

Test Series: March, 2016

**MOCK TEST PAPER – 2**  
**FINAL COURSE: GROUP – II**  
**PAPER – 7: DIRECT TAX LAWS**  
**Question No. 1 is compulsory.**

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

**Time Allowed – 3 Hours**

**Maximum Marks – 100**

1. (a) Sheetal Textile Ltd., is engaged in the manufacture of textile fabrics, provides below the following information in respect of the items of Plant and Machinery purchased for the year ended 31-3-2016.

	(Rs. in crores)
<u>Items of Plant &amp; Machinery purchased after 30th December 2015:</u>	
Lorries for transporting goods to sales depots	3
Fork-lift-trucks, used inside factory	4
Computers installed in office premises	1
Computers installed in factory	2
New imported machinery	12
<u>Other items of Plant &amp; Machinery:</u>	
New machinery installed on 1-5-2015	84
New Windmill purchased and installed on 19-7-2015.	22

The new imported machinery arrived at Mumbai port on 30-03-2016 and was installed on 3-4-2016. All other items were installed during the year ended 31-3-2016. The company was newly started during the year.

You are required to compute the quantum of depreciation available under section 32 of the Income-tax Act, 1961 and any other benefit available to Sheetal Textile Ltd in respect of the above items of Plant & Machinery for the year ended 31.3.2016.

Also, compute the WDV of the various blocks of assets.

Will your answer be different if the above assessee is a partnership firm? (12 Marks)

- (b) Compute the tax liability, if any, for the assessment year 2016-17, of a public charitable trust, created under a trust deed for providing relief to disabled persons, registered under section 12AA, from the following particulars of its receipts during the year ended 31st March, 2016 -

	<i>Particulars</i>	<i>Rs. (in Lacs)</i>
(i)	Income from properties held by trust (net)	20
(ii)	Voluntary contributions from public (including the corpus donation of Rs. 6 Lacs)	11
(iii)	Income (net) from business (incidental to main objects)	17

The trust applied Rs. 20 lacs towards various activities and programmes undertaken for the benefit of autistic persons during the year. The trust has also paid Rs.10 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.  
(8 Marks)

2. For the assessment year 2016-17, you are required to compute the total income of M/s. Lotus, a firm, consisting of three partners namely, Mr. Lalit, Mr. Mohan and Mr. Naresh, carried on the business of purchase and sale of refrigerators in wholesale and manufacture and sale of pencils under a deed of partnership executed on 1.4.2011. Mr. Lalit, Mr. Mohan and Mr. Naresh were partners in their individual capacity.

The deed of partnership provided for payment of salary amounting to Rs. 1,25,000 each to Mr. Lalit and Mr. Naresh, who were the working partners. A new deed of partnership was executed on 1.10.2015 which, apart from providing for payment of salary to the two working partners as mentioned in the deed of partnership executed on 1.4.2011, for the first time provided for payment of simple interest @ 12% per annum on the balances standing to the credit of the Capital accounts of partners from 1.4.2015.

The firm was dissolved on 31.3.2016 and the capital assets of the firm were distributed among the partners on 20.4.2016. The net profit of the firm for the year ended 31.3.2016 after payment of salary to the working partners and debit/credit of the following items to the Profit and Loss Account was Rs. 1,50,000:

- (i) Interest amounting to Rs. 1,00,000 paid to the partners on the balances standing to the credit of their capital accounts from 1.4.2015 to 31.3.2016
- (ii) Interest amounting to Rs. 50,000 paid to the partners on the balances standing to the credit of their Current accounts from 1.4.2015 to 31.3.2016
- (iii) Interest amounting to Rs. 20,000 paid to the Hindu undivided family of partner Mr. Lalit @ 18% per annum.
- (iv) Payment of Rs. 25,000 towards purchase of refrigerators made by crossed cheque on 1.11.2015.
- (v) Rs. 30,000 being the value of gold jewellery received as gift from a manufacturer for achieving sales target.

- (vi) Depreciation amounting to Rs. 15,000 on motor car bought and used exclusively for business purposes, but not registered in the name of the firm.
- (vii) Depreciation under section 32(1)(ii) amounting to Rs. 37,500 of new machinery bought and installed for manufacture of pencils on 1.11.2015 at a cost of Rs. 5,00,000.
- (viii) Interest amounting to Rs. 25,000 received from bank on fixed deposits made out of surplus funds.

