

Test Series: February, 2014

MOCK TEST PAPER – 1
FINAL COURSE: GROUP – II
PAPER – 7: DIRECT TAX LAWS

Question 1 is compulsory.

Answer any five questions from the remaining six questions.

Time Allowed – 3 Hours

Maximum Marks – 100

1. (a) Home Ltd., a company engaged in the business of manufacture of industrial equipments, furnishes the following particulars pertaining to P.Y. 2013-14. Compute the deduction allowable under section 32 and section 32AC for A.Y.2014-15, while computing its income under the head "Profits and gains of business or profession". Also, compute the written down value of plant and machinery as on 1.4.2014.

	Particulars	₹ in crores
1.	Written down value of plant and machinery (15% block) as on 1.4.2013	40.00
2.	Sold plant and machinery on 12.12.2013 (15% block)	6.00
3.	Purchase of second hand machinery (15% block) on 1.8.2013 for business purpose (the machinery was put to use immediately)	30.00
4.	Purchased new computers (60% block) on 25.12.2013 for office use	1.00
5.	Acquired and installed new plant and machinery (15% block) on 16.09.2013 (₹ 52 crore) and on 6.1.2014 (₹ 58 crore)	110.00
6.	New air conditioners purchased and installed in office premises on 21.8.2013	0.40

(10 Marks)

- (b) Blueprint Ltd. furnishes the following particulars of its wealth for the valuation date of 31st March, 2014. The company is engaged in jewellery business.

Compute its net wealth on valuation date 31.03.2014 and the wealth tax payable.

	₹
Land is situated in an area located at a distance of 7 kms from the local limits of the Municipality, the said area has a population of 4,00,000 according to last preceding census.	95,00,000

Land is situated in an area located at a distance of 3 kms from the local limits of the Municipality, the said area has a population of 1,05,000 according to the last preceding census.		48,00,000
Land in urban area (for construction of Mall)		26,00,000
Motor car (including one imported car worth ₹ 8 Lacs)		15,00,000
Jewellery (held as stock-in-trade)		28,00,000
Bank balance		10,00,000
Cash in hand as per cash book		3,10,000
Guest house and land appurtenant thereto in rural area		18,00,000
Residential flats of identical size provided to six employees for their use near factory in rural areas (salaries of three such employees exceed ₹ 10,00,000 p.a.)		60,00,000
Residence provided to managing director (salary ₹ 12,00,000 p.a.)		15,00,000
Residence provided to whole time director (salary ₹ 20,000 p.m.)		20,00,000
The company has taken the following loans :	₹	
(a) for purchase of jewellery	10,00,000	
(c) for residence provided to whole time director	1,90,000	

(10 Marks)

2. Sargam Ltd., engaged in the business of manufacturing, shows a net profit of ₹ 7 crores for the financial year ended 31-3-2014, after debiting/crediting the following items:
- On EPABX and mobile phones (exclusively used for the business purpose) purchased during the year, depreciation amounting to ₹ 24 lacs was claimed at higher rate of 60% treating them at par with computer.
 - 55 lacs paid to Naryana Ltd, towards feasibility study conducted for examining proposals for technological advancement relating to the existing business, where the project was abandoned without creating a new asset.
 - 38 lacs paid for the higher studies of the director's son abroad, with a stipulation that he would be appointed as a trainee in the company under "apprentice training scheme" where there is no evidence of existence of such scheme.
 - Payment of ₹ 32 lacs (without deducting tax at source) towards purchase of software from a non-resident, meant for subsequent resale in the Indian market, was ultimately sold at a profit during F.Y. 2013-14.

- (v) Dividend of ₹ 12 lacs received from a foreign company in which this company holds 28% in nominal value of the equity share capital of the company. ₹ 0.28 lac expended on earning this income.
- (vi) 48 lacs were paid on 13th July, 2013 to a National Laboratory with a stipulation that the said contribution shall be used for the purpose of an approved scientific research programme only.
- (vii) Secret commission of ₹ 10 lacs was paid and debited under commission account.
- (viii) Purchased a brand new bus for ₹ 13 lacs and donated to a school where the children were studying and debited the same to the Workmen and Staff Welfare Account.

Additional Information:

- A debt of ₹ 15 lacs was claimed as bad debt in the previous year 2012-13. However, the Assessing Officer allowed only a sum of ₹ 8 lacs as bad debts. In the previous year 2013-14, a sum of ₹ 5 lacs is recovered ultimately in respect of the debt. The effect of the recovery of bad debt was not given in the books of account.

Compute total income of Sargam. Ltd. for the Assessment Year 2014-15 and work out the amount of tax payable on such income, indicating reasons for treatment of each item. Ignore provision relating to minimum alternate tax. (16 Marks)

3. (a) Ms. Geeta received the following gifts during the P.Y.2013-14 from her friend Mr. Suhesh, -

- (1) Cash gift of ₹ 54,000 on her birthday, 1st August, 2013.
- (2) 80 shares of Veena Ltd., the fair market value of which was ₹ 80,000, on her birthday, 1st August, 2013.

