

PAPER 7: DIRECT TAXES
MAY 1997

Answer all the Questions

Question 1

- (a) A Co-operative Society was engaged in the business of banking or providing credit facilities to its members. It sold goods on credit to its members. Is the Co-operative Society entitled to special deduction under Section 8P (2) (a) (i) in respect of income derived from such an activity? **(3 Marks)**
- (b) In the return for the assessment year 1997-98, B claimed deduction from his income from salary of a sum paid by him to his ex- wife by way of alimony to her and maintenance expenses to their minor son. On 7th January, 1997 by agreement with his employers, B had agreed to the creation of a first **charge** on his salary in favour of his ex-wife for the payment of monthly sum. What is the effect of this charge and the alimony payment on the taxable income in the hands of B? **(3 Marks)**
- (c) A Co-operative Society was engaged in purchasing, developing and leasing out land to its members. Certain amounts were collected from individual members when they executed lease deeds or on transfer of lease from one member to another. The amount which was contributed by an outgoing member was utilized by the society for extending common amenities to members. Is the income of the society exempt on the principles of mutuality? **(3 Marks)**
- (d) B (HUF) was the owner of a house property, which was being used for the purpose of a business carried on by a partnership AB & Co. in which the karta and the other members of the HUF were partners in their individual capacity. The Assessing Officer proposes to assess the annual letting value of the said property as the HUF's income from house property. The HUF contends that the building was used for business purposes, and, therefore, the annual letting value thereof was not taxable in its hands as income from house property under Section 22. Examine the vital contentions. **(3 Marks)**
- (e) Ram voluntarily files his return of income for the Assessment year 1993-94 on 15.09.1996 showing income below taxable limit and claiming a refund of Rs. 75,000. How will the Assessing Officer deal with the case? **(3 Marks)**

Question 2

- (a) Sharath who got allotted a commercial plot, had to pay the lessor of the land, development charges and claimed the same as revenue expenditure. The Assessing Officer rejected his claim on the ground that the said amount was the consideration for the acquisition of leasehold rights in the plot allotted to him by the lessor and by acquiring leasehold rights, Sharath certainly acquired an advantage and an asset of enduring nature. Is the action of the Assessing Officer justified? **(3 Marks)**
- (b) The goods imported by Nishal Textiles Limited were confiscated by the customs authorities. Section 125 of the Customs Act gives an option to the owner to pay in lieu of such confiscation a fine, as may be levied by the authorities. The goods were cleared by the assessee after paying fine of Rs. 72,000. Is the said amount deductible as business expenditure? **(2 Marks)**
- (c) Mr. Saba Karim is a non-resident. The appeal pertaining to the Assessment year 1996-97 is pending before the Appellate Tribunal, the issue involved being computation of income from house property. The same issue persists for the assessment year 1997-98 also. Mr. Saba Karim's friend Mr. Sheikh Ali has obtained an advance ruling under Chapter XIX-B of the Income Tax Act, 1961 from the Authority for Advance Rulings on an identical point. Mr. Saba Karim proposes to use the said ruling for his assessment pertaining to the assessment year 1997-98. Advise Mr. Saba Karim suitably. **(2 Marks)**

- (d) R who was not an assessee earlier commenced business on 1.9.96. His total income for the year ended 31.3.97 from a gross turnover of Rs. 60,00,000 is only Rs. 30,000. though his income is below the taxable limit, what are his obligations under the Income – tax Act, 1961? **(3 Marks)**
- (e) The return of Big B Bros was taken up for scrutiny assessment by issuing notice under Section 143(2). Big Bros were in the business of plying of foods carriages owning 8 lorries and had returned an income of Rs. 1,92,000. The Assessing Officer noticed that a cash payment of Rs. 25,000 made to a single party on the same day for the purpose of purchase of tyres and spares had been claimed as expenses. He wants to add this to the returned income. Is the Assessing Officer correct in his view? **(2 Marks)**

Question 3

- (a) Examine the validity of the following statements:
- Application of income by virtue of Section 11(1)(a) of the Income Tax Act, 1961 should necessarily result in revenue expenditure. **(3 Marks)**
 - The Commissioner is empowered to refuse to exercise reversionary jurisdiction on the ground that the assessee repeatedly admitted concealment of income. **(3 Marks)**
- (b) The summarized Profit and Loss Account of River View Limited engaged in the business of hotel approved by the prescribed authority under Section 80HHD for the previous year ended 31st March, 1996 is as follows:

	(Rs. In lakhs)
Amount received for service rendered to Foreign tourists	60.00
Other business receipts	5.60
Short Term Capital Gain	1.30
	66.90
Less: Expenses	25.40
Transfer to reserve under Section 80HHD	10.00
	35.40
Profit	31.50

Following information is provided to you:

- Expenses include Rs. 4.50 lakhs being interest on term loan taken from a bank not paid by due date for filing return of assessment year 1997-98.
- Services to foreign tourists include Rs. 6 lakhs received in convertible foreign exchange after 30th September, 1996 and also Rs. 0.75 lakhs received by way of sale of articles in a shop owned by the Company.
- Other business receipts include Rs. 3 lakhs received in Indian rupee from an approved tour operator towards the services to foreign tourists.

