
PAPER 7: DIRECT TAXES
NOVEMBER 2003

Answer All Questions

Question 1

- (a) Alpha Ltd., a manufacturing company, which maintains accounts under mercantile system has disclosed a net profit of Rs.12.50 lakhs for the year ending 31st March, 2003. you are required to compute the taxable income of the company for the Assessment Year 2003-2004. You are required to compute the taxable income of the company for the Assessment Year 2003-2004 after considering the following information, duly explaining the reasons for each item of adjustment: **(12 Marks)**
- (i) Advertisement expenditure includes the sum of Rs.60,000 paid in cash to the sister concern of a director, the market value of which is Rs.52,000.
 - (ii) Legal charges include a sum of Rs.45,000 paid to a consultant for framing a scheme of amalgamation duly approved by the Central Government.
 - (iii) Repairs of plant and machinery includes Rs.1.80 lakhs towards replacement of worn out parts of machineries.
 - (iv) A sum of Rs.6,000 on account of liability foregone by a creditor has been taken to general reserve. The same was charged to the Revenue Account in the Assessment Year 1998-99.
 - (v) Sale proceeds of import entitlements amounting to Rs.1.0 lakh has been credited to Profit and Loss Account, which the company claims as capital receipt not chargeable to income tax.
 - (vi) Eeing also engaged in the biotechnology business, the company incurred the following expenditure on in house research and development as approved by the prescribed authority:
 - (a) Research equipments purchased Rs.1,50,000
 - (b) Remuneration paid to scientists Rs.50,000
- The total amount of Rs.2,00,000 is debited to the Profit and Loss Account.
- (b) M/s. Kangaru Australia, a non-resident foreign company had entered into a collaboration agreement on 21-02-2002 with an Indian Company and was in receipt of the following payments during the previous year ended on 31-03-03. how do you deal with them for computation in the case of M/s.Kangaru Australia? **(4 Marks)**
- (i) Interest on 8% debentures for Rs.50 lakhs issued by Indian Company on 01-07-2002 in consideration of providing of technical know how, manufacturing process and designs.
 - (ii) Service charges @ 2 ½% of the value of Plant & Machinery for Rs.500 lakhs leased out to Indian Company payable each year before 31st March.

Question 2

- (a) Shri Rahul was a partner in two partnership firms. He retired from two firms on January, 2003. On the date of retirement, his capital account was credited with a sum of Rs.2,50,000 in each firm, over and above the amount due to him towards his Capital and Profits. He seeks your advice, whether the amount of Rs.2,50,000 credited to his Capital Account, in each firm is taxable for the Assessment Year 2003-2004. **(4 Marks)**
- (b) Discuss the concept of Arm's length price as envisaged in Section 92C of the Income Tax Act **(6 Marks)**
- (c) Explain the circumstances under which the Assessing Officer can resort to provisional attachment of the property of the assessee. Also state the period of time for which such attachment can take place **(4 Marks)**

Question 3

- (a) The WDV of Plant & Machinery on 1-4-2002 of X Ltd., engaged in manufacturing of PVC granules is Rs.1,000 lakhs. Company purchased additional Plant & Machinery for Rs.800 lakhs on 18-4-02 inclusive of a second-hand machine imported from China of Rs.200 lakhs to increase its installed capacity of production from 1000 TPA to 1500 TPA. The production from new machine was taken w.e.f. 1-12-02. Workout by giving reasons the amount of allowable depreciation. **(5 Marks)**

- (b) Parimal, Managing Director of Heavens Engg. Prvt. Ltd., hold 70% of its paid up capital of Rs.20 lakhs. The balance as at 31-03-2002 in general reserve was Rs.6 lakhs. The company on 1-4-02 gave an interest free loan of Rs.5 lakhs to its Supervisor having salary of Rs.4,000 p.m. who in turn on 15-6-2002 advanced the said amount of loan so taken from the company to Shri Parimal. The Assessing Officer had taxed the amount of advance in the hands of Parimal. Is the action of Assessing Officer correct? **(3 Marks)**
- (c) "Tax Recovery Officer, can recover the arrear demands from the assessee in default out of sale proceeds of the property attached after making a proclamation". How such proclamation can be made under the Act? **(4 Marks)**

Question 4

- (a) Roxy Cine Arts of Mumbai engaged in distribution of cinematography films. It started construction of multiplex theatre and convention hall in Navi Mumbai in April, 2002 and completed in December, 2002. the profits for the year ended 31-03-03 of all the activities are: **(4 Marks)**
- | | |
|--|------------|
| (i) Distribution of Cinematography Films | Rs.5 lakhs |
| (ii) Convention Centre | Rs.2 lakhs |
| (iii) Multiplex Theatre | Rs.1 lakhs |
- Compute the Taxable income for the Assessment Year 2003-04 with reasons.

