

Taxation Questions

What is Taxation?

Taxation is one of the mode used by the government to finance their expenditure by imposing charges on citizens and corporate entities. Government levy tax on citizens to encourage or discourage certain economic decisions.

What is alternative minimum tax (AMT)?

The Alternative Minimum Tax (AMT) is a way to restrict wealthy taxpayers from tax evasion. AMT uses a separate set of rules to calculate taxable income after allowed deductions. This is generally for higher income group as AMT sets a limit on certain benefits that reduces a taxpayer's regular tax amount. As a result, if the benefits on tax reduce total tax below AMT limit, taxpayer has to pay the higher AMT amount.

How can a taxpayer get a refund for an overpayment of taxes?

There is a provision in India to get a refund for an overpayment of taxes along with interest. When you have to claim a refund you need to file the income tax return within a specified period. You can even track your refund status from the NSDL-TIN website by clicking in Status of Tax refunds and can track your refund by entering PAN and Assessment year for which the refund is to be claimed.

What are the Streamlined Sales and Use Tax Agreement?

The Streamlined Sales and Use Tax Agreement was introduced in 1999 by the National Governor's Association (NGA) and the National Conference of State Legislatures (NCSL) in order to simplify the collection of sales tax as sales tax is second largest source of state revenue after personal income taxes. It resulted in decveloping a simpler and business friendly sales tax system.

The Agreement decreases costs and administrative burdens of sales tax collection on retailers, especially those operating in multiple states.

Explain deferred tax asset?

When a firm has overpaid on taxes then the amount is recorded in the balance sheet as deferred asset tax which is also known as provision for future taxation. Deferred tax asset arises when the firm, pays taxes early or have paid excess of tax and is entitled to get some money back from the tax authorities.

Define deferred tax Liability? What items come under deferred tax liability?

A tax liability that a company owes and does not pay at that current point, although it will be responsible for paying it at some point in the future. Deferred tax liability (DTL) is a balance sheet item that accounts for the temporary difference between taxes that will come due in the future and taxes paid today.

The unrealized tax that is put into account comes under deferred tax liability.

Depreciation is the main source or the type of an item of deferred tax liability.

Define Amortization & Impairment?

When the assets of the company are written off over a number of years for the purpose of their replacement or renewal and not depending on the life of asset is termed as amortization. It is different from depreciation, which is periodic writing off of the asset based on its normal life expectancy.

Impairment can be termed as the fall in the value of the asset due to any physical damage to the asset, obsolescence, or due to technological innovation. Impairments can be written off. Simply you can say that impairment is the difference between the fair value and the carrying value of an asset.

What is Inter Company Reconciliation?

Every year commonly controlled company prepares a combined or consolidated financial statement for tax and reporting purposes. Inter Company Reconciliation (ICR) is the process that helps parent company to split from its subsidiaries companies by location. Each year, commonly controlled business must prepare a combined or consolidated financial statement for tax and reporting purposes. The inter company accounting process is an important process for parent companies with subsidiaries or companies split by location. ICR helps in avoiding double counting of transactions as it also helps in maintaining accurate reports. Even it helps the companies to avoid misrepresentation of a firm's financial position.

What is the Securities Transaction Tax?

1. Securities Transaction Tax (STT) was introduced in India at time of 2004 budget and is applicable from 1 October 2004. STT is the tax which is payable on the amount of taxable securities transaction.
2. STT is just levied on purchase and sale of those securities that are listed on the Indian Stock Exchanges.
3. Securities Transaction Tax was introduced by the Finance Minister, P. Chidambaram to restrict people from evading tax on capital gains.

What is Permanent Account Number (PAN)?

Permanent Account Number (PAN) is a ten-digit alphanumeric number, which is issued by the Income Tax Department in the form of laminated card as PAN enables the department to link all kinds of transactions of the person with the department.

Transactions include tax payments, TDS/TCS credits, returns of income/wealth/gift/FBT, specified transactions, correspondence, etc. PAN helps the department in maintaining a fair record of every persons transactions through a ten digit number in order to avoid tax evasion in any case.

What is the difference between profit and gain?

Profit is the amount that is left after deducting expenses from revenue that makes the receipt of revenue possible. There are two streams of earnings that is direct earnings and indirect earnings. Direct earnings are incurred from main activities and indirect earnings are incurred from other activities so the profits is calculated as gross profit and net profit.

Gross profit is the amount of revenue from which trading expenses has been deducted (expenses related to main activities of the business). Net profit is the amount of revenue that includes incomes from other activities.

Gain is the amount that is earned on selling assets which is not included in the inventory of the business. This sales activity is not the actual trading and these sales does not includes goods that are sold on regular basis.

What items fall under the category of 'securities'?

