

PAPER – 4: DIRECT TAX LAWS & INTERNATIONAL TAXATION

Part - II

Question No.1 is compulsory.

*Answer any **four** questions out of the remaining **five** questions.*

Working notes should form part of the answer.

All questions relate to Assessment Year 2024-25, unless stated otherwise in the question.

Question 1

Orient Pharmaceuticals Private Limited is an Indian Company, engaged in the business of manufacturing and providing access to affordable and innovative medicines and healthcare solutions. The company is incorporated in the year 2009. The company shows a Net Profit of ₹ 95 lakhs as per the Statement of Profit and Loss for the year ended March 31, 2024.

Net Profit has been arrived at after debiting and crediting the following items:

- (1) Depreciation as per the Companies Act claimed in the Statement of Profit and Loss - ₹ 11.90 lakh.*
- (2) The amount of employee benefits includes a sum of ₹ 13,00,000 in respect of bonus payable to employees. In the previous year 2023-24, the company and its employee's union had a dispute over payment of bonus. In order to avoid late payment of bonus, the company formed a trust and transferred the amount of bonus payable to employees to the said trust. The dispute was settled in the month of August, 2024 and the trust paid the amount of bonus to the employees on 31st August, 2024.*
- (3) An amount paid by the company as regularization fee for violating a law (as prescribed by Medical Council of India) of manufacturing medicines, ₹ 9.50 lakhs.*
- (4) An amount of ₹ 45,000 was paid as late fees to Government for company's failure in performance of a contract within the stipulated time. There was a*

delay of 5 months and according to the agreement, the company had to pay a late fees of ₹9,000 per month to the Government.

- (5) The company earned a profit of ₹ 7.50 lakhs on sale of plot of land on 25.08.2023 to Sudhakar Private Ltd., a domestic Company, the entire shares of which are held by the assessee company. The plot was acquired by Orient Pharmaceuticals Pvt. Ltd. on 20.12.2022. This profit is included in the income of the assessee company.*
- (6) The company earned a profit of ₹ 4.50 lakhs on sale of 2500 shares of M/s Stadel Ltd., a listed Indian company. These shares were sold on 08.11.2023 for ₹ 280 per share. The highest trading price of Stadel Ltd. quoted on the stock exchange as on 31.01.2018 was ₹ 175 per share and the Lowest Trading price quoted on the stock exchange was ₹ 165 per share. The said shares were acquired for ₹ 100 per share on 11.07.2016. STT paid both at the time of purchase and sale of shares.*
- (7) Bank guarantee was given by the company towards disputed tax liabilities - ₹ 11 lakhs.*
- (8) Company debited an interest of ₹ 7.50 lakh which the company remitted as interest to a company incorporated in USA on a loan taken 3 years ago. Tax deducted under section 195 from such interest has been deducted in March 2024, but deposited by the company on 14th July, 2024.*
- (9) The company has contributed ₹ 65,000 to an electoral trust by account payee cheque and the same is debited to Statement of Profit and Loss.*

Following Additional information is provided by the company for P.Y 2023-24:

- (1) Closing Stock includes 1200 pieces of imported machinery spares at its landed cost as on the date of import at US\$ 25 per piece. Exchange rate on the date of import i.e. 15.09.2023 was 1 US\$ = ₹ 82.88 (rounded off). Exchange rate on 31.3.2024 was 1 US\$ = ₹ 83. The market value per pieces as on 31.3.2024 was US\$ 27 per piece.*
- (2) The depreciation charged in the Statement of Profit and Loss of ₹ 11.90 lacs includes the depreciation calculated on following assets:*
 - (i) It incudes an amount of depreciation of ₹ 95,000 in respect of fire fighting equipments installed in the office premises and factories of the assessee. During the year, there was no incidence of fire and hence the equipments were no used.*

(ii) A new machinery which was installed and put to use on 14.05.2023 valuing ₹75 lakhs.

(iii) A machinery which was sold to a domestic company in 2016 at its WDV for ₹35 lakhs was re-acquired on July 5, 2023 for ₹65 lakhs.

There is no other fixed asset included by the company's accountant for calculation of depreciation except above these three assets mentioned above.

You are required to compute total income of the company as per Income-tax Act, 1961 for the Assessment Year 2024-25 indicating reasons for treatment of each item, assuming that the company has not opted for special provisions under section 115BAA or 115BAB. **(14 Marks)**

Answer

Computation of Total Income of Orient Pharmaceutical Pvt. Ltd. for the A.Y. 2024-25

	Particulars	Amount (in ₹)	
I	Profits and gains of business or profession		
	Net profit as per statement of profit and loss		95,00,000
	Add: Items debited but to be considered separately or to be disallowed		
	(1) Depreciation as per Companies Act	11,90,000	
	(2) Bonus transferred to the trust for making payment to the employees after settlement of the dispute	--/Nil	
	[The bonus would be allowable as deduction u/s 36(1)(ii), even though the amount of bonus payable was initially remitted to the trust created for the purpose of avoiding late payment of bonus, since the actual payment of bonus made to the employees is 31 st August, 2024 i.e., on or before due date of filing return of income. Since		

the same has been already debited to the statement of profit and loss, no further adjustment is required]		
(3) Regularization fee for violating a law [Regularization fee paid for violating a law as prescribed by Medical Council of India is a payment to compound an offence. Such expenditure is considered to be the expenses prohibited by the law. Hence, it does not qualify for deduction u/s 37. As the same has been debited to the statement of profit and loss, it has to be added back]	9,50,000	
(4) Late fees to Government for failure in performance of a contract [Late fees of ₹ 45,000 paid for non-fulfilment of a contract within the stipulated time is not for the breach of law but was paid for breach of contractual obligations and therefore, is an allowable expense. Since it is already debited in statement of profit and loss, no further adjustment is required]	--/Nil	
(7) Bank guarantee towards disputed tax liabilities [As per section 43B any tax, duty, cess or fee is allowed as deduction if they are actually paid on or before the due date of filing return of income under section 139(1). Mere furnishing of bank guarantee by the assessee towards tax liabilities does not mean actual payment of taxes. Hence, it is not treated as payment to be eligible for	11,00,000	