You are required to compute the amount of deduction that can be claimed by the Company U/s. 80HHD

(8 Marks)

Question 4

- (a) Ashwin owns a residential house which is self occupied and also a house plot. He sells the house on 31.01.97 and the house plot on 15.02.97 for Rs. 6,50,000 and Rs. 5,00,000 respectively. The house was purchased on 15.1.93 for Rs. 4,00,000 and the plot on 30.03.93 for Rs. 2,00,000. Ashwin has purchased a new residential house on 25.04.97 for Rs. 10,00,000. Compute the income chargeable under the head capital gain for the Assessment Year 1997-98. Cost inflation indices for the financial years 1992-93 and 1996-97 are 223 and 305 respectively. **(7 Marks)**
- (b) Raj & Co. a partnership firm consisting of three partners L, M and N is proposed to be dissolved on 31.03.1997. The firm own a house property purchased 20 years back. One of the proposed terms of dissolution is that the house property, whose present market value is Rs. 10,00,000 should be allotted to M. A suggestion is made to the firm that instead of making an allotment at the time of dissolution, the

firm can gift the said house to M, by making book entries, the firm being not eligible to gift-tax. Describe the pros and cons of the suggestion, advising the firm suitably in the context. **(7 Marks)**

Question 5

Indicate, with reasons, your views in the following cases:

- (a) An individual is an employee of a public sector undertaking owned by the Government of India. The shares are fully held by the President of India and his nominees. Government of India in an attempt to broaden the equity base of the Company, allots each of the employees of the undertaking 200 equity shares at Rs. 200 per share whilst for the members of the public, the allotment price was fixed at Rs. 400 per share.
The Assessing Officer wants to add the difference between Rs. 400 per share and Rs. 200 per share as a perquisite in the hands of the individual employee. **(4 Marks)**
- (b) An employer takes a group personal accident policy with one of the nationalised insurance Companies in India and keeps the policy current by paying premium periodically. X, one of the employees covered by the scheme, meets with an accident and receives Rs. 40,000 as compensation from the insurance Company. Is this receipt taxable in the hands of X? **(3 Marks)**
- (c)who during his life time was a servant of the Government of India. In terms of the family pension scheme of the Government, she receives a monthly family pension of Rs. 4,000 on which a dearness allowance of Rs. 2,600 p.m. is also paid. In computing the total income of A, a claim for standard deduction under section 16 of the Income Tax Act is made. Is this claim allowable? **(3 Marks)**
- (d) An Income Tax Officer issues a requisition under section 133(b) of the Income Tax Act calling on a branch of public sector bank to furnish information on the operations of the accounts of one of its customers. It is understood that neither the bank nor its customer is assessed to income tax by the Income Tax Officer issuing the requisition. The Officer is reported to be engaged on general survey work to rope in new assesses. In neither case is it reported that any assessment proceedings are pending. Can the bank refuse to furnish the information sought? Discuss. **(3 Marks)**

Question 6

- (a) Discuss the provisions under the Income Tax Act, 1961 which authorize the reduction or waiver of penalties by the Commissioner of Income Tax. **(6 Marks)**
- (b) Examine the validity of issue of a notice under Section 148 for reassessment in the following situations: **(2×3=6 Marks)**
- (i) Where the assessee has already been served with an intimation under Section 143(1)(a)?
 - (ii) Where a reassessment has already been made under section 147?
 - (iii) Where a notice under Section 148 has already been issued and the proceedings are still pending before the Assessing Officer.

Question 7

- (a) What is the procedure under the wealth Tax Act, for assessment of persons residing outside India? **(7 Marks)**
- (b) Mr. Girish inherited a house plot situated in the Mumbai Corporation Limits, from his deceased father who had an outstanding income-tax liability of Rs. 12 Lakhs. The property was sold in April, 1997 and the above outstanding liability was collected from the sale consideration by the department. Is the said liability of deceased father a deductible debt while considering the net wealth as on 31.03.1997? **(3 Marks)**

Question 8

The gross total income of Adithya Ltd. For the year ended 31.03.97 is Rs. 5,00,000 of which Rs. 2,00,000 is business income. The following is its summarized Balance Sheet as on 31.03.1997:

Liabilities	Rs.	Assets	Rs.
Share Capital	15,00,000	Vehicles (WDV)	5,00,000
Provision for Gratuity	3,15,000	Closing stock (at cost)	10,00,000
Provision for Taxation	3,50,000	Advance Tax	2,00,000
Creditors	7,35,000	Debtors	7,00,000
		Cash on Hand	40,000
		Cash at Bank	4,60,000
	29,00,000		29,00,000

Share Capital consists of 15,000 (unquoted) equity shares of Rs.100 each. Provision for gratuity has been made on actuarial principles. The market value of vehicles is Rs. 8,00,000. the concern enjoys a gross margin of 25% on sales. The Market value of closing stock is Rs. 11,80,000. of the debtors Rs. 30,000 will not be realizable. Tax payable by the Company including surcharge is Rs. 2,75,000.

Mr. Badang has gifted 500 shares in the above company to Ashok in March 1997. What will be value of the above shares for gift-tax purposes for the Assessment year 1997-98? You may make reasonable assumptions.

(10 Marks)