SUGGESTED ANSWERS

PROFESSIONAL PROGRAMME

ADVANCED TAX LAWS AND PRACTICE
(PP-ATLP/2010)

THE INSTITUTE OF
Company Secretaries of India
IN PURSUIT OF PROFESSIONAL EXCELLENCE
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These answers have been written by competent persons and the Institute hopes that the **SUGGESTED ANSWERS** will assist the students in preparing for the Institute's examinations. It is, however, to be noted that the answers are to be treated as model and not exhaustive answers and the Institute is not in any way responsible for the correctness or otherwise of the answers compiled and published herein.

The Suggested Answers contain the information based on the Laws/ Rules applicable at the time of preparation. However, students are expected to be well versed with the amendments in the Laws/Rules made upto **six** months prior to the date of examination.

Price : Rs. 40.00 *(Excluding Postage & Packing)*
Rs. 70.00 *(By Registered Post)*

Samrat Offset Works/2,000/February 2011

PROFESSIONAL PROGRAMME

ADVANCED TAX LAWS AND PRACTICE

TEST PAPER 1/2010

Time allowed : 3 hours *Max. marks : 100*

NOTE : *All Questions are compulsory.*

PART A

DIRECT TAXATION – LAW AND PRACTICE

Question No. 1

(a) Choose the most appropriate answer from the given options in respect of the following :

(i) Article ________of the Constitution provides that no tax shall be levied or collected except by the authority of law

(a) 263

(b) 264

(c) 265

(d) 266

(ii) The rate of income tax on foreign company in respect of income from royalty received from the Government is _________% plus surcharge

(a) 30

(b) 35

(c) 40

(d) 50

(iii) Rate of Dividend Distribution Tax is _________ %

(a) 10

(b) 15

(c) 20

(d) None of the above

(iv) The last date for filing of income tax return u/s 139 (1) by a company is_____

(a) 31st October of the Assessment year

(b) 30th July of the Assessment year

(c) 30th September of the Assessment year

(d) 31st August of the Assessment year

(v) The income tax return of a company can be signed by __________.

(a) Finance officer

(b) Company Secretary

(c) Any one of the directors in absence of the Managing Director

(d) Any of the above. *(1 mark each)*

(b) What is the meaning of 'company' under the Income Tax Act,1961 ? Discuss the various categories of companies under the Act. (10 marks)

Answer to Question No. 1(a)(i)

(c) 265

Answer to Question No. 1(a)(ii)

(d) 50

Answer to Question No. 1(a)(iii)

(b) 15

Answer to Question No. 1(a)(iv)

(c) 30th September of the Assessment year

Answer to Question No. 1(a)(v)

(c) Any one of the directors in absence of the Managing Director

Answer to Question No. 1(b)

Meaning of Company under Section 2(17) of the Income-tax Act

As per Section 2(17), company means:

(i) any Indian company, or

(ii) any body corporate incorporated by or under the laws of a country outside India, or

(iii) any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Indian Income Tax Act, 1922 (11 of 1922) or was assessed under this Act, as a company for any assessment year commencing on or before April 1, 1970; or

(iv) any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the CBDT to be a company.

Categories of Companies under the Income Tax Act, 1961

Broadly speaking, companies under the Income Tax Act viz.:

(i) Indian company

(ii) Domestic Company

(iii) Foreign Company

(iv) Companies in which the public are substantially interested

(v) Companies in which public are not substantially interested – also referred to as closely held companies.

Indian Company

Section 2(26) of the Income Tax Act, 1961 defines the expression 'Indian Company' as a company formed and registered under the Companies Act, 1956 and includes:

(a) a company formed and registered under any law relating to companies formerly in force in any part of India (other than the State of Jammu and Kashmir, and the Union Territories specified in (e) below);

(b) any corporation established by or under a Central, State or Provincial Act;

(c) any institution, association or body which is declared by the Board to be a company under Section 2(17) of the Income Tax Act, 1961;

(d) in the case of State of Jammu & Kashmir, any company formed and registered under any law for the time being in force in that State; and

(e) in the case of any of the Union Territories of Dadra and Nagar Haveli, Goa, Daman and Diu and Pondicherry, a company formed and registered under any law for the time being in force in that Union Territory;

Provided that the registered or, as the case may be, principal office of the company, corporation, institution, association or body in all cases is in India.

Domestic Company

Section 2(22A) of the Income Tax Act, 1961, defines domestic company as an Indian company or any other company which, in respect of its income liable to tax under the Income Tax Act, has made the prescribed arrangements for the declaration and payment within India, of the dividends (including dividends on preference shares) payable out of such income.

Foreign Company

Section 2(23A) of the Income tax Act defines foreign company as a company, which, is not a domestic company. However, all non-Indian companies are not necessarily foreign companies. If a non-Indian company has made the prescribed arrangements for declaration and payments of dividends within India, such a non-Indian company must be treated as a "domestic company" and not as a "foreign company".

Company in which Public are substantially interested (A widely-held company)

Section 2(18) of the Income Tax, Act defines the expression "company in which the public are substantially interested".

A company is said to be one in which public are substantially interested in the following cases, namely –

(i) If it is a company owned by the Government or the Reserve Bank of India or in which not less than 40 per cent of the shares, whether singly or taken together, are held by the Government or the Reserve Bank of India or a corporation owned by the Reserve Bank of India; or

(ii) If it is a company which is registered under Section 25 of the Companies Act, 1956; or

(iii) If it is a company, having no share capital and if, having regard to its objects, the nature and composition of its membership and other relevant considerations, it is declared by an order of the Board to be a company in which the public are substantially interested. However, such a company shall be deemed to be one in which the public are substantially interested only for the assessment year(s) as may be specified in the declaration; or

(iv) If it is a company which carries on, as its principal business, the business of acceptance of deposits from its members and which is declared by the Central Government under Section 620A of the Companies Act, 1956 to be a Nidhi or Mutual Benefit Society; or

(v) If it is a company in which shares carrying not less than 50 per cent of the voting power have been allotted unconditionally to or acquired unconditionally by, and are throughout the relevant previous year beneficially held by, one or more cooperative societies; or

(vi) If it is a company which is not a private company as defined in Section 3 of the Companies Act, 1956 and equity shares of the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in the profits, i.e. preference shares) were, as on the last day of the relevant previous year, listed in a recognised stock exchange in India;

(vii) If it is a company which is not a private company within the meaning of the Companies Act, 1956, and the shares in the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than 50 per cent (40 per cent in case of an industrial company i.e. an Indian company where business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power) of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant accounting year beneficially held by (a) the Government, or (b) a corporation established by a Central or State or Provincial Act, or (c) any company in which the public are substantially interested or a wholly owned subsidiary company.

Closely held company

A Company in which the public is not substantially interested is known as a closely-held company.

Question No. 2

(a) Explain the provisions of MAT under the Income Tax Act, 1961. *(10 marks)*

(b) What are the factors to be taken into account for organizing a tax planning cell in a medium size company ? *(5 marks)*

Answer to Question No. 2(a)

MAT – Basic Provisions

Every person has to pay tax on his taxable income computed in accordance with the provisions of the Income Tax Act, 1961. However in case of a company, a separate provision has been inserted by Section 115JB which is commonly referred as Minimum Alternate Tax (MAT). As per this section, every company is liable to pay tax of an amount which is higher of following:

(a) Tax liability computed as per the provisions of the Income Tax Act by applying the normal rates applicable to a company.

(b) Tax liability computed as per the provisions of Section 115JB i.e. MAT.

MAT is computed @18% (plus surcharge and cess as applicable) on the book profits of the company. Book profit is computed by making certain adjustments to net profit as per profit and loss account which is to be prepared in accordance with the provisions of the Companies Act, 1956. Therefore in case of a company, the tax payable for any assessment year cannot be less than 18% of book profit.

Meaning of "Book Profit"

According to the Explanation 1 to Section 115JB (2), "Book Profit" means the net profit as shown in the profit and loss account for the relevant previous year prepared under Sub-section (2), as increased by :

(a) the amount of Income tax paid or payable, and the provision therefor; or

(b) the amounts carried to any reserves, by whatever name called other than reserve specified under Section 33AC; or

(c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities, or

(d) the amount by way of provision for losses of subsidiary companies; or

(e) the amount or amounts of dividends paid or proposed; or

(f) the amount or amounts of expenditure relatable to any income to which Section 10 [other than Section 10(38) } or Section 11 or Section 12 apply ;or

(g) the amount of depreciation.

(h) the amount of deferred tax and provision therefore.

(i) the amount or amounts set aside as provision for diminution in the value of any asset.

The net profit as increased by the amounts referred to in Clauses (a) to (i) shall be reduced by the following amounts:

(i) the amount withdrawn from any reserves or provisions if any such amount is credited to the profit and loss account;

However following amounts credited to profit and loss account should not be deducted:

(a) Amount withdrawn from reserve created before 1.4.97 otherwise than by way of a debit to the profit and loss account.

(b) Any other amount withdrawn from reserve or provision on or after 1.4.97, if such amount was not added to profit while computing the book profit of the year in which such amount was transferred to reserve, out of which such amount is withdrawn.

(ii) the amount of income to which any of the provisions of Section 10 {except 10 (38)} or Section 11 or Section 12 apply, if any such amount is credited to the profit and loss account; or

(iii) the amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or

(iv) the amount withdrawn from revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in Clause (iii) above; or

(v) the amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account. For the purposes of this clause, the loss shall not include depreciation. Therefore, in a case where an assessee has shown profit in a year, but after adjustment of depreciation it results profit or loss, no adjustment in book profit is allowed; or

(vi) the amount of profits eligible for deduction under section 80HHC, 80HHE or 80HHF.

(vii) the amount of deferred tax, if any such amount is credited to the profit and loss account.

The amount computed after increasing or decreasing the above is known as 'Book-Profit'.

MAT Credit

MAT paid under section 115JB is called MAT credit. According to section 115JAA the amount of MAT credit shall be allowed to be carried forward and set off in a year when the tax becomes payable on the total income computed under the regular provisions of the Income Tax Act. However, the carry forward shall be allowed only for 10 assessment years immediately succeeding the assessment year in which the tax credit becomes allowable. No interest shall be allowed on the amount of MAT credit.

Answer to Question No. 2(b)

Organisation of tax planning cell in a medium size company

Companies having effective tax planning cells can plan their transactions with a view to attract the least incidence of tax. Important factors which shall determine the organisation of tax planning cell in a mid-size company are as follows:

(a) *Complexity and volume of work* : Volume of tax work to be handled is large and complex in a mid size company, therefore it is required to appoint a special tax expert along with the required staff.

(b) *Separate Documentation* : Documentation is an indispensable ingredient of tax management. The assessee has to keep reliable, complete and updated documentation for all the relevant tax files so that the documentary evidence can be made available at a short notice whenever it is required.

(c) *Data Collection* : The staff concerned with taxation has to collect and keep on collecting data relating to latest circulars, case laws, rules and provisions, and other government notifications to keep abreast of the current developments. This could also guide them in any particular area, when such guidance is needed. This would enable easy availability of information at the relevant time.

(d) *Integration* : Tax planner should be consulted by all the departments of the company to know the impact of taxation on their decisions. It would be necessary to integrate and properly link all the departments of the company with the tax planning department. Any project or blue print may have a tax angle. This has to be identified early enough to facilitate better tax compliance and availing of the several incentives. The department has to deal with all taxes (State, Central and Local Self Governments).

(e) *Constant Monitoring* : In order to obtain the intended tax benefits, persons connected with tax management should ensure compliance of all the pre-requisites, like procedures, rules etc. Besides, there should be constant monitoring, so that all the tax obligations are discharged and penal consequences avoided.

(f) *Developing Tax effective Alternatives* : A managerial decision could be assumed to have been well taken only if all the pros and cons are considered. A tax planner could guide important decisions, by considering varieties of alternatives and choices.

(g) *Take advantage of variance allowances and deductions* : A tax manager has to keep track of the provisions relating to various allowances, deductions, exemptions, and rebates so as to initiate tax planning measures.

PART B

INDIRECT TAXATION – LAW AND PRACTICE

Question No. 3

(a) Choose the most appropriate answer from the given options in respect of the following:

(i) Excise Duty is levied by the Union Government vide Entry No.____ of the Union List:

(a) 82

(b) 83

(c) 84

(d) 85

(ii) Excise Duty is charged under Section _____ of the Central Excise Act, 1944:

(a) 2

(b) 3

(c) 4

(d) 5

(iii) Notice for recovery of Excise duties not levied or not paid or short levied or short paid or erroneously refunded can be served within _______ of the relevant date:

(a) 6 months

(b) 1 year

(c) 2 years

(d) 3 years

(iv) Special Audit under section 14A of the Central Excise Act, 1944 can be ordered by _______________:

(a) Assistant Commissioner of Central Excise

(b) Deputy Commissioner of Central Excise

(c) Either (a) or (b) with previous approval of Chief Commissioner

(d) Chief Commissioner

(v) Any Central Excise officer who exercises his powers of search, seizure etc unreasonably or vexatiously or unnecessarily can be punished with a fine upto __

(a) Rs. 5000/-

(b) Rs. 2000/-

(c) Rs. 3000/-

(d) Rs. 1000/-

(vi) Claim for refund of Custom Duty may be filed within __________;

(a) 1 year in case import made for personal use

(b) 1 year in case import made by educational institute

(c) 1 year in case import made by hospital

(d) All are correct

(vii) Notice for Custom Duty not levied or short levied or wrongly refunded etc can be served within:

(a) 6 months in case import made for personal use

(b) 6 months in case import made by educational institute

(c) 6 months in case import made by hospital

(d) None of the above

(viii) Authority for Advance Rulings under the Customs Act shall pronounce its ruling within ______days of the receipt of application:

(a) 30

(b) 60

(c) 90

(d) 120

(ix) If the imported goods are not cleared within ______ days of unloading at custom station, the custodian may sell them under permission of the proper officer :

(a) 15

(b) 30

(c) 45

(d) 60

(x) Time limit for appeal to commissioner (Appeal) under Customs Act 1962 is:

(a) 60 days but can be extended by another 30 days

(b) 60 days but can be extended by another 60 days

(c) 60 days and cannot be extended

(d) 30 days but can be extended by another 30 days (1 mark each)

(b) What is meant by "Goods" under the Central Excise Act, 1944? Explain with reference to the relevant case laws. (5 marks)

(c) Explain in brief the provisions related to "Records", "Returns" and "Payment" under Central Excise Law. (5 marks)

Answer to Question No. 3(a)(i)

(c) 84

Answer to Question No. 3(a)(ii)

(b) 3

Answer to Question No. 3(a)(iii)

(b) 1 year

Answer to Question No. 3(a)(iv)

(c) Either (a) or (b) with previous approval of Chief Commissioner

Answer to Question No. 3(a)(v)

(b) Rs. 2000/-

Answer to Question No. 3(a)(vi)

(d) All are correct

Answer to Question No. 3(a)(vii)

(d) None of the above

Answer to Question No. 3(a)(viii)

(c) 90

Answer to Question No. 3(a)(ix)

(b) 30

Answer to Question No. 3(a)(x)

(a) 60 days but can be extended by another 30 days

Answer to Question No. 3(b)

The concept of "Goods"

According to the Section 3(1) of the Central Excise Act, 1944 that, excise duty is a duty on the goods. Therefore, it is very important to understand the term 'goods'. The Explanation to the Section 2 (d) of the Central Excise Act (inserted w.e.f 10.05.2008) has provided a definition of the term "goods" for the purpose of defining "excisable goods". Accordingly, "goods" includes any article, material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable. Further, the scope of the term "goods" can be derived from various definitions available elsewhere:

(a) *Article 366(12) of the Indian Constitution* contains an inclusive definition which says that "goods" includes all materials commodities and articles.

(b) *Section 2(22) of the Customs Act, 1962* defines "goods" to include vessels, aircraft and vehicles; stores; baggage; currency and negotiable instruments and "any other kind of moveable property". This definition framed specifically for Customs purposes may not be of much utility as determining the scope of "goods" indigenously manufactured, for purposes of excise taxation.

(c) *Section 2(7) of the Sale of Goods Act, 1930* defines "goods" as to mean "every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale". While the second part of this definition is of an inclusive nature, the first part is quite specific. According to this definition, every kind of movable property other than actionable claims constitutes 'goods'.

(d) *The Supreme Court in the case of Union of India* v. *Delhi Cloth and General Mills* (Civil Appeals 168–170 of 1960) stated that an article can be called goods, if it is known in the market as such and can ordinarily be brought to the market for being bought and sold. Deriving considerable inspiration from the Webster's definition, the Supreme Court stated that for excise purposes, anything will become goods only if it is either sold or is capable of being sold. The stress they placed on saleability as the deciding criterion appears to be on the ground that since excise is a duty on goods at the stage of manufacture, and manufacture is mostly for purposes of sale, it is saleability which is the crucial criterion.

In any event, the principle enunciated by the Supreme Court in the DCM case had stood the test of time, and we can well say that though there is no statutory definition of the word 'goods' in Central Excise law, the correct scope of the word has crystallized by now and it is those movable things that are either sold or are capable of being sold, constitute 'goods' for purposes of levy and collection of excise duties.

Answer to Question No. 3(c)

Records under Central Excise Law

The statutory records required to be maintained under Central Excise Rules, 1944 were dispensed with as a measure of simplification in the year 2000 and reliance is placed on the private records of the assessee. Every assessee shall maintain private records to met the requirements of the rules.

There is a specific requirement about maintenance of 'Daily Stock Account' in Rule 10. Every assessee is also required to furnish to the Range Officer a list of all the records maintained by him for accounting of transactions regard to receipt, purchase, manufacture, storage, sale or delivery of the goods including inputs and capital goods. Every assessee shall, on demand make available to the Range Officer or the audit party, the records maintained by him in terms of sub rule 2 of rule 22, cost audit reports, if any, and income tax audit report, if any,

Filing of returns

Rule 12 of the Central Excise Rules, 2002 lays down the provisions relating to filing of return. As per Sub-rule (1) of this Rule, every assessee is required to submit a monthly return in proper form of production or removal of goods and other relevant particulars to the superintendent of Central Excise, within ten days after the close of the month to which the return relates.

It has also been provided that where an assessee is availing the exemption under a notification based on the value of clearances in a financial year, he shall file a quarterly return in proper form of production and removal of goods and other relevant particulars within twenty days after the close of the quarter to which the return relates. According to Notification, the return is required to be filed in quintuplicate in Form ER-1 (EOU/EPZ/SEZ units are required to file return in Form ER-2). For SSIs Form ER-3 has been prescribed.

Electronic Filing (E-filing of return)

CBEC has introduced the facility of filing the monthly/quarterly excise returns electronically. The facility of e-filing of excise returns has been made effective from 30.06.2004. The facility to file excise returns electronically is optional and all the manufacturers of excisable goods, EOUs and registered dealers may choose this facility.

To avail the facility of e-filing of excise returns, assessees and registered dealers who intend to avail the facility of e-filing of excise returns and TR-6 challans are required to submit an application in the prescribed form to their jurisdictional Assistant/Deputy Commissioner of Central Excise. After receipt confirmation, User ID and Password from the Department, the assessee can file return on-line.

Payment of Duty

Rule 8 of the Central Excise Rules, 2002 lays the provisions relating to manner of payment of duty. Goods are cleared from the factory under an invoice and the duty is paid either by cash and/or CENVAT Credit.

RULE 8 : Liability on goods removed is immediate. But the Government allows the assessee to make the payment in monthly instalments. In case of non-SSI assessee, for all the removals in a month, the duty can be paid by 5th of the following month. In case of an SSI it is payable by 15th of next month. In both the cases, for all removals in the month of March, it is payable by 31st March.

Discontinuation of installment facility : If the assessee is not able to pay duty and the default continues beyond 30 days, the installment payment will be discontinued.

Consequently, the payment is to be made through bank or by PLA for each removal and Cenvat credit cannot be utilized.

E-payment has been made mandatory for the assessee who paid Rs. 50 lakh or more in cash in previous financial year. One extra is allowed for e-payment of excise duty except for the month of March.

Question No. 4

Explain the concept of "valuation based on transaction value" with special focus on the Central Excise Valuation Rules, 2000. (10 marks)

Answer to Question No. 4

Valuation under Section 4 (Transaction Value)

If a product is not notified under Section 4A and there is no tariff value fixed for it under Section 3(2), it has to be assessed according to the transaction value determined under Section 4.

According to Section 4(3)(d) read with sub-section (1) of Section 4, for applicability of transaction value in a given case, for assessment purposes, the following conditions should be satisfied :

(a) The goods are sold by an assessee for delivery at the time and place of the removal.

(b) The assessee and the buyer of the goods are not related, and

(c) The price is the sole consideration for the sale.

If any one of the above requirements is not satisfied, then the transaction value shall not be assessable value and value in such case has to be arrived at under the valuation rules, notified separately as provided in Section 4(1)(b).

1. Time and place of removal

Goods sold at the time and place of removal means:

(i) there is sale at the time of removal; and

(ii) such sale is for delivery at the place of removal i.e. place of removal and place of delivery are same. Obviously, the price is ex-factory price and ownership is changing hands at the place of removal itself.

The place of removal has been defined under Section 4(3)(c) as, (i) "factory or any other place or premises of production or manufacture of the excisable goods;

(ii) a warehouse or any other place or premises wherein the excisable goods have been permitted to be deposited without payment of duty, from where such goods are removed."

(iii) Sales depot, or any such place where goods are sold from after removal from factory.

Assessee has been defined as a person who is liable to pay duty under the Act and includes his agent. [Section 4(3)(a)].

Note. Sales depot, place of consignment agent, branch office etc. are brought within the purview of the place of removal under the new definition but the sale from them is governed by Rule 7 of Valuation Rules.

2. Assessee and Buyer are not related

Even if there is sale, the transaction value on such sale is not acceptable if the assessee (manufacturer) and the buyer are related: Section 4 (3) clarifies that persons shall be deemed to be related if-

— they are inter-connected undertakings;

— they are relatives;

— amongst them the buyer is a relative and distributor of the assessee, or a sub-distributor of such distributor; or

— they are so associated that they have interest, directly or indirectly in the business of each other.