deduction under section 43B. As the same has been debited to the statement of profit and loss, it has to be added back]		
(8) Payment of Interest to a company incorporated in USA [Since the tax has been deducted in March, 2024 and deposited by the company on 14.7.2024 i.e., on or before due date of filing return of income, no disallowance would be attracted under section 40(a)(i). Since the interest has been already debited to the statement of profit and loss, no further adjustment is required]	--/Nil	
(9) Contribution to electoral trust [Contribution to electoral trust is not allowable as deduction while computing business income of the company. Since the contribution has been debited to statement of profit and loss, the same has to be added back while computing business income]	65,000	33,05,000
Less: Items credited but not taxable or chargeable to tax under another head		1,28,05,000
(5) Profit on sale of plot of land to 100% subsidiary [Capital Gain arising on sale of plot of land is taxable under the head "Capital Gains". Since the profit on sale of plot of land has been credited to the	7,50,000	

statement of profit and loss, the same has to be deducted while computing business income]		
(6) Profit on sale of shares of M/s Stadel Ltd. [Capital Gain arising on sale of shares of M/s Stadel Ltd. is taxable under the head "Capital Gains". Since the profit on sale of shares has been credited to the statement of profit and loss, the same has to be deducted while computing business income]	4,50,000	
AI(1) Cost of machinery spares included in closing stock [The cost of imported machinery spares is to be capitalised as per ICDS V. Since cost of machinery spares is included in purchases as well as forms part of closing stock, no adjustment is required to be made. Therefore, the cost of machinery spares has to be added to the machinery cost and depreciation has to be allowed thereunder.] <i>[Note – The cost of imported machinery spares is capitalised as per ICDS V considering such spares can only be used in connection with a tangible fixed asset and their use is expected to be irregular. Accordingly, normal depreciation and additional depreciation has been provided. However, it is possible to assume that the use of such machinery spares are regular in which case it will be dealt with as per ICDS II (Inventories). As per ICDS II, inventories shall be valued at \$25 per piece, being lower of</i>	--/Nil	

cost of \$ 25 per piece or NRV as on 31.3.2024 of \$ 27 per piece. As per ICDS VI, non-monetary items being inventory shall be converted into the reporting currency by using the exchange rate on the transaction date i.e., on 15.9.2023 being the date of purchase. In such a case, no adjustment is required to be made for closing stock while computing business income and no depreciation/ additional depreciation would be provided. Accordingly, the business income and total income would be ₹ 83,60,000 and ₹ 85,57,500, respectively].		
		12,00,000 1,16,05,000
Less: Depreciation as per Income-tax Act, 1961		
Normal depreciation		
- On fire-fighting equipment's¹ [Eligible for depreciation even though such equipment's were not used during the previous year.]	95,000	
- On new machinery [₹ 75,00,000 x 15% since it is put to use for more than 180 days]	11,25,000	
- On machinery sold and reacquired [15% of actual cost of ₹35,00,000, being lower of WDV at the time of sale (i.e., ₹ 35 lakhs) or price paid for re-acquisition (i.e., ₹ 65 lakhs)]	5,25,000	
- On imported machinery spares (to be added to cost of machinery as per ICDS	3,72,960	

¹Assuming depreciation of ₹ 95,000 is computed applying the depreciation rate similar to the rate specified in the Income-tax Rule, 1962.

	V) [₹ 24,86,400 (1200 x \$25 x 82.88) x 15%]		
	Additional depreciation		
	- On new machinery [₹ 75,00,000 x 20%]	15,00,000	
	- On imported machinery spares [₹ 24,86,400 x 20%]	4,97,280	
			41,15,240
			74,89,760
II	Capital Gains		
	Profit on sale of plot of land to 100% subsidiary	--/Nil	
	[Short-term capital gains arise on sale of plot of land held for less than 24 months. However, in this case, since the transfer is to a 100% subsidiary company and the subsidiary company is an Indian company, the same would not constitute a transfer for levy of capital gains tax]		
	Long term capital gain on sale of shares of M/s. Stadel Ltd. [Since shares were held for more than 12 months]		
	[Full value of consideration (2,500 x ₹ 280)]	7,00,000	
	Less: Cost of acquisition - Higher of (i) and (ii)	4,37,500	
		2,62,500	2,62,500
	(i) Actual cost of acquisition (2,500 x ₹100) ₹ 2,50,000		
	(ii) ₹ 4,37,500, being lower of fair market value as on 31.1.2018 (i.e., ₹ 4,37,500, being 2,500 x 175) and sale consideration (i.e., ₹ 7,00,000)		
	Gross Total Income		77,52,260

Less: Deduction under Chapter VI-A		65,000
Under section 80GGB [Contribution by a company to an electoral trust is allowable as deduction, since payment is made otherwise than by cash]		
Total Income		76,87,260

Question 2

- (a) (i) *Mrs. Seema Aggarwal, aged 56 years, a resident individual acquired a residential house at Ayodhya on 01.04.1993 for ₹ 45,00,000. The Fair market value of the property as on 01.04.2001 was ₹ 1,20,00,000 and the stamp duty value as on 01.04.2001 was ₹ 1,02,00,000.*

Mrs. Seema Aggarwal sold her residential house located at Ayodhya to Mr. Shiv Kumar on 15.10.2023 for ₹ 15,50,00,000. The value determined by the Stamp Duty Authority on 15.10.2023 was ₹ 17,00,00,000. Mr. Shiv Kumar was handed over the possession of the property on 15.10.2023 and the registration process was completed on the same date. He paid the sale proceeds in full on the date of registration.

After recovering the sale proceeds from Shiv Kumar, Mrs. Seema Aggarwal purchased one residential plot at Amritsar for ₹ 8 crores on 18.02.2024. She also deposited ₹ 3 crores in a Saving account opened with State Bank of India, Amritsar under Capital gain account scheme on 31.03.2024 for the construction of the residential house on above plot.

