Roll No. ............................ NOV 2018

FINAL
GROUP-II PAPER-7
DIRECT TAX LAWS

Total No. of Questions – 7

Total No. of Printed Pages – 15

Time Allowed – 3 Hours

Maximum Marks – 100

# ACM

Answers to questions are to be given only in English except in the case of candidates who have opted for Hindi Medium. If a candidate has not opted for Hindi Medium, his/her answers in Hindi will not be valued.

Question No. 1 is compulsory.

Answer any **five** questions from the remaining **six** questions.

Working notes should form part of the respective answers.

All questions relate to **Assessment year 2018-2019**, unless stated otherwise in the question.

**Marks**

1. (a) Zenith Formulations Ltd., an Indian Company engaged in pharmaceutical formulations in Tamilnadu, started adoption of Ind AS compliance with effect from 1st April, 2016. The following particulars are furnished for the year ended 31st March, 2018 :- **10**

(i) The book profits after adjustments of all items specified in section 115JB(2) amounted to ₹ 52.26 lakhs (except the adjustment for brought forward losses), for the year ended 31.3.2018.

(ii) Brought forward losses as per books are as under : (₹ In lakhs)

| Financial Year | Business loss | Depreciation |
|---|---|---|
| 2014-15 | 4.60 | 4.90 |
| 2015-16 | 1.75 | 2.20 |

(iii) The business loss of ₹ 4.60 lakhs and ₹ 1.75 lakhs have been deducted while computing book profits under section 115JB for the assessment years 2016-17 & 2017-18 respectively.

Marks

(iv) The particulars of Other Comprehensive Income for the year ended 31.03.2018 : (₹ In lakhs)

| A : Other Comprehensive Income (OCI) that may be re-classified to profit and loss : | Debit | Credit |
|---|---|---|
| (i) Deferred gain Cash flow hedges | | 5.50 |
| (ii) Deferred costs of hedging | 1.00 | |
| (iii) Comprehensive income from discontinued operations | | 4.20 |
| (iv) Exchange Differences of foreign exchange operations | 2.30 | |
| **TOTAL** | **3.30** | **9.70** |

| B : Other Comprehensive Income (OCI) that will not be re-classified to profit and loss : | Debit | Credit |
|---|---|---|
| (i) Changes in fair values of equity instruments | 10.00 | |
| (ii) Deferred gains on cash flow hedges | | 7.25 |
| (iii) Deferred costs of hedging | 4.10 | |
| (iv) Share of other comprehensive income of other associates | | 3.20 |
| (v) Remeasurements of post employment benefit obligations | | 4.45 |
| (vi) Revaluation surplus for assets | | 7.50 |
| **TOTAL** | **14.10** | **22.40** |

Marks

(v) The transition amount as on convergence date (01-04-2016) stood at ₹ 52.50 lakhs (credit balance) including capital reserve of ₹ 8 lakhs and adjustment of ₹ 4.50 lakhs relating to transition difference in a foreign operation.

(vi) The National Company Law Tribunal (NCLT), Chennai Bench has admitted an application under section 7 of Insolvency and Bankruptcy Code, 2016 (IBC) made by financial creditor against the company for initiation of Corporate Insolvency Resolution Process on 30th March, 2018.

(1) Compute the MAT liability for the assessment year 2018-19, applying the provisions relating to Ind AS compliant companies.

(2) Assuming that the Income tax under normal provisions of Income Tax Act, 1961 for the assessment year 2018-19 works out to ₹ 9.20 lakhs, compute the tax credit, if any, to be carried forward by the company including the period up to which it will be available to be carried forward.

(b) SOL Inc, a notified Foreign Institutional Investor (FII) derived the following incomes from various sources for the financial year 2017-18 :- **10**

(1) Income in respect of securities : ₹ 28,50,000

Expenses incurred in respect thereof : ₹ 50,000

(The above income includes an interest of ₹ 16,00,000 received from an Indian Company on the investment of rupee denomination bonds and dividend income of ₹ 3,50,000 from a domestic company referred to in section 115-O).