"Inter-connected undertaking" has been defined under Section 2(g) of MRTP Act and the term "relative" is defined under the Companies Act, 1956.

3. Price is the sole consideration

The price paid by the buyer need not necessarily be the sole consideration. There may be some other considerations in addition to the price. If there is any other consideration that could possibly influence price, the assessable value has to be determined under Rule 6.

Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000: The valuation of excisable goods is made with the help of Rules when transaction value cannot be applied directly. Section 4(1)(b) specifies that rules have to be resorted to, where there is no sale or where the conditions under Section 4(1)(a) are not satisfied.

Rule 4. When there is no sale at the time of removal : When there is no sale at the time of removal, sale price is not available. Naturally, transaction value is not available. Then, the following methodology is prescribed under Rule 4.

— Take the price of such goods sold at the time nearest to the time of removal.

— Make reasonable adjustments. These adjustments may be with reference to any price fluctuations during the time lag between these two removals, difference in the quality, and packing material used and so on.

Rule 5 : Delivery for sale not at the place of removal : Rule 5 is applicable when there is a sale at the time of removal, but delivery is not at factory, but at some other place, say, the place of buyers. This is a situation where F.O.R. [free on road/ rail] price is quoted in the invoice. Since the price is not ex-factory price, transaction value cannot be applied. Hence, valuation is done under Rule 5.

Conditions necessary for the application of Rule 5:

— Place of removal and place of delivery are not same.

— Price quoted is F.O.R. price, including the cost of transportation and insurance from the factory to the place of buyer. [F.O.R. - free on road]

— The price for the purpose of valuation will be the price charged from the buyer i.e. F.O.R. price – the cost of transport up to the point of delivery. (F.O.R. price-cost of transport etc.)

— If the manufacturer uses his own vehicles freight charges as certified by a C.A./ CWA are allowed to be deduced from F.O.R. price.

— Equalised freight charges are allowed to be deducted from F.O.R value.

Equalised freight : This is an average of the freight charges allowed to be deducted uniformly for all sales to different destination. This is possible only when the sale is from factory.

Rule 6 – Price not sole consideration : Apply this rule under the following conditions:

— There is a sale at the place of removal, but the consideration received is not the total consideration. It means, if the same goods are sold in the open market, they would fetch more money.

— Aggregate consideration is arrived at by adding all other considerations to the transaction value, that flowed directly or indirectly from the buyer to the assessee.

— The value of the items given are added to the consideration to make it the transaction value i.e.

— Value of materials, components, parts and similar items relatable to such goods.

— Value of tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods.

— Value of material consumed, including packaging materials in the production of such goods.

— Value of engineering, development, art work, design work and plans and sketches.

— Interest on advance amount received from the buyer is added to the transaction value. In Metal Box Ltd., Ponds India advanced huge amount to Metal Box Company and enjoyed 50% bulk discount on its purchases. HELD: Discount may be allowed when the interest is added to the sale price to arrive at the assessable value.

— Cenvat credit availed on the inputs should be deducted from the cost of such inputs. [*Dai Ichi Karkaria Ltd.* 1999, S.C.]

The value of above items is added to the extent they are not included in the transaction value even if they are received indirectly, or received free of cost. Earlier, in Hindustan Polymers case, the Supreme Court held that the packing material supplied by buyer is not includible in the assessable value. But as per the present scheme of valuation under Rule 6, it is includible.

Rule 7 – When goods are sold from sales depot, or any other place : When there is removal of goods from factory as stock transfer, to the sales depot, place of consignment agent or any other place, the value of the goods will be the price prevailing at the depot, etc. on the date of removal from the factory.

As per the rules, assessment is to be made at the time of removal of goods from the factory or warehouse as the case may be. Dutiability and rate of duty are ascertained on the date of removal. As assessment is necessary on the date of removal, the price prevailing at the place of sale on the date of removal is taken.

— For instance, the goods are cleared from the factory today for sale to be made from the depot, the duty is assessed on the basis of the price prevailing at the depot today. It means it is the price at which actual transaction took place today at the depot.

— If there is no sale and the price is not available at the depot on the date of removal from the factory/ warehouse, then the price at the depot on the date (preceding) nearest to the date of removal shall be taken.

— If different quantities are sold at different rates, then the price of the aggregate quantity [greatest quantity] sold on that day or on the date nearest to the removal shall be taken. If the above scheme can not be applied then rule 11 shall be applied.

Rule 8 – When goods are not sold but captively consumed : Captive consumption means self consumption. When the goods manufactured are not sold but are reused in the factory for the manufacture of other articles, the value for the purpose of excise shall be 110% of the cost of production. Here, the valuation is based on the cost sheet certified by a Cost Accountant/Chartered Accountant.

Rule 9 - Sale to related person other than inter connected undertaking : This rule covers those situations where goods are sold to or through related persons other than the Inter-Connected undertakings. In such a case, the value shall be the normal transaction value at which these are sold by the related person at the time of removal to unrelated persons. Normal transaction value means price of the greatest aggregate quantity. If the related person further sells to his related person who is a retailer, then the price charged to the retailer (even though he is a related person) will be accepted for assessment. If the goods are not sold by the related person, but consumed captively, the value shall be determined as per Rule 8. i.e. 110% of cost of production.

Rule 10 – Sale to / through inter-connected undertakings (and related) : If the inter-connected undertakings also happen to be the related persons under the remaining clauses or they happened to be holding and subsidiary companies, then Transaction Value shall be determined as per Rule 9. In any other case (i.e. the buyer and the seller are merely the inter-connected undertakings), the value shall be determined under Section 4(1)(a), as if they are not related persons at all.

Mere interconnection doesn't affect the valuation. If the Inter-connected Undertakings are otherwise related under other clauses, then only Rule 9 is applied.

Valuation Under Job Work

Earlier there was no specific rule for valuation of goods by job worker. Hence Rule 11 was being applied by using the mechanism given under Rule 6.

Now, in the budget 2007, a new rule 10A has been introduced for valuation of goods under job work.

This rule 10A came into effect from 1-4-2007.

According to this rule, where goods are manufactured by job worker on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, as against the earlier practice where the value is taken as cost of inputs plus the job charges.

— The price charged by the principal manufacturer at the time of removal of goods from the premises of the job worker shall be taken for valuation.

— Such price shall be sole consideration and the principal manufacturer and the buyer shall not be related persons.

— If the price is not sole consideration, follow the mechanism given under Rule 6 and if the transaction is related persons transaction, follow Rule 9.

If the goods are removed at a place other than the place of job worker, then apply normal transaction value of that place of removal as is done under Rule 7.

Rule 11 – Residual method/method of reasonable means : When the value cannot be determined by any of the valuation rules, it shall be determined using reasonable means consistent with the principles and general provisions of these rules and Section 4(1).

Question No. 5

(a) Discuss the various types of Custom Duties which may be levied under the Custom Laws. *(5 marks)*

(b) Describe the procedure of assessment and clearance of imported goods in the lights of the provisions of the Custom Laws. *(10 marks)*

(c) Explain the powers of the Central Government to grant exemption from customs duty. *(5 marks)*

Answer to Question No. 5(a)

Types of Duties under Customs Laws

Basic Duty : It is levied under Section 12 of Customs Act, 1962, and specified under Section 2 of the Customs Tariff Act, 1975. There are different rates for different goods. The basic duty may have two rates under the First Schedule to Customs Tariff Act, 1975; viz. standard rates and preferential rates.

Standard and Preferential Rates : Duty at the "Standard rate" is charged where there is no provision for preferential treatment. To be eligible, for the preferential treatment the goods should be the one imported from any preferential area covered under the Government of India Agreements for charging preferential rate of duty.

Additional Duty/Countervailing Duty : This is levied under Section 3 of the Customs Tariff Act, 1975. The amount is equivalent to the amount of excise duty payable on such goods manufactured in India.

Special CVD [Section 3(5)] (also known as SAD)

This is imposed on imported goods in addition to other duties if any. This is in lieu of sales tax. It is levied on all goods subject to exemption at a fixed rate of 4%.

Exemptions:

— All goods exempt under VAT are also exempt from Spl. CVD.

— When BCD and CVD are exempt, this is also exempt.

— Baggage is exempt.

— EOUs, EHTPs & STPs are exempt for their DTA clearances.

Protective Duty - Section 6 of the Customs Tariff Act, 1975

The objective is to protect the indigenous industry from the imports. Tariff Commission has been established under the Tariff Commission Act. Upon a reference, the Tariff commission makes recommendations to Central Government. If the Central Government is satisfied with the recommendation, it issues a notification.

Safeguard Duty - Section 8B of Customs Tariff Act

The Central Government may impose safeguard duty on specified imported goods, if it is satisfied that the goods are being imported in large quantities and they are causing serious injury to domestic industry". This duty can be imposed only for a limited period, by way of a notification, after an enquiry. It can be imposed provisionally for a maximum period of 200 days.

Anti-Subsidy Duty (Duty on Bounty Fed Articles) - Section 9 of the Customs Tariff Act

If the exporting country pays any subsidy (directly or indirectly) to its exporters for exporting goods to India, the Central Government may impose this duty, by a notification. The amount of duty can be maximum upto the amount of subsidy.

Anti-dumping Duty (ADD) - Section 9A of the Customs Tariff Act

— Dumping means exporting goods to India, at prices lower than the ones in the domestic market of the exporting country, subject to certain adjustments.

— To prevent dumping, the Central Government may levy ADD upto margin of dumping. [MOD].

— MOD is the difference between the normal value and the price charged for exports to India.

— Normal value means comparable price in the ordinary course of trade, in the exporting country, after making adjustments to the extent of conditions of sale, taxation, etc.

National Calamity Contingent Duty (NCCD) : It is levied on pan masala, chewing tobacco and cigarettes, motor cars, crude oil etc.

Education Cess : An education cess has been imposed on imported goods w.e.f. 9.7.2004. The cess will be 2% of the aggregate duty of Customs. However, education cess will not be payable on safeguard duty under sections 8B and 8C, countervailing duty under section 9, anti Dumping duty under sections 9A of the Customs Tariff Act and education cess on imported goods. Further Additional Duty payable under section 3(5) will also not be considered while calculating education cess. Secondary and Higher Education Cess is payable at 1%.

Answer to Question No. 5(b)

Assessment and Clearance Procedure

The assessment and clearance procedure involves, generally, the following steps :

(a) The master of the vessel carrying the goods calls on the port, files the arrival report and the import general manifest IGM number to the manifest to permit the master of the vessel to land and unload the cargo.

(b) Customs authorities check the documents, grant entry inwards to the vessel,assign IGM number to the manifest and permit the master of the vessel to land and unload the cargo.

(c) The vessel discharges the cargo into the custody of the port trust authorities.

(d) The importer of the goods delivers the negotiable bill of lading received from the supplier of the goods to the master of the vessel and obtains the delivery order.

(e) It is the right and responsibility of the importer to file an application for clearance of goods and this application is called the bill of entry.

(f) The customs authorities check the bill of entry with the IGM and note the bill of entry in the IGM.

(g) The bill of entry is then processed by the appraising department to decide upon the tariff classification and valuation.

(h) The customs authorities may physically examine the goods for the purpose of classification and valuation.

(i) If the bill of entry for home consumption is presented, then the customs duty is collected and "pass out of customs charge" issued.

(j) If the bill of entry for warehousing is presented, then the importer executes a warehousing bond equal to twice the amount of duty assessed and then the goods are deposited into the warehouse.

(k) The importer on showing the "pass out of customs charge" to the port trust authorities takes delivery of the goods".

(l) In case the goods are warehoused, the importer files a bill of entry for ex-bond clearance for home consumption at the time of clearance of goods from such warehouse.

(m) The customs duty is then collected and the goods are allowed to be taken from the port.

Answer to Question No. 5(c)

Power to grant Exemption from Duty

The power to the Central Government to grant exemption from duty in respect of any goods liable to Customs duty is provided in Section 25 of the Act. The provisions are explained as follows:

(1) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by notification in the Official Gazette, exempt generally either absolutely or subject to such conditions (to be fulfilled before or after clearance) as may be specified in the notification, goods of any specified description from the whole or any part of duty of customs leviable thereon.

(2) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by special order in each case, exempt from the payment of duty under circumstances of an exceptional nature to be stated in such order, any goods on which duty is leviable.

(2A) The Central Government may, if it considers it necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification issued under Sub-section (1) or order under Sub-section (2), and every such explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.

(3) An exemption under Sub-section (1) or Sub-section (2) in respect of any goods from any part of the duty of customs leviable thereon (the duty of customs leviable thereon being hereinafter referred to as the statutory duty) may be granted by providing for the levy of a duty on such goods at a rate expressed in a form or method different from the form or method in which the statutory duty is leviable and any exemption granted in relation to any goods in the manner provided in this subsection shall have effect subject to the condition that the duty of customs chargeable on such goods shall in no case exceed the statutory duty.

Explanation : "Form or method", in relation to a rate of duty of customs, means the basis, namely, valuation, weight, number, length, area, volume or other measure with reference to which the duty is leviable.

(4) Every notification issued under Sub-section (1) or (2A) shall:

(a) unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette;

(b) also be published and offered for sale on the date of its issue by the Directorate of Publicity and Public Relations of the Board, New Delhi.

(5) Notwithstanding anything contained in Sub-section (4), where a notification comes into force on a date later than the date of its issue, the same shall be published and offered for sale by the said Directorate of Publicity and Public Relations on a date on or before the date on which the said notification comes into force."

(6) Notwithstanding any thing contained in this Act, no duty shall be collected if the amount of duty leviable is equal to, or less than, one hundred rupees.

PART C

INTERNATIONAL TAXATION

Question No. 6

(a) What do you understand by "Passive Foreign Investment Company" ? *(5 marks)*

(b) What do you understand by "uncontrolled transaction" ? *(5 marks)*

(c) What are the benefits available for "amalgamation' under Income tax Act ? *(10 marks)*

Answer to Question No. 6(a)

Passive Foreign Investment Company (PFIC)

A passive foreign investment company (PFIC) is a foreign company with predominantly investment income, or whose assets are primarily intended to generate investment income. Classification as a PFIC occurs when 75% or more of the company's income is passive, or when more than 50% of the company's assets exist in investments earning interest, dividends, and/or capital gains. According to US Tax code a foreign corporation is considered a "passive foreign investment company" if either of two tests are satisfied.

Under the Income Test, a foreign corporation is considered a PFIC if 75 percent or more of the foreign corporation's gross income for the taxable year consist of passive income. Passive income includes dividends, interest, royalties, rents, annuities, net gains from certain commodities transactions, net foreign currency gains, income equivalent to interest, payments in lieu of dividends, income from notional contracts, and income from certain personal service contracts.

Under the Asset Test, a foreign corporation is considered a PFIC if 50 percent of the foreign corporation's assets produce - or are held to produce - passive income.

There are certain exceptions to these rules like a newly-formed corporations frequently hold short-term investments that may create a significant percentage of income prior to the business truly commencing. As such, in the first taxable year in which a foreign corporation has gross income (the "Start-up Year"), the company will not be considered a PFIC.

Answer to Question No. 6(b)

Uncontrolled Transaction

Rule 10A(a) defines an 'Uncontrolled Transaction' to mean 'a transaction between enterprises other than associated enterprises, whether resident or non resident .An uncontrolled transaction can be between :

— A resident and non resident

— A resident and a resident

— A non resident and a non resident.

When an uncontrolled transaction has been entered into it could be said that it has been contracted in an 'uncontrolled condition'

Arm's length price is a price applied or proposed to be applied in a transaction between persons other than associated enterprises in uncontrolled conditions [Section 92F(iii) read with Rule 10A]. It is a price arrived at disregarding any influence from associated enterprise. It is like simulated price arrived between parties not associated with each other.

Answer to Question No. 6(c)

Tax concessions/incentives in case of amalgamation

If any amalgamation takes place within the meaning of Section 2(1B) of the income-tax, the following tax concession shall be available :

(i) Tax concession to amalgamating company

(ii) Tax concession to shareholders of the amalgamating company.

(iii) Tax concession to amalgamated company.

Tax concession to amalgamating company

(i) Capital Gains tax not attracted : According to Section 47(vi), where there is transfer of any capital asset in the scheme of amalgamation, by an amalgamating company to the amalgamated company, such transfer will not be regarded as a transfer for the purpose of capital gain provided the amalgamated company, to whom such assets have been transferred, is an Indian company.

(ii) Tax concession to a foreign company [Section 47(via) : Where a foreign company holds any shares in an Indian company and transfers the same, in the scheme of amalgamation, to another foreign company, such transaction will not be regarded as transfer for the purpose of capital gain under section 45 of the Income-tax Act if the following conditions are satisfied :

(a) Atleast 25% of the shareholders of amalgamating foreign company should continue to remain shareholders of amalgamated foreign company; and

(b) Such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated.

Tax concession to the shareholders of a amalgamating company [Section 47(vii) : Where a shareholder of a an amalgamating company transfers his shares, in a scheme of amalgamation, such transaction will not be regarded as a transfer for capital gain purposes, if following conditions are satisfied :

(i) the transfer of shares is made in consideration of the allotment to him of any share or shares in the amalgamated company, and

(ii) the amalgamated company is an Indian company.

Tax concession to amalgamated company

The amalgamated company shall be eligible for tax concessions only if the following two conditions are satisfied :

(i) The amalgamation satisfies all the three conditions laid down in section 2(1B); and

(ii) The amalgamated company is an Indian company.

These tax concessions are available in respect of expenditure on scientific research under Section 35(5), expenditure incurred for obtaining license to operate telecom services under Section 35ABB(6), preliminary expenses under Section 35D(5), capital expenditure on family planning under Section 36(1)(ix) etc.

Carry forward and set-off of business losses and unabsorbed depreciation of the amalgamating company:

In addition to the above benefit/concessions, the amalgamated company shall be allowed to carry forward and set of the business losses and unabsorbed depreciation of the amalgamating company if all the conditions mentioned in Section 72A are satisfied.

TEST PAPER 2/2010

Time allowed : 3 hours *Max. marks : 100*

NOTE : *All Questions are compulsory.*

PART A

DIRECT TAXATION – LAW AND PRACTICE

Question No. 1

(a) Choose the most appropriate answer from the given options in respect of the following :

(i) Taxes on agriculture income can be levied by _________

(a) Union Government

(b) State Government

(c) Either (a) or (b)

(d) Neither (a) or (b)

(ii) Which of the following is said to be a company in which public are substantially interested:

(a) Company owned by the Government or RBI

(b) Company registered under Sec 25 of the Companies Act

(c) Public Company whose equity shares are listed on a stock exchange

(d) All of the above

(iii) Revised Return can be filed by a company _____________

(a) Any time before expiry of one year from the end of Assessment year

(b) Any time before completion of assessment

(c) At any time whichever is earlier of (a) or (b)

(d) None of the above

(iv) Maximum penalty for failure to file return within due date is _______

(a) Rs. 1000 /- per day till the default continues

(b) Rs. 5000/-

(c) Rs. 10,000/-

(d) None of the above

(v) Every appeal to the Appellate Tribunal shall be filed within _____days of the date on which the order sought to be appealed against is communicated.

(a) 30

(b) 45

(c) 60

(d) None of the above *(1 mark each)*

(b) *What do you understand by a company in which public is substantially interested?* *(5 marks)*

(c) *Discuss the provisions related to 'appeal to the Supreme Court' under Section 261 of the Income Tax Act, 1961.* *(5 marks)*

Answer to Question No. 1(a)(i)

(b) State Government

Answer to Question No. 1(a)(ii)

(d) All of the above

Answer to Question No. 1(a)(iii)

(c) At any time whichever is earlier of (a) or (b)

Answer to Question No. 1(a)(iv)

(b) Rs. 5000/-

Answer to Question No. 1(a)(v)

(c) 60

Answer to Question No. 1(b)

Company in which public are substantially interested

Section 2(18) of the Income Tax, Act defines the expression "company in which the public are substantially interested".

A company is said to be one in which public are substantially interested in the following cases, namely –

(i) If it is a company owned by the Government or the Reserve Bank of India or in which not less than 40 per cent of the shares, whether singly or taken together, are held by the Government or the Reserve Bank of India or a corporation owned by the Reserve Bank of India; or

(ii) If it is a company which is registered under Section 25 of the Companies Act, 1956; or

(iii) If it is a company, having no share capital and if, having regard to its objects, the nature and composition of its membership and other relevant considerations, it is declared by an order of the Board to be a company in which the public are substantially interested. However, such a company shall be deemed to be one in which the public are substantially interested only for the assessment year(s) as may be specified in the declaration; or

(iv) If it is a company which carries on, as its principal business, the business of acceptance of deposits from its members and which is declared by the Central Government under Section 620A of the Companies Act, 1956 to be a Nidhi or Mutual Benefit Society; or

(v) If it is a company in which shares carrying not less than 50 per cent of the voting power have been allotted unconditionally to or acquired unconditionally by, and are throughout the relevant previous year beneficially held by, one or more cooperative societies; or

(vi) If it is a company which is not a private company as defined in Section 3 of the Companies Act, 1956 and equity shares of the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in the profits, i.e. preference shares) were, as on the last day of the relevant previous year, listed in a recognised stock exchange in India;

(vii) If it is a company which is not a private company within the meaning of the Companies Act, 1956, and the shares in the company (not being shares entitled to a fixed rate of dividend whether with or without a further right to participate in profits) carrying not less than 50 per cent (40 per cent in case of an industrial company i.e. an Indian company where business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power) of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant accounting year beneficially held by (a) the Government, or (b) a corporation established by a Central or State or Provincial Act, or (c) any company in which the public are substantially interested or a wholly owned subsidiary company.

Answer to Question No. 1(c)

Appeal to the Supreme Court (Section 261)

The assessee or the Commissioner may prefer an appeal to the Supreme Court against the judgment delivered by the High Court on the reference application made to it by the Tribunal (under Section 256) against an order made under Section 254 before the 1st day of October, 1998 or an appeal made to High Court in respect of an order passed under Section 254 on or after that date provided the High Court certifies the case to be fit for appeal to the Supreme Court. The right of appeal is, therefore, conditional and may be availed of only if the High Court gives a certificate of such fitness.

