PAPER - 7 : DIRECT AND INDIRECT TAXATION

SUGGESTED ANSWERS

SECTION – A

1.

(i) (B)

(ii) (B)

(iii) (A/B)

(iv) (C)

(v) (B)

(vi) (B)

(vii) (B)

(viii) (B)

(ix) (C)

(x) (C)

(xi) (D)

(xii) (A)

(xiii) (A)

(xiv) (A)

(xv) (C)

SECTION - B

2. (a)

(i) Determination of residential status of Mathew:

The first of the basic condition is stay of 182 days or more during the previous year 2025-26.
Mathew stayed in India for 128 days during the previous year 2025-26 and therefore does not satisfy the basic condition.

The second basic condition is Mathew must have stayed in India for 365 days or more in 4 previous years preceding the previous year 2025-26 and stayed for 60 days during the previous year 2025-26.

Whereas his aggregate stay in 4 previous years preceding the previous year was 349 days i.e. (57+62+160+70) and his stay during the year was 128 days. He does not satisfy the second of the basic condition also.
As he does not satisfy both the basic conditions, his status is non-resident.

(ii) In case he is a person of India origin:

If he is a person of Indian origin who comes on a visit to India during the previous year, his stay must be more than 365 days during 4 previous years preceding the previous year 2025-26; and

(a) Stays 120 days or more if his total income other than income from foreign sources (i.e. Indian income) exceeds ₹15 lakhs; or

(b) Stays 182 days or more in other cases (Indian income less than ₹15 lakhs)

Mathew does not satisfy the first condition and therefore his status would be non-resident, whether or not has total income exceeding ₹15 lakhs from Indian sources.

(iii) If he is an Indian citizen who does not pay income tax in any country:

As per section 6(1A) an individual being a citizen of India if does not have to pay income-tax in any other country and has total income in India (other than income from foreign sources) exceeding ₹ 15 lakhs (in this case ₹ 22 lakhs)

he shall be deemed to be resident in India / or resident but not ordinarily resident

2. (b)

Computation of salary income of Ms. Monica for the Asst. Year 2026-27

Particulars	**₹**
Basic salary	12,00,000
Dearness allowance @50%	6,00,000
House rent allowance	3,60,000
Not eligible for exemption under default tax regime	
Fixed transport allowance	60,000
Free refreshment during office hours – exempt	Nil
Mobile phone facility – exempt	Nil
Allowance for transfer – exempt	Nil
Medical facility in the hospital maintained by the employer – Exempt under proviso to section 17(2)(viii)	Nil
Medical expenditure outside India is exempt up to the extent permitted by RBI. Balance amount is taxable	40,000
NPS contribution of employer [@15% of basic salary]	1,80,000
	24,40,000
Less: Standard deduction U/s.16(1)	75,000
Income from salary	23,65,000

3. (a)

Determination the income from house property chargeable in the hands of Rohan and Mohan for the assessment year 2026-27		
	Rohan	**Mohan**
I Self-Occupied Property	₹	₹
Gross Annual Value – In case of self-occupied property,	Nil	Nil
Interest paid on loan - Where the house property is owned by co-owners and is occupied by each of the co-owner then all of them can claim benefit u/s 23(2)(a) and interest on loan shall be allowed to all the co-owners to the extent of ₹2,00,000 as the case may be.	2,00,000	2,00,000
Loss from self-occupied property (A)	(2,00,000)	(2,00,000)
II Let-out Property		
Expected Rent		
Higher of Municipal value or Fair rent (A)	6,30,000	
Standard Rent (B)	6,60,000	
Reasonable Expected Rent – Lower of (A) and (B)– (C)	6,30,000	
Actual rent received (60000 x 12 months) (D)	7,20,000	
GAV (Higher of (C) and (D)	7,20,000	
Less: Municipal Taxes Paid	11,000	

NAV		7,09,000	
Less:			
Standard deduction @30%	2,12,700		
Interest on loan	3,75,000		
		5,87,700	
Income from let out house property (B)		1,21,300	
Income under the head house property (B) – (A)		(78,700)	
Income under the head house property			(2,00,000)

3. (b)

Computation of profits and gains of business in the hands of Mr Prabhat for the assessment year 2026-27

