Paper 7: DIRECT TAXES
MAY 2001

Answer all questions

Question 1. **(5×3=15 Marks)**

How do you deal with the following situations? Give reasons for your answer (The assessment year is 2001-2002):

(i) Basu, Managing Director of a company is entitled to commission on sales as per the service agreement entered into. A part of the commission is converted into purchasing a single premium deferred annuity policy from Life Insurance Corporation of India. Basu claims that the commission diverted to secure the deferred annuity cannot be taxed in his personal assessment.

(ii) Shyam, is a whole time employee as a Development Officer, in Life Insurance Corporation of India. He receives incentive bonus based on quantum of business procured in the year. He claims that incentive bonus cannot be wholly included as his income and he should be allowed deduction for expenses incurred in procuring the business.

(iii) Nija Traders engaged in manufacturing was in receipt of sales-tax subsidy from State Government as the unit was in backward area. The subsidy is related to the sale of its products and payable once the production is commenced. Nija Traders claims that the subsidy is a capital receipt and hence cannot be included as income.

(iv) A Corporation was set up by the State Government transferring all the buses owned by it for a consideration of Rs.75 lakhs, which was discharged by the Corporation by issue of equity shares. The corporation in its assessment claimed depreciation. Can the depreciation be denied in the Corporations hands that there was no registration of the buses in favour of the Corporation?

(v) Ravi succeeded to his father's business in the year 1998. In the precious year ending 31.3.2001, Ravi has written off the balance in the name of 'Y', which relates to supply made by his father, when he carried on business. Ravi desires to know whether the write off could be eligible for deduction.

Question 2.

(i) Mukerjee furnishes the following information:

Purchase of Shares

No.of Shares	Month & Year of purchase	Shares dematted Month & Year
1,000	March, 1992	July, 1999
500	March, 1992	–
1,000	December, 1996	October, 1998

He sold 1,500 shares in January, 2001 out of the dematted shares. He seeks your advice as the taxability towards capital gains for the assessment year 2001-2002. **(3 marks)**

(ii) Chand Ltd. decided to effect buy back of shares capital by purchase of shares in open market. During the previous year ending 31.3.2001, Chand Ltd. purchased 10,000 shares. Discuss the tax implications in the hands of Chand Ltd. and shareholders. **(3 marks)**

(iii) Discuss the tax treatment of surplus arising out of deep discount bonds:

a. On sale of such bonds.
b. On realization of such bonds on maturity. **(4 marks)**

Question 3.

(i) Discuss the circumstances under which the income of a public charitable and religious trust will be subjected to income-tax at maximum marginal rate. **(4 marks)**

(ii) Income computed on the accrual basis is no longer relevant for taxation of income. Critically analyse the validity or otherwise of the same. **(3 marks)**

(iii) Shyam was contributing amount to unrecognized provident fund. On 15th March, 2001, he had finally drawn the deposited amount along with interest. He seeks your advice as to how it has to be dealt in his computation for assessment year 2001-02. **(3 marks)**

Question 4.

Discuss the correctness or otherwise of the following with reference to the provisions of the Income-tax Act:

(i) An assessment reopened under section 147 cannot be dropped. **(4 marks)**

(ii) Commissioner (Appeals) has no power to decide a matter that was not raised before him.

(iii) The Income-tax appellate tribunal cannot amend its orders. **(4 marks)**

(iv) A case before the Appellate Tribunal cannot be dealt when there is a difference of opinion amongst the members of the Bench. **(4 marks)**

(v) An appeal shall lie to the High Court against the order. **(3 marks)**

Question 5.

(a) Distinguish between Tax Planning and Tax Evasion. **(4 marks)**

(b) In the following cases discuss whether the loss could be set off;

i. Smt.Shanti carried on business with the gifted funds of her husband Mahesh. For the previous year ending 31.3.2001, Shanti incurred loss of Rs.2 lakhs which loss Mahesh wants to set-off from his taxable income. **(3 marks)**

ii. Smt.Bhanu succeeded to the business of her husband Sri Bhavesh, who died on 10th September, 2000. Shri carried on the business as proprietrix. The business of Bhavesh upto the date of his death resulted in a loss. Smt. Bhanu earned profit in business for the period ending 10th September, 2000 against her income. **(3 marks)**

Question 6.

(a) A public limited company engaged in the generation and distribution of power had its business acquired by the Government in June, 1999. Certain items of plant and machinery used by the company in its business were taken over by the Government at a price which resulted in the company realizing a surplus of Rs.26,60,000 over its written down value. The compensation was received by the company in April, 2000 which was accepted by it under protest. The company proceeded to initiate arbitration proceedings under law and was granted an additional compensation of Rs.16 lakhs. This was decided by the arbitrators in December, 2000 and received by the company in March, 2001. The company claims that the assessment of the company to tax should not be made since the business was completely taken over by the Government in June, 1999 and at the time of final determination of compensation in March, 2001, the company did not exist.

Do you agree to the company's claim? Discuss with reference to the assessment year(s) to which the claim to tax, if any, can be related. **(6 marks)**

(b) A, an individual, has income taxable only under the head 'Salaries'. In the course of the previous year ended 31st March, 2001, he pays Rs.10,000 to an institution recognized by the prescribed authority under section 35CCA of the Income-tax Act.

Will A be entitled to any deduction under the Act and if so, in what an amount? Discuss. **(4marks)**

Question 7

(a) A is an association governed by the provisions of Section 44A of the Income-tax act. The subscription receipts for the year ended 31st March, 2001 were Rs.60,000. The expenditure in the normal course of its activities was Rs.85,000. Its other income taxable under the Act works out to Rs.75,000. On these facts, you are consulted as to

i. How A's taxable income will be determined for assessment year 2001-2002.

ii. In case the association did not have the other income taxable will there be any difference in the computation of its income?

Please advise. **(5 marks)**

(b) Discuss the following propositions:

i. An advance ruling can become void. **(3 marks)**

ii. Interest levied under Section 220 of the act can be waived. **(3 marks)**

Question 8

(a) Bhaskar, a person of Indian origin was working in Kenya from 1987. He returned to India for permanent settlement in May, 1999, when he remitted money into India. For the valuation date 31st March, 2001, the following particulars were furnished. You are required to compute the taxable wealth. The reason for inclusion or exclusion should be stated: **(10 Marks)**

(i)	Building owned and let out for 270 days for residence. Net maintainable rent (40,000) and the market value (Excess of un-built area over specified area is 20% of the aggregate area)	10,00,000
(ii)	Jewellery:	
	(a)Purchased in April '99 out of money remitted to India from Kenya.	5,00,000
	(b)Purchased in April, 2000 out of sale proceeds of motor car brought from abroad and sold	4,00,000
(iii)	Value of interest in urban land held by a firm in which he is a partner	7,00,000
(iv)	Bonds held in companies	5,00,000
(v)	Motor car used for own business	2,50,000
(vi)	Vacant house plot of 400 sq. mts (purchased in December, 1995) market value	9,00,000
(vii)	Cash on hand	80,000
(viii)	Urban land purchased in the year 1999 out of withdrawals from NRE Account.	10,00,000