Marks

(2) Capital Gains :

(i) Long Term :

| | |
|---|---|
| Sale proceeds on sale of securities on 15.01.2018 : | ₹ 52,00,000 |
| Purchase cost of securities on 25.05.2014 : | ₹ 28,00,000 |
| Cost Inflation Index : 2014-15 : 240; 2017-18 : 272 | |

(ii) Short Term :

| | |
|---|---|
| Sale proceeds of equity shares of Company A (Jan., 18) : | ₹ 13,50,000 |
| (STT paid on Company A shares) | |
| Cost of acquisition (Aug., 2017) : | ₹ 5,50,000 |
| Sale proceeds of equity shares of Company B (Dec., 17) | ₹ 9,25,000 |
| Cost of acquisition (April, 2017) : | ₹ 4,85,000 |
| (STT not paid on Company B Shares) | |

Compute the taxable income of SOL Inc and tax liability for the assessment year 2018-19 as per applicable provisions of the Income Tax Act, 1961, assuming that no other income is derived by SOL Inc (FII) during the financial year 2017-18.

2. Statement of Profit and Loss account of BAS Industries Ltd. engaged in production and marketing of diversified products, shows a net profit (before tax) of ₹ 72,00,000 for the financial year ended 31st March, 2018 after charge of the following items : 16

**A : Items debited to the Statement of Profit and Loss :**

(i) Depreciation as per Companies Act, 2013 : ₹ 24,00,000

(ii) Interest amounting to ₹ 60,000 for short payment of advance tax paid as per section 234 B relating to the assessment year 2016-17.

(iii) Interest and borrowing costs amounting to ₹ 9,50,000 and ₹ 7,00,000 though not meeting the criteria for recognition as a component of cost, included in cost of Opening and Closing inventory respectively.

 Marks

(iv) Expenditure of ₹ 41,000 paid in cash comprising of ₹ 22,000 directly paid to producer of dairy farming products and ₹ 19,000 paid towards printing and stationery items to a trader.

(v) ₹ 3,50,000 paid to a contractor for carrying out repair work at factory premises. Tax was not deducted at source on this payment.

(vi) ₹ 35,000 towards expenditure for earning income from transfer of carbon credits.

(vii) Contribution to electoral trust : ₹ 3,00,000 paid by way of cheque.

(viii) Expenditure towards advertising charges in a brochure of a political party registered under section 29A of Representation of People Act, 1951 : ₹ 40,000 paid by way of cheque.

(ix) Interest on term loans obtained from Cooperative Bank not paid before the due date of filling of return of income : (due date being 30.09.2018) : ₹ 2,60,000

(x) Actual contribution to the pension scheme of employees : ₹ 1,50,000

**B : Items credited to the Statement of Profit and Loss :**

(i) Unrealised rent of ₹ 3,80,000 pertaining to financial year 2014-15 & 2015-16 recovered during the year in respect of a commercial property owned by the company, which was sold by the company on 23.03.2017.

(ii) Dividends from a specified foreign company including the expenditure of ₹ 20,000 incurred on earning such dividends : ₹ 1,60,000

(iii) Profit of ₹ 3,00,000 received from hedging contract entered into for meeting out loss in foreign currency payments towards an imported printing machinery valued at ₹ 95 lakhs, installed on 15th December, 2017 and put to use from that date.

(iv) Interest from banks on fixed deposits net of TDS at 10% : ₹ 1,35,000

Marks

**Additional Information :**

(1) Depreciation as per Income tax rules : ₹ 28,00,000 exclusive of depreciation on the imported printing machine referred to in item B (iii)

(2) Expenditure pertaining to previous financial year allowed on due basis, but paid in current financial year in cash on 18.01.2018 : ₹ 35,000

(3) Audit fee for the previous year 2016-17 : ₹ 75,000. TDS deducted but not paid in the relevant previous year. However TDS was paid on 31.12.2017.

(4) Income from transfer of Carbon Credits amounting to ₹ 4,00,000 included in Net Profit (before tax).

(5) The eligible salary and dearness allowance for the pension scheme referred to under section 80 CCD is ₹ 10,00,000.

