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Further, in the Elective Papers which are Case Study based, the solutions have been worked out on the basis of certain assumptions/views derived from the facts given in the question or language used in the question. It may be possible to work out the solution to the case studies in a different manner based on the assumption made or view taken.

PAPER 6C: INTERNATIONAL TAXATION

The Question Paper comprises **three** case study questions. The candidates are required to answer any **two** case study questions out of three.

Working Notes should form part of your answer.

Question 1

Sigma Corporation Ltd. (SCL), is a company incorporated under the Companies Act, 2013, having factory and registered office in Mumbai. It is engaged in manufacture, purchase and sale of men's wear, selling various kinds of garment products according to the requirement of the buyers across the world. The company has sold different garment products in the Financial Year 2017-18 to different vendors in the Indian and outside Indian market, including sale of T-shirts to one its associated enterprises, namely, John Miller of UK, to whom it had sold 2,50,000 pieces at the rate of ₹ 1,000 per piece.

Major portion of the income of SCL is from sale of manufactured products. The company (SCL) maintains a gross profit margin of 30% on the selling price. However, it has purchased the T-shirts sold to its UK based associated enterprise John Miller from Mudra Garments Ltd. of Ahmedabad at a price of ₹ 840 per piece.

Following functional differences were noted between the transaction with the UK based customer and other parties:

- (a) Sales to third parties had been made with a specialized packaging for which 3% margin is included in the selling price.*
- (b) Tagging on the product purchased is being required by the other clients for which cost was ₹ 3 per piece, whereas in case of sales made to John Miller of UK, no tagging is to be done.*
- (c) Products sold to third parties involve a credit period of 6 months for which 0.5% per month margin on selling price is ensured by Sigma Corporation Ltd.*

SCL, for the purpose of diversification, is now contemplating to expand its business operations by establishing an affiliate in the Mediterranean. Two countries under consideration of the Board of SCL are Spain and Cyprus. SCL intends to repatriate all after-tax foreign source income from the affiliate to India. In India, the corporate income/may be taken as 30 percent.

At this point, Sigma Corporation Ltd. is not certain whether it would be better to establish the affiliate operation in two countries as a branch operation or a wholly-owned subsidiary of the parent company.

In Cyprus, the marginal corporate tax rate is 20 percent and the foreign branch profits are also taxed at the same rate. In Spain, the corporate income is taxed at 25 percent and additionally, foreign branch income is also taxed at the same rate of 25 percent.

The Suggested Answers for Final Paper 6C: International Taxation, in so far as they relate to questions involving application of the provisions of Indian tax laws, are based on the provisions of direct tax laws as amended by the Finance Act, 2017.

The withholding tax treaty rates with India on dividend income paid from Cyprus is 15 percent and when paid from Spain is 20 percent.

The Chief Financial Officer (CFO) of the company appraised the Board of Directors that the matters of the company pending before the tax authorities are involving several issues for which a show cause notice for A.Y. 2015-16 has been issued by the A.O. The issues of concern as has been raised in this notice in brief are:

- (i) The company has not maintained proper records of the international transactions required under the Income-tax Act, 1961 (Act) and has also defaulted in not obtaining the report of the auditors within the prescribed time.
- (ii) The transactions entered into with the associated enterprises during the previous year for determination of ALP have been referred by the AO to the TPO on 22.12.2017 for the reason of under-reporting.
- (iii) The total international transactions carried out by the company during the previous year were of ₹ 200 crores and why penal action should not be taken against the company for the defaults stated in para-1.

The CFO further informed that the TPO to whom a reference was made by the A.O., had of his own, selected one more, party M/s Sun Apparels for determination of the ALP, which is an un-related person and not an associated enterprise but based at UK and whether it is resident or non-resident is also not known.

SCL is contemplating to file an application for advance ruling with the Authority for Advance Ruling.

The Board of SCL now asked you to help them by advising in determination in the context of taxation provisions contained under the Act, relating to international business as prevailing in India and other countries, as well as the expert opinion on the various issues raised in the show cause notice by the AO as appraised by the CFO.

Required:

- (a) (i) Determine the Arm's Length Price (ALP) of the transactions of sale of T-shirts during the year to the AE John Miller of UK and its probable impact on the income of the company for A.Y.2018-19. **(6 Marks)**
- (ii) Can TPO invoke his powers in relation to an international transaction not referred to him? Is the action taken by the TPO in relation to determination of ALP of the transactions undertaken by the company with M/s Sun Apparels of UK justified? **(4 Marks)**
- (b) (i) Where and in which country should the new affiliate be situated and which organizational structure (i.e. wholly owned subsidiary or branch) is to be selected? **(7 Marks)**

- (ii) Discuss whether the total tax liability in Cyprus or in Spain would be the least for operating a foreign branch or a wholly owned subsidiary of the parent company. **(3 Marks)**
- (c) (i) What will be the consequences for the defaults specified by the Assessing Officer in the show cause notice of not maintaining the records, not obtaining of the report from the auditors and under reporting of ALP of the international transactions? **(5 Marks)**
- (ii) What will be the impact on the time limit for completion of assessment by the AO because of reference so made to the TPO and if the company gets a stay for a period of 30 days over the proceedings, then, what will be the fate of the assessment proceedings? **(5 Marks)**
- (d) Choose the most appropriate option for the following (option to be written in **capital letters** A, B, C or D)
- (1) Two methods were found suitable for determination of the Arm's Length Price (ALP). As per CUP methods, it was found to be ₹ 1,200 per unit and as per resale price method, it was ₹ 1,250 per unit. The ALP per unit will be taken as
- (A) ₹ 1,200 since it is more favourable to the assessee
(B) ₹ 1,250 since it is more favourable to the Department
(C) ₹ 1,225
(D) None of the above
- (2) An assessee having specified domestic transactions covered by section 92BA, should furnish audit report, if the value of such transactions exceeds
- (A) ₹ 2 crores
(B) ₹ 20 crores
(C) ₹ 10 crores
(D) None of the above
- (3) An assessee deriving income from profits of business of an eligible industrial undertaking for which 100% deduction is available u/s 80-1B has entered into international transactions with an associated enterprise for ₹ 200 crores. The TPO has made an addition of ₹ 15 crores in respect of the ALP. The normal GP margin is 10%. The additional deduction u/s 80-1B which can be claimed by the assessee on account of the increase in the ALP is
- (A) Nil
(B) ₹ 20 crores
(C) ₹ 25 crores
(D) ₹ 15 crores

- (4) *The OECD member countries have accepted the concept of Arm's Length Price (ALP) for reaping the following benefit:*
- (A) *Minimises double taxation*
 - (B) *Real taxable profits can be determined*
 - (C) *Artificial price distortion is reduced*
 - (D) *All the three above*
- (5) *In the context of transfer pricing provisions, international transaction should be in the nature of*
- (A) *Purchase, sale or lease of tangible or intangible property*
 - (B) *Provision of service*
 - (C) *Lending or borrowing money*
 - (D) *Any of the above*
- (6) *Mr. Dhanush holds shares in both L Ltd., and M Ltd. In the context of transfer pricing provisions,*
- (A) *L Ltd. and M Ltd. can never be associated enterprises.*
 - (B) *L Ltd. and M Ltd. are deemed associated enterprises if Mr. Dhanush holds 26% or more of voting power in each of these companies.*
 - (C) *L Ltd. and M Ltd. are deemed associated enterprises if Mr. Dhanush holds 26% or more of voting power in L Ltd., which in turn holds 26% or more of voting power in M Ltd.*
 - (D) *L Ltd. and M Ltd. are deemed associated enterprises if Mr. Dhanush holds totally 52% or more combined voting power in both these companies.*
- (7) *The book value of assets of SCL is ₹ 200 crores, whereas the market value of the said assets is ₹ 80 crores. Sun Ltd. has advanced a loan of ₹ 45 crores. In the context of transfer pricing provisions, SCL and Sun Ltd. are*
- (A) *Not associated enterprises*
 - (B) *Associated enterprises, considering the book value of assets of SCL and its borrowings from Sun Ltd.*
 - (C) *Deemed to be associated enterprises, considering the book value of assets of SCL and its borrowings from Sun Ltd.*
 - (D) *Deemed to be associated enterprises considering the market value of assets of SCL and its borrowings from Sun Ltd.*