The firm furnishes the following information relating to it:

- (a) Closing stock-in-trade was valued at Rs. 60,000 as per the method of lower of cost or net realizable value consistently followed by it. The net realizable value of the closing stock-in-trade was Rs. 65,000.
  - (b) Brought forward business loss relating to the assessment year 2015-16 was Rs. 50,000.
  - (c) The fair market value of the capital assets as on 31.3.2016 was Rs. 20,00,000 and the cost of their acquisition was Rs. 15,00,000. *(16 Marks)*
3. (a) Stalwart Ltd., a French company has a subsidiary, IND Ltd. in India. Stalwart Ltd. sells computer monitors to IND Ltd. for resale in India. Stalwart Ltd. also sells computer monitors to FMP Ltd., another computer reseller. It sells 50,000 computer monitors to IND. Ltd. at Rs. 11,000 per unit. The price fixed for FMP Ltd. is Rs. 10,000 per unit. The warranty in case of sale of monitors by IND Ltd. is handled by IND Ltd. However, for sale of monitors by FMP Ltd., Stalwart Ltd. is responsible for the warranty for 3 months. Both Stalwart Ltd. and IND Ltd. offer extended warranty at a standard rate of Rs. 1,000 per annum. On these facts, how is the assessment of IND Ltd. going to be affected? *(5 Marks)*
- (b) Mr. Malik held 17% equity shares in Aqua Ltd., a private limited company. He gifted all the shares held by him in Aqua Ltd., to his wife Mrs. Malik on 18/5/2015. The transfer was made without adequate consideration. On 1/8/2015, Mrs. Malik obtained a loan of Rs. 80,000 from Aqua Ltd., when the company's accumulated profit was Rs. 50,000. What are the tax implications of the above transactions? *(5 Marks)*
- (c) From the following particulars, compute the gross total income of Mr. Anshul for the assessment year 2016-17:
- (i) Mr. Sumit transferred his residential house to Mr. Anshul for Rs.10 lakh on 1.4.2015. The value of the said house as per stamp valuation authority was Rs.18 lakhs. Mr. Anshul is a childhood friend of Mr. Sumit.
  - (ii) Land of Mr. Anshul was acquired by railways in 2013. On 20/11/2015, he received Rs.1,70,000 as interest on enhanced compensation on the order of court.

- (iii) On a fixed deposit of Rs. 10 lakhs, in a bank, Mr. Anshul received an interest of Rs.90,000. He had also borrowed Rs. 50 lakhs from the same bank, on security of the fixed deposit and was liable to pay Rs.50,000 by way of interest to the bank. He, therefore, offered the difference between the two amounts i.e. Rs. 40,000 as "Income from Other Sources". (6 Marks)
4. (a) Ravi owns a residential house which is self-occupied and also a residential plot. He sells the house on 28.2.2016 and the residential plot on 4.3.2016 for Rs.13 lacs and Rs.10 lacs, respectively. The house was purchased on 17.10.2000 for Rs.4.5 lacs and the plot on 13.12.1999 for Rs.3 lacs. Ravi has purchased a new residential house on 3.5.2016 for Rs.7 lacs. Compute the income chargeable under the head "Capital Gain" for the A.Y. 2016-17. Cost inflation indices for the financial year 1999-2000, 2000-2001 and 2015-16 are 389, 406 and 1081, respectively. (4 Marks)
- (b) Can the following transactions be covered under section 43B for disallowance?
- (i) A bank guarantee given by a company towards disputed tax liabilities.
- (ii) Interest payable to Sales Tax Department but not paid before the due date specified in section 139(1). (4 Marks)
- (c) Saraf Limited acquired a machine on 1st April, 2015 for Rs. 10 crores by availing 70% loan facility from a bank. The machine was put to regular use from 31st January, 2016. Interest on loan is charged at 12% per annum.
- Advise Saraf Limited on the treatment of interest payment made on this loan and depreciation allowable for A.Y. 2016-17. Assume that this machine is the only machine in the said block of assets. (4 Marks)
- (d) The following are the particulars of income of three investment funds for P.Y.2015-16:

Particulars	Rs. in lakh		
	Cell	Chip	Cubical
Business Income		2	(2)
Capital Gains	16	14	(6)
Income from other sources	4	4	8

Compute the total income of the investment funds and unit-holders for A.Y.2016-17, assuming that:

- (i) each investment fund has 20 unit holders each having one unit; and
- (ii) income from investment in the investment fund is the only income of the unit-holder.

If Investment Fund Cubical has the following income components for A.Y.2017-18, what would be the total income of the fund for that year?

Business Income Rs.2 lakh

Capital Gains Rs.9 lakh

Income from other source Rs.8 lakh (4 Marks)

5. (a) Mandeep, the owner of a land situated in Punjab used for growing thereon different types of fruits, paddy, vegetables and flowers, received from Indiatimes Movies Ltd., Amritsar, Rs.5 lacs as rent towards the use of this land for shooting of a film. The amount so received was accounted by him in the books as revenue derived from land and claimed to be exempt under section 10(1). He now wants to confirm from you whether the amount has been correctly treated by him as agricultural income.