Compute the total income of BAS Industries Ltd., for assessment year 2018-19. Give brief reasons for the treatment given to each of the items taken considered in computation of income of the company.

3. (a) Examine in the context of provisions contained under the Income Tax Act, 1961 each of the following independent cases and state in brief whether there exists business connection in each of the cases in India so as to bring the income earned, if any to tax net in India :- 6

(i) ABC Ltd. a Company resident in Dubai had setup a liaison office at Mumbai to receive trade inquiries from customers in India. The work of the liaison office is not only restricted to forwarding of the trade inquiries to ABC Ltd. but the liaison office also negotiates and enters into the contracts on behalf of ABC Ltd. with the customers in India.

Marks

(ii) XYZ Inc. a resident of USA has set up a branch at Hyderabad for the purpose of purchase of raw materials for manufacturing its products. The branch office is also engaged in selling the products manufactured by XYZ Inc. and in providing sales related services to customers in India on behalf of XYZ Inc.

(iii) Mr. Rajesh, a resident in India and based at Delhi is appointed as an agent by PQR Inc. a company incorporated in UK for tracking the Indian markets. He was canvassing the orders and then communicating to PQR Inc. in UK. He had no authority to accept the orders. All the orders were directly received, accepted and after receipt of the price/value, the delivery of goods was given by PQR Inc. outside India. No purchase of raw material or manufacturing of finished goods took place in India. The agent was entitled to receive the commission on the sales so concluded by PQR Inc.

(b) Mr. Rameshwarm, a non-resident Indian acquired/purchased shares in foreign currency of a company XYZ Ltd. on 1.1.2008 for ₹ 10,00,000. These shares were sold by him in the recognized stock exchange through a broker on 1.1.2017 for ₹ 30,00,000. The amount of sales consideration of the shares of ₹ 30,00,000 so received by him was again invested in purchase of shares of other company ABC Ltd. on 31.03.2017. The shares of ABC Ltd. purchased on 31.03.2017 were also sold by him on 30.06.2017 for ₹ 35,50,000. Discuss the tax implications relating to the two transactions of sales of the shares in the relevant assessment years under the Income Tax Act, 1961 by ignoring the effect of first proviso to section 48. **4**

Marks

(c) Examine whether General Anti-Avoidance Rules (GAAR) can be invoked to deny the treaty benefit in the following case, assuming that all other conditions prescribed for application of GAAR are being satisfied :- **3**

X Pvt. Ltd. a domestic Indian Company and Y Pvt. Ltd. (100% subsidiary of YAN Ltd.) located in country "A" formed a joint venture company XY Pvt. Ltd. in India on 01.04.2017. As per the joint venture agreement, 51% of shares are held by X Pvt. Ltd. and 49% are held by Y Pvt. Ltd in XY Pvt. Ltd. There is no other business activity in Y Pvt. Ltd.

Y Pvt. Ltd. is designated as Permanent Transferee of YAN Ltd. Permanent Transferee means though shares of XY Pvt. Ltd. are held by Y Pvt. Ltd. all rights of voting, management, right to sell etc. are vested with YAN Ltd.

On 19.03.2018, the shares held by Y Pvt. Ltd. in XY Pvt. Ltd. are sold to P Pvt. Ltd. which is a group company of X Pvt. Ltd. As per the tax-treaty between India and Country "A", there is no tax for capital gains either in source country or in Country "A". Consequently, the capital gains arising to Y Pvt. Ltd. are not taxable in India.

(d) Specify the quantum of Fee / Penalty, if any, to be levied in the following cases. Your answer must specify the relevant provisions of Income Tax Act, 1961. **3**

(i) Mr. Abhiram, an individual, whose taxable income working out to ₹ 13.25 lakhs, filed the return of Income on 12-03-2019 for the assessment year 2018-19. The due date for furnishing return of income under section 139(1) is 30-09-2018.

(ii) Mrs. Sirisha, filed the return of income on 31-01-2019 for the assessment year 2018-19. The due date for furnishing return of income is 31-08-2018 under section 139(1) and her taxable income is ₹ 4.98 lakhs.