- (8) *J Ltd. is controlled by Rajeev (HUF). K Ltd. is controlled by Raghav (sole proprietor of RR & Co.), a close relative of Rajeev, a member of Rajeev (HUF). For the purpose of transfer pricing provisions,*
- (A) *J Ltd. and K Ltd. are deemed associated enterprises.*
 - (B) *Rajeev HUF, J Ltd. and K Ltd., are deemed associated enterprises.*
 - (C) *RR & Co., Rajeev HUF, J Ltd. and K Ltd., are deemed associated enterprises.*
 - (D) *There is no associate enterprise relationship involved in this.*
- (9) *There is an arrangement between SCL and Q Ltd., which are associated enterprises. Such arrangement is oral and is also not intended to be legally enforced. For transfer pricing purposes, such arrangement-*
- (A) *is not treated as a "transaction" because it is not in writing.*
 - (B) *is not treated as a "transaction" because it is not intended to be legally enforced.*
 - (C) *is treated as a "transaction".*
 - (D) *is not treated as a "transaction" for (A) and (B) above.*
- (10) *The ALP determined by the TPO for some product is ₹ 2,000 per unit sold by SCL. Considering the tolerance band permitted by the CBDT, the tolerated international transaction price for a transaction with an associated enterprise can be upto*
- (A) *₹ 1,960*
 - (B) *₹ 2,040*
 - (C) *₹ 2,060*
 - (D) *None of the above*
- (11) *Following can be an applicant for advance ruling:*
- (A) *Non-resident entering into a transaction*
 - (B) *Resident entering into a transaction with a non-resident*
 - (C) *Resident entering into a transaction with another resident*
 - (D) *(A) or (B)*
- (12) *An applicant for advance ruling may withdraw an application within days from the date of the application.*
- (A) *30*
 - (B) *60*
 - (C) *90*
 - (D) *120*

- (13) Composition of AAR is as under:
- (A) A Chairman, Vice-Chairman and Revenue Member
 - (B) A Chairman, Vice-Chairman and Law Member
 - (C) A Chairman and such number of Vice-Chairman, Revenue Members and Law Members as the Central Government may, by notification, appoint.
 - (D) Chairman, Vice-Chairman, Law Member and Revenue Member
- (14) Following can make an application for advance ruling:
- (A) Department
 - (B) Applicant
 - (C) Central Government
 - (D) All above
- (15) Application for advance ruling is not allowed in the following situations:
- (A) When the question involved is already pending before any income-tax authority.
 - (B) Where it is for determining the fair market value of a property.
 - (C) Excepting in exceptions, where the transaction in question is designed for avoidance of tax.
 - (D) Any one of the above **(1 x 15 = 15 Marks)**
- (e) Fill up blanks :
- (i) The applicant desiring roll back of the APA may furnish the request for rollback provision in Form No. 3CEDA with proof of payment of an additional fee of _____.
 - (ii) The transfer pricing provisions contained in Section 92 shall not apply if the same has the effect of _____ chargeable to tax.
 - (iii) If there is an arrangement between SCL and TFL (an associate enterprise) for mark up of a semi-finished product and sale thereafter, the ideal method for determining the ALP is _____ method.
 - (iv) In a case where the aggregate value of international transactions exceeds ₹ _____, it will be obligatory for the assessee to maintain the stipulated information and documents required for transfer pricing purposes.
 - (v) Where SCL has maintained proper records and documents, and the TPO has made some adjustments to the ALP, thereby increasing the total income by, say, ₹ 2.68 crores, the penalty leviable u/s 270A will be ₹ _____. **(1 x 5 = 5 Marks)**

Answer

- (a) (i) Sigma Corporation Ltd. (SCL) maintains a gross profit margin of 30% on the selling price. It purchased T-shirts from an unrelated enterprise which are sold to its UK

based AE at a price of ₹ 840 per piece. Under comparable uncontrolled transactions, the sale price of T-shirts would be ₹ 1,200 [₹ 840/(100-30)].

Such sale price has to be adjusted by taking into consideration the functional differences existing between the transactions with the Associated enterprise and other unrelated parties. Accordingly, the arm's length price has to be computed in the following manner:

Computation of Arm's Length Price

Particulars	₹	₹
Sale price of T-shirt	1,200	
Less: Differences to be adjusted		
- Margin on specialized packaging (1,200 x 3%)	36	
- Margin for providing 6 months' credit facility [₹1200 x (0.5% x 6 months)]	36	
- Cost of tagging of ₹ 3 per piece	3	
Adjusted sale price per T-shirt	<u>1,125</u>	
Arm's Length value of the sale transaction (₹ 1,125 x 2,50,000)		28,12,50,000
Less: Transaction value of sales to AE (₹ 1,000 x 2,50,000)		<u>25,00,00,000</u>
Total Income of SCL Ltd to be increased by		<u>3,12,50,000</u>

- (ii) Yes; The TPO can generally do so in respect of international transactions.

As per section 92CA(2A), the Transfer Pricing Officer (TPO) can also determine the ALP of other international transactions not referred to him and identified subsequently in the course of proceedings before him.

As per section 92CA(2B), where in respect of an international transaction, the assessee has not furnished the report under section 92E and such transaction comes to the notice of the TPO during the course of proceeding before him, the transfer pricing provisions shall apply as if such transaction is referred to the TPO by the Assessing Officer under section 92CA(1).

As per section 92B, "International transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of, *inter alia*, purchase, sale or lease of tangible or intangible property.

The transaction entered into by the company, SCL, with M/s Sun Apparels of UK, is not an international transaction, since it is with an un-related person, not being an associated entity.

Therefore, the action taken by the TPO in relation to determination of ALP of the transactions undertaken by the company with M/s Sun Apparels of UK is **not** justified.

(b) (i)

Particulars	Cyprus		Spain	
	Branch	Subsidiary	Branch	Subsidiary
Tax rate in the foreign country	20%	20%	25%	25%
Tax on profit repatriations/withholding tax on dividend	-	15% of 80% = 12%	-	20% of 75% = 15%
Total tax paid in the foreign country	20%	32%	25%	40%
Tax payable in India	30%	12%	30%	15% of 75% = 11.25%
Situation 1 : Assuming that Foreign Tax Credit is available in respect of branch profit tax				
Particulars	Cyprus		Spain	
	Branch	Subsidiary	Branch	Subsidiary
Foreign Tax Credit	20%, if such credit is available in respect of branch profit tax (assuming that full credit is available in respect of branch profit tax)	12%	25%, if such credit is available in respect of branch profit tax (assuming that full credit is available in respect of branch profit tax)	11.25%
Net tax payable	30%	32%	30%	40%
In Situation 1, where FTC is available in respect of the entire branch profit tax, it would be advisable to establish a branch in the place of subsidiary. The branch can be established either in Cyprus or in Spain .				
Situation 2 : Assuming that Foreign Tax Credit is not available in respect of branch profit tax				
Foreign Tax Credit	0%, assuming such credit is not available in respect of branch profit tax	12%	0%, assuming such credit is not available in respect of branch profit tax	11.25%

Net tax payable	50%	32%	55%	40%
In Situation 2, where FTC is not available in respect of branch profit tax, it would be advisable to establish a subsidiary in Cyprus				

Note - The answer to this question may be based on either of the situations given above or on the basis of the following other factors, which also need to be considered for selecting the new affiliate as branch and subsidiary:

Particulars	Branch	Subsidiary
Separate Legal Entity	It is not a separate legal entity; the parent company would be liable to tax in respect of profits attributable to the branch, which is a permanent establishment.	A subsidiary is a separate legal entity from the parent, although owned by the parent corporation. A subsidiary qualifies as a "resident" for treaty benefits in the other Contracting State. Its profits are independently taxed in its hands
Taxability of profits repatriated	The profits repatriated by the branch to the head office do not suffer double taxation.	The profits from which the dividend is distributed may be subject to double taxation. In the country in which the subsidiary company is incorporated, corporate income-tax is leviable in respect of its profits. The profits distributed would be subject to tax on dividends in the hands of the holding company in India.
Set-off of loss incurred	The losses from branch can be offset against the profits of the company.	The losses of the subsidiary are not eligible for setoff against the profits of the parent company.
Compliance cost	Relatively lower compliance cost.	Greater compliances to be met.