You are required to calculate the taxable capital gain in the hands of Mrs. Seema Aggarwal for the A.Y. 2024-25 as per the provisions of Income-tax Act, 1961. Cost Inflation Index for F.Y. 2001-02: 100 and 2023-24: 348.

(4 Marks)

- (ii) *Mr. Manjoo Menon, an assessee from Coimbatore has 20% shareholding in a Private Limited company Aurelia Exports (P) Ltd. The assessee has immovable property in Coimbatore. It was let out to the said company on monthly rent. The assessee permitted the company to provide the said property as collateral security to ABC Bank in order to enable the said company to obtain loan from the said bank.*

Consequently, the property was mortgaged to the bank in 2013. That time Board of Directors passed a resolution authorizing the assessee to obtain from the company interest-free deposit/advance upto ₹ 20 lakhs as and when required for making available the said property as collateral security to the bank for the loan facility enjoyed by the company.

In June, 2023 Mr. Menon asked for advance rent and he received a sum of ₹ 15 lakhs from the company as advance rent in June 2023 which was to be adjusted against the rent payable to the assessee by the said company. After such adjustment for the year ended March 31, 2024, the amount of advance rent stood reduced to ₹ 8,00,000. The accumulated profits of the company as on 01.04.2023 amounted to ₹ 10,00,000.

The Assessing Officer in the assessment order for the assessment year 2024-25 sought to treat the said sum of ₹ 8,00,000 as deemed dividend under section 2(22)(e) of the Income-tax Act.

Can the advance rent given to Mr. Manjoo Menon by the company be deemed as dividend under section 2(22)(e) as per Income-tax Act, 1961?

(4 Marks)

- (b) *Miles Inc., a company incorporated in US, is engaged in development of infrastructure and providing consultancy in the same field. During the Financial Year 2023-24, its shareholders met in India for three times. The first two meetings were held to discuss the modification of rights attached to various classes of shares and the third meeting was held to discuss and decide about sale of companies' assets situated in India. The meetings of Board of Directors are held in Chicago, USA where management and commercial decisions necessary for conduct of company's business are taken.*

It provides the following additional information pertaining to Financial Year 2023-24:

- (i) *Dividend received ₹ 5,50,000 (Net of TDS) on Global Depository Receipts of Z Ltd., an Indian company, issued under a scheme of Central Government against the initial issue of shares of the company and purchased by Miles Inc. in foreign currency through an approved intermediary.*
- (ii) *Fees for technical services received from Government of India: ₹ 5,55,000. The Government of India utilised such technical services for a development project carried out by it in Nepal.*

You are required to determine the residential status of Miles Inc. and compute the total income of Miles Inc. for the assessment year 2024-25 briefly explaining the relevant provisions of the Income-tax Act, 1961.

(6 Marks)

Answer

(a) (i) Computation of taxable Capital gain in the hands of Mrs. Seema Aggarwal for A.Y.2024-25

Particulars	₹
Full value of consideration	15,50,00,000
As per section 50C, the full value of consideration would be actual sales consideration since the stamp duty value as on 15.10.2023 of ₹ 17,00,00,000 does not exceed 110% of actual consideration of ₹ 15,50,00,000.	
Less: Indexed cost of acquisition	3,54,96,000
[₹ 1,02,00,000 (higher of actual cost of ₹ 45,00,000 and Fair market value as on 1.4.2001 of ₹ 1,20,00,000, but restricted to stamp duty value as on 1.4.2001 of ₹ 1,02,00,000) x 348 / 100]	
	11,95,04,000
Less: Exemption under section 54	10,00,00,000
[Purchase of one residential plot of ₹ 8 crores on 18.2.2024 and deposit of ₹ 3 crores in Capital Gain Account Scheme on 31.3.2024 (before the date of filing of return of income) provided that the construction thereon is completed within the stipulated time of three years ² , but restricted to maximum of ₹ 10 crores]	
Taxable long term capital gains	1,95,04,000

(ii) The words "by way of advance or loan" in section 2(22)(e) must be construed to mean those advances or loans which a shareholder enjoys simply on account of being a person who is the beneficial owner of shares holding not less than 10% of the voting power.

² Vide Circular No. 667 dated 18.10.1993, the CBDT has clarified that the cost of the land is an integral part of the cost of the residential house, whether purchased or built.

In case such loan or advance is given to such shareholder as a consequence of any further consideration received from such a shareholder which is beneficial to the company, such advance or loan cannot be a deemed dividend within the meaning of the Act.

Gratuitous loan or advance given by a company to a shareholder, who is the beneficial owner of shares holding not less than 10% of the voting power, would come within the purview of section 2(22)(e) to the extent of accumulated profits of the company but not the cases where the loan or advance is given in return for an advantage conferred upon the company by such shareholder.

In the present case, advance of ₹ 15 lakh was given by Aurelia Exports (P) Ltd. to Mr. Manjoo Menon holding 20% shareholding as advance rent for the property let out by him to the company and out of which ₹ 7 lakhs was adjusted against rent payable of F.Y. 2023-24. The advance was given by the company since Mr. Menon mortgaged his personal property thereby enabling the company to obtain the loan from bank in 2013.

Therefore, such advance of ₹ 8 lakhs outstanding as on 31.3.2024 cannot be brought within the purview of section 2(22)(e), since it was not in the nature of gratuitous advance but was given as advance rent and to protect the interest of the company.

Note – The facts of the case are similar to the facts in *Pradip Kumar Malhotra v. CIT (2011) 338 ITR 538*, wherein the above issue came up before the Calcutta High Court. The above answer is based on the rationale of the Calcutta High Court in the said case.

- (b) Miles Inc., a foreign company, would be resident in India in P.Y. 2023-24 if its POEM, in that year, is in India. Since the meeting of Board of Directors are held outside India i.e., in Chicago, USA where management and commercial decisions necessary for conduct of company's business are taken, its POEM during the A.Y. 2024-25 would be outside India. Hence, Miles Inc. is a non-resident during the P.Y. 2023-24.