The High Court could certify the case as a fit one for appeal and grant leave to the Supreme Court if a substantial question of law is involved or if the question is likely to come up in successive year or if the question is otherwise of great public or private importance.

An application of fitness for appeal to the Supreme Court has to be made within 60 days from the date of High Court's judgment (under Article 132 of the Schedule to the Limitation Act, 1963). The time required for taking a certified copy of the High Court's judgment is to be excluded in computing such period of limitation.

If the High Court refuses to certify a case to be fit for appeal to the Supreme Court, an application may be made to the Supreme Court (under Article 136 of the Constitution) for special leave to appeal against the decision of the High Court.

Where the judgment of the High Court is changed or reversed in the appeal, effect is given to the order of the Supreme Court [Section 262(3)]. The law declared by the Supreme Court is binding on all courts within the territory of India under Article 141 of the Constitution.

To award the cost of an appeal is at the discretion the Supreme Court [Section 262(2)].

Question No. 2

(a) *What are the important areas of tax planning in the context of Income Tax Act, 1961.* *(10 marks)*

(b) *Explain in brief the Appealable orders before the Appellate Tribunal.* *(5 marks)*

Answer to Question No. 2(a)

1. Important areas of Tax Planning at the time of setting up of new business entity:

(a) *Form of organisation/ownership pattern*

The selection of particular form of organisation depends not only on the magnitude of financial requirements and owner's liability, but also on the tax considerations. Normally, depending upon the level of operation, expected profitability need for external financing and expected requirements of technical expertise, a suitable form can be chosen.

The company being a separate legal entity, confers certain valuable benefits in the matter of tax planning to its shareholders and the persons connected with the management of the company.

The important tax privileges and advantages to a company over the other forms can be summarized as under:

(i) Allowability of remuneration, for the persons who are managing the affairs of the company and also owning its shares.

(ii) The provisions relating to clubbing of income under Section 64 of the Income Tax Act, 1961 do not apply. However, if spouse of an individual having a substantial interest in a company receives remuneration from the same company, such remuneration is added to the income of the individual unless the spouse is technically or professionally qualified. [Section 40A(2)(b) of the Income Tax Act, 1961].

(iii) Dividends received by the shareholders from any Indian company have been fully exempt under Section 10(33) from Assessment Year 1998-99 to Assessment Year 2002-2003. However, any income by way of dividend referred to in Section 115-O is exempt under Section 10(34) from Assessment Year 2004-05.

(iv) Companies are subjected to flat rate of tax, regardless of the quantum of their income. The domestic companies now pay tax @ 30% plus surcharge @ 7.5%, if applicable and education cess @ 3% for Assessment Year 2011-12. This, however, may not seem to be an advantage in view of low slab rates applicable to sole proprietorships, but when we look at the total incidence of tax after taking into account the various deductions allowed to companies and the scheme of perquisites, the real owners of companies to stand to benefit.

(v) There are certain special tax concessions, allowances and deductions given under the Income Tax Act, 1961 available only to the company form of business enterprises such as deductions allowed under Section 33AC and Sections 36(1)(ix) and 35D of the Income Tax Act, 1961 etc.

(vi) The shares in companies are treated as long term capital assets if held for more than 12 months and thus qualifying for exemption from capital gain taxation.

On the other hand an individual pays tax on his income on the basis of slab system. He gets the benefit of minimum taxable limit laid down by the respective Finance Acts. Income received by an individual in different capacities, i.e. as a member of a firm is not taxable in hand of partner because the firm has paid tax on it. The owner of a proprietorship firm is treated as an individual for tax purposes.

Entrepreneurs now have an alternative and innovative form of business organization i.e. Limited Liability Partnership (LLP) which combines the benefits of company and general partnership form of business organizations. LLP has separate legal entity, perpetual succession and limited liability of partners. From income tax point of view it is treated same as general partnership firm therefore its profits will be taxed in the hands of the LLP not in the hands of its partners.

(b) *Locational aspects*

In addition to the form of organization, the Income Tax Act provides tax benefits on the basis of the location of the business unit e.g. newly established units in SEZs (Section 10AA), newly established 100% EOU (Section 10B), and therefore, tax planning is relevant from location point of view.

(c) *Nature of business*

Tax planning is relevant from the point of view of the nature of the business also because certain businesses are granted special tax treatment under the Income Tax Act.

2. Important Areas of Tax Planning for the business entities already in existence

(a) *Tax planning relating to corporate restructuring*

Corporate restructuring should be carefully planned to take the maximum benefit through tax planning. The following areas should be given proper attention:

1. Since the unabsorbed losses and unabsorbed depreciation cannot be allowed to be carried forward and set off in the hands of the amalgamated company, except in the cases prescribed under Section 72A of the Act, it is proposed:

   (a) that the scheme of the amalgamation can be put off till such time the full benefit of set off is availed of by the amalgamating company; and

   (b) that the loss carrying company should absorb or take over the business of the profit-making company. This would help in carrying to carry forward the benefits of all unabsorbed losses and depreciation to be set off against the profits derived from the business of the profit-making company.

2. To save from disallowance of the debts of the amalgamating company which subsequently become bad in the hands of the amalgamated company, the amalgamated company should plan to make suitable provision for the expected losses on account of bad debts at the time of fixing the consideration while taking over the business of the amalgamated company.

3. A company whose shares are not quoted on a recognised stock exchange may avail the benefit of amalgamation by amalgamating itself with another company whose shares are quoted on a recognised stock exchange. This would help its shareholders to take the advantage of the quoted price of their shares in the stock exchange while determining their liability for wealth-tax purposes.

4. A loss incurring company and a profit-making company may merge in order to reduce the overall incidence of liabilities to tax under the Income Tax Act, 1961.

5. In case the conditions provided under Sections 2(1B) and 72A of the Act are not satisfied, it may be suggested that the profit making company should merge itself with the loss making company, so that the loss making company does not lose its existence and also enjoys all other benefits.

6. Under Section 2(1B) of the Act, it is provided that for availing the benefits of amalgamation, at least 75% of the shareholders of the amalgamating company should become shareholders of the amalgamated company. In case more than 25% of the shareholders are not willing to become shareholders of the amalgamated company, it is proposed that the amalgamating company may persuade the other shareholders who may be willing, to purchase the shares in the amalgamated company to acquire the shares of the remaining shareholders so that the percentage of dissenting shareholders does not exceed 25%. Alternatively, the amalgamated company prior to, amalgamation, may purchase shares from such dissenting shareholders so as to make such dissenting shareholders to go below the specified percentage of 25%.

(b) *Tax planning relating to financial management decisions*

When a company raises long term loans from financial institutions or by way of public issue of debentures or inviting deposits from the public, it should plan that the expenses incurred on such issues of debentures or expenses towards stamp duty, registration fees, and lawyer's fees should be incurred only after the date of the 'setting-up' of the business. The interest paid before the commencement of production but after setting up of the business on loans taken by the company for the acquisition of its plant and machinery and other assets, forms part of the actual cost of the asset and it should be capitalized in actual cost of asset. Thus, the company would be allowed to capitalise the expenditure and claim a higher depreciation and investment allowance.

The company should also plan the optimum use of the share capital and the borrowed funds. Note that the borrowings should be utilised as far as possible for the acquisition and installation of assets like, buildings, plant and machinery so that interest can be capitalised for the period after setting up of the acquired assets like buildings, plant and machinery but before the commencement of production. The interest and higher amount of depreciation (due to capitalisation of expense) may be claimed as revenue expenditure pertaining to the business of the company.

The company should also plan to purchase the depreciable assets on credit terms and an agreed amount of interest can be paid on such credit purchases or the company may purchase these company assets on the basis of the hire purchase agreement enabling the company to claim the amount of interest paid as revenue business expenditure. The company would also be entitled to claim either the depreciation for use of the asset or may treat the hire charges as the rent for the asset in the normal course of business and claim deduction on revenue account.

The following table will help the finance manager framing suitable plans relating to capital structure:

		Capital	*Borrowings*
(a)	Dividend/Interest	Not deductible	Fully deductible
(b)	Cost of raising finance	1/5th allowed under Section 35D	Fully deductible in first year.

Taking the same sources of finance, the comparison between pre-commencement period and post-commencement period is as follows :

(a) (i) Dividend is not deductible either for pre-commencement period or in the post-commencement period in India.

(ii) Interest is capitalised for pre-commencement period, i.e. added to the cost of project' (cost of fixed assets) and its depreciation is calculated on capitalised value of assets. In post-commencement period, interest is fully deductible.

(b) (i) Cost of raising finance in case of capital is not deductible as revenue expenditure but amortised under Section 35D of the Act. If such expenditure is incurred after the commencement of the business. Section 35D is applicable, provided the expenditure is undertaken for expansion purposes in case of industrial undertaking.

(ii) Cost of borrowing funds in case of pre-commencement period is capitalised and in case of post-commencement period, it is deductible fully in the year.

(c) *Tax planning for employees*

The salary package of the employees should be designed to provide maximum benefit of the tax planning to the employees. The employer should keep the following aspects in view while planning the salary package of their employees:

(i) The salary should be divided into basic pay and allowances and should not be in the form of consolidated salary. This will minimise tax incidence considerably as some of the allowances are exempt from tax upto a certain extent for e.g. conveyance allowance is exempt upto Rs. 800 p.m.

(ii) Under the terms of employment, dearness allowance should form part of the retirement benefits. This will not only increase the employees retirement benefits but also reduce his tax incidence in respect of HRA, gratuity, commuted pension, employer's contribution to RPF, etc.

(iii) Any commission payable as per the terms of employment should be based on turnover so as to form part of salary. This will also reduce the tax incidence in respect of HRA, commuted pension, interest credited to RPF, etc.

(iv) If the employee is allowed the use of more than one car for his private purposes, the horse power of any such car should not exceed 1.6 litre cubic capacity as otherwise he shall be deemed to have been provided with one car of 1.6 cubic litre capacity which would lead to higher valuation of such persuite.

(v) The employer's contribution to RPF should be 12% of salary as it is exempt upto this limit.

(vi) The employees should be given re-imbursement of expenses on medical treatment (on free medical facility) in place of medical allowance because such allowance is taxable whereas the reimbursement is not taxable upto the extent of Rs. 15,000. The same thing holds good for entertainment allowance.

(vii) Perquisites should be preferred to taxable allowances. This shall help not only in lower valuation of a perquisite like rent free house but the employee will also be free from falling into the category of specified employees.

(viii) It may be noted that if furniture is provided without rent free accommodation, it will not be taxable in the hands of non-specified employees.

(d) *Tax planning for Indian collaborators*

While entering into an agreement for foreign collaboration, the Indian collaborator should take into consideration such aspects as will enable him to plan his tax affairs in a manner that ensures maximum after-tax profits and return on investment. In this context, the Indian collaborator may be advised to adopt the following steps for tax planning:

(i) *Capitalisation of installation expenses :* As far as purchase of capital goods from the foreign collaborator is concerned, it is needless to say that this is a capital expenditure on which depreciation is admissible. But care should be taken to see that the cost of installation, including the supervision expenses charged by the collaborator, is also capitalised and depreciation claimed thereon, The Indian company should also be vigilant that the other expenses relating to the collaboration agreement must be incurred after the date of the setting up of the business, because only then it would be entitled to be capitalised as other expenses.

(ii) *Treating purchase of spares as revenue expenditure :* For the purchase of spares for the plant, the Indian collaborator should plan to receive the spares subsequent to the year of commissioning of the plant and preferably execute a separate contract in this behalf. It will enable the Indian company to treat the whole of the amount of spares as revenue expenditure.

(iii) *Treating plans and drawings, etc. as "Plant for availing of full value as depreciation:* In view of the Supreme Court's decision in the case *CIT* v. *Alps Theatre,* (1067) 65 ITR T77 (S.C.) "Plant" includes ships, vehicles, books, scientific apparatus, and surgical equipments used for the purpose of business or profession.

(e) *Tax planning under Double Taxation Avoidance Agreements*

Section 90 of the Income Tax Act empowers the Central Government to enter into an agreement with Government of any country outside India to provide relief from double taxation. The liability to tax arising under the provisions of Income Tax Act is subject provisions of Double Taxation Avoidance Agreements (DTAA) between India and foreign country. However, the assessee will not be denied any beneficial provision in the Act. Therefore, the tax planning should be made to take maximum benefit under the provisions of the Act and the DTAA.

3. Areas of tax planning for a non-corporate assessee

The following factors are important determinants of effective tax planning :

(a) *Residential Status and Citizenship Status* – Tax incident depends upon the residential status of the assessee therefore, an assessee should carefully plan his stay in India and abroad so that his tax incident is minimum.

(b) *Heads of Income* – Each head of income has provisions related to the exemptions/ deductions. Maximum benefit of these exemptions / deductions should be availed of to minimize the tax liability.

(c) *Latest Legal Provision* – The assessee should keep himself abreast of the latest provisions of the tax laws so that he can make effective tax planning

Answer to Question No. 2(b)

Appealable orders [Section 253(1) and (2)]

Any assessee aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order.

1. An order passed by Commissioner (Appeals) under Section 154 ordering a rectification of mistake, or under Section 250 in connection with the disposal of an appeal or Section 271 imposing a penalty for failure to furnish return etc. or Sections 271 A or 272A.

2. An order passed by an assessing officer under Clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account other documents or any assets requisitioned under Section 132A, after the 30th day of June, 1995 but before the 1st day of January, 1997.

3. An order passed by a Commissioner under Section 12AA relating to registration of trust or under Section 263 relating to revision of orders prejudicial to revenue or under Section 272A penalty for failure to answer question, sign statements,

allow inspection etc., on or under Section 154 rectifying a mistake, or an order passed by a Chief Commissioner, or a Director General or a director under Section 272A.

4. An order passed by an Assessing Officer under Sub-section (1) of Section 115VZC.

5. An order passed by a Commissioner for rejection of approval under Section 80G(5)(vi).

The Commissioner may, if he objects to any order passed by Commissioner (Appeals) under Section 154 or 250, direct the Assessing Officer to appeal to the Appellate Tribunal against the order.

PART B

INDIRECT TAXATION – LAW AND PRACTICE

Question No. 3

(a) Choose the most appropriate answer from the given options in respect of the following:

(i) Duties of customs is levied by the Union Government vide Entry No. ____of the Union List ;

(a) 82

(b) 83

(c) 84

(d) 85

(ii) Claim for refund of Excise Duty may be made within _______ from the relevant date :

(a) 6 months

(b) 1 year

(c) 2 years

(d) 3 years

(iii) Excise Duty on molasses of Khandsari Sugar Factory is payable by the_____________

(a) Producer of molasses

(b) Procurer who uses molasses in manufacture of any commodity

(c) Either (a) or (b)

(d) None of the above

(iv) The date for determination of duty and tariff valuation except for molasses shall be the rate in force on the date on which _____________:

(a) Goods are manufactured

(b) Goods are removed from the factory

(c) Goods are sold

(d) Excise duty is recovered from the buyer

(v) CENVAT Return by a non-SSI unit is to be submitted under Self Assessment by_____

(a) 10th day of the succeeding month

(b) 15th day of the succeeding month

(c) 25th day of the succeeding month

(d) End of the succeeding month

(vi) Excise Duty is payable by _______;

(a) 6th day of the following month

(b) 5th day of the following month, if paid electronically

(c) 31st day of March for the month of March

(d) All are correct

(vii) Duties of customs shall be levied as per the provisions of Section _____of Customs Act, 1962 at such rates as may be specified in Custom Tariff Act, 1975

(a) 3

(b) 6

(c) 9

(d) 12

(viii) As per Custom Valuation Rules, 2007 the landing charges shall be taken @___ of CIF value for valuation purpose:

(a) 1 %

(b) 1.125 %

(c) 1.5 %

(d) Non of the above

(ix) Rate of duty and tariff valuation of imported goods for home consumption shall be applicable as on the date on which ___________:

(a) Bill of Entry is presented

(b) Custom Duty is paid

(c) Any of the two which is most beneficial to the assessee

(d) None of the above

(x) The Central Government has power to grant exemption from Custom Duty vide Section __________ of the Customs Act, 1962:

(a) 10

(b) 15

(c) 20

(d) 25 *(1 mark each)*

(b) What is meant by "manufacture" under the Central Excise Act, 1944? Explain by giving reference to the relevant case laws. (5 marks)

(c) Explain in brief the procedure of "refund" under Central Excise Law. (5 marks)

Answer to Question No. 3(a)(i)

(b) 83

Answer to Question No. 3(a)(ii)

(b) 1 year

Answer to Question No. 3(a)(iii)

(b) Procurer who uses molasses in manufacture of any commodity

Answer to Question No. 3(a)(iv)

(b) Goods are removed from the factory

Answer to Question No. 3(a)(v)

(a) 10^{th} day of the succeeding month

Answer to Question No. 3(a)(vi)

(c) 31^{st} day of March for the month of March

Answer to Question No. 3(a)(vii)

(d) 12

Answer to Question No. 3(a)(viii)

(a) 1 %

Answer to Question No. 3(a)(ix)

(a) Bill of Entry is presented

Answer to Question No. 3(a)(x)

(d) 25

Answer to Question No. 3(b)

Concept of Manufacture under the Central Excise Act, 1944

Section 3 of the Central Excise Act, 1944 authorizes levy and collection of excise duties only on excisable goods produced or manufactured in India. Therefore, the concept of "manufacture" is very important.

Section 2(f) of the Act provides an *inclusive* definition of the term by saying that manufacture *"includes any process incidental or ancillary to the completion of a manufactured product"* and which is specified in relation to any goods in the Section or Chapter Notes of the First Schedule to the Central Excise Tariff Act, 1985 as amounting to manufacture, or which in relation to goods specified in the third schedule to Central

Excise Act, 1944, packing, repacking, labelling or relabelling, declaration or alteration of retail sale price or adoption of any other treatment on the goods to render the product marketable also amounts to manufacture.

Thus, the definition of manufacture u/s 2(f) is in three parts, namely:

(i) Incidental or ancillary process to the completion of a manufactured product.

(ii) Deemed manufacturing processes specified in Central Excise Tariff Act, 1985.

(iii) In relation to goods specified processes specific goods under Schedule III of Central Excise Act, 1944.

The phrase *"incidental or ancillary to the completion of a manufactured product"* deserves to be examined. Manufacture of any product is through a series of manufacturing processes taking place in sequence. At a particular stage, after the necessary processes are completed, the product emerging may be *functional.* Nevertheless, a few more processes may be necessary to render the product *saleable. It is saleability which is the crucial criterion for deciding excisability.* Hence, the processes which take place to render the product which is already functional to become one which is also saleable, are those which can be considered as "incidental or ancillary to the completion" of the manufactured product.

Union of India v. *Delhi Cloth and General Mills and others* (ELT - 1977 - J. 199).

This is a landmark judgment of the Supreme Court which settled for all purposes the scope of the concept "manufacture" in Central Excise. The facts in brief were that the parties who were manufacturers of Vanaspati purchased groundnut and Til oil from the open market. The oils thus purchased were subjected to different processes to convert them into Vanaspati. While they were no doubt paying excise duty on Vanaspati, the department contended that when the basic oils were being subjected to a series of processes, they emerged at a particular stage as a product which can be constructed as "Vegetable Non-Essential Oil" (VNE), which would attract duty under a separate Tariff Item. In other words, in the department's view, there was "manufacture" of V.N.E. Oil attracting excisability, before its further conversion into Vanaspati, attracting excisability once again.

The matter to be decided was that whether mere processing itself can be construed to be manufactured. On this, they cited a passage quoted in the Permanent Edition of "Words and Phrases" Volume-26 from an American judgement. The citation which has assumed tremendous import in all disputes pertaining to "manufacture" in Central Excise since then, (being frequently cited by either side to disputes) runs thus:

"Manufacture implies a change, but every change is not manufacture; and yet every change of an article is the result of treatment, labour and manipulation. But something more is necessary and there must be a transformation; a new and different article must emerge, having a distinctive name, character or use".

This succinctly explains what constitutes manufacture. Manufacture implies several processes, and in each of them, by working upon what one starts with, changes are no doubt introduced. Still, such changes alone would not by themselves tantamount to manufacture. For the changes to be considered as manufacture, what results after the change should have different name, different character or different use, as against what one started with.

On this reasoning, the Supreme Court held in the D.C.M, case that *mere processing of the basic oils did not tantamount to manufacture of VNE Oils,* since on the basis of detailed examination of evidence, it was held that for VNE Oil popularly marketed as refined oil, the essential ingredient was that they were deodorised. *On the contrary, in the cases before them, though substantial processes of purification of the basic oils had taken place, still they were not deodorised, before being converted into Vanaspati.* Hence, the learned judges held that there had been no transformation bringing in new name, character or use, and hence there was no manufacture as such.

Answer to Question No. 3(c)

Refund of excise duty arises, when the duty paid is more than the incident of duty or duty payable and includes rebate of duty paid on goods exported out of India or on materials used in the manufacture of goods exported out of India. The refund of excise duty is governed by the provisions of Section 11B of the Central Excise Act, 1944.

Any person claiming refund of any duty of excise and interest, if any, paid on such duty, may make an application for refund to the Assistant Commissioner or Deputy Commissioner of Central Excise before the expiry of one year from the relevant date in such form and manner as may be prescribed and the application shall be accompanied by such documentary and such other evidence as the applicant may furnish to establish that the amount of duty and interest, if any, in relation to which such refund is claimed was collected from or paid by, him and the incidence of such duty and interest, if any, had not been passed on by him to another person.

If, on receipt of any such application, the Assistant / Deputy Commissioner is satisfied that the whole or any part of the duty of excise paid by the applicant is refundable, he may make an order accordingly and the amount so determined shall be paid to the applicant provided that the such amount is relatable to the matters enumerated under the proviso to the Section 11B(2). Where the amount is not relatable to such matters then the same will be credited to the Fund created under Section 12C of the Central Excise Act, 1944. It is also provide that no refund shall be allowed under Section 11B unless in the opinion of the Central Government the incidence of duty and interest, if any, paid on such duty has not been passed on by the claimant to any other person.