(ii) Total tax liability

In Situation 1, where FTC is available in respect of the entire branch profit tax, it would be advisable to establish a branch in the place of subsidiary.

The branch can be established either in Cyprus or in Spain. The tax liability would be 30% (plus applicable surcharge and cess)

Hence, from the tax incidence point of view, the tax liability will remain the same. Choice of the country has to be determined based on other factors.

Where alternative view has been taken for Qn. 1(b)(i)

In Situation 2, where FTC is not available in respect of the entire branch profit tax, it would be advisable to establish a subsidiary in Cyprus.

The tax liability would be 32% (plus applicable surcharge and cess)

(c) (i) Consequences for the defaults specified by the AO in the show cause notice

(i)	<p>Not maintaining the records</p> <p>Section 271AA provides that the Assessing Officer or Commissioner (Appeals) may direct SCL, i.e., the person entering into an international transaction in this case, to pay penalty@2% of the value of the international transaction entered into by it, if SCL fails to keep and maintain any such document and information as required by section 92D(1) and section 92D(2).</p> <p>No penalty will be leviable under this section, if SCL can show that there was reasonable cause for the failure.</p>
(ii)	<p>Not obtaining the report from the auditors</p> <p>As per section 271BA, if SCL fails to furnish a report from an accountant as required by section 92E, the Assessing Officer may direct SCL to pay, by way of penalty, a sum of ₹ 1 lakh.</p> <p>No penalty will be leviable under this section, if SCL can show that there was reasonable cause for the failure.</p>
(iii)	<p>Under reporting of ALP of the international transaction</p> <p>Under section 270A, penalty@50% of tax payable on under-reported income is leviable. In this case, SCL has not maintained proper records of international transaction, the under-reported income will not be excluded for levy of penalty.</p>

- (ii) Where a reference is made to the TPO under section 92CA(1) during the course of proceeding for assessment or reassessment, an additional time period of 12 months is available for completion of assessment/ reassessment in such cases over and above the time limit of 21 months. Thus, the revised time limit in respect of A.Y. 2017-18 or earlier assessment years shall be 33 months from the end of the assessment year in which the income was first assessable.

In computing the above period of limitation, the period during which the assessment proceeding is stayed by an order or injunction of any court, shall be excluded.

Section 92CA(3A) provides that where reference is made to the Transfer Pricing Officer for determination of arm's length price of international transactions, the Transfer Pricing Officer shall make an order at least 60 days before the expiry of the above time limit of 33 months for making an order of assessment by the Assessing Officer.

Where assessment proceedings are stayed by any court and the time available to the Transfer Pricing Officer for making an order is less than 60 days, then, such remaining period shall be extended to 60 days.

Accordingly, for the A.Y. 2015-16 (in the present case) the Assessing Officer has to complete the assessment proceedings by 30.1.2019, within 33 months (plus the stay period of 30 days) from the end of assessment year i.e., 31.3.2016.

The TPO is required to make the order for determination of Arm's Length Price 60 days prior to 30.1.2019 i.e., by 1.12.2018.

- (d) (1) D
(2) B
(3) A
(4) D
(5) D
(6) B
(7) A
(8) A
(9) C
(10) D
(11) D
(12) A
(13) C
(14) B
(15) D
- (e) (i) ₹ 5 lakh
(ii) Reducing the income
(iii) Profit split
(iv) ₹ 1 crore/₹ 99,99,999
(v) Nil

Question 2

About the company

Rup Ram Limited (RRL), is a domestic company, with its head office located at Mumbai. The company has several divisions dealing in manufacture, purchase and sale of several products.

RRL possesses the following assets as on 31-3-2018, whose book values are as under:

Type of asset	(₹ in crores)
Intangible assets	20
Land and Building	250
Plant and Machinery	140
Vehicles	25

The market value of these assets as on 31-3-2018 is ₹ 750 crores.

Information from Manager, HR

Manager, Human Resources (HR) Division informs you that as on 31-3-2018, there were 340 employees, in the rolls of RRL, resulting in wages/salary payments to the tune of ₹ 11.2 crores.

Subsidiary's presence in India

RRL has a foreign subsidiary Snow White & Co. Inc. (SWC), incorporated in Singapore.

The subsidiary has assets present in India. It has 40 godowns in India, whose market value as on 31-3-2018 is ₹ 40 crores, the book value being ₹ 25 crores, split into ₹ 10 crores for land component and balance for building portion. WDV as on 31-3-2018 for income-tax purposes is ₹ 13.2 crores.

Other fixed assets (all purchased on 14-6-2017) are to the tune of ₹ 10 crores (WDV for the purposes of the Income-tax Act, 1961 (Act) ₹ 8.6 crores). Besides these, there is no other asset in India.

At the beginning of the year, SWC had 22 godowns in India, whose market value was ₹ 15 crores, the book value being ₹ 10 crores, split into ₹ 7 crores for land component and balance for building portion. WDV for the Act purposes is ₹ 6.7 crores.

Assets position of SWC outside India

	As on 1-4-2017	As on 31-3-2018
No. of godowns owned	10	11
	(All values in ₹ Crores)	
Godowns : Land portion (Book value)	8	12
(Market value)	20	25
Godowns : Building part (Book value)	5	12
(Market value)	4.5	11
Godowns : Building part (WDV for taxation)	4.2	10.2

Other assets:	(Book value)	12	20
	(Market value)	14	22
	(WDV for taxation)	4.2	10.2

Employees strength of SWC

There are 30 persons employed in India, for whom annual payment of ₹ 1.2 crores is incurred by SWC. There are 10 other persons, who, though not directly employed by SWC, perform the work like other employees. Outlay to them is ₹ 34 lakhs. All these employees are residents in India,

SWC employs 42 employees outside India, for whom the total payroll expenditure involved is ₹ 3 crores (converted into INR)

Income pattern from Indian operations of SWC

The income earned by SWC during the year ended 31-3-2018 from its Indian operations as well as other operations is as under:

Type of Income	₹ in crores)	
	In India	Outside India
From sale made to RRL	42	-
From purchases made from RRL and sold to third parties	10	15
Income from other trading operations with third parties	5	70
Dividends and interest	8	5

Technical know how

RRL has entered into a complicated technical know-how agreement with Jew Inc., of Israel. The tax rate applicable and the amount taxable are posing to be ticklish. The annual payment of the technical know-how is likely to be around ₹ 150 crores. Jew Inc., has entered into identical agreements with three other Indian companies.

Sponsorship activities

RRL utilized the services of Graham Stokes, a British cricketer for playing in an important cricket league matches for a team sponsored by the company. He was paid a sum of ₹ 25 lakhs for playing in such matches. In addition, RRL paid him a sum of ₹ 6.76 lakhs for appearing in company's advertisement for its product. Graham Stokes has incurred an expenditure of ₹ 1.2 lakhs in India for earning the said income.