The decisions made by shareholders in India on modification of the rights attaching to various classes of shares and sale of company's assets situated in India are not relevant for determination of Miles Inc.'s place of effective management.

Computation of total income of Miles Inc. for the A.Y. 2024-25

Particulars	Amount (₹)
Dividend received on GDR of an Indian company [Taxable, since income is from any asset or source of income is in India. Tax @10.4% would have been deducted on dividend of GDR] [₹ 5,50,000 / 89.6%]	6,13,839
Fees for technical services received from Government of India [Taxable, since it is deemed to accrue or arise in India on account of being received from Government of India even though services are utilised for development project carried out outside India. Tax @20.8% would have been deducted on FTS received from Government] [5,55,000/79.2%] <i>Note – Since, the word “received” is mentioned after fees for technical services, the solution has been worked out considering the FTS amount as net of TDS and accordingly grossing up has been done. However, on account of using the word “Net of TDS” after dividend amount but not after FTS amount, it is possible to assume the FTS amount of ₹ 5,55,000 as gross amount. In such a case, total income would be ₹ 11,68,839.</i>	7,00,758
Total Income	13,14,597

Question 3

- (a) Please answer the following independent questions with regard to provisions applicable to Charitable Trust as per the Income-tax Act, 1961.
- (i) Devayani Trust is a registered charitable trust under section 12AB. During the previous year 2023-2024, the trust had applied ₹ 4,50,000/- for the benefit of the trustee and ₹ 2,50,000/- for the benefit of Mr. Sujan Dave, who has donated ₹ 3,75,000/- to the trust up to 31.3.2024. Also, an amount of ₹ 2,50,000/- set apart in the P.Y. 2021-2022 by the trust for charitable purposes under section 11(2) has been utilized in the P.Y. 2023-2024 for making donation to another registered charitable trust with similar object as Devayani Trust.

What is the amount of 'specified income' liable to tax @30% under section 115BBI for assessment year 2024-2025? Explain with reasons.

- (ii) Parivartan, a public charitable trust has been incorporated on 01.06.2022 and immediately commenced its activities of providing "Relief of Poor". During the previous year 2022-23, it failed to file application for Provisional registration under section 12A(1)(ac). However, on 1.1.2024, it applied for the final registration as per section 12AB read with section 12A(1)(ac) in prescribed Form to avail exemption under section 11 for A.Y. 2024-25.

Is the action of the trust justified? Can a trust apply for Final registration before applying for Provisional registration? If yes, what is the time period upto which the Principal Commissioner or Commissioner will have to pass the order granting or rejecting the registration? The registration, if granted will be applicable from which assessment year? Explain your answer based on the latest Income tax provisions.

(4 x 2 = 8 Marks)

- (b) Following are the particulars of income earned by Mr. Kumar Saurav, a resident Indian aged 56 years in India and from Country P for the assessment year 2024-2025

Income from India	Amount in ₹
Income from Profession in India	10,75,000
Interest on Fixed Deposit with XYZ Bank	95,000
Interest on Savings Bank Account	47,000
Income from Country P	
Rate of Tax is 16%	
Agricultural Income in Country P (Gross)	65,000
Royalty Income form literary book from Country P	4,50,000
Expenses incurred for earning royalty	35,000
Dividend from a company incorporated in Country P	1,59,000
Rent from a house situated in Country P (Gross)	1,92,000
Municipal Tax paid in respect of the above house	9,500
(not allowed as deduction in Country P)	

You are required to compute the total income and net tax liability of Mr. Kumar Saurav in India for the assessment year 2024-25 assuming that India has not entered into double taxation avoidance agreement with Country P.

Assume that Mr. Kumar Saurav pays tax under the default tax regime under section 115BAC. **(6 Marks)**

Answer

(a) (i) "Specified income" under section 115BBI includes the following:

- income which has been applied for the benefit of prohibited persons u/s 13(3)
- deemed income under section 11(3) on account of violation of certain conditions stipulated for accumulation of income.

Specified income of Devyani Trust liable to tax@30% under section 115BBI for A.Y. 2024-25

Particulars	Amount (₹)
Amount applied for the benefit of the trustee [Trustee of the trust is one of the persons specified u/s 13(3)]	4,50,000
Amount applied for the benefit of Mr. Sujan Dave [Since Mr. Sujan Dave's total contribution to the trust upto 31.3.2024 is more than ₹ 50,000, he is a person specified u/s 13(3)]	2,50,000
Donation made to another trust out of accumulated income of P.Y. 2021-22 [Donation to another charitable trust out of accumulated income is one of the violations of condition specified for accumulation of income – section 11(3)]	2,50,000
Specified income liable to tax @30% under section 115BBI	9,50,000

(ii) Since Parivartan trust has already commenced its activities and has not availed exemption under section 11 for any P.Y. ending on or

before 1.1.2024, (being the date of application) it need not first apply for provisional registration.

It can at any time after the commencement of such activities directly apply for final registration under section 12AB³.

Thus, the action of trust for applying for the final registration as per section 12AB before applying for provisional registration for exemption under section 11 is valid.

The Principal Commissioner or Commissioner has to pass the order granting or rejecting the registration before expiry of 6 months from the end of the month in which application is received i.e., by 31.07.2024.

Exemption under section 11 and 12 would be applicable from the assessment year immediately following the financial year in which such application is made i.e., from A.Y. 2024-25 (PY 2023-24).

(b) Computation of total income and net tax liability of Mr. Kumar Saurav for A.Y.2024-25 under the default tax regime

Particulars	₹	₹
Income from house property		
Gross Annual Value ⁴ of property in Country 'P'	1,92,000	
Less: Municipal taxes paid in Country 'P'	9,500	
Net Annual Value	1,82,500	
Less: Deduction under section 24 – 30% of NAV	54,750	
		1,27,750
Profits and Gains of Business or Profession		
Income from profession in India	10,75,000	

³ Read with section 12A(1)(vi)(B), w.e.f. 1.10.2023

⁴ Rental income has been taken as GAV in the absence of other information relating to fair rent, municipal value etc.