On 10th August 2013, 120 shares of Drama Ltd., was purchased by her from Mr. Suhesh for ₹ 20,000 the fair market value of which was ₹ 80,000 on the date of transfer. Mr. Suhesh had originally purchased the shares on 12.10.2012 at a cost of ₹ 12,000.

Further, on 12th October, 2013, Ms. Geeta purchased land from her sister's mother-in-law for ₹ 3,50,000. The stamp value of land was ₹ 5,00,000.

On 23rd March, 2014, she sold the 120 shares of Drama Ltd. for ₹ 1,20,000.

Compute the income of Ms. Geeta chargeable under the head "Income from other sources" and "Capital Gains" for A.Y.2014-15. (5 Marks)

- (b) Graeme Smith, a foreign national and a cricketer came to India as a member of South Africa cricket team in the year ended 31st March, 2014. He received ₹ 10 lakhs for participation in matches in India. He also received ₹ 1.5 lakh for an advertisement of a product on TV. He contributed articles in a newspaper for which

he received ₹ 50,000. When he stayed in India, he also won a prize of ₹ 35,000 from horse racing in Kolkata. He has no other income in India during the year.

- (i) Compute tax liability of Graeme Smith for Assessment Year 2014-15.
- (ii) Are the income specified above subject to deduction of tax at source?
- (iii) Is he liable to file his return of income for Assessment Year 2014-15?
- (iv) What would have been his tax liability, had he been a match referee instead of a cricketer? (5 Marks)

- (c) Alliya LLP, a limited liability partnership in India, is engaged in development of software and providing IT enabled services through two units, one of which is located in a notified Special Economic Zone (SEZ) in Noida. The particulars relating to previous year 2013-14 furnished by the assessee are as follows:

Total Turnover: SEZ unit ₹ 140 lakhs and the other unit ₹ 80 lakhs

Export Turnover: SEZ unit ₹ 80 lakhs and the other unit ₹ 40 lakhs

Profit: SEZ unit ₹ 70 lakhs and the other unit ₹ 20 lakhs.

The assessee has no other income during the year.

- (i) Compute tax payable by Alliya LLP for the Assessment Year 2014-15.
- (ii) Will the amount of tax payable change, if Alliya LLP is an overseas entity? (6 Marks)

4. (a) Deluxe, a partnership firm engaged in real estate business, sold a land for ₹ 70 lacs on 07-08-2013, in the course of its business. The buyer was a stranger to the assessee firm. The valuation adopted by the stamp valuation authority was ₹ 1 crore. The Assessing Officer wants to adopt the value of ₹ 1 crore for computing the profit arising from the sale of land, by invoking the provisions of section 50C. Is the same justified?
- (b) Fine Ltd is a public limited company. As a good corporate citizen and as a measure of gaining goodwill of the people living in and around its industry, which is to some extent a polluting industry, it provided funds for establishing drinking water facilities to the residents in the vicinity of the refinery and also provided aid to the school run for the benefit of the children of those local residents. The Assessing Officer declined to allow that expenditure on the ground that it was not an item of expenditure incurred by the assessee for earning the income. The company, however, claimed that such social costs can be claimed as deduction. Is the claim of Fine Ltd. tenable in law? Discuss.
- (c) Mr. Rajan is a retail trader and his returned income for the last five years ranged between ₹ 10 lakh to ₹ 13 lakh. Mr. Rajan celebrated his silver wedding anniversary on 12th January, 2014 by hosting a grand cruise party in the luxury cruise liner "The

Oyster", for which he had spent ₹ 30 lakh. The Assessing Officer, in the course of scrutiny assessment of Mr. Rajan, asked him to explain the source of such expenditure. The explanation offered by Mr. Rajan that the same was out of his savings for the last ten years, was not found satisfactory by the Assessing Officer, since two years ago, he had spent to tune of ₹ 50 lakh on the lavish wedding of his daughter. You are required to examine the tax consequences.

- (d) Mr. Krishna, a sole proprietor was previously a partner of True India Partnership firm. On 23rd February, 2014, in accordance with the partnership deed, he took over the entire business of partnership firm on its dissolution including fixed assets, current assets and liability.

Krishna in his return of income for the Assessment Year 2014-15 claimed ₹ 7 lakhs as set-off of losses, suffered by the erstwhile partnership firm against his income earned as an individual proprietor, considering the case as inheritance of business.

However, the Assessing Officer disallows the claim of set off on the ground that it is not a case of inheritance. Discuss the validity of the action of Assessing officer.

(4 × 4 = 16 Marks)

5. (a) Royal Ltd., an Indian company, exports strawberries to Deluxe Inc for an amount of ₹ 47 Lacs. Deluxe Inc. is located in a Notified Jurisdictional Area (NJA).

Royal Ltd. charges ₹ 48 lacs and ₹ 52 lacs for sale of similar goods to Coral Inc and Mirage Inc, respectively, which are not located in NJA and both of them are not associated enterprises of Royal Ltd.

Assuming that permissible variation notified by Central Government for such class of international transactions is 3% of the transaction price, state the tax implications under section 94A in respect of the above transaction by Royal Ltd. with Deluxe Inc.