'Securities' are defined under Section 2(h) of the Securities Contracts (Regulation) Act, 1956 (SCRA) to include:

1. Shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate derivatives.
2. Units or any other instrument issued by any collective investment scheme to the investors in such schemes.
3. Security receipt as defined in Section 2(zg) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
4. Such other instruments as declared by the central government and Rights or interest in securities.

5. Equity-oriented mutual funds (not debt-oriented mutual funds).

When Deferred Tax Asset & Deferred tax liability arises?

Deferred tax asset arises when the expenses are recorded in the income statement before they are required to be recognized by the taxing authority. Also when revenue is being taxed before it is taxable in the income statement.

Deferred tax liability arises from different depreciation methods being used for tax as depreciable assets are reported as non current.

What is the difference between Fund flow vs. Cash Flow?

Fund Flow

1. Fund flow is based on working capital.
2. Fund flows tells about the various sources from where the funds are generated.
3. Fund flow is useful for understanding long term financial strategy.
4. Changes in current assets and current liabilities are shown through the schedule of changes in working capital.

Cash Flow

1. Cash flow is based on only one element of working capital that is cash.
2. Cash flow starts with the opening balance of cash and closes with the closing balance of cash.
3. Cash flow is useful for understanding short term strategies that affects liquidity of the business.
4. Changes in current assets and current liabilities are shown in the cash flow.

If a NRI buys property in India, does he has to pay property tax?

Any income or capital gain that the NRI generates from the sale/ rent or lease of a valued property or an asset based in India will be taxed as per the Income Tax rules. If the property is more than 3 years old, long term capital gains tax will be incurred on the sale of the property. On long term capital gains, tax is payable at 20%.

Can a person fill a NRI in an Income tax form if he has been out of India for six months though he is Indian citizen?

He can fill NRI in an Income tax form only if he does not satisfy any of these two conditions:

1. He is in India in the previous year for a period of 182 days or more or
2. He is in India for a period of 60 days or more during the previous year and 365 days or more during the four years immediately preceding the previous year.

What is the difference between the excise duty and the sales tax?

Excise Duty is an indirect tax imposed on goods that are manufactured and produced within the country. This is paid by the manufacturer on the finished good when it goes out of the factory. Excise Duty is levied on all goods, except certain goods that are exempted. There are three types of Central Excise duties collected in India namely: Basic Excise Duty, Additional Duty of Excise, Special Excise Duty.

Sales Tax is imposed on the finished product which is paid by the consumer. Sales tax is imposed on sale or purchase within the State. Different states levy different levels of sales tax, while there is a Central Sales Tax levied on sale or purchase in the course of interstate trade.

What do you mean by fair rent?

Fair rent is the rent charged for a private property that is fixed and registered by a rent officer. Fair rent is decided on the basis of size, condition, and usefulness of the property. Fair rent is calculated in place of mortgage interest, other financing costs and depreciation related to certain property, including land, buildings and non movable equipment. It is calculated only once; at the time the facility begins operation.

Explain the procedure to calculate Provident Fund, ESI, VAT and Sales Tax.

Provident Fund: Provident fund is calculated at 12% on the basic salary which is deducted from employee's salary plus 12% on the basic is contributed by the employer. So, the aggregate 12% + 12 % is remitted to the Provident Fund Department.

ESI: Stands for Employee State Insurance and is calculated at 1.75% on the gross salary of the employees whose salary is below Rs. 10000 per month and employer contributes 4.75% on the gross salary of the employee and aggregate 1.75% + 4.75% is remitted to the ESI Department

VAT: VAT percentage is 1, 4, 12.5%. It is a tax which is charged on the basic value of the product by the seller from the buyer and the same is remitted to the Sales Tax Department.

Sales tax: Same as VAT

What is Excise & Service Tax? What is the difference?

Excise tax is an indirect tax that is imposed on the manufacture, sale or use on certain types of goods and products. Excise taxes are generally imposed on goods such as cigarettes or alcohol, also in the price of an activity such as gambling. Excise taxes may be imposed by both Federal and state authorities.

Service tax is an indirect tax imposed by the government on service providers on certain service transactions, but is actually paid by the customers. Services provided by air-conditioned restaurants and short term accommodation provided by hotels, inns, etc are included in the taxable services.

The major difference between excise tax and service tax is that excise tax is charged on manufactured goods and sales tax is imposed on certain services provided.

What is luxury tax?

A tax imposed on goods and services that are non-essential or not included in the necessities. Luxury tax is included in the indirect tax and is incurred by those who purchase or use the product. Ad valorem tax or progressive tax are some luxury tax that is imposed on high priced goods such as cars above a certain value or engine size, villas etc.

What do you mean by Commercial Tax?