(iii) Mr. Robert received a sum of ₹ 2.50 lakhs from Mr. Rajiv on 31-01-2018 in cash in contravention of provisions of section 269ST.

Marks

4. Answer any **four** out of the following five cases. (Your answer should cover these aspects : (i) Issue involved, (ii) Provisions applicable, (iii) Analysis and (iv) Conclusion)

(a) Anil Food Products (P) Ltd. is engaged in manufacturing and selling various food products. It engaged two transporters for carrying its products to various distributors. In previous year 2016-17 it made payments to two transporters towards freight charges without deduction of tax at source. In course of assessment the Assessing Officer disallowed 30% freight charges invoking section 40(a)(ia) for failure to deduct tax at source. The assessee contends that section 40(a)(ia) is not applicable as the amount of freight was not 'payable' at the year-end, but had been actually paid during the previous year. Examine the correctness of the contention of the assessee. 4

(b) The assessee, X & Sons (HUF) holds 30% of shares in PQR (P) Ltd. During the previous year 2016-17 the assessee received loan from the company. The Assessing Officer treated the loan so received as deemed dividend under section 2(22)(e) in the assessment of the HUF. The company declared in its annual return that the loan was given to the HUF, but the share certificates were issued in the name of the Karta i.e. Mr. X. Is the action of the Assessing Officer valid ? 4

(c) B. Ltd. is amalgamated with A. Ltd. under a scheme of amalgamation duly approved by the Court. A. Ltd. paid excess consideration over the value of net assets acquired by it, which is treated as goodwill as the extra consideration was paid keeping in view the reputation and existing clientele of B. Ltd. A Ltd. has claimed depreciation on the said goodwill. The Assessing Officer disallowed such depreciation on the ground that the goodwill is not an asset falling under Explanation 3 to section 32(1) of the Income Tax Act, 1961. Is the action of the Assessing Officer correct ? 4

Marks

(d) BSL Ltd. a company formed for manufacturing steel has started setting up a steel plant in Odisha on 1st April, 2016 and estimated time for completion of construction is two years. The company's application for term loan has been sanctioned and 30% of the sanctioned amount was disbursed on 1st July, 2016. Part of the loan amount received was not immediately required and the unspent amount was kept in short-term fixed deposit on which the company received interest of ₹ 10 lakhs. The company has not included such interest received in its total income on the ground that such interest is a capital receipt and to be reduced from the interest paid during construction period and net interest paid during construction period is to be allocated to various assets on completion of construction. The Assessing Officer proposes to include such interest in its total income under the head "income from other sources." **4**

Is the proposition of the Assessing Officer correct ?

(e) Agroha Education Institution was established under section 10(23C) (iiiad) to impart and spread education. It earned net surplus during the previous year 2016-17 and 2017-18 ₹ 6 lakhs and 5 lakhs respectively. It claimed exemption under section 10(23C) (iiiad). **4**

The assessing officer rejected the claim of exemption of the institution on the ground that the assessee had made profit and did not exist solely for the purpose of education.

Examine, the validity of the view taken by the Assessing Office.

5\. (a) Konark Digital Solutions Ltd. is an Indian Company in which Yokohoma Inc. a Singapore based company holds 30% shareholding and voting power. During the previous year 2016-17, the Indian Company supplied laptops to the Singapore based company @ \$ 800 per piece. The price of laptop supplied to other unrelated parties in Singapore is @ \$ 1200 per piece. During the course of assessment proceedings, the AO carried out primary adjustments and added a sum of ₹ 130 lakhs, being the difference between actual price of laptop and arm's length price for 500 pieces and it was duly accepted by the assessee. On account of this adjustment, the excess money of ₹ 130 lakhs is available with Yokohoma Inc, Singapore. In this context, you are requested to briefly explain the relevant provisions of Income Tax Act, 1961 and suggest suitable solution for the following issues : **6**

Marks

(i) What is the effect of this transaction on the taxable income of Konark Digital Solutions Ltd. for the assessment year 2018-19 on the basis that it declared an income of ₹ 250 lakhs and the excess money is still lying with Yokohoma Inc. till today ?

