

MOCK TEST PAPER - 1
FINAL (NEW) COURSE: GROUP – II
PAPER – 7: DIRECT TAX LAWS & INTERNATIONAL TAXATION

Question 1 is compulsory

*Answer any **four** questions from the remaining **five** questions*

Working Notes should form part of the answer. Wherever necessary, suitable assumptions may be made by the candidates and disclosed by way of a note.

All questions relate to Assessment Year 2018-19, unless stated otherwise in the question.

Total Marks: 100 Marks

Time Allowed: 3 Hours

1. (a) Penta Ltd., a domestic company, provides the following information of its Statement of Profit and Loss for the year ended on 31/03/2018. It earned profit of Rs. 15 lakhs after debiting/crediting of the below items:

Items debited to Statement of Profit and Loss:

No.	Particulars	Rs.
1.	Provision for the loss of subsidiary	70,000
2.	Provision for doubtful debts	75,000
3.	Provision for income-tax	1,05,000
4.	Provision for gratuity based on actuarial valuation	2,00,000
5.	Depreciation	3,60,000
6.	Interest to financial institution (unpaid before filing of return)	1,00,000
7.	Penalty for infraction of law	50,000

Items credited to Statement of Profit and Loss:

No.	Particulars	Rs.
1.	Profit from unit established in special economic zone	5,00,000
2.	Share in income of an AOP as a member	1,00,000
3.	Income from units of UTI	75,000
4.	Long term capital gains on sale of a plot	3,00,000

Other Information:

- (i) Provision for income-tax includes Rs. 45,000 of interest payable on income-tax.
- (ii) The capital gain has been invested in specified assets under section 54EC.
- (iii) Depreciation includes Rs. 1,50,000 on account of revaluation of fixed assets.
- (iv) Depreciation as per Income-tax Rules is Rs. 2,80,000.
- (v) Brought forward loss of Rs. 10 lakhs include unabsorbed depreciation of Rs. 4 lakhs.
- (vi) The AOP, of which the company is a member, has paid tax at maximum marginal rate.

Compute minimum alternate tax under section 115JB of the Income-tax Act, 1961, for A.Y. 2018-19, assuming that Penta Ltd. is not required to comply with the Indian Accounting Standards.

(14 Marks)

- (b) Ms. Mamta, a resident Individual has earned income from the following sources during the previous year 2017-18:
- (i) Share of profit from a partnership firm in Kolkata Rs. 30 lakhs.
 - (ii) Income (taxable) from a sole-proprietary concern in Kolkata Rs. 50 lakhs.
 - (iii) Agricultural Income from tea estate in Country XYZ which has no DTAA with India, USD 70000 (gross). Withholding Tax on the above income USD 10500 (Assume 1 USD = Rs 64).
 - (iv) Brought forward Business Loss for the previous year 2014-15 in Country XYZ was USD 10000 which is not permitted to be set off against other income as per the laws of that country. (Assume foreign currency conversion rate on 31.3.2015 was Rs. 64/USD)

Compute taxable income and tax payable by Ms. Mamta for the A.Y. 2018-19 **(6 Marks)**

2. (a) Compute the total income of M/s. LMN, a firm, consisting of three partners namely, Lalit, Mohit and Gagan for the assessment year 2018-19 from the following information. Lalit, Mohit and Gagan were partners in their individual capacity.
- (i) The firm carried on the business of purchase and sale of refrigerators in wholesale and manufacture and sale of footballs under a deed of partnership executed on 1.4.2010. The deed of partnership provided for payment of salary amounting to Rs. 1,25,000 each to Lalit and Gagan, who were the working partners.
 - (ii) A new deed of partnership was executed on 1.10.2017 which, apart from providing for payment of salary to the two working partners as mentioned in the deed of partnership executed on 1.4.2010, 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 1.4.2017.
 - (iii) The firm was dissolved on 31.3.2018 and the capital assets of the firm were distributed among the partners on 20.4.2018.
 - (iv) The net profit of the firm for the year ended 31.3.2018 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:
 - Interest amounting to Rs. 1,00,000 paid to the partners on the balances standing to the credit of their capital accounts from 1.4.2017 to 31.3.2018.
 - Interest amounting to Rs. 50,000 paid to the partners on the balances standing to the credit of their Current accounts from 1.4.2017 to 31.3.2018
 - Interest amounting to Rs. 20,000 paid to the Hindu undivided family of partner Lalit @ 18% per annum.
 - Depreciation amounting to Rs. 15,000 on motor car bought and used exclusively for business purposes, but registered in the name of partner 'Lalit'.
 - Depreciation under section 32(1)(ii) amounting to Rs. 37,500 on new machinery bought and installed for manufacture of footballs on 1.11.2017 at a cost of Rs. 5,00,000. Payment was made by an A/c Payee Cheque.
 - Interest amounting to Rs. 25,000 received from bank on fixed deposits made out of surplus funds.
 - Payment of Rs. 25,000 towards purchase of refrigerators (stock in trade) made by crossed cheque on 1.11.2017.
 - Rs. 30,000 being the value of gold jewellery received as gift from a manufacturer for achieving sales target.