Question No. 4

Discuss the salient features of CENVAT Credit Rules, 2004. *(10 marks)*

Answer to Question No. 4

Salient features of CENVAT Credit Rules, 2004

(a) New CENVAT Credit Rules, 2004 have been introduced with effect from 10.9.2004 in place of earlier CENVAT Credit Rules, 2002 and Service Tax Credit Rules, 2002. Now credit can be taken for inputs, capital goods as well as for input services used in or in relation to manufacture or production of final products or for providing of any taxable service.

(b) This credit can be utilized for payment of excise duty on final products and service tax on putout services. Credit taken on input services can be used for payment of excise duty and vice versa.

(c) Credit can be taken for all services used in relation to setting up, modernization or repairs of a factory, services relating to advertisement or sales promotion, management, recruitment, etc.

(d) All services which are received in relation to the offices of a manufacturer or service provider, like, telephone, market research, advertising etc. Full credit shall be allowed for these services.

(e) Earlier there was restriction regarding availment of credit on charges of mobile phone. But now there is no such restriction. So now credit can be taken on the service tax paid on mobile phone charges also.

(f) If a manufacturer is manufacturing dutiable as well as exempted goods he is required to maintain separate accounts. But if he opts for not maintaining separate accounts than he shall pay an amount equal to 10% of the price of such exempted final goods at the time of their clearance. In the same way if a service provider does not maintain separate accounts for taxable/exempted service and take credit on inputs/input services used for exempted services, he shall utilize credit only to the extent of an amount not exceeding 20% of the amount of service tax payable on taxable output services.

(g) Refund of CENVAT Credit & Service Tax Credit: When any input or inputs services are used in relation to export goods or for services which are exported, credit in relation to such inputs and input services shall be utilized for payment of duty on any final goods cleared for home consumption or for payment of service tax on other output services. Where such adjustment is not possible, refund of such amount shall be allowed. So now exporter can claim refund of service tax.

(h) In many cases bill/invoices are raised in the name of a particular branch or head office but all the branches utilized services. In such cases service tax credit can be distributed among different branches or offices provided the total credit allowed would not exceed the eligible credit amount. The offices, which will distribute credit, will get themselves registered and required to submit a half-yearly statement, giving the details of credit received and distributed.

(i) Utilisation of CENVAT Credit: Credit in respect of following duties shall be utilized only for payment of those respective duties:

(a) ADE(T&T)

(b) NCCD

(c) Education cess on Excise Duty

(d) Education cess on Service Tax

(e) Additional duty under section 3 of Customs Tariff Act.

(f) Additional duty under section 157 of Finance Act, 2003

But credit in respect of education cess on excisable goods and education cess on taxable services can be utilized for each other.

(j) CENVAT Credit taken can be utilized for the payment of education cess but credit taken in respect of education cess can be utilized only for payment of education cess.

(k) The Service tax will not be levied on job work if the job work involves any process which amount to manufacture or any activity incidental or ancillary to manufacture.

(l) If the goods are sent for job work and the job work is exempt from excise under Notification 214/86 and the job worker has paid excise duty/service tax on the inputs/services used to do job work than the CENVAT Credit of the same can be availed.

(m) Where the assessee is providing any service and it has been covered under service tax in the Finance (No.2) Bill, 2004 then the payment received against these services before 10.9.2004 will be exempt from service tax.

Question No. 5

(a) Explain the Rules of Classification under the Custom Laws. (5 marks)

(b) What do you understand by " warehousing bond" ? (5 marks)

(c) Explain the provisions related to valuation under section 14 of the Customs Act and Custom Valuation Rules, 2007. (10 marks)

Answer to Question No. 5(a)

Rules for Interpretation of Central Excise Tariff Act, 1985 (CETA)

The rules are laid down in CETA for interpretation of Schedules to the Act, for the purpose of classification of goods. The classification is to be first tested in the light of Rule1. Only when it is not possible to resolve the issue by applying this Rule, recourse is taken to rules 2, 3 and 4 in seriatum. The rules are as follows;

Rule 1. In case of Chapter Notes Clearly Determine Classification

The titles of Sections, Chapters and Sub-Chapters are provided for ease of reference only and therefore do not have any legal bearing. The classification shall be determined according to the terms of the headings and any relative Section or Chapter Notes and provided such headings or Notes do not otherwise require, according to the following provisions.

Rule 2. In case of Classification of incomplete or unfinished goods

(a) Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented, the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or falling to be classified as complete or finished by virtue of this rule), presented unassembled or disassembled.

(b) Any reference in a heading to a material or substance shall be taken to include a reference to mixtures or combinations of that material or substance with other materials or substances. Any reference to goods of a given material or substance shall be taken to include a reference to goods consisting wholly or partly of such material or substance. The classification of goods consisting of more than one material or substance shall be according to the principles of rule 3.

Rule 3. In case of goods made of several materials or substances

When by application of rule 2(b) or for any other reason, goods are, *prima facie*, classifiable under two or more headings, classification shall be effected as follows:

(a) the heading which provides the most specific description shall be preferred to headings providing a more general description. However, when two or more headings each refer to part only of the materials or substances contained in mixed or composite goods or to part only of the items in a set put up for retail sale, those headings are to be regarded as equally specific in relation to those goods, even if one of them gives a more complete or precise description of the goods.

(b) mixtures, composite goods consisting of different materials or made up of different components, and goods put up in sets for retail sale, which cannot be classified by reference to (a), shall be classified as if they consisted of the material or component which gives them their essential character, insofar as this criterion is applicable.

(c) when goods cannot be classified by reference to (a) or (b), they shall be classified under the heading which occurs last in numerical order among those which equally merit consideration.

Rule 4. Classification in case of residuary goods

Goods which cannot be classified in accordance with the above rules shall be classified under the heading appropriate to the goods to which they are most akin.

Rule 5. Classification under sub-headings

For legal purposes, the classification of goods in the sub-headings of a heading shall be determined according to the terms of those sub-headings and any related sub-heading Notes and mutatis mutandis, to the above rules, on the understanding that only sub-headings at the same level are comparable. For the purposes of this rule the relative Section and Chapter Notes also apply, unless the context otherwise requires.

Answer to Question No. 5(b)

The goods imported into India are cleared on arrival either for home consumption or for warehousing. The cleared for warehousing means deposit of the goods into the custody of a bonded warehousing for subsequent removal.

Warehousing bond (Section 59)

(1) The importer of any goods specified in section 61(1), which have been entered for warehousing and assessed to duty under section 17 or section 18 shall execute a bond binding himself in a sum equal to twice the amount of the duty assessed on such goods :

(a) to observe all the provisions of this act and the rules and regulations in respect of such goods;

(b) to pay on or before a date specified in a notice of demand—

(i) all duties and interest, if any, payable.

(ii) rent and charges claimable on account of such goods under this Act, together with interest on the same form the date so specified at such rate not below 18 per cent per annum and not exceeding 36 per cent per annum as is for the time being fixed by the Central Government by notification in the Official Gazette; and

(c) to discharge all penalties incurred for violation of the provisions of this Act and the rules and regulations in respect of such goods.

(2) The assistant Commission of Customs or Deputy Commissioner of Customs may permit an importer to enter into a general bond in such amount as the Assistant Commission of Customs or Deputy Commission of Customs may approve in respect of the warehousing of goods to be imported by him within a specified period.

(3) A bond executed under this section by an importer in respect of any goods shall continue in force, notwithstanding the transfer of the goods to any other person or the removal of the goods to another warehouse;

Where the whole of the goods or any part thereof are transferred to another person, the proper officer may accept a fresh bond from the transferee in a sum equal to twice the amount of duty assessed on the goods transferred and thereupon the bond executed by the transferor, shall be enforceable only for a sum mentioned therein less the amount for which a fresh bond is accepted from the transferee.

Answer to Question No. 5(c)

Valuation of Imported Goods and Export Goods

The provisions related to valuation of imported goods and export goods contained in the section 14 of the Customs Act and Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 and the Customs Valuation (Determination of Value of Export Goods) Rules, 2007 are explained here under ;

(1) Section 14 of the Customs Act read with the valuation rules—the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 and the Customs Valuation (Determination of Value of Export Goods) Rules, 2007—establishes the international valuation norms under the World Trade Organization in India. The deemed value concept still survives but only as a residual method or the last resort method or cap value in Rule 9 when all other methods fail. There is no condition in the new Section 14 that it applies only to goods subject to ad valorem duties. Hence, it applies to all goods, whether imported or export goods and whether dutiable or duty free or on which export promotion benefit is claimed.

(2) The Rules spell out statutorily as to in what circumstances the buyer and seller would be considered related persons", they illustrate reasons for which customs may doubt declared values and give a list of items which if the buyer bears but have not been added to the declared value ought to be added. Finally, the

exhaustive Interpretative Notes in the Schedule appended to the import valuation rules, which are statutory, would aid in authoritative interpretation of the rules in case a valuation dispute does develop.

(3) The transaction value concept recognizes the sanctity of seller's right to sell the goods at any price he can get in given circumstances, such as sale price during seasonal offers, clearance sale, festival occasions, offering heavier discount than usual have to be accepted if that is the price actually paid.

(4) *Imported Goods* - For assessment of duty or for purposes of any other law, it should be the transaction value of the imported goods, that is to say:

— the price actually paid or payable for the goods when sold for export to India;

— for delivery at the time and price of importation;

— where the buyer and seller of the goods are not related;

— price is the sole consideration for the sale;

— there are no abnormal restrictions as to the disposition or use of the goods by the buyer; and

— includes the amount paid or payable for costs and service including:

(a) Commissions and brokerage, except buying commissions;

(b) engineering,

(c) design work,

(d) royalties and licence fees related to the imported goods (these are includible even for some post-importations processes, vide explanation tor Rule 10(1)].

(e) Costs of transportation to the place of importation (including shift demurrage charges on chartered vessels, lighterage or barge charges);

(f) insurance;

(g) loading;

(h) unloading;

(i) handling charges;

(j) cost of containers; and

(k) cost of packing whether, for labour or materials.

(5) Where actuals of cost of transport, loading, unloading, handling charges and insurance are not available, ad hoc additions would be made at the rates specified in Rule 10 (2).

(6) Nine circumstances have been specified in Rule 2(2) read with explanation II thereof in which the buyer and seller would be regarded as related persons. However, if the buyer can demonstrate that the relationship did not influence the price [See Rule 3(3) for details], the transaction value "shall" be accepted.

(7) Customs can resort to valuation under the Rules only if the transaction value is not determinable, such as when there is no sale, or the declared value is properly rejected in terms of Rule 12. In order to avoid arbitrary and irrational doubts leading to proceedings for rejection of declared transaction values, Rule 12 sets out illustrative circumstances in which such proceedings may be initiated. In

that event, the value shall be determined by proceeding sequentially through Rule 4 to 9. Among the rules, most commonly used ones are Rules 4 and 5 which provide for comparison with transaction values (not provisional values) of identical or similar goods [see their definitions in Rule 2(1)] at about the same time and in a sale at the same commercial level and in substantially the same quantity as the goods being valued, due adjustment to be made if the commercial level/quantity differs. Where such comparative values area not available, only then resort can be had sequentially to Rule 7 (deductive value), Rule 8 (Computed value) or Rule 9 (residual method), in that sequential order.

(8) Export goods – The value shall be the transaction value, that is :

— The price actually paid or payable for the goods when sold for export from India;

— For delivery at the time and place of exportation,

— Where the buyer and seller of the goods are not related, or if related, the relationship has not influenced the price;

— Price is the sole consideration for the sale.

The Ministry has decided that from 1.1.2009, transaction value will from the basis i.e., the export duty will be calculated simply on FOB Price [Circular No.18/ 2008-Cus., dated 10.11.2008].

(9) In case the declared value is not acceptable as transaction value, the Export Valuation Rules provide for the following three valuation methods to be adopted sequentially.

(10) *Rule 4. Determination of export value by comparison* : The value shall the based on the transaction value of goods of like kind and quality exported at or about the same time to other buyers in the same destination country of importation or in its absence another destination country of importation after making adjustments for :

(i) Difference in the dates of exportation;

(ii) Difference in commercial levels and quantity levels;

(iii) Difference in composition, quality and design between the goods to be valued and the goods with which they are being of compared; and

(iv) Difference in domestic freight and insurance charges depending on the place of exportation.

(11) *Rule 5. Computed value method* : If the value cannot be determined on the basis of transaction value of goods of like and quality, it shall be based on a computed value which shall include:

(a) Cost of production, manufacture or processing of export goods;

(b) Charges, if any, for the design or brand, and

(c) An amount towards profit.

(12) *Rule 6. Residual method* : The above two methods failing, the value shall be determined using reasonable means consistent with the principles and general provisions of the valuation rules. The local market price of the export goods may not be the only basis for determining the value of export goods.

(13) The exporter should give his value declaration in the prescribed format along with the shipping bill to comply with Rule 7.

(14) Rule 8 gives three illustrative reasons for which the customs offices may doubt the declared value, call for further information and then either accept the declared value or determine the export value by proceeding sequentially in accordance with Rules 4 to 6.

(15) *Tariff Values* : The Board has the power to fix tariff values for any class of imported goods or export goods and in that event the notified tariff value shall be the value for purposes of assessment of duty. Section 3 of the Customs Tariff Act is amended so as to provide that where the Central Government has fixed tariff value for collection of Central Excise duty on an article produced or manufactured in India, the value of a like imported article for the purpose of charging additional duty shall be such tariff value. [Proposed vide Finance (No.2) Bill, 2009].

(16) *Value base for additional customs duty (c.v. duty)* : It would comprise of the transaction value CIF plus basic customs duty plus anti-dumping duty plus surcharge.

(17) *Exchange Rate* : The rate notified by the Board and as in force on the date of presentation of the bill of entry (for home consumption or for warehousing) will be the one applicable.

PART C

INTERNATIONAL TAXATION

Question No. 6

(a) Explain the provisions related to "Advance Ruling" in the Income Tax Act? *(10 marks)*

(b) Write a brief note on "Controlled Foreign Corporation (CFC)". *(5 marks)*

(c) How the Foreign Institutional Investors are taxed for the capital gains arising from transfer of securities ? *(5 marks)*

Answer to Question No. 6(a)

The Income Tax Act provides for giving advance rulings by an independent adjudicatory body and to ensure further that the procedure is simple, inexpensive, expeditious and authoritative. The provisions pertaining to the advance ruling are given under Sections 245N to 245V of the Income Tax Act, 1961.

Authority for Advance Ruling 245O

The Central Government shall constitute an authority for giving advance rulings, to be known as Authority for Advance Rulings. The Authority will consist of the following members appointed by the Central Government:

(i) a chairman who will be a retired judge of the Supreme Court,

(ii) an officer of the Indian Revenue Service who is qualified to be member of CBDT, and

(iii) an officer of the Indian Legal Service who is qualified to be an Additional Secretary to the Government of India.

Applicant for Advance Ruling

As per Section 245N (b) of the Income Tax Act, the advance ruling under the income-tax act could be sought by:

(a) A non-resident;

(b) Resident having transactions with non-residents.

(c) Specified categories of residents.

Procedure of application for advance ruling

An applicant desirous of obtaining an advance ruling should apply to the authority in the prescribed form stating the question(s) on which the ruling is sought. The application has to be made in quadruplicate in the prescribed form accompanied with a demand draft of Rs.250 in favour of the Authority made pay as legally.

Salient Features

(a) The benefit of advance ruling is available only under the Income Tax Act, 1961.

(b) Must relate to a transaction entered into or proposed to be entered into by the applicant.

The advance ruling is to be given on questions specified in relation to such a transaction by the applicant.

(c) The questions may be on points of law as well as on facts or could be mixed questions of law and facts.

(d) The application may be withdrawn within 30 days from the date of the application.

(e) The authority shall pronounce it ruling within six months of receipt of the application.

Powers of the Authority

Section 245U deals with the Powers of the Authority. Sub-section (1) provides that for the purpose of exercising its powers, the Authority shall have all the powers of a Civil Court under the Code of Civil Procedure, 1908 (5 of 1908) as are referred to in Section 131 of the Income-tax Act.

Applicability of Advance Ruling (Section 245S)

The advance ruling pronounced by the Authority under Section 245R shall be binding only:

(a) On the applicant who had sought it;

(b) In respect of the transactions in relation to which the ruling had been sought; and

(c) On the Commissioner, and the income-tax authorities subordinate to him, in respect of the applicant and the said transaction.”

Question precluded

Under Section 245R, the Authority shall not allow the application where the question raised in the application

(i) is already pending before any income tax authority or Appellate Tribunal (except in the case of a resident applicant falling in sub-clause (ii) of clause (b) of section 245N) or any court;

(ii) Involves determination of fair market value of any property; or

(iii) It relates to a transaction or issue which is designed *prima facie* for the avoidance of income-tax.

Answer to Question No. 6(b)

Controlled Foreign Corporation (CFC)

Income from a foreign source is taxed usually after it is accrued or received as income in the country of residence of the taxpayer. The use of intermediary entities in a tax-free or low-tax jurisdiction enables a tax resident to defer (or avoid) the domestic tax on the income until it is repatriated to the residence state.

This tax deferral could lead to an unjustifiable loss to the domestic tax revenue. As countries increasingly ease their exchange control rules, some have enacted Controlled Foreign Corporation rules to prevent the use of low-tax jurisdictions by their tax residents to defer the taxability of foreign income. Under the CFC rules, the domestic law effectively extends the residence rules to tax the income. It requires that the tax on profits, whether distributed or not, be paid by resident tax-payers. Normally, the CFC rules apply only to foreign companies controlled by residents, but certain countries extend it to foreign permanent establishments and trusts.

A CFC is a legal entity that exists in one jurisdiction but is owned or controlled primarily by taxpayers of a different jurisdiction. The CFC rules may also be termed 'anti-deferral rules'. If income is taxed at some point of time, then the taxpayer will have a greater after-tax retention of income if tax is paid during a future year as opposed to being paid in the present year. An anti-deferral tax regime could compel the foreign company to repatriate the profits, thus resulting in a favorable impact on the foreign exchange inflows as well as shoring up the domestic tax base.

The U.S, the UK, Germany and 25 other countries have adopted CFC regulations. Generally, the CFC regime is enacted by states in which tax liability is imposed on the worldwide income of resident taxpayers.

Answer to Question No. 6(c)

Tax on Income of Foreign Institutional Investors (FII) from Capital Gains arising from Transfer of Securities (Section 115AD)

According to Section 115AD, the income tax on the income of FII from capital gain arising from transfer of securities shall be chargeable as under:

(i) On the income by way of short-term capital gains included in the total income - at the rate of thirty per cent;

Provided that short-term capital gains arising from the transfer of equity shares referred to in Section 111A shall be taxable at the rate of fifteen per cent provided such transaction is subject to Securities Transaction Tax. Also, no deduction shall be allowed under Chapter VIA from such short term capital gain.

(ii) On the income by way of long-term capital gains included in the total income- at the rate of ten per cent;

TEST PAPER 3/2010

Time allowed : 3 hours *Max. marks : 100*

NOTE : *All Questions are compulsory.*

PART A

DIRECT TAXATION – LAW AND PRACTICE

Question No. 1

(a) Choose the most appropriate answer from the given options in respect of the following :

(i) MAT Rate is __________% of book profit as per the Finance Act, 2010

(a) 5

(b) 15

(c) 18

(d) 20

(ii) The parliament and the legislature of States shall have the concurrent powers under:

(a) Union List

(b) State list

(c) Concurrent List

(d) Any of the above

(iii) Once the bill has been passed by the parliament after necessary amendments then it goes to the ___________ for his assent

(a) Speaker of the Lok Sabha

(b) President

(c) Finance Minister

(d) None of the above

(iv) A closely held company is a company in which:

(a) Public is not substantially interested

(b) A widely held company

(c) Either public is not substantially interested or a widely held company

(d) Both public is not substantially interested and a widely held company

(v) _____________ is an honest and rightful approach to the attainment of maximum benefits of the taxation laws within their framework

(a) Tax Evasion

(b) Tax avoidance

(c) Tax Planning

(d) Any of the above *(1 mark each)*

(b) What items to be added or deducted from the net profit to arrive at 'Book Profit' for Minimum Alternate Tax. *(10 marks)*

Answer to Question No. 1(a)(i)

(c) 18

Answer to Question No. 1(a)(ii)

(c) Concurrent List

Answer to Question No. 1(a)(iii)

(b) President

Answer to Question No. 1(a)(iv)

(a) Public is not substantially interested

Answer to Question No. 1(a)(v)

(c) Tax Planning

Answer to Question No. 1(b)

MAT – Basic Provision

Every person has to pay tax on his taxable income computed in accordance with the provisions of the Income Tax Act, 1961. However in case of a company, a separate provision has been inserted by Section 115JB which is commonly referred as Minimum Alternate Tax (MAT). As per this section, every company is liable to pay tax of an amount which is higher of following:

(a) Tax liability computed as per the provisions of the Income Tax Act by applying the normal rates applicable to a company.

(b) Tax liability computed as per the provisions of Section 115JB i.e. MAT.

MAT is computed @18% (plus surcharge and cess as applicable) on the book profits of the company. Book profit is computed by making certain adjustments to net profit as per profit and loss account which is to be prepared in accordance with the provisions of the Companies Act, 1956.

Meaning of "Book Profit"

According to the Explanation 1 to Section 115JB (2), "Book Profit" means the net profit as shown in the profit and loss account for the relevant previous year prepared under sub-section (2), as increased by :

(a) the amount of Income tax paid or payable, and the provision therefor; or

(b) the amounts carried to any reserves, by whatever name called other than reserve specified under Section 33AC; or

(c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities, or

(d) the amount by way of provision for losses of subsidiary companies; or

(e) the amount or amounts of dividends paid or proposed; or

(f) the amount or amounts of expenditure relatable to any income to which Section 10 [other than section 10(38) } or Section 11 or Section 12 apply; or

(g) the amount of depreciation.

(h) the amount of deferred tax and provision therefore.

(i) the amount or amounts set aside as provision for diminution in the value of any asset.

The net profit as increased by the amounts referred to in Clauses (a) to (i) shall be reduced by the following amounts:

(i) the amount withdrawn from any reserves or provisions if any such amount is credited to the profit and loss account;

However following amounts credited to profit and loss account should not be deducted:

(a) Amount withdrawn from reserve created before 1.4.97 otherwise than by way of a debit to the profit and loss account.