Assume the rate of exchange as 1 $ = ₹ 65 and the marginal cost of lending rate of SBI as on 01.04.2017 at 10.75%.

(ii) Would taxable income of Konark Digital Solutions Ltd. undergo any change, if the above adjustment carried out resulted in addition of ₹ 90 lakhs as against ₹ 130 lakhs ?

(iii) What is the impact of this adjustment on taxable income of Konark Digital Solutions Ltd. for assessment year 2018-19, if such adjustment pertains to the previous year 2015-16 as against 2016-17 ?

(b) On 08.12.2017, search operations were conducted on the business premises of Mr. Sadanandam, Stock Broker in Mumbai by IT authorised Officials. Upon conclusion of search, certain documents/assets, which were not recorded in books of account, pertaining to various previous years were found, detailed as under : 4

| | | |
|---|---|---|
| An agreement for purchase of flat indicating total consideration at ₹ 50 lakhs together with cash receipt for ₹ 23 lakhs and cheque receipt for ₹ 27 lakhs whereas sale deed registered for ₹ 27 lakhs. | ₹ 23 lakhs | PY : 2009-10 |
| Jewellery based on the bill held in his desk drawer in his name. | ₹ 28 lakhs | PY 2008-09 |
| Promissory note executed by his uncle in proof of loan taken from assessee. | ₹ 15 lakhs | PY 2010-11 |
| Fixed deposit receipts from a bank in the name of assessee. | ₹ 12 lakhs | PY 2012-13 |
| Shares and securities in name of family members. | ₹ 22 lakhs | PY 2013-14 |

**Marks**

Pursuant to the above documents/assets found, the Assessing Officer, under section 153A of the Income Tax Act, 1961 has issued notice for all the previous years from 2008-09 to 2016-17.

Mr. Sadanandam contends that the Assessing Officer cannot issue notice under section 153A beyond 6 years i.e. prior to P.Y. 2011-12.

Advise suitably on the matter in the context of relevant provisions of Income Tax Act, 1961.

(c) Examine the applicability of provisions relating to deduction/collection of tax at source and compute the liability, if any, for deduction/collection of tax at source in the following cases for financial year ended 31st March, 2018 as per provisions contained under the Income Tax Act, 1961 :- **6**

(i) In terms of agreement between A (the Owner of land) and B (Developer and Builder) the Developer, B agrees to allot 5 apartments to the owner in part consideration for providing his land and also agreed to pay a sum of ₹ 25,00,000. In terms of the agreement, Mr. B issued a cheque for ₹ 15,00,000 towards part of consideration on 30.03.2018.

(ii) (1) Rent of ₹ 60,000 per month deposited by Mr. Shrikanth, Software employee on 1st of every month in advance, in the account of Mr. Ashok, who does not provide his PAN. The house was taken on rent with effect from 01.07.2017 and he vacated the house on 28.02.2018.

(2) Would there be any change in TDS, if Mr. Ashok furnished his PAN to the tenant ?

(iii) ₹ 19,50,000 credited to the account of Digitec Studios (a partnership firm) on 31.03.2018 by B-TV, Television channel, towards part consideration for shooting of Tele Episode for 10 weeks as per the storyline, contents and specifications of B-TV channel.

Marks

6. (a) Examine and state the correctness or otherwise of each of the following statements in the context of provisions contained under the Income Tax Act, 1961 and answer by giving brief reasons/contents thereof : 12

(i) Tax Avoidance is not defined in taxing statue. It is the outcome of actions taken by the assessee, none of which or no combination of which is illegal or forbidden by the law as such. The international literature tends to describe the tax avoidance in many ways. If, yes state briefly ways of Tax avoidance.

(ii) The double taxation avoidance treaties entered into by the Government of India do not override the domestic law.

(iii) The contents of a business transaction done through e-commerce are not different from that of a business transaction carried out through traditional means. Which are the distinct means/methods of doing for e–business ?