(v) **Other information:**

- (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 2017-18 was Rs. 50,000.
- (c) The fair market value of the capital assets as on 31.3.2018 was Rs. 20,00,000 and the cost of their acquisition was Rs. 15,00,000.

You are required to furnish the explanations for the treatment of the above items. **(14 Marks)**

- (b) Mr. Berlin Kidman, a foreign hockey player and his brother, Mr. Thomas Kidman, a foreign dancer, non-residents in India, furnished the following details for the A.Y. 2018-19:

	Particulars	Mr. Berlin Kidman	Mr. Thomas Kidman
(1)	Income from participation in hockey tournaments in India	Rs. 45,00,000	
(2)	Winnings from lotteries (net)	Rs. 69,100	
(3)	Contribution of an article relating to the sport of hockey in a sports magazine in India	Rs. 10,000	
(4)	Performance in an entertainment shows in India		Rs. 3,00,000

With reference to the provisions of the Income-tax Act, 1961, you are required to –

- (i) Compute their tax liability for the A.Y.2018-19.
- (ii) Decide whether it is necessary for them to file their return of income for A.Y.2018-19.

(6 Marks)

3. (a) (i) Petal Limited, engaged in the business of manufacturing of mobile accessories also effected the sales and purchase of shares of other companies. It suffered loss from such transactions:

- (1) Whether such company can set off its losses from share trading from the profit of manufacturing business?
- (2) If principal business of such company is sale and purchase of shares of other company, then, what would be your answer?

(4 Marks)

- (ii) Mr. Rahim sold his residential house in Chennai and purchased two residential flats adjacent to each other on the same day vide two separate registered sale deeds from two different persons. The builder had certified that he had effected necessary modification to make it one residential apartment. Mr. Rahim sought exemption under section 54 in respect of the investment made in purchase of the two residential flats. The Assessing Officer, however, gave exemption under section 54 to the extent of purchase of one residential flat only contending that sub-section (1) of section 54 clearly restricts the benefit of exemption to purchase one residential house only and the two flats cannot be treated as one residential unit since –

- (1) the flats were purchased through different sale deeds; and
- (2) it was found by the Inspector that, before its sale to the assessee, the residential flats were in occupation of two different tenants.

Examine the correctness of the contention of the Assessing Officer.

(4 Marks)

- (iii) A charitable trust, whose income can be exempt under section 11 of the Income-tax Act, 1961, was formed on 1st March, 2015. For the accounting year ended 31st March, 2018, it earned an income of Rs. 5,30,000.

It filed with the Commissioner of Income-tax its application for registration on 31st August, 2017 explaining that for good and sufficient reasons, it was prevented from filing the application for so long.

Examine by which date the application for registration should have been filed by the trust. Can the trust be deemed to be registered, in case the order of registration is not passed by the Commissioner. **(6 Marks)**

- (b) Shine Inc., a Korean company has a subsidiary, Sahara Ltd. in India. Shine Inc. sells ROs (water purifiers) to Sahara Ltd. for resale in India. Shine Inc. also sells ROs to Rich Ltd., another ROs reseller in India. It sells 30,000 ROs to Sahara Ltd. at Rs. 22,000 per unit. The price fixed for Rich Ltd. is Rs. 18,000 per unit. The warranty in case of sale of ROs by Sahara Ltd. is handled by itself. However, for sale of ROs by Rich Ltd., Shine Inc. is responsible for the warranty for 6 months. Both Shine Inc. and Sahara Ltd. offer extended warranty at a standard rate of Rs. 2,500 per annum. On these facts, examine how the assessment of Sahara Ltd. is going to be affected. **(6 Marks)**

4. (a) (i) Prime (P) Ltd., an Indian company established in the year 2010, reports total income of Rs. 15 lakh for the previous year ended 31st March, 2018. Tax deducted at source by different payers amounted to Rs. 1,35,600 and tax paid in foreign country on a doubly taxed income amounted to Rs. 22,000 for which the company is entitled to relief under section 90 as per the double taxation avoidance agreement.

During the year, the company paid advance tax as under:

Date of payment	Advance tax paid (Rs.)
13-06-2017	38,000
15-09-2017	73,000
12-12-2017	92,000
14-03-2018	77,000

The company filed its return of income for the A.Y. 2018-19 on 22nd October, 2018.

Compute interest, if any, payable by the company under sections 234A, 234B and 234C and fee payable under section 234F. Assume that transfer pricing provisions are not applicable.