SUGGESTED ANSWER**DIRECT TAX LAWS & INTERNATIONAL TAXATION**

Royalty income from literary book from Country 'P' (after deducting expenses of ₹ 35,000)	4,15,000	
		14,90,000
Income from Other Sources		
Interest on Fixed deposit with XYZ Bank	95,000	
Interest on savings bank account	47,000	
Agriculture income in Country 'P'	65,000	
Dividend from a company incorporated in Country 'P'	1,59,000	
		3,66,000
Gross Total Income		19,83,750
Less: Deductions under Chapter VI-A [Not available under default tax regime]		Nil
Total Income		19,83,750
Tax liability on ₹19,83,750		
Tax on total income [30% of ₹ 4,83,750 + ₹ 1,50,000]		2,95,125
Add: Health and Education cess@4%		11,805
		3,06,930
Less: Deduction u/s 91 (See Working Note below)		1,18,632
Net Tax Liability		1,88,298
Net Tax Liability (Rounded off)		1,88,300

Working Note: Calculation of deduction under section 91

Particulars	₹
Doubly Taxed Income – Country P	
Income from house property	1,27,750

Royalty Income [₹ 4,50,000 – ₹ 35,000 (Expenses)]	4,15,000
Agricultural income	65,000
Dividend	1,59,000
	7,66,750
Rate of tax in Country P = 16%	
Indian rate of tax = $3,06,930/19,83,750 \times 100 = 15.472\%$	
Lower of the above = 15.472%	
Deduction u/s 91 [15.472% x ₹ 7,66,750]	1,18,632

Question 4

(a) *Examine the applicability of Tax Deducted at source/Tax Collected at source and calculate the amount of TDS/TCS in the following independent cases as per the provisions applicable for A.Y. 2024-25:*

(i) *Raj Keshri Hotels and Resorts Limited is engaged in business of owning, operating and managing hotels during the previous year 2023-24. The tips are paid by the guests by way of charge to the Credit Cards, UPI or Net Banking in the bills. The company disburse the same to the employees at periodic intervals. Explain with reason whether the company is responsible for deducting tax at source from disbursement of tips to its employees.* **(3 Marks)**

(ii) *Lalit, an individual whose total sales in business during the year ended 31.3.2023 was ₹ 1.50 crores, opted to compute income under section 44AD for A.Y. 2023-24. He paid ₹ 5,00,000 by cheque on 1.2.2024 to a contractor (an individual), for construction of his factory building. No amount was credited earlier to the account of the contractor in the books of Lalit. The turnover of Mr. Lalit for previous year 2023-24 is ₹ 95 Lacs.*

He also pays a monthly rent starting from 1st April, 2023 to 31st March, 2024 of ₹ 16,000 p.m. for the office premises to Mr. Hemant, the owner of building. Besides, he also pays service charges of ₹ 5,500 per month to Mr. Hemant towards the use of furniture, fixtures and vacant land appurtenant to office. Examine the obligation of the tax deducted at source for A.Y. 2024-25. **(3 Marks)**

(iii) XY and Co., a partnership firm selling its products 'R' through the digital facility provided by ABC Limited (an E-commerce Operator). On 28th February, 2024, ABC Limited credited in its books of account, the account of XY and Co. with a sum of ₹ 4,90,000 for the online sale of products 'R' made during the month of February-2024.

The company released a payment of ₹ 4,30,000 on 6th March 2024 to XY and Co. out of above sales made during February. Mr. Rai, who purchases products 'R' through the digital facility of ABC Limited made payment of ₹ 60,000 directly to XY and Co. on 15th March, 2024.

(2 Marks)

(b) Yalin Ltd. is located in Country X, a notified jurisdictional area (NJA). Armo Ltd., a domestic company (the assessee) sold goods to Yalin Ltd. on 15.01.2024 for ₹ 11.75 crore.

During the current financial year, Armo Ltd. sold identical goods to KB Inc., of Edinburgh, U.K. for ₹ 13 crore. KB Inc. is neither situated in any NJA nor it is associated person of Armo Ltd.

While sales to KB Inc., were on CIF basis, the sale to Yalin Ltd. was on FOB basis, which paid ocean freight and insurance amounting to ₹ 25 Lakhs on purchases from Armo Ltd. India has a double taxation avoidance agreement with UK. The assessee has a policy of providing after sales support service to the tune of ₹ 19 lakhs to all customers except Yalin Ltd. which procured the same locally at a cost of ₹ 23 lakhs.

Whether Yalin Ltd. and Armo Ltd. are Associated Enterprises. If yes, compute the Arm's Length Price for the sales made to Yalin Ltd. and the amount of consequent adjustment, if any, in the profits of Armo Ltd., the assessee company for A.Y. 2024-25. Explain with reasons.

(6 Marks)

Answer

(a) (i) In respect of tips collected by the company from the guests and distributed to the employees, the person responsible for paying the employee was not the employer at all, but a third person, namely the guest.

The payments of collected tips included and paid by way of a credit cards, UPI or Net Banking in the bills by guest, would not be payments made "by or on behalf of" an employer.

The contract of employment not being the proximate cause for the receipt of tips by the employee from a guest, such payments would be outside the scope of sections 15 and 17.

There is no employer-employee relationship between customers and the employees of Raj Keshri Hotels and Resorts Ltd. and therefore such payments do not fall in the nature of salary.

On account of such tips being received from guests and not from the employer, section 192 would not get attracted at all in the hands of Raj Keshri Hotels and Resorts Ltd.⁵ Thus, the company is not responsible for deducting tax at source from disbursement of tips to its employees.

- (ii) Lalit is required to deduct TDS under section 194C for contract payments and under section 194-I for rent paid for office premises during the previous year 2023-24 since Lalit's turnover for the previous year 2022-23 exceeded ₹ 1 crore.

Thus, tax deduction under section 194C would be ₹ 5,000⁶, being 1% of ₹ 5 lakhs.