- (b) Vijay Agencies, a partnership firm constituted by three partners with equal shares was dissolved on 1/4/1999 after a search. The liability to tax finally decided against the firm outstanding to be paid was Rs.15 lakhs. Out of three partners, one was declared insolvent on 18/3/2001 by the court. The Assessing Officer for recovering the demand attached the Bank Accounts of other two partners and could recover an amount of Rs.6 lakhs from the Account of one such partners. You are asked by the partners of dissolved firm: **(4 Marks)**
- (i) About the liability of each of them to pay outstanding demand
- (ii) Whether the action of A.O to attach the Bank Account of Partners against demand of dissolved firm is justified?
- (c) X Ltd., a domestic company holds 50% of share capital of Y Ltd., which is another domestic Co., Y Ltd., paid total dividend during the year ended on 31/3/03 of Rs.50 lakhs. Out of the dividends received from Y Ltd., X Ltd., had distributed dividend of Rs.15 lakhs. Explain with reasons the amount of dividend chargeable to tax in the hands of X Ltd., **(3 Marks)**

Question 5

- (a) In the course of search on 25/3/2003, assets were seized. State the procedure laid down to deal with such assets seized under the Act. **(3 Marks)**
- (b) The Director of Income Tax received information that Mr."X" has unaccounted cash exceeding Rs.50 lakhs. Can the Director pass orders for seizure of the cash invoking his powers U/s. 131(1A)? Does the Director have any other course open to him for the seizure of cash? **(4 Marks)**
- (c) Discuss the following propositions:
- (i) The Income Tax Appellate Tribunal cannot admit additional evidence during the hearing of the appeal **(3 Marks)**
- (ii) The Commissioner of Income Tax can revise an order during the pendency of an appeal before the First Appellate Authority. **(3 Marks)**
- (iii) The Commissioner of Appeals cannot admit an appeal filed beyond 30 days from the date of receipt of order by an Assessee. **(2 Marks)**

Question 6

- (a) X had taken a loan under registered mortgage deed dated 16/7/2000 against the house, which was purchased by him on 26/3/81 for Rs.5 lakhs. The said property was inherited by his son "A" under will who for obtaining a clear title thereof had paid the outstanding amount of loan on 12/2/03 of Rs.15 lakhs.

The said house property was sold by "A" on 16/3/03 for Rs.50 lakhs. State with reasons the amount chargeable to capital gains for A.Y.2003-04 (Cost of Index Rs.44) **(5 Marks)**

- (b) XY Pvt Ltd., a company having registered head office in Singapore for the first time had carried out operations during 02-03 of purchase of goods in India on four occasions. Immediately after purchase the company exported the same to China. The total value of such exports was Rs.100 lakhs on which it earned profits of Rs.20 lakhs before the expenses of Rs.12 lakhs, which were directly paid by H.O. The company seeks your advice to its liability to tax in India:
- (i) How much Income for A.Y.2003-04 shall be subject to tax?
- (ii) To what extent deduction U/s. 80HHC shall be available?
- (c) Explain with reasons about the taxability of the following transactions for the Assessment Year 2003-04:
- (i) Raja was declared winner in a lucky DIP on 15th August, 2002. He was paid cash of Rs.1,00,000 as prize money. **(2 Marks)**
- (ii) Mr. Ravi, citizen of India and a non-resident purchased the Savings Certificates issued by Central Government from out of Dollars remitted from U/s. on 11/7/02 on which the interest for the year ended on 31/03/03 was Rs.3 lakhs. **(2 Marks)**

Question 7

- (a) XY & Co., a partnership concern had established an undertaking for manufacturing of Computer software in Free Trade Zone. It furnishes the following particulars of its 2nd year of operations ended on 31-03-03. **(6 Marks)**
- | | |
|---------------------------|--------------|
| - Total sales of business | Rs.100 lakhs |
| - Export sales | Rs.80 lakhs |
| - Profits of business | Rs.10 lakhs |
- Out of the total export sales, realization of sales of Rs.5 lakhs is difficult because of insolvency of buyer. Realization of rest of the sales is received in time.
- The Plant & Machinery used in the business had been depreciated @15% on SLM basis and depreciation of Rs.3 lakhs was charged in Profit & Loss Account.

Compute the Taxable income of XY & Co., for the Assessment year 2003-04.

- (b) Rajesh & Co., the sole proprietary concern of Mr. Rajesh got converted into partnership after his death on 02/04/02 by his sons and the business of Rajesh & Co., was continued to be carried in the same manner. There were business losses of Rs.4.25 lakhs till 31/03/02. the net results of the business for the year ended 31/03/03 were profit of Rs.5 lakhs. The partners want to set off the losses of Rs.4.25 lakhs from the profits of the firm. Can they do so? **(3 Marks)**

Question 8

- (a) State with reasons whether the following constitute assets chargeable under Wealth Tax Act as the wealth of Raja, a former ruler? (Assume that there is taxable wealth as on valuation date 31/03/03):
- (i) Jewellery transferred to a minor handicapped daughter on 31/12/02. **(2 Marks)**
- (ii) 50% of the Palace (occupied by him and declared by Government as his official residence) was rented out throughout the previous year ending 31/03/03. **(2 Marks)**
- (b) State the circumstances in which the Wealth Tax Officer can refer valuation of an asset to the Valuation Officer **(2 Marks)**
- (c) Return of net wealth declaration wealth of Rs.55.50 lakhs for Assessment year 2000-01 was filed by Ravi on 30-09-2001. The Assessing Officer issued notice U/s. 16(2), which was served upon the assessee on

28-02-02. The assessment was completed by the Assessing Officer on 13/03/03 on the Wealth of Rs.85 lakhs. Ravi wants to know: **(4 Marks)**

- (i) Whether the order passed by the Assessing Officer is a valid order under the Act?
- (ii) Will his case be fit for levy of penalty, if assessed wealth is not disputed?