Brian Thorpe, an ex-cricketer hailing from London, was used as a match referee in the said cricket tournaments. He was paid a sum of ₹ 5 lakhs for his services.

Required:

- (a) Find the most suitable alternative to the following (option to be given in **capital letters A, B, C or D**)

- (i) *The person responsible for making payment of income by way of interest or dividends in respect of bonds or Global Depository Receipts referred to in section 115AC, shall deduct tax at the rate of*
- (A) 10%
 - (B) 10.3%
 - (C) 20%
 - (D) (B) or at the rate specified in the DTAA, whichever is lower.
- (ii) *The rate of deduction of tax from interest payable to a foreign company (located in a country with which there is no DTAA) by an Indian company on borrowings made on 12-6-2017 in foreign currency from sources outside India is*
- (A) 5.15%
 - (B) 10.3%
 - (C) 15.45%
 - (D) None of the above
- (iii) *Surcharge applicable to a foreign company whose total income is ₹ 1.2 crores is*
- (A) Nil
 - (B) 2%
 - (C) 7%
 - (D) 10%
- (iv) *Following income which is accruing or arising outside India, directly or indirectly, is not deemed to be income accruing or arising in India:*
- (A) *Through or from any business connection in India.*
 - (B) *Through or from any property in India.*
 - (C) *Through transfer of capital asset located outside India.*
 - (D) *Through or from any asset or sources of income in India.*
- (v) *Remuneration received for services rendered in India by a foreign national employed by foreign enterprise is exempt, if the number of days stay in India of such foreign national does not exceed*
- (A) 60 days
 - (B) 90 days
 - (B) 30 days
 - (D) None of the above

- (vi) A resident in relation to his tax liability arising out of one or more transactions valuing ₹ _____ in total which has been undertaken or is proposed to be undertaken would be eligible to be an applicant for advance ruling:
- (A) 60 crore or more
 - (B) 80 crore or more
 - (C) 100 crore or more
 - (D) 200 crore or more
- (vii) An applicant, who has sought for an advance ruling, may withdraw the application within _____.
- (A) 30 days from the date of the application
 - (B) 30 days from the end of the month in which the application has been made
 - (C) 60 days from the date of the application.
 - (D) 60 days from the end of the month in which the application has been made
- (viii) In case of a non-notified resident, the AAR will not allow an application in respect of certain matters. The following is not covered in the hit list:
- (A) Matter pending with income-tax authorities/tribunal/court.
 - (B) Determination of fair market value of a property.
 - (C) Relates to a transaction or issue which is designed prima facie for avoidance of income-tax.
 - (D) Whether an arrangement, which is proposed to be undertaken by any person being a resident or a non-resident, is an impermissible avoidance arrangement as referred to in Chapter X-A or not.
- (ix) The advance ruling given by the Authority for Advance Ruling (AAR) is not binding on the following person(s) :
- (A) On the applicant who sought the ruling.
 - (B) On the other person to the transaction entered into by the applicant, if it is a non-resident.
 - (C) On the other person to the transaction entered into by the applicant, whether it is resident or non-resident.
 - (D) On the Principal Commissioner or Commissioner and the income-tax authorities subordinate to the Principal Commissioner or Commissioner who has jurisdiction over the application.
- (x) Following income from 'Salaries' which is payable by _____ would be deemed to accrue or arise in India:
- (A) The Government to a citizen of India for services rendered outside India.

- (B) *The Government to a non-resident for services rendered outside India.*
- (C) *The Government to a non-citizen or non-resident for services rendered outside India.*
- (D) *The Government or any other person to a non-citizen or non-resident for services rendered outside India.* **(1 x 10 = 10 Marks)**

(b) State **with reasons**, whether the following statements are true or false:

- (i) *When interest payable to a non-resident by the Government or a public sector bank within the meaning of section 10(23D), deduction of tax shall be made at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, or at the time of credit of such interest to the account of the non-resident, whichever is earlier.* **(2 Marks)**
- (ii) *Where payment is made to a non-resident, even if such non-resident falls within the specified class notified by the CBDT, even if the payment is not chargeable to tax in India, the payer has to make an application to the Assessing Officer, before making the impugned payment.* **(5 Marks)**
- (iii) *Where any interest is payable by a person resident in India, the same is deemed to accrue or arise in India* **(3 Marks)**

(c) *Graham Stokes and Brian Thorpe wish to avail the special provisions applicable to non-residents. The Managing Director of RRL wants to know about the obligation to deduct tax at source from the payments made to the aforesaid two persons.*

If in both the situations above, there is an agreement between RRL and the two British persons that the tax payable on such income in India will be borne by RRL, then, what is the amount of tax to be deducted at source?

Assume that there is no DTAA provision, conferring a lower rate of withholding tax.

(7 Marks)

(d) *Jew Inc. has a sister concern, Silver LLC., which has obtained advance ruling on an identical technical know-how agreement with another Indian company. Can RRL make use of this ruling for its assessment proceeding? What course of action will you advise?*

(4 Marks)

(e) *RRL has made an application to the Assessing Officer for determination of the tax rate applicable for the technical know-how payment to be made to Jew Inc. When this is pending, Jew Inc., has filed an application before the AAR. Can the AAR reject the application on the ground that similar issue is pending before the Assessing Officer?*

(6 Marks)

- (f) *The Board of Directors wish to know whether the foreign subsidiary SWC will be regarded as a company engaged in active business outside India for POEM purposes. Advise them suitably. The Board is also looking for your suggestions in this regard. (13 Marks)*

Answer

- (a) (i) D
(ii) A
(iii) B
(iv) C
(v) B
(vi) C
(vii) A
(viii) D
(ix) C
(x) A

- (b) (i) **The statement is false.**

As per the proviso to section 195(1), in the case of interest payable by the Government or a public sector bank within the meaning of section 10(23D), deduction of tax shall be made **only at the time of payment thereof** in cash or by the issue of a cheque or draft or by any other mode.

- (ii) **The statement is true/partly true.**

Under section 195(2), where the person responsible for paying any such sum chargeable to tax under the Act (other than salary) to a non-resident, considers that the whole of such sum would not be income chargeable in the hands of the recipient, he **may** make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of such sum so chargeable. When the Assessing Officer so determines the appropriate proportion, tax shall be deducted under section 195(1) only on that proportion of the sum which is so chargeable.

Section 195(7) provides that, notwithstanding anything contained in sections 195(1) and 195(2), the CBDT may, by notification in the Official Gazette, specify a class of persons or cases, where the person responsible for paying to a non-corporate non-resident or to a foreign company, any sum, whether or not chargeable under the provisions of this Act, shall make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of sum chargeable to tax. Where the Assessing Officer determines the appropriate proportion of the sum chargeable, tax shall be deducted under section 195(1) on that proportion of the sum which is so chargeable.

Consequently, where the CBDT specifies a class of persons or cases, the person responsible for making payment to a non-corporate non-resident or a foreign company in such cases has to mandatorily make an application to the Assessing Officer, whether or not such payment is chargeable under the provisions of the Act.

In other cases, the person responsible for making payment, if he considers that the whole of such sum would not be income chargeable to tax in the hands of the recipient, may make an application to the Assessing Officer.

(iii) The statement is true/partly true.

As per section 9(1)(v)(b), income by way of interest payable by a resident is deemed to accrue arise in India.

However, if interest is payable in respect of any debt incurred or money borrowed and used, for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India, such interest would not be deemed to accrue or arise in India.

- (c) (i)** As per section 115BBA, ₹ 25 lakhs earned by Graham Stokes, a non-resident sports person, who is not a citizen of India, from participation in cricket matches and ₹ 6.76 lakhs from advertisement i.e., ₹ 31.76 lakhs earned by him totally is chargeable to tax@20.6%.