Particulars	(₹)	(₹)
Net Profit as per Profit and Loss account		3,56,700
Add: - Expenses not allowable		
Depreciation charged		1,05,000
Salary paid to brother [unreasonable under section 40A (2)]		2,500
GST liability		Nil
Since GST liability has been paid before the 'due date' of filing return of income under section 139(1). Hence, the same is allowable as deduction under section 37).		
Printing and stationery		25,000
Whole amount of printing & stationery paid in cash would be disallowed, since such amount exceeds ₹ 10,000 under section 40A (3)		
Donation to public charitable trust – disallowed		2,000
Under valuation of closing stock		18,000
Short term capital loss on shares		9,500
		5,18,700
Less: - Income not forming part of business income		
Depreciation as per Income-tax Act, 1961	1,20,000	
Income from UTI	3,000	
Taxable under the head Income from Other Sources (or not taxable under the head Profits and gains from business or profession)		
Under valuation of opening stock	9,000	
		1,32,000
Profits and Gains of business		3,86,700

Alternative solution:

Computation of Income from Business of Mr Prabhat for the Asst. Year 2026-27

Particulars	₹	₹
Sales		90,00,000
Closing stock [85,000 +18,000]		1,03,000
		91,03,000
Less:		
Opening stock [95,000 +9,000]	1,04,000	
Purchases	84,00,000	

Salary [60,000 – 2,500]	57,500	
Rent and rates	24,000	
Since GST liability has been paid before the 'due date' of filing return of income under section 139(1). Hence, the same is allowable as deduction under section 37).		
Interest on loan	5,000	
Depreciation	1,20,000	
Printing & Stationery – disallowed	Nil	
Whole amount of printing & stationery paid in cash would be disallowed, since such amount exceeds ₹ 10,000 under section 40A (3).		
Postage & telegram	800	
Loss on sale of shares – not allowed	Nil	
Other general expenses [7,000 – 2,000]	5,000	
		87,16,300
Income from business		3,86,700
Income from UTI ₹3,000 taxable under the head Income from Other Sources or not taxable under the head income from business	3,000	

4. (a)

Computation of capital gain of Mr. Harvinder Shah for the Asst. Year 2026-27

Particulars	₹	₹
Sale consideration		150,00,000
Stamp duty value		170,00,000
As the stamp duty value exceeds 110% of the actual sale consideration, the stamp duty value is to be adopted as deemed sale consideration		
Sale consideration	170,00,000	
Less: Cost of acquisition	30,00,000	
Long-term capital gain		140,00,000
Sale of equity shares:		
Sale consideration 300 shares @₹ 1700 each	5,10,000	
Less: Cost of acquisition @ ₹ 1900 per share		
FMV as on 31.01.2018 @ ₹ 2400 per share		
Whichever is less to be adopted ₹ 1900 X 300 shares	5,70,000	
Long-term capital loss		(60,000)
		139,40,000
Less: Exemption under section 54: In respect of acquisition of residential building		(80,00,000)
As the difference between the actual cost of acquisition and stamp duty value is less than 10% the stamp duty value is not to be considered.		
Exemption under section 54EC:		
As the bonds were acquired beyond 6 months after the date of sale of residential building, no exemption would be allowed.		
Net Long-term capital gain		59,40,000
Note: Advance money forfeited is taxable under the head 'Other sources' and therefore not considered.		

4. (b)

Computation of income chargeable under the head "Other sources" in the case of Mr Narottam for the Asst. Year 2026-27

Particulars		₹
Rent from vacant land given for rearing livestock		45,000
Rent from vacant land given for rearing livestock is not agricultural income.		
Dividend from Indian company		1,00,000
Gold bracelet from wife's father		Nil
Wife's father would come under the definition of "relative" and therefore the gift is not taxable		
Winning from horse race		10,000
Honorarium from University		60,000
		2,15,000
Less: Interest on loan for investment in shares of Indian company	20,000	
₹ 30,000 or 20% of ₹ 1,00,000- whichever less is deductible		
Collection charges – not eligible for deduction	Nil	
		20,000
Income from other sources		1,95,000

5. (a)

Computation of total income of Mr. Amit for the Asst. Year 2026-27 (Old regime)