(iv) Rakesh is resident in India during the previous year ended 31.03.18 and had agricultural income of ₹ 20 lakhs from the lands located in Pakistan. He had paid tax on such agricultural income in Pakistan for which he is not entitled for a deduction from the tax payable in India.

(v) Rose N. LLP of UK carried business in India against which a demand of ₹ 50 lakhs for A.Y. 2016 - 17 is outstanding. The LLP does not have any assets in India and has also closed the business. The tax recovery officer (TRO) cannot recover such demand by having attachment on the assets of Rose N. LLP located in UK.

(vi) A non-resident Indian despite having during the year ended on 31.3.18 income in India from the investment and long term capital gains is not required to file the return of income for A.Y. 2018-19.

**Marks**

(b) During the pendency of reassessment proceedings, the Assessing Officer has provisionally attached the property of the Assessee, Mr. Malhothra in accordance with powers vested under section 281B of the Income Tax Act, 1961 on 21st December, 2017. The fair market value of the said property is ₹ 90 lakhs. Mr. Malhothra proposes to furnish bank guarantee to the tune of ₹ 90 lakhs in lieu of provisional attachment of property and approached the AO to revoke the attachment. AO refused such proposal. Answer the following issues in the context of relevant provisions of the Act :- **4**

(i) Whether AO can refuse to accept bank guarantee, if not, is it mandatory on his part to pass revocation order for the provisional attachment of property ?

(ii) Specify circumstances under which the AO is empowered to invoke the bank guarantee.

7. (a) Pranab, a non-resident Indian (aged 41) has furnished the following particulars of income relating to financial year 2017-18 : **6**

| **Particulars** | ₹ |
|---|---|
| Loss from house property located in India | 2,50,000 |
| Income from business carried on in India | 7,50,000 |
| Income from mutual funds specified in section 10(23D) | 65,000 |
| Interest on debentures of Indian company subscribed in US $ | 1,50,000 |
| Interest on loan taken for purchase of above debentures | 20,000 |
| Long-term capital gains on sale of debentures subscribed in US $ in the year 2008-09 for ₹ 5,00,000 and sold in the year 2017-18 for ₹ 8,00,000.<br>(Cost Inflation Index- Financial Year 2008-09: 137;<br>Financial Year 2017-18: 272) | |
| Brokerage on sale of debentures | 12,000 |

Compute tax payable by Pranab for Assessment Year 2018-19 assuming that he opts for provisions of Chapter XII-A of the Income-tax Act, 1961.

Marks

(b) Ashoke's assessment was made under section 143(3) of the Income-tax Act, 1961 for A.Y. 2015-16. Being aggrieved with certain additions, he preferred an appeal to the Commissioner (Appeals), which is pending at present and not being adjudicated.

In the above situation, give your opinion on the following issues in the context of provisions contained under the Income Tax Act, 1961 :

(i) There is new information that certain income for the same assessment year had escaped assessment. Is it possible for the Assessing Officer to issue notice under section 148 ? **2**

(ii) Certain mistake in respect of issue which is not subject matter of appeal is noticed by the Assessing Officer. Can he pass an order under section 154 for rectifying the mistake ? **1**

(iii) If Ashoke files petition for revision under section 264 for a matter not being subject matter of appeal, will such petition be maintainable ? **2**

(c) SG Securities Private Ltd. is engaged in the business of trading in shares and securities. The details of shares held by it as stock-in-trade as on 31st March, 2018 are given below : **5**

| Shares | Cost per share (₹) | Net realisable value per share (₹) |
|---|---|---|
| 500 shares of P. Ltd | 50 | 65 |
| 200 shares of Q. Ltd | 35 | 32 |
| 300 shares of R. Ltd. | 125 | 110 |
| 250 shares of S. Ltd | 25 | 40 |

The company values its year-end stock-in-trade in accordance with Accounting Standard (AS) 13 – "Accounting for investments of the Companies (Accounting Standards) Rules, 2006".

Determine the amount of adjustments, if any required to be made in computation of income for Assessment Year 2018-19.

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