Mr. Lalit is also required to deduct tax at source @10% u/s 194-I on the rent paid for office premises and for furniture, fixtures and vacant land appurtenant to office to Mr. Hemant, since aggregate of rent i.e., ₹ 2,58,000 [(16,000 + ₹ 5,500) x 12] paid during the P.Y. 2023-24 exceeds the threshold limit of ₹ 2,40,000.

The tax deduction under section 194-I would be ₹ 25,800, being 10% of ₹ 2,58,000.

- (iii) As per section 194-O, ABC Limited, an e-commerce operator is required to deduct tax at source @1% on ₹ 4,90,000, being the gross amount of sale of products 'R' of XY and Co., a partnership firm, an e-commerce participant, since such sale of goods is facilitated by ABC Limited through its digital facility.

ABC Ltd. is also required to deduct tax @1% on the payment of ₹ 60,000 directly made to XY and Co., since such amount is deemed to be amount credited or paid by ABC Ltd. to XY and Co.

⁵ ITC Ltd v. CIT (2016) 384 ITR 14 (SC)

⁶ TDS would be ₹ 5,050, if it is assumed that ₹ 5,00,000 is the net amount after TDS.

Thus, ABC Ltd. is required to deduct tax of ₹ 5,500, being 1% of ₹ 5,50,000.

Note – Alternatively, it is possible to assume that the gross amount of sales is ₹ 4,90,000 of which ₹ 4,30,000 was paid to e-commerce operator and the balance of ₹ 60,000 is directly paid to the XY and Co., a partnership firm by one of the buyers (Mr. Rai). In such case, ABC Ltd. is required to deduct tax@1% on the entire amount of ₹ 4,90,000. Thus, ABC Ltd. is required to deduct tax of ₹ 4,900, being 1% of ₹ 4,90,000.

- (b) Since Armo Ltd. entered into a transaction with Yalin Ltd., in Country X which is located in a notified jurisdictional area (NJA), Armo Ltd. and Yalin Ltd. would be deemed as associated enterprises and the transactions between them would be deemed to be international transactions. Accordingly, all the provisions of transfer pricing would be attracted in case of such a transaction.

The transactions of Armo Ltd. with KB Inc., U.K. for sale of identical goods are comparable uncontrolled international transactions, since it is neither associated enterprises of Armo Ltd. nor it is situated in NJA.

Hence, Comparable Uncontrolled Price (CUP) method can be used to determine ALP.

Computation of ALP using CUP method

Particulars	₹ in crores
Price charged by KB Inc. (on CIF basis)	13.00
Less: Ocean freight and insurance, has to be reduced since the price charged to Yalin Ltd. is on FOB basis	0.25
Less: Cost of after-sales support service (has to be reduced, since such services are being provided to KB Inc. but not to Yalin Ltd.)	0.19
Arm's Length Price	12.56
Less: Price at which goods were sold to Yalin Ltd.	11.75
Arm's length adjustment [increase in profit of Armo Ltd.]	0.81

Question 5

- (a) Answer any **two** out of the following three sub-parts, viz. (i), (ii) and (iii)
Your answer should cover:

- (1) Issue involved
- (2) Provision Applicable
- (3) Analysis and conclusion

- (i) Assessee had taken an engine on lease under an agreement with a foreign company (lessor), a tax resident of the Germany, having no permanent establishment (PE) in India. The foreign company also does not have PAN in India. The assessee company deducted tax at source @10% on lease rental as per the provisions contained under DTAA between India and Germany.

However, revenue contended that in the absence of furnishing of PAN, the assessee was under an obligation to deduct tax at a higher rate of 20% following the provisions of section 206AA. In the light of the latest Supreme Court rulings, discuss whether the contention of Revenue is correct or not. **(4 Marks)**

- (ii) The Assessing Officer passed an assessment order u/s 143(3) on 20.11.2018 in which the assessee committed the mistake of reducing the depreciation in computation of Income instead of adding to the income resulting in double deduction of depreciation. The AO did not correct the said mistake in his order.

The assessee went up in appeal on other issues to the CIT(A) for the same Assessment year, who decided the appeal on 28.6.2023. The AO gave effect to the CIT(A)'s order vide order dated 23.7.2023. The AO thereafter passed an order u/s 154 dated 26.4.2024 in which he rectified the mistake of double deduction of depreciation committed in the order dated 20.11.2018.

Please discuss whether the time limit of 4 years as per section 154(7) would apply from the date of original assessment order or the order of the Appellate Authority? **(4 Marks)**

- (iii) ABC Pvt Ltd, a domestic company is engaged in a software development business at Techno Park, which employed 700 employees, deducted tax at source (TDS) in respect of salaries, contract payments,

etc., totalling ₹ 1.10 crores upto 31.03.2024 for the assessment year (AY) 2024-25. In March 2024, the assessee deposited part of the TDS being ₹ 38 lakhs and balance of ₹ 72 lakhs was deposited later in July 2024. However, the Additional Commissioner of Income Tax issued a show cause notice proposing to levy penalty under Section 271C of the Income-tax Act 1961 of the amount equal to TDS and also levied penal interest under section 201(1A) of the Income-tax Act 1961. Feeling aggrieved and dissatisfied with the levy of interest/penalty under the Income-tax Act, 1961 on late deposit of TDS, the company has approached you to seek your advice in the matter. (4 Marks)

- (b) (i) *Explain the term "Exchange of information" as per Article 26 of Model Tax Conventions under OECD Model and UN Model and explain importance of Article 26. (4 Marks)*
- (ii) *What do you understand by "GloBE Rules"? Which entities are covered under these Rules? (2 Marks)*

Answer

- (a) (i) **Issue Involved:** The issue under consideration is whether the provisions of section 206AA, which prescribe a higher rate of tax deduction at source in case of non-furnishing of PAN by a foreign company, override the Double Taxation Avoidance Agreement (DTAA) that specify a lower rate of tax.

Provisions Applicable: As per section 206AA, in case of non-furnishing of PAN by the deductee to the deductor, the tax is required to be deducted at higher of the rate specified in the relevant provision or at the rates in force or at the rate of 20%.