Note – Turnover of Prime (P) Ltd. for P.Y. 2015-16 was Rs. 55 crore. **(8 Marks)**

- (ii) Examine the applicability of the provisions relating to deduction of tax at source in the following transactions:

- I. Mr. Shivam, a resident, is due to receive Rs. 4.50 lakhs on 31.3.2018, towards maturity proceeds of LIC policy taken on 1.4.2015, for which the sum assured is Rs. 4 lakhs and the annual premium is Rs. 1,25,000.
- II. On 1.6.2017, Mr. Sahil made three nine month fixed deposits of Rs. 1 lakh each carrying interest@9% with Shatabadi Puram Branch, Adarsh Nagar Branch and Gayatri Vihar Branch of PQR Bank, a bank which has adopted CBS. The fixed deposits mature on 28.2.2018.
- III. Champion India Club, a renowned hockey club, has engaged Shaurya Mishra, a resident in India, as its coach at a remuneration of Rs. 6 lacs per annum. **(6 Marks)**

- (b) (i) Pearl Ltd. is an Indian Company involved in manufacturing and trading in kids garments under the brand name "CHICOO". In order to expand its exports sale, it launched a massive publicity campaign in overseas market. For the purpose of online advertising, it hired the Beauty Inc., a Japanese based company which has no permanent establishment in India and paid Rs. 12

lakhs for its services in the previous year 2017-18.

Discuss the tax and TDS implications of such transaction both in the hands of Pearl Ltd. and Beauty Inc. **(3 Marks)**

- (ii) "The term 'Advance ruling' includes within its scope, a determination by the Authority for Advance Rulings only in relation to a transaction undertaken by a non-resident applicant". Discuss the correctness or otherwise of this statement, as per the income tax law.

(3 Marks)

5. (a) (i) Cash of Rs. 51 lacs was seized on 12.9.2017 in a search conducted as per section 132 of the Act. The assessee moved an application on 27.10.2017 to release such cash after explaining the sources thereof, which was turned down by the department (not satisfied with the explanation given by the assessee). Can the department withhold the explained money? Examine.

(4 Marks)

- (ii) An assessee had credited a sum of Rs. 80,000 in cash in the account of Manan, said to represent a loan obtained from him. The Assessing Officer, having gone into the genuineness of the transaction, disbelieved the story of loan and treated the sum of Rs. 80,000 as the income of the assessee from undisclosed sources. He also started proceedings under section 271D and levied a penalty of Rs. 1,00,000 on the assessee for having accepted the loan in contravention of section 269SS. Examine the correctness of the levy.

(4 Marks)

- (iii) The assessment of Vijaya Ltd. was completed under section 143(3) with an addition of Rs. 28 lakhs to the returned income. Vijaya Ltd. preferred appeal before the Commissioner (Appeals) which is pending now.

In this backdrop, examine the following issues:

- (I) Can the Assessing Officer pass an order under section 154 for rectification of mistake in respect of issues not being subject matter of appeal?
- (II) Can the assessee-company seek revision under section 264 in respect of matters other than those preferred in appeal?
- (III) Can the Commissioner make a revision under section 263 both in respect of matters covered in appeal and other matters?

(6 Marks)

- (b) Explain how the income derived by a resident of a Contracting State in respect of professional services is taxable as per the UN Model Convention. In this context, discuss the scope of professional services.

(6 Marks)

6. (a) (i) "Proceedings cannot be initiated under the Act, unless a proper notice to this effect has been served upon." In this context answer:

- (I) What are the prescribed modes of service of such notice?
- (II) On whom should the notice be addressed and served upon in the cases where the assessee is a
- dissolved firm
 - partitioned HUF.

(5 Marks)

OR

- (i) In respect of the taxes due from a private limited company, which could not be recovered from it, the Tax Recovery Officer attached the properties of an erstwhile director for recovery thereof. It was contended by the director that a notice under section 156 had not been served on him and therefore, the proceedings for recovery were not valid. What is the correct legal position? **(5 Marks)**
- (ii) (I) An Indian company, Sai Ltd., is a closely held company and it is a subsidiary of company Hari Ltd. incorporated in country X. Sai Ltd. was regularly distributing dividends but stopped distributing dividends from 1.4.2003, the date when dividend distribution tax was introduced in India. Sai Ltd. allowed its reserves to grow by not paying out dividends. As a result, no DDT was paid by the company. Subsequently, buyback of shares was offered by Sai Ltd. to its shareholder company Hari Ltd.
- Hari Ltd. paid taxes on the capital gains arising on buyback of shares at the applicable rate. Can GAAR be invoked on the ground that there is a deferral of tax liability by Sai Ltd., the Indian company? **(3 Marks)**
- (II) Ria Ltd. issued a credit note for Rs. 90,000 as brokerage payable to Mr. Swarnim who is the son of the managing director of the company. The purpose is to increase the total income of Mr. Swarnim from Rs. 3,60,000 to Rs. 4,50,000 and reduce the income of Ria Ltd. correspondingly. Specify with reason, the nature of transaction as (i) Tax planning; or (ii) Tax management; or (iii) Tax evasion. **(2 Marks)**
- (iii) Shipra Ltd. filed its return of income for assessment year 2017-18 on 6th June, 2017. The return is selected for regular assessment under section 143(3) for which notice under section 143(2) is served on the company on 3rd October, 2018. The company responded to the notice under section 143(2). Examine whether the service of the notice is within time and if not, whether the assessment order can be challenged by the assessee. **(4 Marks)**
- (b) What is the meaning of, and difference between, a hybrid mismatch and branch mismatch? Briefly mention the reasons why hybrid mismatch arrangements arise. Which Action Plan of BEPS gives recommendations in this regard? **(6 Marks)**