No deduction is allowable in respect of any expenditure to earn such income.

Section 194E requires tax deduction at source @20.6% from such income paid to a non-resident sportsperson.

$$\text{TDS} = ₹ 31.76 \text{ lakhs} \times 20.6\% = ₹ 6,54,256$$

Section 195A provides that if such tax is to be borne by the person by whom the income is payable, RRL, in this case, then the net amount of ₹ 31.76 lakhs payable has to be grossed up in the following manner:

$$₹ 31.76 \text{ lakhs} \times 100/79.4 \text{ (i.e., } 100 - 20.6) = ₹ 40 \text{ lakhs}$$

$$\text{TDS} = ₹ 40 \text{ lakhs} \times 20.6\% = ₹ 8,24,000$$

- (ii)** A match referee is, however, not a sportsperson. Therefore, he is not entitled to the benefit of section 115BBA. The rate at which the sum of ₹ 5 lakhs received by him would be taxable at normal rates.

Tax would be deductible under section 195 at the rates in force, i.e., 30.9%.

$$\text{TDS} = ₹ 5,00,000 \times 30.9\% = ₹ 1,54,500$$

Applying the grossing up provisions under section 195A,

$$₹ 5 \text{ lakhs} \times 100/69.1 \text{ (i.e., } 100 - 30.9) = ₹ 7,23,589$$

$$\text{TDS} = ₹ 7,23,589 \times 30.9\% = ₹ 2,23,589$$

- (d) As per section 245S(1), the advance ruling pronounced under section 245R by the Authority for Advance Rulings shall be binding only on the applicant who had sought it and in respect of the transaction in relation to which advance ruling was sought. It shall also be binding on the Principal Commissioner/Commissioner and the income-tax authorities subordinate to him, in respect of the concerned applicant and the specific transaction.

In view of the above provision, RRL cannot use the advance ruling, obtained on an identical issue by Silver LLC, a sister concern of Jew Inc., in its assessment proceedings.

Hence, the best course would be to file a fresh application for advance ruling in respect of this agreement between RRL and Jew Inc.

Note - *The Madras High Court, in CIT v. P. Sekar Trust (2010) 321 ITR 305, observed that though the advance ruling pronounced does not become a precedent, it has persuasive value where the facts warrant such reference to the rulings of AAR. There is no legitimate bar for relying on the reasoning in an advance ruling.*

Accordingly, there is no legitimate bar in RRL relying on advance rulings obtained on an identical issue by Silver LLC in its assessment proceedings.

Therefore, based on the Madras High Court ruling, RRL may be advised to use the advance ruling pronounced in Silver LLC's case in its assessment proceedings.

- (e) This issue came up before the AAR in, *Nuclear Power Corporation of India Ltd. In Re, [2012] 343 ITR 220*, wherein it was held that an advance ruling is not only applicant specific, but is also transaction specific. The advance ruling is on a transaction entered into or undertaken by the applicant. That is why section 245S specifies that a ruling is binding on the applicant, **the transaction** and the Principal Commissioner or Commissioner of Income-tax and those subordinate to him, and not only on the applicant.

What is barred by the first proviso to section 245R(2) of the Act in the context of clause (i) thereof is the allowing of an application under section 245R(2) of the Act where "the question raised in the application is already pending before any Income-tax authority, or Appellate Tribunal or any court". The significance of the dropping of the words, "in the applicant's case" with effect from June 1, 2000, cannot be wholly ignored.

On the basis of this view expressed by the AAR in the above case, explaining the impact of the dropping of the words "in the applicant's case" with effect from 1.6.2000, a view can be taken that the AAR can reject the application made by Jew Inc before the AAR on the ground that similar issue is pending before the Assessing Officer in respect of the same transaction i.e., provision of technical know to RRL.

Note – *The issue relates to the admission or rejection of the application filed before the Advance Rulings Authority on the grounds specified in clause (i) of the first proviso to sub-section (2) of section 245R of the Income-tax Act, 1961.*

The first proviso to section 245R(2) has been substituted by the Finance Act, 2000 with effect from 1.6.2000. Clause (i) of the first proviso, prior to and post amendment, reads as follows:

Prior to 1.6.2000	On or After 1.6.2000
<p>Provided that the Authority shall not allow the application <u>except in the case of a resident applicant</u> where the question raised in the application is already pending <u>in the applicant's case</u> before any income-tax authority, the Appellate Tribunal or any court;</p>	<p>Provided that the Authority shall not allow the application where the question raised in the application is already pending before any income-tax authority or Appellate Tribunal or any court.</p>

The words “except in the case of a resident applicant” and “in the applicant’s case” has been removed in clause (i) of the first proviso with effect from 1.6.2000. However, the Explanatory Memorandum to the Finance Act, 2000, explaining the impact of the substitution, reads as follows “It is proposed to substitute the proviso to provide that the Authority shall not allow the application when the question raised is already pending in the applicant’s case before any income-tax authority, Appellate Tribunal or any court in regard to a non-resident applicant and resident applicant in relation to a transaction with a non-resident”. Therefore, according to the intent expressed in the Explanatory Memorandum, the AAR shall not allow the application both in the case of resident and non-resident applicant if the question raised is already **pending in the applicant’s case** before any income-tax authority. Thus, as per the Explanatory Memorandum, it is possible to take a view that even post-amendment, the Authority shall not allow the application where a question is **pending in the applicant’s case** before any income-tax authority. Thus, an alternative view is possible on the basis of the AAR ruling in Ericsson Telephone Corporation India AB v. CIT (1997) 224 ITR 203, which continues to hold good even after the amendment, if we consider the intent expressed in the Explanatory Memorandum. **Accordingly, based on this view, the AAR can allow the application made by Jew Inc., even if the question raised in the application is pending before the Assessing Officer in RRL’s case.**

(f)

<p>A company shall be said to be engaged in “active business outside India” for POEM, if</p> <ul style="list-style-type: none"> ➤ the passive income is not more than 50% of its total income; and ➤ less than 50% of its total assets are situated in India; and ➤ less than 50% of total number of employees are situated in India or are resident in India; and ➤ the payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.
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Snow White & Co. Inc (SWC) shall be regarded as a company engaged in active business outside India for POEM purpose only if it satisfies all the four conditions cumulatively.	
Condition 1: Passive income test	
The passive income of SWC should not be more than 50% of its total income	
Passive Income	Rs. in crores
From sales made by SWC to RRL [See Note below]	-
From purchases made from RRL and sold to third parties	-
Dividend and Interest	<u>13</u>
Total passive global income	<u>13</u>
Total income of SWC	155
Percentage of passive income earned	8.4%
<p>Total income of SWC during the P.Y. 2017-18 is ₹ 155 crores, being ₹ 65 crores in India [₹ 42 crores + ₹ 10 crores + ₹ 5 crores + ₹ 8 crores] and ₹ 90 crores outside India [₹ 15 crores + ₹ 70 crores + ₹ 5 crores]</p> <p>Since passive income of SWC i.e., 8.387% is less than 50% of its total income, the first condition (Passive income test) is satisfied.</p>	
<p>Note - <i>Passive income, inter alia, includes income from the transactions where both the purchase and sale of goods is from/to its associated enterprises. In the facts of the case study, income of ₹ 42 crores earned from sales made to RRL is given, but whether these sales are made out of purchases from associated enterprises or out of third party purchases is not given in the question. This income of ₹ 42 crores is not included in the passive income assuming that the purchases have not been made from associated enterprises. However, if it is assumed that the sales are made out of the purchases made from associated enterprises ₹ 42 crores has to be included in computing passive income. In such a case, passive income and the percentage of passive income to total income would be ₹ 55 crores and 35.48%, respectively.</i></p> <p><i>Even in this case, since passive income of SWC is only 35.48% of total income (i.e., less than 50% of total income), the first condition is satisfied.</i></p>	
Condition 2: Assets Test	
SWC should have less than 50% of its total assets situated in India	
Value of assets is determined in the following manner:	
In case of pool of fixed asset, being treated as a block for depreciation	The average of its value for tax purposes in the country of incorporation of the company at the beginning and at end of the year;
In case of any other asset	Value as per books of account