(b) Any other amount withdrawn from reserve or provision on or after 1.4.97, if such amount was not added to profit while computing the book profit of the year in which such amount was transferred to reserve, out of which such amount is withdrawn.

(ii) the amount of income to which any of the provisions of Section 10 { except 10 (38)} or Section 11 or Section 12 apply, if any such amount is credited to the profit and loss account; or

(iii) the amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or

(iv) the amount withdrawn from revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in Clause (iii) above; or

(v) the amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account. For the purposes of this clause, the loss shall not include depreciation. Therefore, in a case where an assessee has shown profit in a year, but after adjustment of depreciation it results profit or loss, no adjustment in book profit is allowed; or

(vi) the amount of profits eligible for deduction under Section 80HHC, 80HHE or 80HHF.

(vii) the amount of deferred tax, if any such amount is credited to the profit and loss account.

The amount computed after increasing or decreasing the above is known as ‘Book-Profit’.

Question No. 2

(a) *What are the important areas of tax planning in the context of Income Tax Act, 1961. (10 marks)*

(b) *Explain in brief the Appealable orders before Commissioner (Appeals). (5 marks)*

Answer to Question No. 2(a)

1. Important areas of Tax Planning at the time of setting up of new business entity:

(a) *Form of organisation/ownership pattern*

The selection of particular form of organisation depends not only on the magnitude of financial requirements and owner's liability, but also on the tax considerations. Normally, depending upon the level of operation, expected profitability need for external financing and expected requirements of technical expertise, a suitable form can be chosen.

The company being a separate legal entity, confers certain valuable benefits in the matter of tax planning to its shareholders and the persons connected with the management of the company.

The important tax privileges and advantages to a company over the other forms can be summarized as under:

(i) Allowability of remuneration, for the persons who are managing the affairs of the company and also owning its shares.

(ii) The provisions relating to clubbing of income under Section 64 of the Income Tax Act, 1961 do not apply. However, if spouse of an individual having a substantial interest in a company receives remuneration from the same company, such remuneration is added to the income of the individual unless the spouse is technically or professionally qualified. [Section 40A(2)(b) of the Income Tax Act, 1961].

(iii) Dividends received by the shareholders from any Indian company have been fully exempt under Section 10(33) from Assessment Year 1998-99 to Assessment Year 2002-2003. However, any income by way of dividend referred to in Section 115-O is exempt under Section 10(34) from Assessment Year 2004-05.

(iv) Companies are subjected to flat rate of tax, regardless of the quantum of their income. The domestic companies now pay tax @ 30% plus surcharge @ 7.5%, if applicable and education cess @ 3% for Assessment Year 2011-12. This, however, may not seem to be an advantage in view of low slab rates applicable to sole proprietorships, but when we look at the total incidence of tax after taking into account the various deductions allowed to companies and the scheme of perquisites, the real owners of companies to stand to benefit.

(v) There are certain special tax concessions, allowances and deductions given under the Income Tax Act, 1961 available only to the company form of business enterprises such as deductions allowed under Section 33AC and Sections 36(1)(ix) and 35D of the Income Tax Act, 1961 etc.

(vi) The shares in companies are treated as long term capital assets if held for more than 12 months and thus qualifying for exemption from capital gain taxation.

On the other hand an individual pays tax on his income on the basis of slab system. He gets the benefit of minimum taxable limit laid down by the respective Finance Acts. Income received by an individual in different capacities, i.e. as a member of a firm is not taxable in hand of partner because the firm has paid tax on it. The owner of a proprietorship firm is treated as an individual for tax purposes.

Entrepreneurs now have an alternative and innovative form of business organization i.e. Limited Liability Partnership (LLP) which combines the benefits of company and general partnership form of business organizations. LLP has separate legal entity, perpetual succession and limited liability of partners. From income tax point of view it is treated same as general partnership firm therefore its profits will be taxed in the hands of the LLP not in the hands of its partners.

(b) *Locational aspects*

In addition to the form of organization, the Income Tax Act provides tax benefits on the basis of the location of the business unit e.g. newly established units in SEZs (Section 10AA), newly established 100% EOU (Section 10B), and therefore, tax planning is relevant from location point of view.

(c) *Nature of business*

Tax planning is relevant from the point of view of the nature of the business also because certain businesses are granted special tax treatment under the Income Tax Act.

2. Important Areas of Tax Planning for the business entities already in existence

(a) *Tax planning relating to corporate restructuring*

Corporate restructuring should be carefully planned to take the maximum benefit through tax planning. The following areas should be given proper attention:

1. Since the unabsorbed losses and unabsorbed depreciation cannot be allowed to be carried forward and set off in the hands of the amalgamated company, except in the cases prescribed under Section 72A of the Act, it is proposed:

   (a) that the scheme of the amalgamation can be put off till such time the full benefit of set off is availed of by the amalgamating company; and

   (b) that the loss carrying company should absorb or take over the business of the profit-making company. This would help in carrying to carry forward the benefits of all unabsorbed losses and depreciation to be set off against the profits derived from the business of the profit-making company.

2. To save from disallowance of the debts of the amalgamating company which

subsequently become bad in the hands of the amalgamated company, the amalgamated company should plan to make suitable provision for the expected losses on account of bad debts at the time of fixing the consideration while taking over the business of the amalgamated company.

3. A company whose shares are not quoted on a recognised stock exchange may avail the benefit of amalgamation by amalgamating itself with another company whose shares are quoted on a recognised stock exchange. This would help its shareholders to take the advantage of the quoted price of their shares in the stock exchange while determining their liability for wealth-tax purposes.

4. A loss incurring company and a profit-making company may merge in order to reduce the overall incidence of liabilities to tax under the Income Tax Act, 1961.

5. In case the conditions provided under Sections 2(1B) and 72A of the Act are not satisfied, it may be suggested that the profit making company should merge itself with the loss making company, so that the loss making company does not lose its existence and also enjoys all other benefits.

6. Under Section 2(1B) of the Act, it is provided that for availing the benefits of amalgamation, at least 75% of the shareholders of the amalgamating company should become shareholders of the amalgamated company. In case more than 25% of the shareholders are not willing to become shareholders of the amalgamated company, it is proposed that the amalgamating company may persuade the other shareholders who may be willing, to purchase the shares in the amalgamated company to acquire the shares of the remaining shareholders so that the percentage of dissenting shareholders does not exceed 25%. Alternatively, the amalgamated company prior to, amalgamation may purchase shares from such dissenting shareholders so as to make such dissenting shareholders to go below the specified percentage of 25%.

(b) *Tax planning relating to financial management decisions*

When a company raises long term loans from financial institutions or by way of public issue of debentures or inviting deposits from the public, it should plan that the expenses incurred on such issues of debentures or expenses towards stamp duty, registration fees, and lawyer's fees should be incurred only after the date of the 'setting-up' of the business. The interest paid before the commencement of production but after setting up of the business on loans taken by the company for the acquisition of its plant and machinery and other assets, forms part of the actual cost of the asset and it should be capitalized in actual cost of asset. Thus, the company would be allowed to capitalise the expenditure and claim a higher depreciation and investment allowance.

The company should also plan the optimum use of the share capital and the borrowed funds. Note that the borrowings should be utilised as far as possible for the acquisition and installation of assets like, buildings, plant and machinery so that interest can be capitalised for the period after setting up of the acquired assets like buildings, plant and machinery but before the commencement of production. The interest and higher amount of depreciation (due to capitalisation of expense) may be claimed as revenue expenditure pertaining to the business of the company.

The company should also plan to purchase the depreciable assets on credit terms and an agreed amount of interest can be paid on such credit purchases or the company may purchase these company assets on the basis of the hire purchase agreement enabling the company to claim the amount of interest paid as revenue business expenditure. The company would also be entitled to claim either the depreciation for use of the asset or may treat the hire charges as the rent for the asset in the normal course of business and claim deduction on revenue account.

The following table will help the finance manager framing suitable plans relating to capital structure:

	Capital	*Borrowings*
(a) Dividend/Interest	Not deductible	Fully deductible
(b) Cost of raising finance	1/5th allowed under Section 35D	Fully deductible in first year.

Taking the same sources of finance, the comparison between pre-commencement period and post-commencement period is as follows:

(a) (i) Dividend is not deductible either for pre-commencement period or in the post-commencement period in India.

(ii) Interest is capitalized for pre-commencement period, i.e. added to the cost of project' (cost of fixed assets) and its depreciation is calculated on capitalized value of assets. In post-commencement period, interest is fully deductible.

(b) (i) Cost of raising finance in case of capital is not deductible as revenue expenditure but amortized under Section 35D of the Act. If such expenditure is incurred after the commencement of the business. Section 35D is applicable, provided the expenditure is undertaken for expansion purposes in case of industrial undertaking.

(ii) Cost of borrowing funds in case of pre-commencement period is capitalized and in case of post-commencement period, it is deductible fully in the year.

(c) *Tax planning for employees*

The salary package of the employees should be designed to provide maximum benefit of the tax planning to the employees. The employer should keep the following aspects in view while planning the salary package of their employees:

(i) The salary should be divided into basic pay and allowances and should not be in the form of consolidated salary. This will minimize tax incidence considerably as some of the allowances are exempt from tax upto a certain extent for e.g. conveyance allowance is exempt upto Rs. 800 p.m.

(ii) Under the terms of employment, dearness allowance should form part of the retirement benefits. This will not only increase the employee's retirement benefits but also reduce his tax incidence in respect of HRA, gratuity, commuted pension, employer's contribution to RPF, etc.

(iii) Any commission payable as per the terms of employment should be based on turnover so as to form part of salary. This will also reduce the tax incidence in respect of HRA, commuted pension, interest credited to RPF, etc.

(iv) If the employee is allowed the use of more than one car for his private purposes, the horse power of any such car should not exceed 1.6 litre cubic capacity as otherwise he shall be deemed to have been provided with one car of 1.6 cubic litre capacity which would lead to higher valuation of such persuite.

(v) The employer's contribution to RPF should be 12% of salary as it is exempt upto this limit.

(vi) The employees should be given re-imbursement of expenses on medical treatment (on free medical facility) in place of medical allowance because such allowance is taxable whereas the reimbursement is not taxable upto the extent of Rs. 15,000. The same thing holds good for entertainment allowance.

(vii) Perquisites should be preferred to taxable allowances. This shall help not only in lower valuation of a perquisite like rent free house but the employee will also be free from falling into the category of specified employees.

(viii) It may be noted that if furniture is provided without rent free accommodation, it will not be taxable in the hands of non-specified employees.

(d) *Tax planning for Indian collaborators*

While entering into an agreement for foreign collaboration, the Indian collaborator should take into consideration such aspects as will enable him to plan his tax affairs in a manner that ensures maximum after-tax profits and return on investment. In this context, the Indian collaborator may be advised to adopt the following steps for tax planning:

(i) *Capitalisation of installation expenses:* As far as purchase of capital goods from the foreign collaborator is concerned, it is needless to say that this is a capital expenditure on which depreciation is admissible. But care should be taken to see that the cost of installation, including the supervision expenses charged by the collaborator, is also capitalised and depreciation claimed thereon, The Indian company should also be vigilant that the other expenses relating to the collaboration agreement must be incurred after the date of the setting up of the business, because only then it would be entitled to be capitalised as other expenses.

(ii) *Treating purchase of spares as revenue expenditure:* For the purchase of spares for the plant, the Indian collaborator should plan to receive the spares subsequent to the year of commissioning of the plant and preferably execute a separate contract in this behalf. It will enable the Indian company to treat the whole of the amount of spares as revenue expenditure.

(iii) *Treating plans and drawings, etc. as "Plant for availing of full value as depreciation:* In view of the Supreme Court's decision in the case *CIT* v. *Alps Theatre,* (1067) 65 ITR T77 (S.C.) "Plant" includes ships, vehicles, books, scientific apparatus, and surgical equipments used for the purpose of business or profession.

(e) *Tax planning under Double Taxation Avoidance Agreements*

Section 90 of the Income Tax Act empowers the Central Government to enter into an agreement with Government of any country outside India to provide relief from double taxation. The liability to tax arising under the provisions of Income Tax Act is subject provisions of Double Taxation Avoidance Agreements (DTAA) between India and foreign country. However, the assessee will not be denied any beneficial provision in the Act. Therefore, the tax planning should be made to take maximum benefit under the provisions of the Act and the DTAA.

3. Areas of tax planning for a non-corporate assessee

The following factors are important determinants of effective tax planning :

(a) *Residential Status and Citizenship Status* – Tax incident depends upon the residential status of the assessee therefore, an assessee should carefully plan his stay in India and abroad so that his tax incident is minimum.

(b) *Heads of Income* – Each head of income has provisions related to the exemptions/ deductions. Maximum benefit of these exemptions / deductions should be availed of to minimize the tax liability.

(c) *Latest Legal Provision* – The assessee should keep himself abreast of the latest provisions of the tax laws so that he can make effective tax planning

Answer to Question No. 2(b)

Appealable orders before Commissioner (Appeals) (Section 246A)

Any assessee aggrieved by any of the following orders may appeal to the Commissioner (Appeals) against:

(a) an order passed by a Joint Commissioner under section 115VP(3)(ii) or an order against the assessee where he denies his liability to be assessed under the Income Tax Act, under Section 143(3) except an order passed in pursuance of directions of Dispute Resolution Panel or Section 144 where assessee object to the amount of income assessed or amount of tax determined or amount of loss computed or status under which he is assessed;

(aa) an order of assessment under Sections 115WE or 115WF where the assessee being an employer objects to the value of fringe benefits assessed;

(b) an order of assessment, re-assessment or re-computation under Section 147 or Section 150;

(ba) an order of assessment or reassessment under Section 153A;

(c) an order of rectification made under Section 154 or Section 155 having effect of enhancing assessment or reducing refund or order refusing to allow claim made by assessee under these sections;

(d) an order under Section 163 treating the assessee as the agent of a non-resident;

(e) an order under Section 170(2) of 170(3) relating to succession of business otherwise on death;

(f) an order made under Section 171;

(g) an order under Section 185;

(h) an order under Section 237;

(i) A person deemed to be an assessee in default for not collecting the whole or any part of tax or after collecting the tax, failing to pay the same, may appeal before Commissioner (Appeals) on or after April 1, 2007.

(j) an order imposing a penalty under Section 221, 271, 271A, 271F, 271FB, 272AA, Section 272, 272B, 272BB or Section 273;

(k) an order of assessment made by an assessing officer under clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account, other documents or any assets requisitioned under Section 132A;

(l) an order imposing a penalty under Sub-section (2) of Section 158BFA;

(m) an order imposing penalty under Section 271 B or Section 271 BB;

(n) an order made by a Joint Commissioner imposing a penalty under Section 271 C, Section 271 D or Section 271 E;

(o) an order made by a Joint Commissioner imposing a penalty under Section 272AA and by a Joint Commissioner or Joint Director under Section 279A;

(p) an order imposing a penalty under Chapter XXI of Income tax Act;

(q) an order made by an Assessing Officer other than a Joint Commissioner under the provisions of this Act, in case of specified person or classes of persons.

PART B

DIRECT TAXATION – LAW AND PRACTICE

Question No. 3

(a) Choose the most appropriate answer from the given options in respect of the following:

(i) Excisable goods means goods specified in the _________________ to the

Central Excise Tariff Act, 1985 as being subject to a duty of excise and include salt:

(a) First Schedule

(b) Second Schedule

(c) First and Second Schedule

(d) Neither in First Schedule nor Second Schedule

(ii) Safeguard duty shall remain in force from the date of its imposition for a period of;

(a) 5 years

(b) 3 years

(c) 4 years

(d) 2 years

(iii) HSN stands for _____________

(a) Harmonised System Number

(b) Harmonised System Nomenclature

(c) Harmonised Supplementary Number

(d) Hierarchy System Nomenclature

(iv) Section 5 of the Central Excise Act, 1944 empowers the Central Government to make rules providing for remission of duty on loss of Quantity due to:

(a) Natural causes

(b) Unavoidable accident

(c) Goods are unfit for consumption or marketing

(d) Any of the above

(v) The custodian may sell the goods under appropriate permission of the proper officer, if the goods are not cleared for home consumption or warehoused or transshipped within a period of;

(a) 45 days

(b) 30 days

(c) 60 days

(d) 15 days

(vi) How much amount of CENVAT Credit can be taken by the provider of output services on capital goods in the same financial year;

(a) 100 %

(b) 50%

(c) 30%

(d) Nil

(vii) Exempted goods means goods exempted by a notification under section ____________ of the Central Excise Act, 1944:

(a) 3A

(b) 4A

(c) 25A

(d) 5A

(viii) Where the goods are thrown into the sea with a view to lighten the ship in order to prevent it from sinking is called:

(a) Derelict

(b) Flotsam

(c) Wreck

(d) Jetsam

(ix) What amount of CENVAT credit is available in case where capital goods exclusively used in the manufacture of exempted goods or exempted services:

(a) Full

(b) Half

(c) One-third

(d) Nil

(x) Time limit for appeal to commissioner (Appeal) is:

(a) 30 days

(b) 45 days

(c) 15 days

(d) 60 days *(1 mark each)*

(b) What is meant by "Special Audit"? Explain the provisions for directing special audit under section 14A. *(5 marks)*

(c) Explain in brief the procedure of registration under Central Excise Law. *(5 marks)*

Answer to Question No. 3(a)(i)

(c) First and Second Schedule

Answer to Question No. 3(a)(ii)

(c) 4 years

Answer to Question No. 3(a)(iii)

(b) Harmonised System Nomenclature

Answer to Question No. 3(a)(iv)

(d) Any of the above

Answer to Question No. 3(a)(v)

(b) 30 days

Answer to Question No. 3(a)(vi)

(b) 50%

Answer to Question No. 3(a)(vii)

(d) 5A

Answer to Question No. 3(a)(viii)

(d) Jetsam

Answer to Question No. 3(a)(ix)

(d) Nil

Answer to Question No. 3(a)(x)

(d) 60 days

Answer to Question No. 3(b)

Special Audit

Section 14A was introduced in the Central Excise Act by 1995 budget enabling the Chief Commissioner of Central Excise to order for special audit of the accounts of any factory, depots or distributors by a nominated chartered accountant (as proposed in Finance (No.2) Bill, 2009] or a Cost Accountant at Government cost for the purpose of enquiry, investigation or any other proceeding. The intention evidently is to use the services of accounts experts in complicated cases of suspected undervaluation etc. where stakes involved are heavy. Under Section 14AA introduced in 1997 Budget, similar special edit at Government cost may be ordered in cases where CENVAT Credit of duty availed or utilized is not consider within normal limits.

Directing Special Audit under section 14A

According to section 14A of the Central Excise Act, 1944 if at any stage of enquiry, investigation or any other proceedings before him, any Central Excise Officer not below the rank of an Assistant Commissioner or Deputy Commissioner of Central Excise, having regard to the nature and complexity of the case and the interest of revenue, is of opinion that the value has not been correctly declared or determined by a manufacturer or any person, he may, with the previous approval of the Chief Commissioner of Central Excise, direct such manufacturer or such person to get the accounts of his factory, office depots, distributors or any other place, as may be specified by the said Central Excise Officer, audited by a cost accountant or chartered accountant (vide Finance Act, 2009), nominated by the Chief Commissioner of Central Excise in this behalf.

Answer to Question No. 3(c)

Every person who manufactures or deals in excisable goods is required to obtain Central excise Registration as per Rule 9 of the Central excise Rules, 2002. Registration is provided free of cost. Persons manufacturing goods, fully exempted or chargeable to nil rate of duty, are not required to seek registration. Separate registration is required for separate premises/units. Application for registration in prescribed format, along with PAN number, is submitted to the jurisdictional Deputy/Assistant Commissioner. Computer generated Registration Certificate, based on 15-digit PAN number, is handed over either immediately or within 7 days in all cases. Registration Certificate is non-transferable. An application is required to be made to the department for carrying out any additions/

deletions in the registration certificate. The premises and the details given by the applicant are verified by the Range Officer within 5 working days after issue of the Registration Certificate. No bond or bank guarantee is required for obtaining registration. Formats of application for registration as well as registration certificate, given in Form A-I.

The registration granted under Central Excise Rules can be revoked/suspended by the jurisdictional Deputy/Assistant Commissioner in case of breach of any of the provisions of the Central Excise Act or Rules, Where the law so requires, failure to obtain Central Excise Registration attracts penal provisions under Central Excise Act & Rules

Question No. 4

(a) Write Short Note on:

(i) Unjust Enrichment in Central Excise Law

(ii) Exempted and Nil rated goods. *(5 marks each)*

(b) Explain the charging section in the Customs Act. Do goods imported by Government also attract import duty ? *(5 marks)*

Answer to Question No. 4(a)(i)

Doctrine of Unjust Enrichment

In case of refunds, there is a major controversy that a claim of refund can be entertained only if the duty has not already been passed to the buyers. The reason being that if the claim of refund is allowed when the duty has already been passed to others, it would tantamount to unintended profit to the assessee resulting into his unjust enrichment. Thus, no manufacturer would be entitled to the refund of excise duty, if e has already passed on the incidence of such duty to the buyer.

There is a presumption that the manufacturer has already passed on the incidence to the buyer and hence the manufacturer has to prove to the contrary that he has not passed on the incidence to the buyer. In view of this, deciding a refund claim is a quasi-judicial function and the Assistant Commissioner has to issue a notice to the claimant and hear him before rejecting the claim in full or in part.

Law on Refunds under Central Excise — To Prevent Unjust Enrichment

To prevent unjust enrichment of the manufacturers through such refunds, the following provisions have been made in the Central Excise Act:

(a) Section 11B makes it obligatory for any person wishing to claim refund of the excise duty paid by him to make an application within one year from the relevant date, (relevant date being defined by Explanation (B) to Section 11B) in the prescribed form and manner.

(b) The situations in which refund of the duties of excise paid can be made, to a claimant, have been enumerated in the Section 11B(2) and in case the claim is not covered by any of these situations, the refundable amount will be credited to the Consumer Welfare Fund specified in Section 12C and will be utilised for the purposes and in the manner specified in Section 12D.