Particulars		₹	₹
Income from salary		11,75,000	
Less: Standard deduction		50,000	
			11,25,000
Income from House property			
Loss from let out property		(1,40,000)	
Loss from self-occupied property – representing interest on housing loan		(80,000)	
		(2,20,000)	
Loss from house property eligible for set off against salary income – limited to			(2,00,000)
Balance of loss from house property eligible for carry forward under the old regime ₹ 20,000.			
			9,25,000
Income from Business:			
Income from intra-day trade in shares		4,10,000	
Less: Loss from business before depreciation	2,40,000		
Depreciation for the year	60,000		
Eligible for set off against speculation business income from intra-day trade in shares		3,00,000	
Net income from business after set off			1,10,000
Capital gains:			
Long-term capital gain (STT paid shares)		4,60,000	
Less: Short-term capital loss – Jewellery – set off		(75,000)	
			3,85,000
Other sources:			
Loss from the activity of owning and maintaining race horses ₹ 3,00,000 eligible for carry forward			
Loss from horse races ₹ 1,20,000 not eligible for carry forward			
		Gross Total Income	14,20,000

5. (b)

Computation of total income of Mr Shetty for the Asst. Year 2026-27

(i) Computation of total income as per old regime		₹
Income from manufacture business		25,00,000
Profit from SEZ unit ₹ 12 lakhs less deduction U/s.10AA @ 50%		6,00,000
Income by way of royalty		4,50,000
Gross Total Income		35,50,000
Less: Chapter VI-A deductions:		
Section 80JJAA	10,20,000	
Section 80QQB	3,00,000	
		13,20,000
Total Income		22,30,000
Tax thereon	4,81,500	
Add: HEC @ 4%	19,260	
Tax liability		5,00,760
(ii) Alternate Minimum Tax under section 115JC		
Total income		22,30,000
Add: Income from SEZ		6,00,000
Deduction U/s.80JJAA		10,20,000
Deduction U/s.80QQB		3,00,000
Adjusted total income		41,50,000
Tax thereon @ 18.5%		7,67,750
Add: HEC @ 4%		30,710
Tax liability		7,98,460
Conclusion: As the adjusted total income exceeded ₹ 20 lakhs, the alternate minimum tax to be ascertained. The higher of two tax liabilities would be the actual tax liability. Therefore, the final tax liability of Shetty would be ₹ 7,98,460.		

6. (a)

Difference between Direct taxes & Indirect taxes are as under:

Sl. No.	Basis	Direct Tax	Indirect Tax
(i)	Meaning	Direct tax is referred to as the tax, levied on person's income and wealth and is paid directly to the government	Indirect Tax is referred to as the tax, levied on a person who consumes the goods and services and is paid indirectly to the government.
(ii)	Nature	Progressive in nature i.e., higher tax is levied on a person earning higher income and vice versa.	Regressive in nature i.e., all persons will bear equal wrath of tax on goods or service consumed by them irrespective of their ability.
(iii)	Incidence and Impact or Burden	Falls on the same person. Assessee, himself bears such taxes. Thus, it pinches the taxpayer.	Falls on different person. Tax is recovered from the assessee, who passes such burden to another person. Thus, it does not pinch the taxpayer.
(iv)	Evasion	Tax evasion is possible	Tax evasion is hardly possible because it is included in the price of the goods and services.

(v)	Inflation	Direct tax helps in reducing the inflation.	Cost of goods and services increases due to levy of indirect tax thus indirect taxes promote inflation. However, sometimes it is useful tool to promote social welfare by checking the consumption of harmful goods or sin goods through higher rate of tax.
(vi)	Imposition and collection	Imposed on and collected from the same person	Imposed on and collected from consumers of goods and services but paid and deposited by the assessee.
(vii)	Event	Taxable income of the assessee.	Supply of goods or services.

6. (b)

Functions of the Goods and Services Tax Network

The functions of the GSTN would, inter alia, include:

(i) facilitating registration;

(ii) forwarding the returns to Central and State authorities;

(iii) computation and settlement of IGST;

(iv) matching of tax payment details with banking network;

(v) providing various MIS reports to the Central and the State Governments based on the tax payer return information;

(vi) providing analysis of tax payers' profile; and

(vii) running the matching engine for matching, reversal and reclaim of input tax credit.

7. (a)

Eligibility for composition levy scheme

(i) A supplier engaged in the manufacture of goods as notified under section 10(2)(e), is not eligible for composition scheme under section 10(1) and 10(2).

Ice-cream and pan masala are notified under this category.

Since, Diwakar Sons is engaged in manufacture of, inter alia, ice-cream and pan masala, is not eligible to opt for composition levy even if his aggregate turnover does not exceed ₹150 lakh in the preceding financial year.

(ii) The turnover limit for composition scheme under section 10 (1) and section 10(2) in the case of Special Category States (Manipur in this case) is ₹ 75 lakh in the preceding financial year.