Value of assets of SWC:		
Particulars	In India (₹ in crores)	Outside India (₹ in crores)
Godowns (building portion only), being depreciable asset, at average of its WDV as on 31.3.2017 and as on 31.3.2018	$\frac{6.7 + 13.2}{2} = 9.95$	$\frac{4.2 + 10.2}{2} = 7.20$
Other fixed assets, being depreciable assets, at average of its WDV as on 31.3.2017 and as on 31.3.2018	$\frac{0 + 8.6}{2} = 4.30$	$\frac{4.2 + 10.2}{2} = 7.20$
Land [Value as per books of account on 31.3.2018]	10.00	12.00
Total	24.25	26.40
Percentage of assets situated in India to total assets = ₹ 24.25 crores/₹ 50.65 crores x 100 = 47.88%		
Since the value of assets of SWC situated in India is less than 50% of its total assets, the second condition (Assets test) is also satisfied.		
Condition 3: Number of employees test		
Less than 50% of the total number of employees of SWC should be situated in India or should be resident in India		
SWC employed 30 persons in India and 10 other persons, who are resident in India but not directly employed by SWC though they perform work like any other employee.		
For counting the number of employees in India, the average of the number of employees as at the beginning and at the end of the year has to be considered and it would include persons, who, though not employed directly by the company, perform tasks similar to those performed by the employees.		
Therefore, number of employees situated in India or are resident in India is 40 i.e., 30+10¹		
Total number of employees of SWC is 82, being 42 employed outside India and 40 in India or resident in India.		
Percentage of employees situated in India or are resident in India to total number of employees is $40/82 \times 100 = 48.78\%$		

¹ It is assumed that the number of employees are same throughout the year, in the absence of information to the contrary in the question.

Since employees situated in India or are residents in India of SWC are less than 50% of its total employees, **the third condition (Number of employees test) is satisfied** for active business outside India test.

Condition 4: Payroll expenses Test

The payroll expenses incurred on employees situated in India or residents in India should be less than 50% of its total payroll expenditure

Payroll expenditure on employees situated in India or are residents in India is ₹ **1.54 crores** i.e., ₹ 1.20 crores **plus** ₹ 0.34 crores

Total payroll expenditure of SWC is ₹ **4.54 crores** being expenditure on employees situated in India or are residents in India and expenditure on employees outside India [i.e., ₹ 1.54 crores + ₹ 3 crores].

Percentage of payroll expenditure on employees situated in India or are resident in India to total payroll expenditure is ₹ 1.54 crores/₹ 4.54 crores x 100 = **33.92%**

Since payroll expenditure on employees situated in India or are residents in India of SWC is less than 50% of its total payroll expenditure, **the fourth condition (Payroll expenses test) is also satisfied.**

Conclusion:

Since SWC satisfies all the above four conditions cumulatively, SWC will be **regarded as a company engaged in active business outside India**

Suggestions to the Board of Directors

The following suggestions may be offered to the Board of Directors:

- (a) Income from transactions with associated enterprises like RRL should be scrupulously and constantly monitored, so that the conditions above continue to be satisfied in future years;
- (b) Steps may be taken to improve trade with unrelated third parties;
- (c) Percentage of Indian assets to total assets is almost 48%. If there is any plan to acquire assets in India, it must be ensured that this does not cross 50%
- (d) Percentage of employees situated in India or are resident in India to the total number of employees is 48.78%. In case of any future employment, this ratio has to be borne in mind.

Question 3

About the assessee

The assessee is a famous movie actor Mr. Ajitabh Khan (AK). He has business interest in few other nations as well. He is a resident in India for the Assessment Year 2018-19.

About yourself

You are the CEO with CA background. You have sound knowledge of the Indian and Foreign tax laws. The date on which various events happened and have been summarized in this case study is 31-3-2018.

Phone call from Manager (Legal) 09.40 hours

A phone call has been received from the Manager (Legal) that a search is being conducted by the Income-tax department at one of the premises of the assessee. No further details are available now.

E-mail from Taxation Manager at 18.00 hours

The Taxation Manager has emailed you the summarized information of income earned by AK during the year ended 31-3-2018 as under: (₹ in crores)

Income from house property (Computed)	4.3
Business income:	
From being the owner of cricket team in Asian Premier League	12.4
Acting in movies	9.415

AK has paid PPF of ₹ 1.2 lakhs and Life Insurance Premium of ₹ 2 lakhs.

Phone call from Manager (Legal) 20.30 hours

The search conducted by the IT Department has come to an end. It appears that some incriminating documents have been unearthed. It is likely that it has come to the notice of the Department that the assessee has earned income of ₹ 12 crores (as converted into INR) in Dubai during the Financial Year 2015-16, which has not been reflected in the return of income filed by AK for the Assessment Year 2016-17 or in any other year.

Further, the presence of certain building, in Panama Islands, which are not appearing in the books of account and financial statements filed with the IT Department. These buildings were purchased for 35.2 million USD on 12-3-2014. For acquiring this asset, brokerage of 2% has been paid to a real estate agent.

Additionally, there are materials to show that the assessee owns 5 rare pieces of art work, acquired on 12-6-2016 in Macau Islands for a price of 3.8 million USD.

E-mail from International Division Manager at 21.00 hours

The International Division Manager has intimated details of income earned from two countries outside India, L and M, with which India does not have any Double Taxation Avoidance Agreement. The summarized data are as under: (₹ in crores)

Type of Income	L	M
Loss from house property (Computed)	1.3	-
Business income:		
Own	7.2	2.9
Share income from partnership firm	4.8	-
Agricultural income	-	1.2

In country L, share income is not exempt and loss from house property is not eligible for being set off against other income. In country M, agricultural income is also chargeable to income-tax.

In country L, AK has paid income-tax of ₹ 2.16 crores and in country M ₹ 80 lakhs on the total income earned there.

Inputs from Forex Team (Email received at 21.15 hours)

The prevailing rates of exchange on various dates are as under:

Date	1-4-2013	12-3-2014	1-7-2015	31-3-2016	1-4-2016	1-6-2016	1-4-2017
1 USD = INR	64.05	64.50	65.10	64.75	65.20	65.40	65.55

Email from Xavier LLP (Registered valuers) at 23.45 hours

The fair market value of the assets acquired abroad were indicated by the registered valuers on various dates are thus:

Sl. No.	Description of Asset	Date	Amount (million USD)
1	Buildings in Panama Island	01-07-2015	38
		31-03-2016	38
		01-04-2017	40
2	Art pieces in Macau	12-06-2016	4
		01-04-2017	4.2

Payment made to foreign player

Mr. Ajmal Kamal, a non-resident player, was called for one of the Asian Premier League Matches, for which ₹ 20 lakhs was paid to him. The withholding tax mentioned in the DTAA with the nation in which the said actor resides, is 15%.