(c) Section 11B(3) prohibits refund of the duties except in the situations specified in Sub-section (2) thereof, contrary judgement, decree, order or direction of the Appellate Tribunal or any Court or in any other provisions of the Act and the Rules or any other law notwithstanding.

(d) The provisions will also govern refunds of duty under Section 11C.

(e) Section 11 D provides that where any person has collected any amount in any manner from the buyer as representing the duty of excise and interest, if any, paid on such duty, he shall forthwith pay the said amount to the credit of the Central Government. This is irrespective, of any order or direction of the Appellate Tribunal or any Court or in any other provision of the Act or the Rules to the Contrary.

(f) Section 12A stipulates that every person who is liable to pay duty, shall prominently indicate, at the time of clearance of the goods, in all the documents relating to assessment, sales invoices etc., the amount of duty which will form part of the price at which such goods will be sold.

(g) Section 12B provides for presumption that the incidence of duty has been passed on the buyer unless contrary is proved by the person who paid the duty.

Answer to Question No. 4(a)(ii)

Exempted Goods

Exempted Goods mean and include such goods, on which exemption is granted under Section 5A of the Act by a notification. Excisable goods, which are mentioned in the Tariff Schedule, may be exempted from payment of duty by a notification. In such case, although the goods continue to remain excisable, but nil duty is charged on removal of such goods. However, such excisable goods do not become non-excisable merely upon their being exempted from duty.

Nil Rated Goods

An excisable goods may be nil duty paid goods, if the rate of excise duty applicable on such goods is shown as nil in the Tariff Schedule. Such a situation may arise, when by virtue of any notification, the rate of excise duty any goods is reduced to nil.

However, in such a situation also, the goods shall continue to be treated as excisable and it would be treated as 'duty paid' goods on its removal, even if nil duty is paid on such goods. This would be so, because nil duty is also a rate of duty.

Answer to Question No. 4(b)

Section 12 is a charging Section which lays down the conditions of levy. As per Section 12, customs duty is imposed on goods imported into or exported out of India as per the rates specified under the Customs Tariff Act, 1975. The provisions are equally applicable to goods belonging to the Government.

On analysis of Section 12, we derive the following points:

(i) Customs duty is imposed on goods when such goods are imported into or exported out of India;

(ii) The levy is subject to other provisions under this Act or any other law;

(iii) The rates of duty are as specified under the Tariff Act, 1975;

(iv) Even goods belonging to Government are subject to levy, though they may be exempted by some notifications under Section 25

Question No. 5

(a) Explain the method by which transaction value determined under rule 3, 4 and 5 of Customs Valuation (Determination of price of imported goods) Rules, 2007. *(5 marks)*

(b) Explain whether the following items can be included in/excluded from the transaction value under section 4 of the Central Excise Act, 1944:

(i) Collection expenses incurred in respect of empty bottles for filling aerated waters form the premises of buyers to the manufactures.

(ii) Delivery and collection charges of gas cylinders and collection of empty cylinders.

(iii) Interest notional or real accruing on deposits for sale/return of gas cylinders as well as rentals.

(iv) Cash discount known at the time of clearance of goods but not availed by the customer.

(v) Value of system software in case of computers. *(2 marks each)*

Answer to Question No. 5(a)

Determination of the Method of Valuation under the Customs Valuation (Determination of Price of Imported Goods) Rules, 2007

Rule 3

(1) Subject to rule 12, the value of imported goods shall be the transaction value adjusted in accordance with provisions of Rule 10;

(2) Value of imported goods under sub-rule (1) shall be accepted:

Provided that—

(a) there are no restrictions as to the disposition or use of the goods by the buyer other than restrictions which—

(i) are imposed or required by law or by the public authorities in India; or

(ii) limit the geographical area in which the goods may be resold; or

(iii) do not substantially affect the value of the goods;

(b) the sale or price is not subject to some condition or consideration for which a value cannot be determined in respect of the goods being valued;

(c) no part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless an appropriate adjustment can be made in accordance with the provisions of rule 10 of these rules; and

(d) the buyer and seller are not related, or where the buyer and seller are related, that transaction value is acceptable for customs purposes under the provisions of sub-rule (3) below.

(3) (a) Where the buyer and seller are related, the transaction value shall be accepted provided that the examination of the circumstances of the sale of the imported goods indicate that the relationship did not influence the price.

(b) In a sale between related persons, the transaction value shall be accepted, whenever the importer demonstrates that the declared value of the goods being valued, closely approximates to one of the following values ascertained at or about the same time.

(i) the transaction value of identical goods, or of similar goods, in sales to unrelated buyers in India;

(ii) the deductive value for identical goods or similar goods;

(iii) the computed value for identical goods or similar goods:

Provided that in applying the values used for comparison, due account shall be taken of demonstrated difference in commercial levels, quantity levels, adjustments in accordance with the provisions of rule 10 and cost incurred by the seller in sales in which he and the buyer are not related;

(c) Substitute values shall not be established under the provisions of clause (b) of this sub-rule.

(4) If the value cannot be determined under the provisions of sub-rule (1), the value shall be determined by proceeding sequentially through rule 4 to 9.

Rule 4. Transaction Value of Identical Goods

(1) (a) Subject to the provisions of rule 3, the value of imported goods shall be the transaction value of identical goods sold for export to India and imported at or about the same time as the goods being valued;

Provided that such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

(b) In applying this rule, the transaction value of identical goods in a sale at the same commercial level and in substantially the same quantity as the goods being valued shall be used to determine the value of imported goods.

(c) Where no sale referred to in clause (b) of sub-rule (1), is found, the transaction value of identical goods sold at a different commercial level or in different quantities or both, adjusted to take account of the difference attributable to commercial level or to the quantity or both, shall be used, provided that such adjustments shall be made on the basis of demonstrated evidence which clearly establishes the reasonableness and accuracy of the adjustments, whether such adjustment leads to an increase or decrease in the value.

(2) Where the costs and charges referred to in sub-rule (2) of rule 10 of these rules are included in the transaction value of identical goods, an adjustment shall be

made, if there are significant differences in such costs and charges between the goods being valued and the identical goods in question arising from differences in distances and means of transport.

(3) In applying this rule, if more than one transaction value of identical goods is found, the lowest such value shall be used to determine the value of imported goods.

Rule 5. Transaction Value of Similar Goods

(1) Subject to the provisions of rule 3, the value of imported goods shall be the transaction value of similar goods sold for export to India and imported at or about the same time as the goods being valued:

Provided that such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

The provisions of clauses (b) and (c) of sub-rule (1), sub-rule (2) and sub-rule (3), of rule 4 shall, mutates mutandis, also apply in respect of similar goods.

Answer to Question No. 5(b)

(i) Transaction value includes any amount charged in addition to the price of the goods by reason of or in connection with the sale. Since collection expenses are incurred by reason of or in connection with the sale, it would be included in the transaction value.

(ii) CBEC has vide Circular No.643/34/2002, dated 1.7.2002 clarified that delivery and collection charges of gas cylinders are by reason of or in connection with the sale of goods and therefore, the same would be included in the transaction value.

(iii) The interest on advances taken from the customers would not be included in the assessable value, unless the receipt of such advance had no effect of depressing the wholesale price.

In VST Industries Ltd. v. *CCEx, Hyderabad 1998 (97) ELT 395 (SC),* where interest free deposits wee taken because of commercial consideration of covering the risk of credit sales, no special consideration flowing from the assessee to the buyer keeping the deposit was found and the Supreme Court held that notional interest cannot be included in the assessable value.

However, in such case, the burden of proof lies on the Department to prove a nexus between the fact of advance taken and the depression in the value.

(iv) The transaction value is the price actually paid or payable for the goods. In the given situation, as the case of cash discount has not been passed on to the customer, it will not be allowed as deduction.

(v) As per the CBEC & Circular No.644/35/2002-CS, dated 12.7.2002 the Software can be of the following types —

Systems software/Operating Software —which is designed to control the operation of the computer system.

Application Software—which is developed for specific applications only.

Valuation of goods is done in the form in which it is cleared. Therefore, computer systems will be valued by including the value of the software loaded on the hard disc. No distinction is to be made between'opening software' and an 'application software'.

PART C

INTERNATIONAL TAXATION

Question No. 6

(a) Re-write the following sentences after filling up the blank spaces with appropriate word(s)/figure(s):

(i) The Advance Ruling under the Income Tax Act can be sought by:

(a) Specified category of residents

(b) A non resident

(c) Resident having transaction with non-residents

(d) Any of the above

(ii) An uncontrolled transaction can be between:

(a) A resident and non resident

(b) A resident and a resident

(c) A non resident and a non resident

(d) Any of the above

(iii) The advance ruling pronounced by the authority shall not be binding only:

(a) On the applicant who had sought it.

(b) On the other applicant for the same transaction

(c) In respect of the transaction in relation to which the ruling had been sought

(d) On the Commissioner in respect of the applicant and the said transaction.

(iv) Double Taxation Avoidance Agreement is a kind of bilateral treaty or agreement between the Government of India and:

(a) A company

(b) A society

(c) An association of persons

(d) None of the above

(v) GATT stands for ________________:

(a) General Agreement on Tariff and Trade

(b) General Agreement on Tax and Tariff

(c) General Agreement on Tax and Trade

(d) General Agreement on Trade and Treaty. *(1 mark each)*

(b) Write a brief note on "Foreign Direct Investment (FDI)". (5 marks)

(c) What are the 'tax exemptions' available with respect to foreign income under Income tax Act. (5 marks)

(d) What do you mean by "Double Taxation relief provisions in India". (5 marks)

Answer to Question No. 6(a)(i)

(d) Any of the above

Answer to Question No. 6(a)(ii)

(d) Any of the above

Answer to Question No. 6(a)(iii)

(b) On the other applicant for the same transaction

Answer to Question No. 6(a)(iv)

(d) None of the above

Answer to Question No. 6(a)(v)

(a) General Agreement on Tariff and Trade

Answer to Question No. 6(b)

Foreign Direct Investment

Foreign capital is an important ingredient for the development of the any economy. Therefore, the Government of India encourages foreign direct investment (FDI) and investment from Non-Resident Indians (NRIs) including Overseas Corporate Bodies (OCBs), that are predominantly owned by them, to complement and supplement domestic investment. Investment and returns are freely repatriable, except where the approval is subject to specific conditions such as lock-in period on original investment, dividend cap, foreign exchange neutrality, etc. as per the notified sectoral policy.

Foreign direct investment is freely allowed in all sectors including the services sector, except where the existing and notified sectoral policy does not permit FDI beyond a ceiling. FDI for virtually all items/activities can be brought in through the Automatic Route under powers delegated to the Reserve Bank of India (RBI), and for the remaining items/activities through Government approval. Government approvals are accorded on the recommendation of the Foreign Investment Promotion Board (FIPB).

Answer to Question No. 6(c)

Tax Exemptions with respect to foreign income

Special tax incentives provided to FII's in respect of income from securities and capital gains.

Dividends and interest on investments made by FII's are taxed at a concessional rate of 20% and long term capital gains @ 10%. Short term capital gains on sale of securities are subject to tax @30%.Short term capital gain covered under section 111A are taxed at 15%. However, foreign companies and non-resident non-corporate tax payers are charged at a rate of 20% on long term capital gains.

Other exemptions include:

(a) Exemptions for new industrial undertakings in FTZ's

(b) Deductions in case of royalties and fees for technical services earned by foreign nationals in India

Special tax concessions is made available EEC investors under Section 10(23BBB) of the Income Tax Act 1961.

There are other incentives for tax holidays specially relating to investments made in new industrial undertakings in under–developed areas. Moreover tax holiday facilities available for power generating sector and investment in building infrastructures.

There is also provision for deduction for capital expenditure for scientific research under Section 35 of the Act. The government of India from time to time issue notifications and circulars relating to granting of concessions to corporate or non-corporate entities under Sections 35,10(6), etc., of the Act.

To encourage venture capital financing, Section 10(23FB) of the act provides an income tax exemption for all dividends and long term capital gains of a venture capital fund or a venture capital company from investments made by way of equity shares in venture capital undertakings. To obtain this exemption, venture capital fund or company must obtain approval from the prescribed authority and satisfy the prescribed conditions.

Answer to Question No. 6(d)

Double Taxation Relief

Section 90 : Agreements with Foreign Countries or specified territories

Government of India can enter into agreement with a foreign government vide Entry 14 of the Union List regarding any matter provided Parliament verifies it. Double Tax Avoidance Agreement is a kind of bilateral treaty or agreement, between Government of India and any other foreign country or specified territory outside India. Such treaty or agreement is permissible in terms of Article 253 of the Constitution of India.

India has entered into bilateral agreements with many countries regarding avoidance of double taxation including tax avoidance and tax evasion issues. Section 90 of the income Tax deals with relief granted to assesses involved in paying taxes twice that is, paying taxes in India as well as in Foreign Countries or specified territory outside India.

It has been stated in the provision that charge of tax in respect of a foreign company at a higher rate than the rate at which a domestic company is chargeable shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

The provision (Section 90) of the Act shall apply to the extent that is more beneficial to the assessee.

Section 90A

Any specified association in India may enter into an agreement with any specified association in the specified territory outside India for the purpose of double taxation relief and the Central Government may, by notification in the Official Gazette, make such provisions as may be necessary for adopting and implementing such agreement.

TEST PAPER 4/2010

Time allowed : 3 hours *Max. marks : 100*

NOTE : *All Questions are compulsory.*

PART A

DIRECT TAXATION – LAW AND PRACTICE

Question No. 1

(a) Choose the most appropriate answer from the given options in respect of the following:

(i) The MAT credit can be carried forward for :

(a) 7 years

(b) 10 years

(c) 8 years

(d) Cannot be carried forward

(ii) The following shall be reduced from the net profit while calculating book profits under Minimum Alternate tax:

(a) Depreciation debited to profit and loss a/c

(b) The amount of loss brought forward or unabsorbed depreciation whichever is less

(c) Income to which the provisions of section 10 or 11 is applicable if credited to P& L A/c

(d) All the above

(iii) A company is said to be resident in India in any previous year, if:

(a) It is an Indian Company

(b) The control and management is wholly situated in India

(c) Either it is a Indian company or the control and management is wholly situated in India

(d) It is both an Indian Company and the control and management is wholly situated in India.

(iv) ________________ is tax planning under the express provisions of tax laws

(a) Short range planning

(b) Permissive tax planning

(c) Purposive tax planning

(d) Long range planning

(v) An appeal to the High Court shall be filled within ______________ of the date on which the order appealed against is received

(a) 60 days

(b) 30days

(c) 45 days

(d) 120 days *(1 mark each)*

(b) Explain how is the residential status of a company determined under the Income Tax Act, 1961. *(5 marks)*

Answer to Question No. 1(a)(i)

(b) 10 years

Answer to Question No. 1(a)(ii)

(d) All the above

Answer to Question No. 1(a)(iii)

(c) Either it is a Indian company or the control and management is wholly situated in India

Answer to Question No. 1(a)(iv)

(b) Permissive tax planning

Answer to Question No. 1(a)(v)

(d) 120 days

Answer to Question No. 1(b)

Residential Status of a Company - Section 6(3)

A company is said to be a resident in India in any previous year if :

(a) it is an Indian company; or

(b) during the relevant previous year, the control and management of its affairs is situated wholly in India.

A company will be a non-resident in any previous year if:

(a) it is not an Indian company; and

(b) the control and management of its affairs is situated wholly or partially outside India.

Indian Company

Section 2(26) of the Income Tax Act, 1961 defines the expression 'Indian Company' as a company formed and registered under the Companies Act, 1956 and includes:

(a) a company formed and registered under any law relating to companies formerly in force in any part of India (other than the State of Jammu and Kashmir, and the Union Territories specified in (e) below);

(b) any corporation established by or under a Central, State or Provincial Act;

(c) any institution, association or body which is declared by the Board to be a company under Section 2(17) of the Income Tax Act, 1961;

(d) in the case of State of Jammu & Kashmir, any company formed and registered under any law for the time being in force in that State; and

(e) in the case of any of the Union Territories of Dadra and Nagar Haveli, Goa, Daman and Diu and Pondicherry, a company formed and registered under any law for the time being in force in that Union Territory;

Provided that the registered or, as the case may be, principal office of the company, corporation, institution, association or body in all cases is in India.

Question No. 2

(a) Explain the concept of MAT and the MAT Credit. *(5 marks)*

(b) Which are the areas in Income Tax Act where Tax planning can be applied. *(5 marks)*

Answer to Question No. 2(a)

MAT – Basic Concept

Every person has to pay tax on his taxable income computed in accordance with the provisions of the Income Tax Act, 1961. However in case of a company, a separate provision has been inserted by Section 115JB which is commonly referred as Minimum Alternate Tax (MAT). As per this section, every company is liable to pay tax of an amount which is higher of following:

(a) Tax liability computed as per the provisions of the Income Tax Act by applying the normal rates applicable to a company.

(b) Tax liability computed as per the provisions of Section 115JB i.e. MAT.

MAT is computed @18% (plus surcharge and cess as applicable) on the book profits of the company. Book profit is computed by making certain adjustments to net profit as per profit and loss account which is to be prepared in accordance with the provisions of the Companies Act, 1956. Therefore in case of a company, the tax payable for any assessment year cannot be less than 18% of book profit.

MAT Credit

MAT paid under section 115JB is called MAT credit. According to section 115JAA the amount of MAT credit shall be allowed to be carried forward and set off in a year when the tax becomes payable on the total income computed under the regular provisions of the Income Tax Act. However, the carry forward shall be allowed only for 10 assessment years immediately succeeding the assessment year in which the tax credit becomes allowable. No interest shall be allowed on the amount of MAT credit.

Answer to Question No. 2(b)

Areas of Tax Planning for a Corporate Assessee

At the time of setting up of new business entity:

(a) Form of organisation/ownership pattern;

(b) Locational aspects;

(c) Nature of business.

For the business entities already in existence:

(d) Tax planning in respect of corporate restructuring;

(e) Tax planning in respect of financial management;

(f) Tax planning in respect of employees remunerations;

(g) Tax planning in respect of Foreign Collaborations and Joint Venture Agreements;

(h) Tax planning in the light of various Double Taxation Avoidance Agreements

Areas of Tax Planning for a Non-Corporate Assessee

The following factors are important determinants of effective tax planning :

(a) *Residential Status and Citizenship Status* – Tax incident depends upon the residential status of the assessee therefore, an assessee should carefully plan his stay in India and abroad so that his tax incident is minimum.

(b) *Heads of Income* – Each head of income has provisions related to the exemptions/ deductions. Maximum benefit of these exemptions / deductions should be availed of to minimize the tax liability.

(c) *Latest Legal Provision* – The assessee should keep himself abreast of the latest provisions of the tax laws so that he can make effective tax planning.

Question No. 3

(a) Distinguish between Tax Avoidance and Tax Evasion. (5 marks)

(b) Explain the provisions relating to revision of assessment order prejudicial to the interest of assessee. (5 marks)

Answer to Question No. 3(a)

Tax Avoidance *vis-à-vis* Tax Evasion

Tax avoidance is minimizing the incidence of tax by adjusting the affairs in such a manner that although it is within the four corners of the taxation laws but the advantage is taken by finding out loopholes in the laws. The shortest definition of tax avoidance is that it is the art of dodging tax without breaking the law.

In the case of tax avoidance, the tax payer apparently circumvents the law, without giving rise to a criminal offence, by the use of a scheme, arrangement or device, often of a complex nature but where the main purpose is to defer, reduce or completely avoid the tax payable under the Law.

Whereas tax evasion refers to circumvent the tax liability by illegal and dishonest means. Some of which are :

(a) Concealment of income;
(b) Inflation of expenses to suppress income;
(c) Falsification of accounts;
(d) Conscious violation of rules.

These devices are unethical. The courts also do not favour such unethical means. Evasion, once provided, not only attracts heavy penalties but may also lead to prosecution.

Answer to Question No. 3(b)

Revision of orders in favour of Assessee [Section 264]

Revision of orders not covered by Section 263, can be made by the Commissioner either on his own motion or on an application made by the assessee, provided orders have been passed by an authority subordinate to him. The application made by the assessee shall be accompanied by a fee of Rs.500. The Commissioner may call for the record of any proceeding under this Act on the basis of which such order has been passed and may make such inquiry or cause such inquiry to be made. He may pass such orders thereon as he thinks fit as are not prejudicial to the assessee. The Commissioner, under this section can cancel the assessment and direct the Assessing Officer to make a fresh assessment but such direction shall not be prejudicial to the assessee.

The Commissioner shall not revise any order under this section in the following cases :

(a) where the order has been made more than one year previously, the Commissioner shall not, on his own motion, revise such an order; or

(b) where the application for revision by the assessee has been made after one year from the date on which the order in question was communicated to him or the date on which he otherwise came to know of it, whichever is earlier. However, if the Commissioner is satisfied that the assessee was prevented by sufficient cause from making the application within the prescribed period he may admit an application made after the expiry of that period.

(c) where an appeal against the order lies to the Commissioner (Appeals) but it has not been made and the time within which such appeal may be made has not expired; and the assessee has not waived his right of appeal; or

(d) where the order has been made the subject of an appeal to the Commissioner (Appeals) i.e. where an appeal ahs been filed to CIT (Appeals) on any issue relating to such order.

Time limit for passing the revision order under Section 264 : On application made by the assessee under this section, the Commissioner shall pass an order within one year from the end of the financial year in which the application is made by the assessee.

