appropriate to a person.

6.(a) Mahesh, aged 64 years, is resident and ordinarily resident in India. His income is ₹ 16,80,000 from a business in India and ₹ 5,45,000 from a business in a foreign country with whom India has agreement for avoidance of double taxation (ADT). According to the ADT agreement, income is taxable in the country in which it is earned and not in other country. However, in the other country, such income can be included for computation of tax rate.

According to the tax laws of the foreign country, Mahesh has paid ₹ 32,000 as tax in that country. During the previous year, Mahesh has paid ₹ 28,000 as tuition fee for his daughter in India and ₹ 90,000 as tuition fee for his son outside India for full time education. Mahesh has also received an interest of ₹ 48,000 on Government securities. Find out the tax liability of Mahesh for the assessment year 2018-19. [8]

(b) Write short note on “berry ratio”. [8]

Answer:

(a) Computation of Total Income of Mahesh for the Assessment Year 2018-19

Particulars	₹
Business income in India	16,80,000
Interest on Government Securities	48,000
Gross Total Income	17,28,000

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Less: Deduction u/s 80C	28,000
Total Income	17,00,000
Add: Foreign income to be included for rate purpose	5,45,000
Total	22,45,000
Tax on above	4,98,005
Less: Relief u/s 90 [$\text{₹ } 5,45,000 \times 22.18\%$]	1,20,881
Tax Payable (Rounded off)	3,77,120

¹Average rate of tax = $\text{₹ } 4,98,005 / \text{₹ } 22,45,000 \times 100 = 22.18\%$

(b) Berry ratio is the ratio of gross profit to operating expenses. It measures the return on operating expenses. As the functions performed by the tax-payers are often reflected in the operating expenses, this ratio determines the relationship of the income earned in relation to the functions performed. This ratio helps in overcoming the difficulties in applying the RPM, which does not explain the creation of gross profit. This ratio is used in conducting an arm's length analysis of service-oriented industry such as limited risk distributor, advertising, marketing and engineering services. The Berry ratio may be used to test whether service providers have earned enough mark-up on their operating expenses. In essence, the Berry ratio implicitly assumes that there is a relationship between the level of operating expenses and the level of gross profits earned by routine distributors and service providers.

7.(a) J Inc. of Korea and CD Ltd, an Indian Company are associated enterprises. CD Ltd manufactures Cell Phones and sells them to J.K. & F Inc., a Company based at Nepal. During the year CD Ltd. supplied 2,50,000 Cellular Phones to J Inc. Korea at a price of ₹ 3,000 per unit and 35,000 units to JK & F Inc. at a price of ₹ 5,800 per unit. The transactions of CD Ltd with JK & F Inc. are comparable subject to the following considerations:

Sales to J Inc. are on FOB basis, sales to JK & F Inc. are CIF basis. The freight and insurance paid by J Inc. for each unit @ ₹ 700. Sales to JK & F Inc. are under a free warranty for Two Years whereas sales to J Inc. are without any such warranty. The estimated cost of executing such warranty is ₹ 500. Since J Inc.'s order was huge in volume, quantity discount of ₹ 200 per unit was offered to it.

Compute the Arm's Length Price and the subsequent amount of increase in the Total Income of CD Ltd, if any. [8]

(b) How to compute total undisclosed foreign income and asset u/s 5 of Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015? [8]

Answer:

(a) Computation of Arm's Length Price of Products sold to J Inc. Korea by CD Ltd

Particulars	₹	₹
Price per Unit in a Comparable Uncontrolled Transaction		5,800
Less: Adjustment for Differences -		
(1) Freight and Insurance Charges	700	
(2) Estimated Warranty Costs	500	
(3) Discount for Voluminous Purchase	200	(1,400)
Arms's Length Price for Cellular Phone sold to J Inc. Korea		4,400

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Computation of Increase in Total Income of CD Ltd

Particulars	₹
Arm's Length Price per Unit	4,400
Less: Price at which actually sold to J Inc. Korea	(3,000)
Increase in Price per Unit	1,400
No. of Units sold to J Inc. Korea	2,50,000
Increase in Total Income of CD Ltd (2,50,000 x ₹ 1,400)	₹ 35 Crores

(b)

- ✳ In computing the total undisclosed foreign income and asset of any previous year of an assessee:
 - ☛ No deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee, whether or not it is allowable in accordance with the provisions of the Income-tax Act.
 - ☛ Any income,—
 1. which has been assessed to tax for any assessment year under the Income-tax Act prior to the assessment year to which this Act applies; or
 2. which is assessable or has been assessed to tax for any assessment year under this Act,shall be reduced from the value of the undisclosed asset located outside India, if, the assessee furnishes evidence to the satisfaction of the Assessing Officer that the asset has been acquired from the income which has been assessed or is assessable, as the case may be, to tax.
- ✳ The amount of deduction in case of an immovable property shall be the amount which bears to the value of the asset as on the first day of the financial year in which it comes to the notice of the Assessing Officer, the same proportion as the assessable or assessed foreign income bears to the total cost of the asset.