Required:

(a) Find the most suitable alternative for the following (Option to be given in **capital letters A, B, C or D**):

- (i) A shopping complex was purchased by the assessee in Colombo for ₹ 5 crores on 12-3-2015. Out of this, investment of ₹ 3 crores is from disclosed sources, which had been offered for tax. This asset comes to the knowledge of the Assessing Officer on 27-12-2017. If the fair market of the house as on the relevant date to be adopted is ₹ 8 crores, the undisclosed foreign income under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 (BM Act) will be taken as (₹ crores)

(A) 5

- (B) 3.2
(C) 3.8
(D) None of the above
- (ii) Under the BM Act, the rate of exchange to be adopted for conversion purposes will be the rate specified by
(A) RBI
(B) SBI
(C) Central Government
(D) CBDT
- (iii) The Assessing Officer has detected undisclosed foreign income of ₹3 crores earned during the year ended 31-3-2017. There is foreign loss of ₹1.2 crores also, hitherto not shown in the income-tax return filed for the Assessment Year 2017-18. The quantum of undisclosed foreign income assessed under the BM Act will be
(A) ₹1.8 crores
(B) ₹1.2 crores
(C) ₹3 crores
(D) None of the above
- (iv) Unquoted shares acquired in Tokyo on 21-3-2016 came to the notice of the Assessing Officer on 12-3-2018. There is no explanation of the source for the same. The converted value of the shares on 21-3-2016, 1-4-2016, 1-4-2017 and 1-4-2018 are ₹12, 13, 14 and 15 crores, respectively. The undisclosed foreign income representing the value of the undisclosed foreign asset, as per the BM Act is
(A) ₹12 crores
(B) ₹13 crores
(C) ₹14 crores
(D) ₹15 crores
- (v) Under the BM Act, a tax authority below the rank of Commissioner can retain the impounded books normally for a period of
(A) 120 days
(B) 90 days
(C) 60 days
(D) 30 days

- (vi) In a typical Tax Convention based on OECD model or UN model, the definition of the term "national" is primarily relevant to the Article dealing with _____.
- (A) Persons covered / General scope
 - (B) Non-discrimination
 - (C) Resident
 - (D) Credit Method
- (vii) Controlled Foreign Corporations (CFCs) are _____ entities incorporated in an overseas low tax jurisdiction.
- (A) Corporate
 - (B) Non-Corporate
 - (C) Both corporate and Non-corporate
 - (D) None of the above
- (viii) Existence of a _____ in a jurisdiction is a pre-requisite for the purpose of taxation of business profit of an enterprise in that jurisdiction, major Tax Convention:
- (A) Business connection
 - (B) Permanent establishment
 - (C) Business or professional connection
 - (D) Any connection giving rise to the said profit
- (ix) For the purpose of equalization levy, "specified service" means
- (A) Online advertisement
 - (B) Any provision for digital advertising space or any other facility or service for the purpose of online advertisement.
 - (C) Specified Service also includes any other service as may be notified by the Central Government.
 - (D) All of the above.
- (x) Following is not an anti-tax avoidance measure in the context of international taxation:
- (A) TIEAS
 - (B) POEM
 - (C) GAAP
 - (D) Transfer pricing provisions
- (1 x 10 =10 Marks)**
- (b) Test the correctness of the following statements, with brief reasons :
- (i) A tax authority under the BM Act shall be deemed to be a civil court for all intents and purposes. **(3 Marks)**

- (ii) Any payment received for online advertisement will attract equalization levy of 6%
(3 Marks)
- (iii) ABC Ltd. is a domestic company. It has a foreign subsidiary FGH Inc., in a tax haven. If the place of effective management is found to be in India, under the CFC legislation, the entire income of can be taxed in India and FGH Inc., can be treated as a domestic company for several other purposes as well.
(4 Marks)
- (c) Discuss whether AK has fulfilled the requisite conditions for grant of relief under section 91.
(5 Marks)
- (d) AK wants to know the income-tax liability for the Assessment Year 2018-19, with workings. You are required to provide the same.
(11 Marks)
- (e) Discuss briefly about the amount of TDS applicable for payment to Ajmal Kamal.
(3 Marks)
- (f) In respect of the foreign income and foreign assets unearthed by the Department during the search, discuss the tax implications under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 (BM Act). AK wants to know the year of taxability and the tax amount. Your answer should also cover discussion on the applicable provisions concerned.
(11 Marks)

Answer

- (a) (i) B
(ii) A
(iii) C
(iv) C
(v) D
(vi) B
(vii) A
(viii) B
(ix) D
(x) C

- (b) (i) The statement is not correct.

A tax authority shall be deemed to be a civil court for the purposes of section 195 of the Code of Criminal Procedure, 1973, which provides for prosecution for contempt of lawful authority of public servants, for offences against public justice and for offences relating to documents given in evidence.

However, he would not be so deemed for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973, containing the provisions as to offences affecting the administration of justice.

Therefore, the statement that a tax authority shall be deemed to be civil court for all intents and purposes is not correct.

(ii) The statement is not correct.

Chapter VIII of the Finance Act, 2016, titled "Equalisation Levy", provides for an equalisation levy of 6% of the amount of consideration for specified services, which includes online advertisement, received or receivable by a non-resident not having permanent establishment in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India.

Therefore, only if payment is received by a non-resident not having a PE in India, would provisions of equalization levy be attracted and not otherwise.

(iii) The statement is partly correct.

As per section 6(3), a foreign company FGH Inc. would be resident in India in any previous year, if, its place of effective management, in that year, is in India. Therefore FGH Inc. would be a resident in India by virtue of section 6(3) of the Income-tax Act, 1961 and its entire income would be taxable in India.

If FGH Inc. becomes a resident on account of its POEM being in India, the provisions of tax deduction at source under Chapter XVII-B as applicable to income received by a resident, would be attracted in respect of income received by FGH Inc.

The rate of tax applicable to FGH Inc. would be the tax rate applicable to a foreign company and not a domestic company. Further, the provisions of dividend distribution tax under section 115-O would not be attracted in the hands of FGH Inc. in respect of the dividend distributed by it, since FGH Inc. is not a domestic company.

In effect, the provisions of the Income-tax Act, 1961 relating to companies resident in India would apply to FGH Inc. However, it cannot be treated as a domestic company for the purposes of the Act.

(c) Conditions to be fulfilled to claim relief u/s 91

In the case of income arising to an assessee in countries with which India does not have any double taxation agreement, relief would be granted under section 91 provided all the following conditions are fulfilled:

- (a) The assessee is a resident in India during the previous year in respect of which the income is taxable.
- (b) The income accrues or arises to him outside India.
- (c) The income is not deemed to accrue or arise in India during the previous year.

- (d) The income in question has been subjected to income-tax in the foreign country in the hands of the assessee.
- (e) The assessee has paid tax on the income in the foreign country.
- (f) There is no agreement for relief from double taxation between India and the other country where the income has accrued or arisen.

Ajitabh Khan is resident for the A.Y. 2018-19. He has income accrues or arises in Country L and Country M and such income is not deemed to accrue or arise in India. The income earned in Country L and Country M is chargeable to tax there and AK has also paid income-tax on such income there. India does not have a Double taxation avoidance agreement with Country L and Country M.

AK has fulfilled the necessary conditions for grant of relief u/s 91.

- (d) Since Ajitabh Khan is resident in India for the P.Y.2017-18, his global income would be subject to tax in India. Therefore, income earned by him in Country L & M would be taxable in India. He is however entitled to deduction under section 91, since India does not have a DTAA with Country L & M, and all conditions under section 91 are satisfied.

Computation of tax liability of Ajitabh Khan for A.Y.2018-19

Particulars	₹	₹
I Income from house property		
Income from house property in India	4,30,00,000	
Less: Loss from house property in Country L	<u>1,30,00,000</u>	
		3,00,00,000
II Profits and gains of business or profession		
Business income in India		
From being the owner of cricket team in Asian Premier League	12,40,00,000	
From acting in movies	<u>9,41,50,000</u>	
	21,81,50,000	
Business income in Country L		
Own	7,20,00,000	
Share income from firm ²	<u>4,80,00,000</u>	12,00,00,000
Business income in Country M	<u>2,90,00,000</u>	
		36,71,50,000

² It is logical to take a view that exemption under section 10(2A) in hands of the partner would be available only in respect of share income from an Indian firm. In this case, since the share income is from a foreign firm, the same is taxable in India in the hands of the partner. The above solution has been worked out on the basis of this view.