Analysis and Conclusion: Section 90(2) provides that the provisions of the DTAA would override the provisions of the Act in cases where the provisions of DTAA are more beneficial to the assessee.

Even the charging sections 4 and 5 of the Act, which deal with the principle of ascertainment of total income under the Act, are also subordinate to the principle enshrined in section 90(2).

Thus, in so far as the applicability of the scope/rate of taxation with respect to the impugned payments made to the non-residents is concerned, no fault can be found with the rate of taxation invoked by

the assessee based on the DTAA, which prescribed for a beneficial rate of taxation.

The provisions of tax withholding, i.e., section 195 of the Act, would apply only to sums that are otherwise chargeable to tax under the Act. The provisions of DTAA, along with sections 4, 5, 9, 90 & 91 of the Act, are relevant while applying the provisions of tax deduction at source. Therefore, section 206AA of the Act cannot be understood to override charging sections 4 and 5 of the Act.

Accordingly, the contention of the revenue that in the absence of furnishing of PAN, the assessee was under an obligation to deduct tax at a higher rate of 20% is not correct.

Note – *The facts given in the question are similar to the facts in CIT (International Taxation) v. Air India Ltd. [2023] 456 ITR 139 (SC). The above answer is based on the rationale of the Supreme Court ruling in the said case.*

- (ii) **Issue Involved:** The issue under consideration is whether the time limit of 4 years as per section 154(7) would apply from the date of original assessment order or the order of the Appellate Authority.

Provisions Applicable: As per section 154(7), no amendment under section 154 shall be made after the expiry of four years from end of the financial year in which the order sought to be amended was passed.

Analysis and Conclusion: Once an appeal against the order passed by an authority is preferred and is decided by the appellate authority, the order of the Assessing Officer merges with the order of the appellate authority. After merger, the order of the original authority ceases to exist and the order of the appellate authority prevails.

The final order passed by the appellate authority was dated 28.6.2023 and acting thereupon the AO passed assessment order, giving appeal effect thereto, on 23.7.2023. Thus, it is the order passed by the CIT(A) which remains on record for all intent and purposes as the original order of assessment has been merged.

Once the matter is viewed from this angle, it does not matter that the error which is sought to be rectified occurred in the original

assessment order and was not subject matter of appeal. Obviously, it was a calculation error which could not have been the subject matter of appeal.

Thus, the period of limitation of 4 years for the purpose of section 154(7) has to be counted from the date of the order of the Appellate Authority.

Note – *The facts given in the question are similar to the facts in CIT v. Tony Electronics Limited (2010) 320 ITR 378 (Delhi). The above answer is based on the rationale of the Delhi High Court ruling in the said case.*

Note – *Since concept of partial merger is applicable in case of section 154, the rationale of Supreme Court rulings in case of CIT v. Alagendran Finance Ltd (2007) 293 ITR 1 or CIT v. Industrial Development Bank of India Ltd. [2023] 454 ITR 811 which is in relation to section 263, can be applied in the present case. Accordingly, the analysis and conclusion alternatively would be as follows:*

Analysis and Conclusion: *Once an appeal against the order passed by an authority is preferred and is decided by the appellate authority, the order of the Assessing Officer merges with the order of the appellate authority but limited to the subject matter of appeal.*

In the present case, the final order passed by the appellate authority dated 28.6.2023 was on other issues.

Thus, the period of limitation of 4 years for the purpose of section 154(7) has to be counted from the date of the original order of the Assessing Officer on matters other than the matter decided by the Appellate Authority.

(iii) Issue Involved: The issue under consideration is whether penalty u/s 271C and interest u/s 201(1A) both are leviable on late deposit of TDS.

Provisions applicable: Section 271C(1)(a) provides that if any person fails to deduct the whole or any part of the tax as required by or under the provisions of Chapter XVII-B, then, such person is liable to pay, by way of penalty, a sum equal to the amount of tax which such person failed to deduct.

Section 201(1A) provides that in case a tax has been deducted at source but is subsequently remitted belatedly, such a person is liable to pay interest as provided under section 201(1A).

Analysis and Conclusion: On a plain reading of section 271C(1)(a), no penalty would be leviable on belated remittance of TDS after it is deducted by the assessee.

Similarly, section 276B speaks about prosecution for failure to pay the tax deducted at source to the credit of the Central Government within the prescribed time.

The words "fails to deduct" in section 271C(1)(a) cannot be read as "failure to deposit/pay the tax deducted".

Accordingly, no penalty would be leviable under section 271C on delay in remittance of the tax deducted at source after deducting it on time.

However, interest u/s 201(1A) for late deposit of TDS is leviable.

Note – *The facts given in the question are similar to the facts in US Technologies International Pvt. Ltd. v. CIT [2023] 453 ITR 644 wherein the issue came up before the Supreme Court. The above answer is based on the rationale of the Supreme Court in the said case.*

- (b) (i) In order to complete tax cases, a country may require certain information which may be available with the treaty partner.

Article 26 provides for the information which may be exchanged and the manner in which such a request has to be made.

The OECD and UN Model Conventions are similar with respect to this Article.

Importance of Article 26:

- facilitates effective exchange of information between Contracting States.
- curtails cross-border tax evasion and avoidance,
- curtails the capital flight that is often accomplished through tax evasion & avoidance. This is particularly relevant in the perspective of developing countries.

- (ii) Pillar Two consists of GloBE Rules which means Global Anti-Base Erosion rules, through which 15% global minimum tax has been introduced.

The GloBE Rules apply to Constituent Entities that are members of an MNE Group that has annual revenue of EURO 750 million or more in the Consolidated Financial Statements of the Ultimate Parent Entity (UPE) in at least two of the four Fiscal Years immediately preceding the tested Fiscal Year.