Illustration:

A house property located outside India was acquired by an assessee in the previous year 2009-10 for ₹ 50 lakhs. Out of the investment of ₹ 50 lakhs, ₹ 20 lakhs was assessed to tax in the total income of the previous year 2009-10 and earlier years. Such undisclosed asset comes to the notice of the Assessing Officer in the year 2018-19. If the value of the asset in the year 2018-19 is ₹ 1 crore, the amount chargeable to tax shall be ₹ 60,00,000 i.e.,:

$$₹ 1,00,00,000 - (₹ 20,00,000 / ₹ 50,00,000) = ₹ 60,00,000$$

8. Write short note:

[4x4=16]

- (a) Power of income tax authority u/s 131
- (b) Revision u/s 263
- (c) Factor for determining Most Appropriate Method
- (d) 'Case' in light of provision of settlement commission

Answer:

(a) Power regarding discovery, production of evidence, etc. [Sec. 131]

Power of income tax authority while trying a suit:

The income-tax authority [being Assessing Officer, Deputy Commissioner (Appeals), Joint Commissioner, Commissioner (Appeal), Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner and the Dispute Resolution Panel] have the same

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powers as are vested in a court under the Code of Civil Procedure, 1908, when trying a suit in respect of the following matters —

- i. Discovery and inspection;
- ii. Enforcing the attendance of any person, including any officer of a banking company and examining him on oath;
- iii. Compelling the production of books of account and other documents; and
- iv. Issuing commissions

Power before initiating search and seizure u/s 132 [Sec. 131(1A)]:

The income-tax authority [being Principal Director-General or Director-General or Principal Director or Director or Joint-Director or Assistant Director or Deputy Director or any authorized officer referred u/s 132(1)] before taking any action u/s 132, can exercise above power if he has reason to suspect that any income has been concealed (or is likely to be concealed), by any person (or class of persons), within his jurisdiction and for the purposes of making any enquiry or investigation relating thereto, it shall be competent for him to exercise above powers.

Taxpoint:

- Above action can be taken even though no proceedings with respect to such person is pending before any income-tax authority.
- In case inquiry (even no proceedings are pending) or investigation is related to an agreement referred to in sec. 90 or 90A, such power can be exercised by any notified income-tax authority (not below the rank of Assistant Commissioner) [Sec. 131(2)]

Power to impound or retain books [Sec. 131(3)]:

Any income tax authority [referred in sec. 131(1) or (1A) or (2)] may impound and retain in its custody any books of account or other documents produced before it in any proceedings under this Act. However, an Assessing Officer or an Assistant Director or Deputy Director shall not -

- a) Impound any books of account or other documents without recording his reasons for doing so; or
- b) Retain in his custody any such books or documents for a period exceeding 15 days (*exclusive of holidays*) without obtaining (prior) approval of the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General or Principal Commissioner or Commissioner or Principal Director or Director.

(b) Revision of order prejudicial to the revenue [Sec. 263]

Orders which may be revised	<p>Any order passed by the Assessing Officer, which is -</p> <ol style="list-style-type: none"> a) Erroneous; b) Prejudicial to the interests of the revenue; and c) Passed by an authority subordinate to the Principal Commissioner or Commissioner. <p>Notes</p> <ol style="list-style-type: none"> a) Orders passed by the Assessing Officer includes - <ol style="list-style-type: none"> i. An order of assessment made by the Assistant Commissioner on the basis of the directions issued by the Joint Commissioner u/s 144A; ii. An order made by the Joint Commissioner as an Assessing Officer. b) Even an intimation u/s 143(1) can be revised <p><i>Taxpoint</i></p>
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	<ul style="list-style-type: none"> - Order made by the Assessing Officer after making proper enquiries and considering relevant details and decisions of Supreme Court cannot be said to be erroneous and prejudicial to the interest of the revenue, hence such order cannot be revised. - An order passed by the Assessing Officer shall be deemed to be erroneous in so far as it is prejudicial to the interests of the revenue, if, in the opinion of the Principal Commissioner or Commissioner: <ol style="list-style-type: none"> a) the order is passed without making inquiries or verification which should have been made; b) the order is passed allowing any relief without inquiring into the claim; c) the order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or d) the order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person
<p>Treatment of an order, which is subject matter of the appeal</p>	<p>Revision u/s 263 of an order, which is subject matter of appeal, cannot be made.</p> <p>Notes:</p> <ul style="list-style-type: none"> • The Principal Commissioner or Commissioner can revise such order (which has been a subject matter of appeal) which had not been considered and decided in such appeal. <p>E.g., From the perusal of the order u/s 143(3) passed by the Assessing Officer following was observed:</p> <ul style="list-style-type: none"> – Point A: Against the assessee – Point B: In favour of the assessee <p>The assessee being aggrieved with point A in the order passed by the Assessing Officer, preferred an appeal to the Commissioner (Appeals). However, the Commissioner wants to revise the order u/s 263 for point B (subject to other conditions being fulfilled). It is possible as doctrine of partial merger of the order is applicable in case of sec. 263. However, the Commissioner cannot revise the order for point A (as the same is subject matter of an appeal)</p> <ul style="list-style-type: none"> • An order cannot be said to have been made subject of an appeal if the appeal has been disposed of by the appellate authority without passing an order
<p>Procedure to be followed</p>	<ol style="list-style-type: none"> 1. Examination of Records: The Principal Commissioner or Commissioner may call for and examine the records of any proceeding under the Act. If he considers that any order passed by the Assessing Officer is prejudicial to the interest of the revenue, he can revise and rectify the assessment. <u>Record</u> shall include all records relating to any proceeding under this Act available at the time of examination by the Principal Commissioner or Commissioner. This means that any material, which was not available at the time of assessment but available at the time of examination by the Principal Commissioner or Commissioner, shall also be considered for order u/s 263. 2. Inquiry: He must make or cause to be made such inquiry as he deems necessary. 3. Opportunity of being heard: No revision order shall be passed u/s