- (b) Avinash Kumar, a resident individual, is a musician deriving income of ₹ 89,000 from concerts performed outside India. Tax of ₹ 8,900 was deducted at source in the country where the concerts were performed. India does not have any double tax avoidance agreement with that country. His income in India amounted to ₹ 3,45,000. Compute tax liability of Avinash Kumar for the assessment year 2014-15 assuming he has deposited ₹ 30,000 in Public Provident Fund and paid medical insurance premium in respect of his father, aged 65 years, ₹ 30,000.
- (c) A public charitable trust, created under a trust deed for providing relief to disabled persons, registered under section 12AA, furnishes the following particulars of its receipts during the year ended 31st March, 2014 -

	Particulars	₹ (in Lacs)
(i)	Income from properties held by trust (net)	23
(ii)	Income (net) from business (incidental to main objects)	20

(iii)	Voluntary contributions from public (including the corpus donation of ₹ 8 Lacs)	14
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The trust applied ₹ 23 Lacs towards various activities and programmes undertaken for the benefit of autistic persons during the year. The trust has also paid ₹ 13 Lacs towards repayment of a loan taken a year back for the purpose of construction of its centre for training the disabled persons in various handicraft works.

Determine the tax liability, if any, of the trust for the assessment year 2014-15.

- (d) Dear Ltd., a domestic company, purchases its own unlisted shares on 16th September, 2013. The consideration for buyback amounted to ₹ 28 lakh, which was paid on the same day. Dear Ltd. had received ₹ 21 lakh on issue of these shares one year back. Compute the additional income-tax payable by Dear Ltd. Further, determine the interest, if any, payable if such tax is paid to the credit of the Central Government on 15th December, 2013. Would there be any tax implication in the hands of the shareholders? Discuss. *(4 × 4 = 16 Marks)*
6. (a) On an application made by Mr. Jain, an order was passed by the Settlement Commission on 28-01-2014 under section 245D. The said order had a mistake apparent on record. The Settlement Commission passed an amended order dated 28-04-2014 which resulted in modifying the liability of Mr. Jain.

Mr. Jain is of the view that order of the Settlement Commission is final and conclusive and it has no power to rectify the said mistake.

You are required to examine the following:

- (i) Correctness of claim made by Mr. Jain
 - (ii) Validity of the order amended by the Settlement Commission *(6 Marks)*
- (b) Examine the following cases and state whether the same are liable for penalty as per the provisions of the Income-tax Act, 1961.
- (i) Jack & Associates had made payment in excess of the limits prescribed to the contractors for carrying out labour job work at various sites, but had not deducted tax at source as per section 194C.
 - (ii) Pan Asia Hotels were asked by Income-tax Officer (CIB) to furnish details of all such tourists who stayed in their hotels and had paid bill amount in excess of ₹ 10,000. They have not furnished the requisite information in spite of various reminders. *(6 Marks)*
- (c) Explain the applicability of the provision relating to the deduction of tax at source in the following transactions:
- (i) Canara Bank pays ₹ 100,000 per month as rent to the Central Government for a building in which one of its branches is situated.

- (ii) A notified infrastructure debt fund eligible for exemption under section 10(47) of the Income-tax Act, 1961 pays interest of ₹ 8 lakhs to Mr. John, a resident of Notified Jurisdictional area. (2 x 2 = 4 Marks)
7. (a) A search was conducted under section 132 in the business premises of Harsh on 30th November, 2013. At that time, assessments under section 143(3) for A.Y. 2011-12 and A.Y. 2012-13 and reassessment proceeding under section 147 for A.Y. 2010-11 were pending before the Assessing Officer.
- (i) What are the assessment years for which notice can be issued for making post-search assessment?
- (ii) What would be the fate of pending assessments and reassessment?
- (iii) What would be the effect, if the post-search assessment orders are annulled by the Income-tax Appellate Tribunal? (3 x 2 = 6 Marks)
- (b) Discuss the correctness or otherwise of the following with reference to the provisions of the Income-tax Act, 1961.
- (i) Commissioner (Appeals) has no power to decide a matter that was not raised before him.
- (ii) The Income-tax Appellate Tribunal cannot amend its orders.
- (iii) A case before the Appellate Tribunal cannot be dealt when there is a difference of opinion amongst the members of the Bench. (3 x 2 = 6 Marks)
- (c) Diksha received a notice under section 148 from the Assessing Officer for A.Y. 2010-11 on the ground that depreciation on certain assets was allowed in excess. The Assessing Officer recorded the reason for reopening. The original assessment was completed under section 143(3). In course of reassessment proceeding, the Assessing Officer also disallowed certain sum under section 14A in respect of expenses purported to be in relation to dividend from companies and tax-free interest. However, the Assessing Officer did not record the reason for applying the provisions of section 147 in respect of the issue of disallowance under section 14A and passed the order disallowing the excess depreciation and also certain sum under section 14A. Is there any infirmity in the order passed by the Assessing Officer? (4 Marks)