Question 6

- (a) (i) *Club U Travels Private Limited, engaged in the business of travel agency remitted substantial amount to Australia as per the information collected by the Income-tax department from PTU Bank. The department collected documents from PTU Bank, which include Form 15CB issued by the chartered accountant, list of passengers, copy of their passports, date of travel and invoices raised by the foreign party.*

On enquiry from the passengers and verifying their passports, it is found that they did not travel abroad on the dates mentioned in the documents. On the top of it the passengers also denied there was no transaction with Club U Travels Private Limited.

The Income-tax department concluded that the amounts were remitted by the company on the basis of false invoices and for wrong reasons. It led to FEMA violations and Form 15CB issued by the chartered accountant was a vital document in these transactions. During the six-month period in question, the chartered accountant had issued 78 certificates in Form 15CB involving remittances of ₹ 35 crores for Club U Travels Private Limited.

A representation was given by the concerned CA that he had issued Form 15CB based on invoices produced by the company and verifying the KYC documents of the signatory to the invoices. His contention was that since he was not the statutory auditor of the company, he did not examine the books of account before issuing Form 15CB or conduct due diligence of its business activities. He had charged ₹ 2,500 per certificate. Mostly, the fees were collected in cash. Some parts of the fees were credited to his bank account.

Can the chartered accountant be held guilty of professional misconduct for failure to obtain sufficient information and failure to exercise due diligence in discharging the professional responsibilities? (6 Marks)

(ii) *Specify with reason, whether the following acts can be considered as:*

(A) Tax planning; or (B) Tax management; or (C) Tax evasion.

- 1. Mr. D has FDR with SBI in his name amounting to ₹ 50 lakhs. He gifted this sum of ₹ 50 lakhs to his son, on 10.04.2023, the date on which he attained 18 years of age. The purpose is to shift interest income from his hands to his son, so that there may be Zero tax implication, since his son has no other income and the total interest would be lower than taxable limits for P.Y. 2023-24.*
- 2. Mr. Ram's Annual income is ₹ 49.50 lakhs for A.Y. 2024-25 excluding commission receivable from ABC Limited. During March 2024, he earned a commission of ₹ 6 lakhs from ABC Limited. He asked ABC Limited to transfer the commission in his wife's account, who is a housewife. He also asked them to deduct TDS in her wife's name. He did it so that his total income may not cross ₹ 50 lakhs and he can save surcharge on taxes applicable on total income exceeding ₹ 50 lakhs. His wife has no other income.*

(4 Marks)

- (b) *A Non-resident Foreign Company entered into contracts with several Indian Companies for installation of mobile telephone system and made an application to the Board of Advance Rulings, for advance ruling in relation to the tax liability arising out of such transaction.*

One of the above said Indian Companies also made an application to its Assessing Officer for determination of a question of law with regard to payments to be made to the said Foreign Company.

The Board of Advance Rulings rejected the application of the Foreign Company on the ground that the question raised is pending before an Income Tax Authority. Is the rejection of the application of the Foreign Company justified in law?

(4 Marks)

Answer

- (a) (i) Form 15CB is a certificate of an accountant wherein he certifies that he has examined the agreement between the remitter and the beneficiary requiring such remittance he has examined also the relevant documents and books of account required for ascertaining the nature of remittance and for determining the rate of deduction of tax at source.

The Chartered Accountant certifying the Form 15CB undertakes to have verified the agreement between the remitter and the beneficiary as well as the relevant documents and books of account to ascertain the nature of remittance and determine the rate of TDS.

In this case, however, the Chartered Accountant mentioned that he had only verified KYC of signatory to invoice and the invoices thereof.

He had not only failed to justify as to how verification of invoices was considered as sufficient compliance for certifying the forms but also failed to bring on record the said invoices.

Thus, he failed to provide any basis on which he relied for issuing Form 15CB certificates to the company.

On account of such failure, clauses (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949 for failure to exercise due diligence in discharging his professional responsibilities and failure to obtain sufficient information may be invoked.

- (ii) 1. **Tax Planning** – Gifting of fixed deposits of ₹ 50 lakhs by Mr. D to his son who attained the age of 18 years for the purpose of shifting interest income from his hands to his son so that there may be zero tax implication, is a permitted **tax planning** measure under the provisions of income-tax law.

Note – It has been assumed that such transfer is irrevocable and Mr. D does not derive any direct or indirect benefit from such income. In case transfer of fixed deposit is revocable then the interest income on fixed deposits would be included in the hands of Mr. D and hence the same would not be considered as Tax Planning.

2. **Tax Evasion** – Mr. Ram's annual income is ₹ 49.50 lakhs for the A.Y. 2024-25. He also earned commission of ₹ 6 lakhs from ABC Limited. Accordingly, his total income would be ₹ 55.50 lakhs which exceeds ₹ 50 lakhs and hence surcharge is applicable on tax on total income.

However, for the purpose of saving tax, he instructed ABC Ltd. to transfer the commission in his wife's account. This is the case of application of income and not of diversion of income by overriding title, since such transfer of commission is not under any obligation but to evade tax.

This is tax evasion.

(b) Application for Advance Ruling

As per section 245R, the Board for Advance Rulings (BAR), after examining the application and the records called for, may either allow or reject an application. However, the Board shall not allow an application where the question raised in the application is already pending before any income-tax authority, or Appellate Tribunal or any court.

In the present case, the question raised by a non-resident foreign company with respect to tax liability on income arising from installation of mobile telephone system is already pending before the Assessing Officer on account of application made by one of the Indian Companies for determination of question of law with regard to the payments made to the said foreign company.

Since such question is already pending before the Income-tax Authority, the rejection of application of the foreign company by the BAR is justified in law.

Alternate Answer

However, as per the Explanatory Memorandum to the Finance Bill, 2020 (See Note below) the BAR shall not allow the application only if the question raised is already pending in the applicant's case before any income-tax authority.

Accordingly, based on this view, the rejection of application by the BAR is not justified in law, since the question raised in the application made by the foreign company is pending before the Assessing Officer in the case of one of the Indian Companies, and not in the applicant's case.

Note - 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
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;	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.

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 only where a question is pending in the applicant's case before any income-tax authority.