PART B

INDIRECT TAXATION – LAW AND PRACTICE

Question No. 4

(a) Choose the most appropriate answer from the given options in respect of the following:

(i) As per the Central Excise Rules, PLA Stands for _________________:

(a) Permanent Ledger Account

(b) Periodical Ledger Account

(c) Payment Ledger Account

(d) Personal Ledger Account

(ii) In case the goods removed during the month of March, the excise duty shall be paid by

(a) 5th April of following month

(b) 6th April of following month

(c) 31st March of the same month

(d) Any of the above

(iii) The assessee shall himself assess the duty payable on any excisable goods except:

(a) Pan Masala

(b) Cigarettes

(c) Cement

(d) Air Conditioner

(iv) A situation where excise duty is not payable on goods lost/destroyed and found deficient in quantity on account of natural causes, unavoidable accidents etc. is called:

(a) Rebate of duty

(b) Remission of duty

(c) Discount

(d) None of the above

(v) Excise duty shall be leviable if:

(a) They are goods

(b) They are excisable

(c) They are produced or manufactured in India

(d) All the above

(vi) Manufacturers, whose aggregate value of clearances in the preceeding financial year had not exceeding rupees _____________ are entitled to the concession of a Small Scale Industries:

(a) 300 Lakhs

(b) 150 Lakhs

(c) 400 Lakhs

(d) 450 Lakhs

(vii) ______________ means the transaction value at which the greatest aggregate Quantity of goods is sold:

(a) Transaction Value

(b) Normal price

(c) Normal transaction value

(d) Assessable value

(viii) The Superintendent of Central Excise has the power to grant remission of duty upto rupees:

(a) 15,000

(b) 20,000

(c) 11,000

(d) 10,000

(ix) The duty paid on export shall be refunded if the goods are re-imported within ______ from the date of exportation :

(a) 3 months

(b) 6 months

(c) 1 year

(d) 2 years

(x) Loading, unloading and handling charges associated with the delivery of the imported goods at the place of importation shall be charged at the rate:

(a) .5 %

(b) 1%

(c) 2%

(d) 1.125% *(1 mark each)*

(b) What are the conditions to be satisfied to accept the transaction value as assessable value under the Central Excise Act, 1944 ? *(5 marks)*

(c) Explain the provisions of 'Remission of Duty' in relation to rule 21 of Central Excise Rules, 2002. *(5 marks)*

Answer to Question No. 4(a)(i)

(d) Personal Ledger Account

Answer to Question No. 4(a)(ii)

(c) 31st March of the same month

Answer to Question No. 4(a)(iii)

(b) Cigarettes

Answer to Question No. 4(a)(iv)

(b) Remission of duty

Answer to Question No. 4(a)(v)

(d) All the above

Answer to Question No. 4(a)(vi)

(c) 400 Lakhs

Answer to Question No. 4(a)(vii)

(b) Normal transaction value

Answer to Question No. 4(a)(viii)

(d) 10,000

Answer to Question No. 4(a)(ix)

(c) 1 year

Answer to Question No. 4(a)(x)

(b) 1%

Answer to Question No. 4(b)

Essential Conditions of Transaction Value

The Essential conditions of Transaction Value are :

(i) the goods are sold by an assessee for delivery at the time of place of removal; the term "place of removal" has been defined basically to mean a factory or a warehouse;

(ii) the assessee and the buyer of the goods are not related; and

(iii) the price is the sole consideration for the sale.

(i) *Goods must be sold at the time of Removal"*

Section 4(1) lays down 'sale' as an essential ingredient in removal of excisable goods. As per Section 2(h), 'sale' …"means any transfer of goods by one person to another in the ordinary course of trade or business for cash or deferred payment or other valuable consideration.

The following are treated not to be 'sale' of 'goods' for the purpose of levy of Central Excise :

(a) Transfer to depots or branches, as there is no 'sale' at the time and place of removal.

(b) Job work or processing, as there is no sale' of goods and the job charges received by the Job Worker cannot be treated as 'consideration'.

(c) Free samples or supply under warranty claims.

(d) Hypothecation, as in hypothecation, possession is not transferred to the person to whom goods are hypothecated. Similarly, 'charge' will not be 'sale' if possession is not transferred.

(e) If the contract is for FOR delivery at destinations.

(ii) *Assessee and buyer are not Related*

Each transaction in which transaction value is to be treated as assessable value, should be in arms' length and on principal to principal basis. If the transaction is not on principal to principal basis the charges to be added back.

(iii) *Price is the Sole Consideration*

The price should be the sole consideration in accepting the transaction value as assessable value. In case consideration has been received in any other form, its monetary value should be considered and added back.

Answer to Question No. 4(c)

Power to make Rules

Section 5 empowers the Central Government to make rules relating to remission of excise duty leviable on excisable goods, which are found deficient in quantity due to any natural cause.

It is also provided that such rules may, having regard to the nature of the excisable goods or of processing or of curing thereof, provide for the period of their storage or transit and other relevant considerations an fix the limit or limits of percentage beyond which no such remission shall be allowed. Further, different limit or limits of percentage may be fixed for different varieties of the same excisable goods or for different areas or for different seasons.

Rules of Remissions

Rule 21 of the Central Excise Rules, 2002 provides that where it is shown to the satisfaction of the Commissioner that goods have been lost or destroyed by natural causes or by unavoidable accident or are claimed by the manufacturer as unfit for consumption or for marketing, at any time before removal, he may remit the duty payable on such goods, subject to such conditions may be imposed by him by order in writing.

Provided that where such duty does not exceed ten thousand rupees, the provisions of this rule shall have effect as if for the expression “Commissioner”, the expression “Superintendent of Central Excise” has been substituted

Provided further that where such duty exceeds ten thousand rupees but does not exceed one lakh the provisions of this rule shall have effect as if for the expression “Commissioner”, the expression “Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise, as the case may be,” has been substituted.

Provided also that where such duty exceeds one lakh but does not exceed five lakh the provisions of this rule shall have effect as if for the expression “Commissioner”, the expression “Joint Commissioner of Central Excise or Additional Commissioner of Central Excise, as the case may be,” has been substituted.

Question No. 5

(a) Write short notes on:

(i) Self Assessment method

(ii) Compounded Levy Scheme *(5 marks each)*

(b) What are the procedure for filing an appeal before Central Excise and Service Tax Appellate Tribunal. *(5 marks)*

Answer to Question No. 5(a)(i)

Self Assessment Method

All excisable goods are covered by self removal procedure, except cigarettes. Lots of procedural relaxations have been made under Self Removal Procedure Scheme paving way for payment of duty by the assessee on self-assessment basis.

Rule 6 of the Central Excise Rules, 2002 states that the assessee shall himself assess the duty payable on any excisable goods and discharge the same, provided that in case of cigarettes, the Superintendent or Inspector of Central Excise shall assess the duty payable before removal by the assessee.

The assessee is required to submit monthly return in ER-1 (earlier RT-12) Form. This return has to be filed along with "Self Assessment Memorandum" whereby, the assessee declares that the particulars contained in ER-1 return are correctly stated, duty has been correctly assessed and paid as per the provisions of this Act. The return made shall be subject to scrutiny by the Departmental Officers, who may carry out surprise checks along with routine audit procedures.

Answer to Question No. 5(a)(ii)

Compounded Levy Scheme

Compounding of levies implies the assessee being authorised to pay a pre-determined sum to the department, at fixed periodical intervals, instead of paying duty on a consignment-to-consignment basis. The amount of duty to be paid is pre-determined by the department on the basis of various parameters pertaining to production. The advantage of compounding is that the assessee is freed from the procedural formalities being fulfilled by him for each consignment. The advantage to the department is that it reduces the need to control various factors pertaining to production and removal. The option has been made available in case of manufacturers in unorganised sectors where accounting records are not adequate or proper for consumption and collection of duty payable on goods manufactured.

However, the system has been very selectively resorted to and applies only to a few items. Currently the scheme is applicable only to stainless steel patties/pattas and aluminum circles". The compounded levy scheme has been recently extended to panmasala and gutkha vide Notification No. 38/2007.

The procedure is that the assessee eligible under the scheme will first file an application for special procedure (ASP) before the Assistant Commissioner. The Assistant Commissioner will have the necessary investigations made to verify the eligibility as well as the amount to be paid by the assessee. The duty compounded, as prescribed in the schedule current at the time, will have to be paid by the assessee in the form prescribed therefor. The assessee is thus freed from almost all fetters such as maintaining separate accounts and submitting returns etc

Answer to Question No. 5(b)

Filing Appeal before CESTAT (Section 35B)

(1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order

(a) A decision or order passed by the Commissioner of Central Excise as an adjudicating authority;

(b) An order passed by the Commissioner (Appeals) under section 35A;

(c) An order passed by the Central Board of Excise and Customs or the Appellate Commissioner of Central Excise under section 35, as it stood immediately before the appointed day;

(d) An order passed by the Board or the Commissioner of Central Excise, either before or after the appointed day, under section 35A, as it stood immediately before that day

Provided that no appeal shall lie to the Appellate Tribunal in respect of any order referred to in clause (b) if such order relates to loss of goods in transit, rebate of duty of excise on goods exported, goods exported outside India (except to Nepal or Bhutan) without payment of duty, credit of any duty allowed to be utilised towards payment of excise duty on final products under the provisions of this Act or the rules made there under and such order is passed by the Commissioner (Appeals) on or after the date appointed.

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or clause (d) where, the amount of fine or penalty determined by such order does not exceed fifty thousand rupees.

(2) The Committee of Commissioners of Central Excise may, if it is of opinion that an order passed by the Appellate Commissioner of Central Excise under section 35, as it stood immediately before the appointed day, or the Commissioner (Appeals) under section 35A, is not legal or proper, direct any Central Excise Officer authorised by him in this behalf to make an appeal to the Appellate Tribunal against such order.

Provided that where the Committee of Commissioners of Central Excise differs in its opinion regarding the appeal against the order of the Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Chief Commissioner of Central Excise who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct any Central Excise Officer to appeal to the Appellate Tribunal against such order.

(3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Commissioner of Central Excise , or, as the case may be, the other party preferring the appeal.

(4) The party against whom the appeal has been preferred may file a memorandum of cross-objections within forty-five days of the receipt of the notice.

(5) The Appellate Tribunal can condone the delay in filing an appeal or memorandum of cross-objections if it is satisfied that there was sufficient cause for not presenting it within that period.

(6) An appeal to the Appellate Tribunal shall be in the prescribed form and shall be accompanied by a fee of;

(a) Rupees one thousand where the amount of duty and interest demanded and penalty rupees five lakh or less.

(b) Rupees five thousand, where the amount of duty and interest demanded and penalty levied is more than rupees five lakh but not exceeding fifty lakh rupees.

(c) Ten thousand rupees, where the amount of duty and interest demanded and penalty levied is more than fifty lakh rupees,

Provided that no fee shall be payable in the case where an appeal filed by the department or for submitting a memorandum of cross-objections.

Both the parties to the dispute will be heard together by the bench. The Department will be represented normally by departmental officers functioning as Departmental Representatives. The assessee can appear in person or through counsel. In this regard, Section 35Q prescribes that any party to a dispute may otherwise than when required by the Tribunal to attend personally for examination on oath, can appear through an authorised representative.

Question No. 6

(a) Discuss briefly with reference to decided case laws as to how the 'value' shall be determined under the Customs Act, 1962 and Valuation Rules made there in the following cases:

(i) Goods are offered at specially reduced price to buyer and the buyer is asked not to disclose the specially reduced price to any other party in India.

(ii) There has been a price rise between the date of contract and the date of importation. The contract was over 6 months before the date of shipment.

(iii) The sale involves special discounts limited to exclusive agents.

(iv) The goods are purchased on High seas. (2 marks each)

(b) How Transaction Value of identical goods to be determined under Customs law ? (3 marks)

(c) Explain the concept of Duty on Pilfered Goods under section 13 of Customs Act, 1962. (4 marks)

Answer to Question No. 6(a)

(i) Where sales are made to buyers at specially reduced prices, the prices so offered cannot be said to be the ordinary prices. In Padia Sales Corporation v. Collector of Customs (1993) 66 ELT 35 (SC) the Supreme Court held that where the goods are offered to the buyers at specially reduced prices and the buyer is asked not to disclose the specially educed price to any other party, then the said price will not be acceptable.

(ii) Where there is a price rise at the time when the goods are imported in comparison to the price when the contract was made then, the price at the time of importation will be taken to the value of the goods. In *Rajkumar Knitting Mills Pvt. Ltd.* v. *Collector of Customs (1998)* 98 ELT 292(SC), the Supreme Court held that the contract price may have bearing while determining the value of the goods, but the value is to be determined at the time of importation of the goods.

(iii) In *Eicher Tractors Ltd.* v. *Commissioner of Customs*, Mumbai (2000), 122 ELT

321 (SC) the Supreme Court held that the price paid by the importer to the vendor in the ordinary course of commerce shall be taken to the value of imported goods. Since the buyer and the seller are not related and the price is the sole consideration for sale, the discounted price was taken as the assessable value. However, this decision has been nullified by the Customs Valuation Price of Imported Goods Rules, 2002 and consequently, where the sale involves special discounts limited to exclusive agents, such discounted price shall not be accepted as the assessable value.

(iv) Where high sea sales are made, the price charged by the importer from the assessee will be taken to the value of the goods. Similar view was expressed by the Tribunal in *Godavari Fertilizers* v. *C.C. Ex.* (1996) 81 ELT 535 (Tri).

Answer to Question No. 6(b)

Transaction Value of Identical Goods

(1) (a) Subject to the provisions of rule 3, the value of imported goods shall be the transaction value of identical goods sold for export to India and imported at or about the same time as the goods being valued;

Provided that such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

(b) In applying this rule, the transaction value of identical goods in a sale at the same commercial level and in substantially the same quantity as the goods being valued shall be used to determine the value of imported goods.

(c) Where no sale referred to in clause (b) of sub-rule (1), is found, the transaction value of identical goods sold at a different commercial level or in different quantities or both, adjusted to take account of the difference attributable to commercial level or to the quantity or both, shall be used, provided that such adjustments shall be made on the basis of demonstrated evidence which clearly establishes the reasonableness and accuracy of the adjustments, whether such adjustment leads to an increase or decrease in the value.

(2) Where the costs and charges referred to in sub-rule (2) of rule 10 of these rules are included in the transaction value of identical goods, an adjustment shall be made, if there are significant differences in such costs and charges between the goods being valued and the identical goods in question arising from differences in distances and means of transport.

(3) In applying this rule, if more than one transaction value of identical goods is found, the lowest such value shall be used to determine the value of imported goods.

Answer to Question No. 6(c)

Duty on Pilfered Goods

Section 13 provides that if any goods are pilfered after the unloading thereof and before the proper officer has made an order for clearance for home consumption or deposit in a warehouse, the importer shall not be liable to pay the duty leviable on such goods except where such goods are restored to the importer after pilferage.

Under the section, duty is not payable on pilfered goods only in cases where the goods are pilfered after the unloading and before the customs authorities issue the order for clearance. If, therefore, the goods are pilfered after the order of clearance is made but before they are actually cleared, duty is leviable.

PART C

INTERNATIONAL TAXATION

Question No. 7

(a) Re-write the following sentences after filling up the blank spaces with appropriate word(s)/figure(s):

(i) The application filed for advance ruling may be withdrawn within ____ from the date of the application

(ii) Uncontrolled transaction means a transaction between enterprises other than _______.

(iii) OECD stands for ____________________.

(iv) CFC stands for ___________.

(v) Financial Institutional Investors can invest in government securities as well as private securities subject to guidelines prescribed by the RBI and ________ . *(1 marks each)*

(b) What is Transfer Pricing ? Explain it with reference to relevant provisions of the Income Tax. *(5 marks)*

(c) What are the restrictions imposed on admissibility of application under Advance Ruling. *(5 marks)*

(d) What do you mean by Permanent Establishment in context of Double Taxation Avoidance Agreements. *(5 marks)*

Answer to Question No. 7(a)

(i) The application filed for advance ruling may be withdrawn within **30 days** from the date of the application

(ii) Uncontrolled transaction means a transaction between enterprises other than **associated enterprises**.

(iii) OECD stands for **Organisation for Economic Cooperation and Development**.

(iv) CFC stands for **Controlled Foreign Corporation**.

(v) Financial Institutional Investors can invest in government securities as well as private securities subject to guidelines prescribed by the RBI and **Securities and Exchange Board of India**.

Answer to Question No. 7(b)

The transfer price is the price which is arrived at when two associated or related enterprises deal with each other. Since, the enterprises involved are related entities, they can manipulate prices in a manner whereby the profits are transferred to the entity of the country, where the tax rates are lower. This would deprive the Government the revenue which would otherwise be payable by assesses.

With a view to provide a statutory framework which can lead to computation of reasonable, fair and equitable profits and tax in India, in case of such associated or related entities, a set of special provisions have been introduced in the Income Tax Act and Regulations.

Section 92 provides for computation of income from international transactions having regard to the principle of arm's length pricing. It is further provided that not only the income but the expenses or interest also to be determined at arm's length price. However, the provisions of arm's length price shall not apply if these result into reduction of income or increase of loss.

Arm's length price means a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises in uncontrolled conditions.

As per Section 92C of the Income Tax Act, 1961 the arm's length price in relation to an international transaction shall be determined by any of the following methods :

(a) Comparable uncontrolled price method;

(b) Resale Price Method;

(c) Profit split method;

(d) Cost plus method;

(e) Transactional Net Margin Method;

(f) Such other method as may be prescribed by the Board

Out of the above the most appropriate method shall be adopted having regard to the nature of transaction or class of transactions or class of associated persons or functions performed.

There are provisions also under which arm's length price may be determined by the Assessing Officer in certain cases or he may refer the computation of the arm's length price to the Transfer Pricing Officer with the previous approval of the Commissioner. The Act also provides for maintenance, keeping of information and documents by persons entering into an international transaction.

Answer to Question No. 7(c)

Procedure on receipt of Application [Section 245R]

The authority on receipt of the application will send a copy to the Commissioner concerned and, wherever necessary, also call upon the Commissioner to furnish the relevant records. Such records will be returned to the Commissioner as soon as possible.

The authority may, after examining the application and the records called for, either allow or reject the application.

Cases where the authority shall not allow the application : It has been provided specifically that the Authority shall not allow an application, in the following cases:

(a) Where the question of law or fact raised in the application is already pending in case of the applicant either before (i) any income tax authority, or (ii) the Appellate Tribunal or (iii) Any Court.

However, this will not be applicable in case of notified residents, if it is pending before Income-tax Authority or the Appellate Tribunal. But the application in c case of notified resident shall also not to be entertained if the issue is pending before any Court.

(b) Where the question raised relate to the determination of the fair market value of any property.

(c) Where the transaction in relation to which the question is raised, is designed for the avoidance of income-tax. However, this will not be applicable in case of notified residents.

However, no application shall be rejected unless an opportunity has been given to the applicant of being heard. Further where the application is rejected, reasons for such rejection shall be given in the order and copy of the same shall be sent to the applicant and to the Commissioner.

Answer to Question No. 7(d)

Permanent Establishment (PE)

The term 'Permanent Establishment' (PE) is one of the important terms that occur in all the Double Taxation Avoidance Agreements. The term has not been defined in the Income Tax Act. However as per the Double Taxation Avoidance Agreements, PE includes, a wide variety of arrangements i.e. a place of management, a branch, an office, a factory, a workshop or a warehouse, a mine, a quarry, an oilfield etc. Imposition of tax on a foreign enterprise is done only if it has a PE in the contracting state. Tax is computed by treating the PE as a distinct and independent enterprise.

Some Salient aspects concerning a PE are as under:

— PE is defined with reference to place and persons;

— PE could be a fixed place, a construction site, service PE, agency PE branch etc.

— PE denotes non-resident's business preserves. The degree of preserve which could constitute PE has been illustrated by 'inclusions and exclusions'.

— An enterprise is liable to tax on its profits in a foreign country, if it conducts its subsidiary in that country through PE.

Isolated or occasional transactions through some persons or agency do not create liability for tax is the basis of PE. There has to be continuity of activities contributing to the earning of income—something more than mere transaction of purchase and sale or transactions of preparatory or auxiliary nature. Such activities must be value creating activities requiring capital.

TEST PAPER 5/2010

Time allowed : 3 hours *Max. marks : 100*

NOTE : *All Questions are compulsory.*

PART A

DIRECT TAXATION – LAW AND PRACTICE

Question No. 1

(a) *Choose the most appropriate answer from the given options in respect of the following:*

(i) *The Union Government has exclusive power to levy tax on income other than agricultural income of Item No. __________ of Union List*

(a) *84*

(b) *92A*

(c) *97*

(d) *82*

(ii) *The Finance Act, 2009 has abolished ___________*

(a) *Dividend Distribution Tax*

(b) *Fringe Benefit Tax*

(c) *Securities Transaction Tax*

(d) *None of the above*

(iii) *A Situation where a person tries to reduce his tax liability by deliberately suppressing the income or by inflating the expenditure showing the income lower than the actual income and restoring to various types of deliberate manipulations is known as:*

(a) *Tax Planning*

(b) *Tax Avoidance*

(c) *Tax Evasion*

(d) *All the above*

(iv) *For Carry Forward of loss under various heads the assessee shall file a return of loss under section 139(3) of Income Tax Act,1961 within the prescribed time limit except:*

(a) *Loss under head Capital gain*

(b) *Loss under head Profits and Gains from business or profession*

(c) *Loss under head House property*

(d) *All the above*

(v) *"Book Profits" means the net profit as shown in the profit and loss account* *for the relevant previous year prepared under this sub-section as increased by;*

(a) The provision for income tax

(b) Proposed Dividend

(c) Depreciation

(d) All the above (1 mark each)

(b) Discuss in detail the areas where the tax planning can be resorted by an assessee. (5 marks)

Answer to Question No.1 (a)(i)

(d) 82

Answer to Question No.1 (a)(ii)

(b) Fringe Benefit Tax

Answer to Question No.1 (a)(iii)

(c) Tax Evasion

Answer to Question No.1 (a)(iv)

(c) Loss under head House property

Answer to Question No.1 (a)(v)

(d) All the above

Answer to Question No. 1(b)

Areas of Tax Planning for a Corporate Assessee

At the time of setting up of new business entity:

(a) Form of organisation/ownership pattern;

(b) Locational aspects;

(c) Nature of business.

For the business entities already in existence:

(d) Tax planning in respect of corporate restructuring;

(e) Tax planning in respect of financial management;

(f) Tax planning in respect of employees remunerations;

(g) Tax planning in respect of Foreign Collaborations and Joint Venture Agreements;

(h) Tax planning in the light of various Double Taxation Avoidance Agreements

Areas of Tax Planning for a Non-Corporate Assessee

The following factors are important determinants of effective tax planning:

(a) Residential Status and Citizenship Status – Tax incident depends upon the residential status of the assessee therefore, an assessee should carefully plan his stay in India and abroad so that his tax incident is minimum.