(4 Marks)

- (b) The concept of Permanent Establishment is one of the most important concepts in determining the tax implications of cross border transactions. Explain the significance thereof, when such transactions are governed by Double Taxation Avoidance Agreements (DTAA).

(4 Marks)

- (c) The Assessing Officer has served a notice proposing to levy penalty under section 271(1)(c) of the Income-tax Act, 1961, as the variation of income assessed to income returned and also the tax effect was more than thirty percent. The addition arose consequent to the disallowance of claim of assessee relating to certain exemption. The assessee wants to reply to the effect that there was no *mens rea* or conscious act of concealment on his part and that the claim made was bonafide, the levy of penalty under section 271(1)(c) is not valid. You are requested to help the assessee in this regard in drafting a suitable reply.

(4 Marks)

- (d) The premises of Shivam were subjected to a search under section 132 of the Act. The search was authorized and the warrant was signed by the Joint Commissioner of Income-tax having jurisdiction over the assessee. The assessee challenged the validity of search, since section 132(1) does not empower Joint Commissioner to authorise a search under the Act. Decide the correctness of the contention raised by the assessee.

(4 Marks)

6. (a) An enterprise engaged in manufacturing of Aluminum wires discontinued its activities and decided to lease out its factory building, plant and machinery and furniture from 1.4.2015 on a consolidated lease rent of Rs.50,000 per month. Compute the income for Assessment Year 2016-17 of the assessee from following information:

	Rs.
(i) Interest received on deposits	1,00,000
(ii) Brokerage paid on hundi loan taken	2,000
(iii) Factory licence fees paid for the year	1,000

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| (iv) Interest paid on hundi and other loans which were given as deposits on interest to others  | 75,000           |
| (v) Expenses incurred on repairs of building, plant and machinery   | 15,000           |
| (vi) Fire insurance premium of plant and machinery and furniture  | 12,000           |
| (vii) Depreciation for the year   | 1,47,500         |
| (viii) Legal fees paid to an advocate for drafting and registering the lease agreement  | 1,500            |
| (ix) Interest paid includes an amount of Rs. 25,000 remitted to a non-resident outside India on which tax was not deducted at source. |                  |
| (x) There is unabsorbed depreciation of Rs. 2,75,000 of the Assessment Years 2014-15 and 2015-16.                                     | <i>(6 Marks)</i> |
- (b) Compute the deduction available to Mr. Himanshu, employed with XYZ Ltd., under Chapter VI-A for A.Y.2016-17 from the following particulars of investments and payments made by him during the previous year 2015-16:
- Deposited Rs.1,20,000 in public provident fund
  - Paid life insurance premium of Rs.15,000 on the policy taken on 1.5.2012 to insure his life (Sum assured – Rs.1,20,000).
  - Deposited Rs.30,000 in a five year term deposit with bank.
  - Contributed Rs.1,80,000, being 15% of his salary, to the NPS of the Central Government. A matching contribution was made by XYZ Ltd. *(6 Marks)*
- (c) Dishant received a notice under section 148 from the Assessing Officer for A.Y. 2012-13 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)*
7. (a) Discuss the correctness or otherwise of the following propositions in the context of the Income-tax Act, 1961:
- (i) The powers of the Commissioner of Income-tax (Appeals) to enhance the assessment are plenary and quite wide.
  - (ii) A High Court does not have an inherent power to review an earlier order passed by it on merits. *(6 Marks)*

- (b) Butter Cocoa Co. of UK entered into contracts with three Indian companies namely XYZ Ltd., Goodday Co. Ltd. and Bakers Ltd. for supplying know-how. Butter Cocoa Co. made an application to the Authority for Advance Rulings (AAR) on the rate of withholding tax on receipts applicable to it.

Also, Bakers Ltd. also made an application to the Assessing Officer for determination of the rate at which tax is deductible on the payment made to non-resident company i.e., Butter Cocoa Co.

The Authority for Advance Rulings (AAR) rejected the application of Butter Cocoa Co. on the ground that the question raised in the application is already pending before an Income-tax authority.

Explain whether the rejection of application by the AAR is justified in law?

*(6 Marks)*

- (c) "Air Pacific Ltd." has paid a sum of Rs.12 lakhs during the year ended 31-3-2016 to Airports Authority of India towards landing and parking charges. The company has deducted tax at source@2% under section 194C on the said payment and remitted the tax deducted within the prescribed time. The Assessing Officer contended that landing and parking charges were levied for use of the land of the airport and hence, the payment was in the nature of rent attracting TDS@10% under section 194-I. Discuss the correctness or otherwise of the contention of the Assessing Officer.

*(4 Marks)*