Commercial Tax is a tax imposed on the scheduled Commercial goods as indirectly collected by the seller or purchaser against his business transaction which now comprises of Sales Tax, Entertainment, Luxury Tax, Entry Tax and Profession Tax.

What are the deductions under Salary Head? Name the items.

Deductions that are made under salary head are Entertainment allowance and Professional tax.

Entertainment Allowance- Entertainment allowance received is already included in the income of the employee and then a deduction is made only for government employees. A sum equal to 1/5th of salary (excluding all allowances, benefits and other perquisites) or Rs. 5,000, whichever is less is being deducted.

Professional Tax- Professional Tax is imposed by the government on employment by whatever name called, under Article 80C 276 of the Constitution and shall be allowed as a deduction. [Sec. 16(iii)]

What is Entertainment Tax?

Entertainment tax is imposed on every financial transaction that is related to entertainment such as movie tickets, major commercial shows and big private festivals, amusement parks, video games, exhibitions, celebrity stage shows, sports activities etc.

As per the Indian Constitution, entertainment is included in List 2. Revenue collected from entertainment tax is reserved primarily for the state governments.

What is form c & d in sales tax?

Form C

The sales tax on inter-state sale is 4% or the applicable sales tax rate for sale within the State whichever is lower if the sale is to a dealer registered under CST and the goods are covered in the registration certificate of the purchasing dealer. The purchasing dealer is eligible to get these goods at concessional rate if a declaration in C form is submitted to the selling dealer.

Form D

Sale to government is taxable 4% or applicable sales tax rate for sale within the State whichever is lower. This concession on CST is applicable if Form D is issued by the government department which purchases the goods.

What is excise duty?

Central Excise duty is an indirect tax levied on those goods which are manufactured in India and are meant for home consumption. The taxable event is 'manufacture' and the liability of central excise duty arises as soon as the goods are manufactured. It is a tax on manufacturing, which is paid by a manufacturer, who passes its incidence on to the customers.

What do you understand by transfer income?

Transfer of Income means when someone retains the ownership of an asset but makes an agreement to transfer its income, but still the income is considered as your income and it will be added to the total income.

What are the types of Provident funds?

Below listed are the 4 types of provident funds

Recognized Provident Fund (RPF)- RPF schemes must be approved by The Commissioner of Income Tax and applicable to an organization which employs 20 or more employees.

Unrecognized Provident Fund (URPF)- URPF are not approved by The Commissioner of Income Tax and is started by employer and employees in an establishment.

Statutory Provident Fund (SPF)- This Fund is mainly meant for Government/University/Educational Institutes (affiliated to university) employees.

Public Provident Fund (PPF)- PPF involves minimum contribution of Rs.500 per annum and the maximum contribution is Rs. 100,000 per annum. The contribution made along with interest earned is repayable after 15 years, unless extended.

How will you calculate House Rent Allowance (HRA)?

Minimum of following three amounts is available as HRA exemption:

1. Actual House Rent Allowance provided by employer to employee.
2. House Rent paid in excess of 10% of Salary.
3. 50% of Salary in case House is located in Metro cities (Mumbai, Delhi, Kolkata, Chennai) or 40% in case of any other cities.

For all three conditions mentioned above relevant period is very important. Means if there is any change in Salary, HRA paid to employee, location of rented house and actual rent paid by employee HRA need to calculate from that relevant change Hence one should avoid calculating HRA on annual basis if there is any change in above factors.

Meaning of Salary for calculating HRA (Basic Salary + Dearness allowance if terms of employment so provide + fixed percentage of turnover achieved by employee)

What are allowable and dis-allowable expenditure?

Allowable expenditure

1. the cost of goods bought for the business
2. the prime costs of running a business asset
3. wages and salaries of employees
4. heat, light and cleaning of business premises
5. repairs to and maintenance of business premises
6. postage and stationery
7. business telephone and rental
8. bank charges and interest on business loans and overdrafts
9. travel and entertaining if the sole purpose is to retain or acquire business
10. legal costs of defending business rights and renewing leases of less than 50 years duration
11. bad debts and specific doubtful debts
12. protective clothes necessary for the business

Dis allowable expenditure

1. private expenditure
2. clothes bought for ordinary everyday wear
3. acquisition and depreciation of business assets
4. your own wages or salary
5. your business partner's wages or salary
6. payments to charities
7. travel expenses between your home and place of business
8. a general (non-specific) provision against doubtful debts
9. legal costs of acquiring land and buildings

10. fines for breaking the law

11. your own life, accident or sickness assurance

12. costs of alterations, additions or improvements to business premises

What do you understand by dissolution of firm?

Dissolution of firm means assets of firm are realized and liabilities are paid off and the surplus, if any is distributed among the partners according to their right. It is to be noted that 'dissolution of Firm' involves dissolution of partnership but dissolution of partnership may not lead to dissolution of firm.