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	263 without giving the assessee an opportunity of being heard. 4. Order: Finally, he may pass such revision order as the circumstances of the case justify including an order enhancing, modifying or cancelling the assessment and directing a fresh assessment.
Time limit for passing revision order	2 years from the end of the financial year in which the order sought to be revised was passed. In computing the above period of limitation following period shall be excluded - <ul style="list-style-type: none"> • Time taken in giving an opportunity to the assessee of being re-heard u/s 129; & • Any period during which any proceeding under this section is stayed by an order or injunction of any court. Exception: There is no time limit for passing a revision order to give effect to, or in consequence of, an order of the ITAT, the High Court or the Supreme Court.
Appeal against order u/s 263	A revisional order passed by the Principal Commissioner or Commissioner u/s 263 can be appealed to the Tribunal.
Sec.263 vs. sec.154: Principal Commissioner or Commissioner can exercise the power even in a case where the issue is debatable. Revisional power u/s 263 is not comparable with the power of rectification of mistake u/s 154	

(c) Factor for determining Most Appropriate Method:

As per Rule 10C, the most appropriate method shall be the method which is best suited to the facts and circumstances of each particular international transaction or specified domestic transaction, and which provides the most reliable measure of an arm's length price in relation to the international transaction or specified domestic transaction. In selecting the most appropriate method, the following factors shall be taken into account:

1. the nature and class of the international transaction or specified domestic transaction;
2. the class or classes of associated enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises;
3. the availability, coverage and reliability of data necessary for application of the method;
4. the degree of comparability existing between the international transaction or specified domestic transaction and the uncontrolled transaction and between the enterprises entering into such transactions;
5. the extent to which reliable and accurate adjustments can be made to account for differences, if any, between the international transaction or specified domestic transaction and the comparable uncontrolled transaction or between the enterprises entering into such transactions;
6. the nature, extent and reliability of assumptions required to be made in application of a method.

(d) "Case" in light of provision relating to Settlement Commission:

Case means any proceeding for assessment, of any person in respect of any assessment year or assessment years which may be pending before an Assessing Officer on the date on which an application is made.

Taxpoint:

1. A proceeding for assessment or reassessment or recomputation u/s 147 shall be deemed to have commenced:
 - A. from the date on which a notice u/s 148 is issued for any assessment year;
 - B. from the date of issuance of the notice referred above, for any other assessment year or assessment years for which a notice u/s 148 has not been issued, but such notice could have been issued on such date, if the return of income for the other assessment year or assessment years has been furnished u/s 139 or in response to a notice u/s 142;
2. A proceeding for making fresh assessment in pursuance of an order u/s 254 or sec. 263 or sec. 264, setting aside or cancelling an assessment shall be deemed to have been commenced from the date on which such order, setting aside or cancelling an assessment was passed;
3. A proceeding for assessment or reassessment for any of the assessment years u/s 153A / 153C shall be deemed to have commenced on the date of issue of notice initiating such proceeding and concluded on the date on which the assessment is made;
4. A proceeding for assessment for any assessment year, other than aforesaid proceedings shall be deemed to have commenced from the date on which the return of income for that assessment year is furnished u/s 139 or in response to a notice served u/s 142 and concluded on the date on which the assessment is made; or on the expiry of the time specified for making assessment u/s 153(1), in case where no assessment is made.