An alternate view that the share income from foreign firm is also exempt under section 10(2A) may also be possible, in which case, the answer would accordingly undergo a change.

III Income from Other Sources		
Agricultural income from Country M		<u>1,20,00,000</u>
Gross Total Income		40,91,50,000
Less: Deductions under Chapter VI-A		
Under section 80C		
PPF ₹ 1,20,000 & LIC ₹ 2,00,000		
Total ₹ 3,20,000, restricted to		<u>1,50,000</u>
Total Income		40,90,00,000
Computation of tax liability:		
Tax on total income	12,25,12,500	
[30% x ₹ 40,80,00,000 + ₹ 1,12,500]		
Add: Surcharge@15% (since his total income exceeds ₹1 crore)	<u>1,83,76,875</u>	
	14,08,89,375	
Add: Education Cess & SHEC @3%	<u>42,26,681</u>	
	14,51,16,056	
Tax liability (rounded off)		14,51,16,060
Less: Deduction under section 91 [See Working Notes 1 & 2 below]		<u>2,72,60,000</u>
Net Tax liability (rounded off)		11,78,56,060

Working Note 1: Computation of deduction under section 91		
Particulars		₹
I	Deduction under section 91 in respect of income doubly taxed in India and Country L	
	Doubly taxed income:	
	Country L (i.e., ₹ 7.2 crores, being business income (+) ₹ 4.8 crores, being taxable share income from firm (-) ₹ 1.3 crores, loss from house property)	₹ 10,70,00,000
	Lower of Indian rate of tax and rate of tax in Country L [See Working Note 2 below]	18%
	Deduction u/s 91 = 18% x ₹ 10.70 crores	1,92,60,000

II	Deduction under section 91 in respect of income doubly taxed in India and Country M Doubly taxed income: Country M (i.e., ₹ 2.9 crores, being business income (+) ₹ 1.2 crores, being taxable agricultural income) Lower of Indian rate of tax and rate of tax in Country M [See Working Note 2 below] Deduction u/s 91 = 19.512% x ₹ 4.10 crores	₹ 4,10,00,000 19.51%	 80,00,000
Deduction under section 91			2,72,60,000

Working Note 2: Computation of average rate of tax in India, Country L & M		
(1)	Average rate of tax in India [14,51,16,060 x 100/40,90,00,000]	35.48%
(2)	Average rate of tax in Country L [2,16,00,000 x 100/12,00,00,000]	18%
(3)	Average rate of tax in Country M [80,00,000 x 100/4,10,00,000]	19.512%

- (e) Where any income referred to in section 115BBA is payable to a non-resident non-citizen sportsman, the person responsible for making payment is liable to deduct tax at source @20% on such income under section 194E.

Income referred to in section 115BBA includes income by way of participation in India in any game or sport.

Payment of ₹ 20 lakh by Ajitabh Khan to Mr. Ajmal Kamal³, a non-resident, for participation in one of the Premier League Matches is income referred to in section 115BBA, hence, Ajitabh Khan is liable to deduct tax at source on such payment @20% under section 194E.

Since Ajmal Kamal is a non-resident, the amount of tax to be deducted would be increased by education cess @2% and secondary and higher education cess @1%. So, the effective rate of tax to be deducted by Mr. Ajitabh Khan is 20.6%

However, DTAA of India with the other Country in which Mr. Ajmal Kamal resides, provides for withholding tax at 15%.

Section 90(2) of Income-tax Act, 1961 provides that where the Central Government has entered into a DTAA with a country outside India, then, in respect of an assessee to whom

³ It is logical to assume that Mr. Ajmal Kamal is a non-citizen, since the question mentions that he is a foreign player

such agreement applies, the provisions of act shall apply to the extent they are more beneficial to the assessee.

Therefore, Mr. Ajitabh Khan is liable to deduct tax @15%, being the most beneficial rate contained in the DTAA, from payment of ₹ 20 lakhs made to Mr. Ajmal Kamal, a non-resident sports person.

- (f) As per section 3(1) of Black Money and Imposition of Tax Act, 2015, every assessee would be liable to tax@30% in respect of his undisclosed foreign income and asset of the previous year.

However, an undisclosed asset located outside India shall be charged to tax on its value in the previous year in which such asset comes to notice of the Assessing Officer.

As per section 41, in case, where tax has been computed in respect of undisclosed foreign income and asset, the Assessing Officer may direct the assessee to pay by way of penalty, in addition to tax, if any, payable by him, a sum equal to three times the tax so computed.

As per section 43, if any person, being a resident other than not ordinarily resident in India, who has furnished the return of income for any previous year, fails to furnish any information in relation to an asset (including financial interest in any entity) outside India held as a beneficial owner or otherwise, or in respect of which such person was a beneficiary, or if such failure is in relation to any income from a source located outside India, at any time during such previous year, the Assessing Officer may direct such person to pay, by way of penalty, a sum of ₹ 10 lakh.

In this case, search by IT department is conducted on Mr. Ajitabh Khan's, a resident, premises on 31.3.2018 and undisclosed foreign income and assets were found. The undisclosed foreign income would be charged to tax@30% in the P.Y.2015-16. The undisclosed foreign asset would be charged to tax@30% in the P.Y.2017-18, being the year in which it came to the notice of the Assessing Officer. The Assessing Officer may direct penalty, in addition to tax payable by him, a sum equal to three times the tax so computed and ₹ 10 lakh for not disclosing foreign assets and income.

Undisclosed foreign income

Undisclosed foreign income of ₹ 12 crores earned in Dubai during the F.Y.2015-16 is chargeable to tax in the A.Y.2016-17.

The tax payable is 30% of ₹ 12 crores = ₹ 3.6 crores.

Undisclosed foreign assets

Though the building in Panama Islands was purchased in the P.Y.2013-14 and pieces of art work was acquired in the P.Y.2016-17 in Macau islands, the same is chargeable to tax in India under the Black Money Act in the A.Y.2018-19 only, since these assets came to the notice of the Assessing Officer in the P.Y.2017-18.

Particulars	Million \$	₹ (in crores)
Undisclosed foreign assets:		
<u>Building in Panama Islands</u>		
Purchase price	35.200	
Add: Brokerage (2% of \$ 35.2 million)	<u>0.704</u>	
Cost of acquisition	35.904	
Market value as on valuation date, being value on 1 st April of the previous year i.e., on 01.04.2017	40.00	
Fair market value of building in Panama Islands [being higher of cost of acquisition and the price that the property shall ordinarily fetch if sold in the open market on the valuation date]	40.00	
Relevant rate of exchange for the purpose of conversion into Indian currency [being the rate of exchange on 1 st April of the previous year i.e., on 01.04.2017] - 65.55		
Fair market value in Indian currency in crores (40 million x 65.55/10)		262.200
<u>5 pieces of art work</u>		
Cost of acquisition	3.80	
Market value as on valuation date, being value on 1 st April of the previous year i.e., on 01.04.2017	4.20	
Fair market value [being higher of cost of acquisition and the price that the artistic work shall ordinarily fetch if sold in the open market on the valuation date]	4.20	
Relevant rate of exchange for the purpose of conversion into Indian currency [being the rate of exchange on 1 st April of the previous year i.e., on 01.04.2017] – 65.55		
Fair market value in Indian currency in crores (4.2 million x 65.55/10)		<u>27.531</u>
Total undisclosed foreign assets		<u>289.731</u>
Tax payable @ 30%		86.92