Bhaskar Trader being a registered person in Manipur had a turnover of ₹55 lakh in the preceding financial year. Therefore, it would be eligible for the composition scheme under section 10(1) if it continued to engage exclusively in the restaurant business.

Under second proviso to section 10(1), a person opting for composition scheme under CGST may supply services (other than restaurant services) up to a maximum of 10% of the turnover in the preceding financial year or ₹ 5 lakh, whichever is higher.

However, in the current financial year, Bhaskar Trader decides to shut down the restaurant business and exclusively provide computer repairing services. Since it no longer engaged in restaurant service it violates the conditions of section 10 (2)(a). Thus, Bhaskar Trader cannot opt for the composition levy under section 10(1) and (2) in the current financial year for computer repair services.

The benefit of composition scheme under section 10(2A) (commonly known as composition scheme for service provider) is available in case of a registered person who is not eligible to pay tax under sub-sections (1) and (2) of section 10 provided its aggregate turnover in the preceding financial year does not exceed ₹ 50 lakh.

Bhaskar Trader cannot avail the benefit of composition scheme under section 10(2A) also as its aggregate turnover in the preceding financial year was more than ₹ 50 lakh i.e. ₹55 lakhs.

7. (b)

Determination of taxable value of supply

(i) Where none of the currency exchanged is INR

Value of supply =

1% of the lesser of the two amounts the person changing the money would have received by converting any of the two currencies into Indian Rupee on that day at RBI reference rate

Euros = 11,000 x ₹ 86 = ₹ 9,46,000

Dirham = 42,000 x ₹ 23 = ₹ 9,66,000

1% of ₹ 9,46,000 = ₹ 9,460

(ii) Where one of the currency exchanged is INR

Value of supply =

(Buying rate or the selling rate - RBI reference rate for that currency at that time) X Total units of currency exchanged

₹ 83.50- ₹ 81.50) x 1,800 = ₹ 3,600

(iii) However, where the RBI reference rate for a currency is not available, the value shall be 1% of the gross amount of Indian Rupees provided or received by the person changing the money

1% of ₹ 1,70,000 = ₹ 1,700

8. (a)

Computation of Input tax credit in the case of Vinit Ltd for the month of November, 2025

		GST (₹)
(i)	Goods used for activities related to corporate social responsibility [ITC in respect of goods used for activities related to its obligation under corporate social responsibility (CSR) is blocked / under section 17(5) of the CGST Act, 2017]	Nil
(ii)	Goods given as free sample to prospective customers [ITC on goods disposed of by way of free samples is blocked / under section 17(5) of the CGST Act, 2017]	Nil
(iii)	Cement used for making foundation and structural support to plant and machinery	48,800
	(ITC on goods used for construction of plant and machinery is not blocked. Plant and machinery include foundation and structural supports through which the same is fixed to earth)	

(iv)	Confectionery items for consumption of employees working in the factory under statutory obligation	45,000
	(ITC is available since the same is provided under statutory obligation)	
(v)	Purchase of computer where debit note is issued	45,500
	(ITC can be availed on the basis of debit note issued by the supplier in accordance with Rule 36 of CGST Rules, 2017)	
(vi)	Car purchased for making further supply of such car	Nil
	[Though ITC on motor vehicles used for further supply of such vehicles is not blocked.	
	ITC on goods destroyed is blocked under section 17(5)]	
	Total Input Tax Credit (ITC) available	1,39,300

8. (b)

Computation of Assessable value

Particular	**(UK Pounds)**
Case I : Where actual freight and insurance given	
Cost of machine (ex-factory)	5,000
Add: Charges for carriage of machine to the airport of the exporter's country	100
FOB	5,100
Add: Air Freight (restricted to maximum of 20% of FOB) 20% of 5,100	1,020
Add: Insurance (Actual paid)	600
CIF/Assessable Value	6,720
CASE II Where Freight and Insurance not given	
Cost of machine (ex-factory)	5,000
Add: Charges for carriage of machine to the airport of the exporter's country	100
FOB	5,100
Add: Air Freight (20%of FOB) 20% of 5,100	1,020
Add: Insurance (1.125% of FOB) 1.125% of 5,100	57.38
CIF/Assessable Value	6,177.38

Notes:

(1) Charges for carriage of machine to the airport of the exporter's country are includible.

(2) Freight maximum 20% of FOB value as per customs is allowed in case of air transport.

(3) Insurance is 1.125% of FOB value in case actual insurance amount not ascertainable.