(b) Heads of Income – Each head of income has provisions related to the exemptions/ deductions. Maximum benefit of these exemptions / deductions should be availed of to minimize the tax liability.

(c) Latest Legal Provision – The assessee should keep himself abreast of the latest provisions of the tax laws so that he can make effective tax planning.

Question No. 2

Write short notes on the following:

(i) Tax Planning

(ii) Tax Evasion. *(5 marks each)*

Answer to Question No. 2(i)

Tax Planning

Tax planning is an honest and rightful approach to the attainment of maximum benefits of the taxation laws within their framework. The objectives of tax planning cannot be regarded as offending any concept of the taxation laws and subjected to reprehension of reducing the inflow of revenue to the Government's coffers, so long as the tax planning measures are in conformity with the statute laws and the judicial expositions thereof. The basic objectives of tax planning are:

(a) Reduction of tax liability

(b) Minimisation of litigation

(c) Productive investment

(d) Healthy growth of economy

(e) Economic stability

Answer to Question No. 2(ii)

Tax Evasion

Unscrupulous citizens evade their tax liability by dishonest means. Some of which are :

(a) Concealment of income;

(b) Inflation of expenses to suppress income;

(c) Falsification of accounts;

(d) Conscious violation of rules.

These devices are unethical and illegal and the courts do not favour such unethical means. Evasion, once proved, not only attracts heavy penalties but may also lead to prosecution.

Question No. 3

(a) Under what circumstances can an assessee appeal to the Appellate Tribunal. *(5 marks)*

(b) *What do you understand by "Book Profit" in the context of Minimum Alternate Tax.* *(5 marks)*

Answer to Question No. 3(a)

Appealable orders [Section 253(1) and (2)]

Any assessee aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order.

1. An order passed by Commissioner (Appeals) under Section 154 ordering a rectification of mistake, or under Section 250 in connection with the disposal of an appeal or Section 271 imposing a penalty for failure to furnish return etc. or Sections 271 A or 272A.
2. An order passed by an assessing officer under Clause (c) of Section 158BC, in respect of search initiated under Section 132 or books of account other documents or any assets requisitioned under Section 132A, after the 30th day of June, 1995 but before the 1st day of January, 1997.
3. An order passed by a Commissioner under Section 12AA relating to registration of trust or under Section 263 relating to revision of orders prejudicial to revenue or under Section 272A penalty for failure to answer question, sign statements, allow inspection etc., on or under Section 154 rectifying a mistake, or an order passed by a Chief Commissioner, or a Director General or a director under Section 272A.
4. An order passed by an Assessing Officer under Sub-section (1) of Section 115VZC.
5. An order passed by a Commissioner for rejection of approval under Section 80G(5)(vi).

The Commissioner may, if he objects to any order passed by Commissioner (Appeals) under Section 154 or 250, direct the Assessing Officer to appeal to the Appellate Tribunal against the order.

Answer to Question No. 3(b)

MAT – Basic Provision

Every person has to pay tax on his taxable income computed in accordance with the provisions of the Income Tax Act, 1961. However in case of a company, a separate provision has been inserted by Section 115JB which is commonly referred as Minimum Alternate Tax (MAT). As per this section, every company is liable to pay tax of an amount which is higher of following:

(a) Tax liability computed as per the provisions of the Income Tax Act by applying the normal rates applicable to a company.

(b) Tax liability computed as per the provisions of Section 115JB i.e. MAT.

MAT is computed @18% (plus surcharge and cess as applicable) on the book profits of the company. Book profit is computed by making certain adjustments to net profit as per profit and loss account which is to be prepared in accordance with the provisions of the Companies Act, 1956.

Meaning of "Book Profit"

According to the Explanation 1 to Section 115JB (2), "Book Profit" means the net profit as shown in the profit and loss account for the relevant previous year prepared under Sub-section (2), as increased by :

(a) the amount of Income tax paid or payable, and the provision therefor; or

(b) the amounts carried to any reserves, by whatever name called other than reserve specified under Section 33AC; or

(c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities, or

(d) the amount by way of provision for losses of subsidiary companies; or

(e) the amount or amounts of dividends paid or proposed; or

(f) the amount or amounts of expenditure relatable to any income to which Section 10 [other than section 10(38) } or Section 11 or Section 12 apply ;or

(g) the amount of depreciation.

(h) the amount of deferred tax and provision therefore.

(i) the amount or amounts set aside as provision for diminution in the value of any asset.

The net profit as increased by the amounts referred to in Clauses (a) to (i) shall be reduced by the following amounts:

(i) the amount withdrawn from any reserves or provisions if any such amount is credited to the profit and loss account;

However following amounts credited to profit and loss account should not be deducted:

(a) Amount withdrawn from reserve created before 1.4.97 otherwise than by wayof a debit to the profit and loss account.

(b) Any other amount withdrawn from reserve or provision on or after 1.4.97, if such amount was not added to profit while computing the book profit of the year in which such amount was transferred to reserve, out of which such amount is withdrawn.

(ii) the amount of income to which any of the provisions of Section 10 { except 10 (38) } or Section 11 or Section 12 apply, if any such amount is credited to the profit and loss account; or

(iii) the amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or

(iv) the amount withdrawn from revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in Clause (iii) above; or

(v) the amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account. For the purposes of this clause, the loss shall not include depreciation. Therefore, in a case where an assessee has shown profit in a year, but after adjustment of depreciation it results profit or loss, no adjustment in book profit is allowed; or

(vi) the amount of profits eligible for deduction under section 80HHC, 80HHE or 80HHF;

(vii) the amount of deferred tax, if any such amount is credited to the profit and loss account.

The amount computed after increasing or decreasing the above is known as 'Book-Profit'.

PART B

INDIRECT TAXATION – LAW AND PRACTICE

Question No. 4

(a) Choose the most appropriate answer from the given options in respect of the following:

(i) Rules are subsidiary legislation under the Act and framed by;

(a) Central Board of Excise and Custom

(b) Central Government

(c) Parliament

(d) None of the above

(ii) Interest under section 11BB for interest on delayed refunds will be payable for the period beyond ____________ from the date of receipt of application upto date of refunds.

(a) 3 months

(b) 6 months

(c) 4 months

(d) 1 Year

(iii) In the case of cigarettes, the assessment will be done by:

(a) Assessee

(b) Assistant Commissioner

(c) Superintendent

(d) Any of the above

(iv) The Daily Stock Account shall be preserved for a period of _________ immediately after the financial year to which such records pertain.

(a) 8 years

(b) 3 years

(c) 5 years

(d) 4 years

(v) For the contravention of the provisions for which no penalty has been provided in the Cenvat Credit Rules, 2004 then assessee shall be liable to a penalty which may extend to rupees:

(a) 10,000

(b) 8,000

(c) 5,000

(d) 15,000

(vi) In case of captive consumption of goods for production of other article by the assessee, the value will be _______________ of cost of production.

(a) 105%

(b) 110%

(c) 120%

(d) None of the above

(vii) Any article which is imported into India shall, in addition, be liable to a duty equal to the excise duty for the time being leviable on a like article, that duty is called:

(a) Basic custom duty

(b) Countervailing duty

(c) Safeguard duty

(d) None of the above

(viii) The period for which the goods may remain in warehouse in case of Capital goods for use by 100% EOU is:

(a) Till the expiry of 5 years

(b) Till the expiry of 1 years

(c) Till the expiry of 3 years

(d) None of the above

from the date of deposit in the warehouse

(ix) The Advance Ruling as provided under the Customs Act, 1962 should be given within a time limit of __________ from the date of receipt of application:

(a) 30 days

(b) 60 days

(c) 90 days

(d) 120 days

(x) As per the Customs Act, 1962 condonation of delay by commissioner (Appeals) on sufficient cause being shown can be given for a further period of_____________

(a) 45 days

(b) *60 days*

(c) *30 days*

(d) *15 days* *(1 mark each)*

(b) *Write Short Notes on the following:*

(i) *Duty under Protest under Central Excise Act,1944*

(ii) *Remission of Duty under section 23 of Customs Act,1962.*

(5 marks each)

Answer to Question No. 4(a)(i)

(b) Central Government

Answer to Question No. 4(a)(ii)

(a) 3 months

Answer to Question No. 4(a)(iii)

(c) Superintendent

Answer to Question No. 4(a)(iv)

(c) 5 years

Answer to Question No. 4(a)(v)

(c) 5,000

Answer to Question No. 4(a)(vi)

(b) 110%

Answer to Question No. 4(a)(vii)

(b) Countervailing duty

Answer to Question No. 4(a)(viii)

(a) Till the expiry of 5 years

Answer to Question No. 4(a)(ix)

(c) 90 days

Answer to Question No. 4(a)(x)

(c) 30 days

Answer to Question No. 4(b)(i)

Excise duty is paid under protest

Where an assessee desires to pay duty under protest he shall deliver to the Proper Officer a letter to this effect and give grounds for payment of the duty under protest. On receipt of the said letter, the Proper Officer shall give an acknowledgement to it.

The acknowledgement so given shall, subject to the provisions of Sub-rule (4), be the proof that the assessee has paid the duty under protest from the day on which the letter of protest was delivered to the Proper Officer. An endorsement "Duty paid under protest" shall be made on all copies of the invoice, the Application for Removal and form ER-I / ER-II, as the case may be.

In cases where the remedy of an appeal or revision is not available to the assessee against an order or decision which necessitated him to deposit the duty under protest, he may, within three months of the date of delivery of the letter of protest give a detailed representation to the Assistant/Deputy Commissioner of Central Excise.

In cases where the remedy of an appeal or revision is available to the assessee against an order or decision which necessitated him to deposit the duty under protest, he may file an appeal or revision within the period specified for filing such appeal or revision, as the case may be.

On service of the decision on the representation referred to in Sub-rule (5) or of the appeal or revision referred to in Sub-rule (6) the assessee shall have no right to deposit the duty under protest:

Provided that an assessee shall be allowed to deposit the duty under protest during the period available to him for filing an appeal or revision, as the case may be, and during the pendency of such appeal or revision, as the case may be.

If any of the provisions of this rule has not been observed, it shall be deemed that the assessee has paid the duty without protest.

Answer to Question No. 4(b)(ii)

Remission of Duty under Section 23 of Customs Act, 1962

(1) Without prejudice to the provisions of section 13, where it is shown to the satisfaction of the Assistant Commissioner of Customs [or Deputy Commissioner of Customs] that any imported goods have been lost (otherwise than as a result of pilferage) or destroyed, at any time before clearance for home consumption, the Assistant Commissioner of Customs or Deputy Commissioner of Customs shall remit the duty on such goods.

(2) The owner of any imported goods may, at any time before an order for clearance of goods for home consumption under Section 47 or an order for permitting the deposit of goods in a warehouse under Section 60 has been made, relinquish his title to the goods and thereupon he shall not be liable to pay the duty thereon:

Provided that the owner of any such imported goods shall not be allowed to relinquish his title to such goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

Question No. 5

(a) Re-write the following sentences after filling up the blank spaces with appropriate word(s)/figure(s):

(i) Imported goods which are pilfered after unloading thereof and before the

proper officer ordered clearance for ______________ or deposit in a warehouse are not liable to duty.

(ii) Manufacturers, whose aggregate value of clearances in the preceeding financial year had not exceeded rupees _____________, are entitled to the concession to Small Scale Industry unit.

(iii) If the goods have been used for some time after importation, then the draw back will be proportionate to the __________________ in value and the period for which it was put to use.

(iv) ______________ means the import of any goods in contravention of the provisions of the Customs Act, 1962 or any other law for the time being in force.

(v) Regulations are made by ________________ under the provisions of the Customs Act, 1962. *(1 mark each)*

(b) State the situation in which an order of an adjudicating authority becomes appealable in Customs Law. *(5 marks)*

(c) Explain the provision for claiming drawback of duty paid on imported goods when they are re-exported. *(5 marks)*

Answer to Question No. 5(a)

(i) Imported goods which are pilfered after unloading thereof and before the proper officer ordered clearance for **home consumption** or deposit in a warehouse are not liable to duty.

(ii) Manufacturers, whose aggregate value of clearances in the preceding financial year had not exceeded rupees **400 lakhs**, are entitled to the concession to Small Scale Industry unit.

(iii) If the goods have been used for some time after importation, then the draw back will be proportionate to the **depreciation** in value and the period for which it was put to use.

(iv) **Illegal import** means the import of any goods in contravention of the provisions of the Customs Act, 1962 or any other law for the time being in force.

(v) Regulations are made by **Central Board of Excise and Customs** under the provisions of the Customs Act, 1962.

Answer to Question No. 5(b)

Orders passed by adjudicating authorities give rise to disputes between the assessee and Customs Department. These generally arise in connection with the classification and valuation of goods or in regard to infraction of legal provisions and/or procedures.

An incorrect assessment to a duty might take place on account of various factors. An incorrect assessment is as detrimental to the exchequer as it is to the assessee. Therefore, an elaborate mechanism of appeals has been provided in the Customs Law.

Section 128 of the Customs Act, provides that any person aggrieved by any decision or order passed under this Act by an officer of customs lower in rank than a Commissioner of Customs may appeal to the Commissioner (Appeals) within 60 days from the date of the communication to him of such decision or order.

Any person aggrieved by a decision or order passed by the Commissioner of Customs as an adjudicating authority, may file an appeal before the Appellate Tribunal under Section 129A.

Answer to Question No. 5(c)

Drawback on re-export of duty paid goods (Section 74)

The necessary conditions for claiming Duty Drawback under Section 74 Customs Act, 1962 are as follows:

(i) The goods on which the drawback is claimed must have been previously imported;

(ii) Import duty must have been paid on these goods when they were imported;

(iii) The goods must be entered for re-export within two years from the date of payment of duty. However, it is provided that in any particular case this period of two years may, on sufficient cause being shown, be extended by the Board by such further period it may deem fit;

(iv) The goods are identified to the satisfaction of the Assistant Commissioner of Customs as the goods that were imported;

(v) The goods must be actually re-exported to any place out-side India;

(vi) The goods must be capable of easy identification; and

(vii) The market price of such goods must not be less than the amount of drawback claimed.

The Central Government has been empowered to make rules for the purpose of carrying out the provisions of Section 74 and, in particular, such rules may:

(a) provide for the manner in which the identity of goods imported in different consignments which are ordinarily stored together in bulk, may be established;

(b) specify the goods which shall be deemed to be not capable of being easily identified; and

(c) provide for the manner and the time within which a claim for payment of drawback is to be filed.”

Rates of Drawback of Import Duty Admissible under Section 74

Two types of cases are covered in the above category. They are:

(i) Imported goods exported as such i.e. without putting into use — the drawback given is 98% of duty paid on import.

(ii) Imported goods exported after use. In such case the percentage of duty refunded will be according to the period of usage, between the date of clearance for home consumption and the date when the goods are “placed under Customs Control” for exports. The rate of drawback in this case is not fixed and progressively decreases as the period of use increases.

Question No. 6

(a) *Having regard to the provisions of section 4 of the Central Excise Act, 1944, compute/derive the assessable value of excisable goods, for levy of duty of excise, given the following information:*

- *Cum-Duty wholesale price including sales tax of Rs.2500*	*15,000*
Normal secondary packing cost	*1,000*
Cost of special secondary packing	*1,500*
Cost of durable and returnable packing	*1,500*
Freight	*1,250*
Insurance on freight	*200*
Trade discount (normal practice)	*1,500*
Rate of Central Excise duty as per Central Excise tariff	*15% Adv.*

(10 marks)

(b) *What do you understand by "Doctrine of Unjust Enrichment".* *(5 marks)*

Answer to Question No. 6(a)

The assessable value from cum-duty price can be worked out by the under-mentioned formula :

$$\text{Assessable value} = \frac{\text{(Cum - duty price - Permissible deductions x 100}}{100 + \text{rate of duty}}$$

Computation of Assessable value

	Rs.	*Rs.*
Cum-duty price		15,000
Deductions (See Notes)		
Sales Tax	2,500	
Durable & Returnable packing	1,500	
Freight	1,250	
Insurance	200	
Trade-Discount	1,500	
	6950	8,050
Less : Central Excise Duty		
Thereon @ 15% Adv.		
8050 x 15/115		1,050
Assessable Value		7,000

Notes :

1. The transaction value does not include Excise Duty, Sales Tax and other Taxes.
2. The Excise Duty is to be charged on the net price; hence trade discount is allowed as deduction.
3. With regards to packing, all kinds of packing except durable and returnable packing are included in the assessable value. The durable and returnable packing not included as such packing is not sold and is durable in nature.
4. Freight and insurance on freight will be allowed as deduction only if the amount charged is actual and it is shown separately in the invoice as per Rule 5 of the Central excise Valuation Rules, 2000.

Answer to Question No. 6(b)

Doctrine of Unjust Enrichment

In case of refunds, there is a major controversy that a claim of refund can be entertained only if the duty has not already been passed to the buyers. The reason being that if the claim of refund is allowed when the duty has already been passed to others, it would tantamount to unintended profit to the assessee resulting into his unjust enrichment. Thus, no manufacturer would be entitled to the refund of excise duty, if e has already passed on the incidence of such duty to the buyer.

There is a presumption that the manufacturer has already passed on the incidence to the buyer and hence the manufacturer has to prove to the contrary that he has not passed on the incidence to the buyer. In view of this, deciding a refund claim is a quasi-judicial function and the Assistant Commissioner has to issue a notice to the claimant and hear him before rejecting the claim in full or in part.

The statutory provisions to prevent unjust enrichment have been provided in Section 11B, 11D, 12A, 12B, 12C and 12D of the Central Excise Act. However, the following types of refunds have been kept out of the bar of unjust enrichment:

(i) Rebate on account of exports

(ii) Unspent advance deposits lying in balance in PLA

(iii) Refund of CENVAT Credit

(iv) Duty of Excise paid and borne by the manufacturer

(v) Duty of Excise paid and borne by the buyer.

PART C

INTERNATIONAL TAXATION

Question No. 7

(a) Re-write the following sentences after filling up the blank spaces with appropriate word(s)/figure(s):

(i) ______ means a transaction between enterprises other than associated enterprises.

(ii) A ____ is a place where there is no tax on income or it is taxed at low rated of tax structure.

(iii) The application of Advance Ruling may be withdrawn within ____ from the date of application.

(iv) The amount of income tax shall in case of foreign company be increased by a surcharge @ ___ per cent.

(v) CFC stands for _______. *(1 mark each)*

(b) What do you mean by Arm's Length Price. What are the methods of calculating it ? *(6 marks)*

(c) Explain the Authority for Advance Rulings under the Income Tax Act, 1961? Who can seek Advance Ruling ? *(6 marks)*

(d) What do you mean by foreign tax credit ? *(3 marks)*

Answer to Question No. 7(a)

(i) **Uncontrolled Transaction** means a transaction between enterprises other than associated enterprises.

(ii) A **tax heaven** is a place where there is no tax on income or it is taxed at low rated of tax structure.

(iii) The application of Advance Ruling may be withdrawn within **30 days** from the date of application.

(iv) The amount of income tax shall in case of foreign company be increased by a surcharge **@2.5%** per cent.

(v) CFC stands for **Controlled Foreign Corporation** .

Answer to Question No. 7(b)

The transfer price is the price which is arrived at when two associated or related enterprises deal with each other. Since, the enterprises involved are related entities; they can manipulate prices in a manner whereby the profits are transferred to the entity of the country, where the tax rates are lower. This would deprive the Government the revenue which would otherwise be payable by assesses.

With a view to provide a statutory framework which can lead to computation of reasonable, fair and equitable profits and tax in India, in case of such associated or related entities, a set of special provisions have been introduced in the Income Tax Act and Regulations.

Therefore, Section 92 provides for computation of income from international transactions having regard to the principle of arm's length pricing. Arm's length price means a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises in uncontrolled conditions. It is further provided that not only the income but the expenses or interest also to be determined at arm's length price. However, the provisions of arm's length price shall not apply if these result into reduction of income or increase of loss.

As per Section 92C of the Income Tax Act, 1961 the arm's length price in relation to an international transaction shall be determined by any of the following methods:

(a) Comparable uncontrolled price method;

(b) Resale Price Method;

(c) Profit split method;

(d) Cost plus method;

(e) Transactional Net Margin Method;

(f) Such other method as may be prescribed by the Board

Out of the above the most appropriate method shall be adopted having regard to the nature of transaction or class of transactions or class of associated persons or functions performed.

Answer to Question No. 7(c)

Authority for Advance Rulings – Section 245O

The Central Government shall constitute an authority for giving advance rulings, to be known as Authority for Advance Rulings. The Authority will consists of the following members appointed by the Central Government :

(i) a chairman who will be a retired judge of the Supreme Court,

(ii) an officer of the Indian Revenue Service who is qualified to be member of CBDT, and

(iii) an officer of the Indian Legal Service who is qualified to be an Additional Secretary to the Government of India.

Applicant for Advance Ruling

As per Section 245N(b) of the Income Tax Act, the advance ruling under the income-tax act could be sought by :

(a) A non-resident;

(b) Resident having transactions with non-residents.

(c) Specified categories of residents.

Answer to Question No. 7(d)

Foreign Tax Credit

The US Government has opted for foreign tax credit system being a system involving crediting income tax paid by US entities to the country of the source – as the principal method of accommodation to be used in its international tax relations. The credit is given unilaterally and is thus the key factor in the tax calculation relating to foreign income. Tax credit may be direct or indirect. A direct tax credit is one which is attributable directly on the US tax payers which includes earning from a foreign branch of US Company. Indirect tax is equal to dividend (including withholding tax) multiplied by foreign tax and divided by earnings net of foreign income taxes. In no case the credit for taxes paid abroad should exceed the US tax payable on total foreign source income for the same year. Due to increased globalilsation of businesses more and more transactions are being undertaken where the residents need to claim the tax credit of the income-tax paid in other countries.

Wipro Ltd. v. *DCIT-ITA Nos.895 & 896/Bang/03 and 881&882/Bang/03* dated 21st June 2005. In this case the Bangalore Tribunal as held that foreign taxes in respect of income earned abroad will be available as per the provisions of the tax treaty, irrespective of whether income is taxable in India or not provided the income is included in the return of income filed in India. The Tribunal also held that incentive provisions/deductions available should not be brushed aside on a technical consideration.