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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.

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, 2018.

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.*

Answer in respect of Multiple Choice Questions are to be indicated in capital letters i.e., A or B or C or D, as the case may be.

Working Notes should form part of your answer. However, in answers to objective type questions (MCQs carrying two marks each), working notes are not necessary.

All questions relate to Assessment Year 2019-20, unless states otherwise in the questions/case studies.

Case Study 1

Good Day Inc of USA and its associates:

Good Day Inc of USA is engaged in multiple trading and manufacturing activities throughout the world. It has a liaison office at Mumbai meant for sourcing raw materials in India for the purpose of carrying out manufacturing activity at USA. It also provided plant and machinery on hire to be used for extraction of mineral oils in India. During the previous year 2018-19, it received mobilization advance of ₹ 2 crores from an Indian company for movement of rigs from a foreign country to an offshore site at Mumbai and subsequently they were put to use (i.e.) for extraction of mineral oil. It also received ₹ 5 crores by way of hire towards provision of plant and machinery for the previous year 2018-19 in India. Good Day Inc. has a subsidiary company by name Kite Inc. at Portugal, which is engaged in supply of electronic goods worldwide.

Good Day Inc. also has another subsidiary by name Becker Inc. at Germany. On 01.04.2018, Becker Inc. advanced ₹ 2 crores to Manna Dey (P) Ltd. of Mumbai by remitting the amount directly from Germany to the bank account of Manna Dey (P) Ltd. For the previous year 2018-19, interest is receivable from Manna Dey (P) Ltd @ 9%. For the Assessment Year 2019-20, Becker Inc. having significant activities in India became resident assessee because of POEM.

On 01.07.2018, Manna Dey (P) Ltd borrowed ₹ l0 crores from Jimmy Connors Ltd, United Kingdom for which interest is payable at 9% per annum. The pre-tax profit of Manna Dey (P) Ltd. was ₹ 160 lakhs before deducting depreciation of ₹ 40 lakhs and interest on moneys borrowed by it. The total borrowing of Manna Dey (P) Ltd is ₹ 12 crores, which is 80% of its total assets.

Democrat (P) Ltd, Chennai

Democrat (P) Ltd is a subsidiary of Giant Trade Ltd of UK. It is engaged in manufacturing and trading of consumer durables both by import and export. It is also engaged in executing turnkey projects. It had 4 directors viz. Ashok Chatterjee, Mithun Banerjee, Dr Deepak Mitra and Meenakshi Jain. The director, Ashok Chatterjee, sold 30% of the shares owned by him to his son, Santhosh Chatterjee, in June 2015 and resigned from the directorship of the company. The whereabouts of Ashok Chatterjee are not known to the company.

Democrat (P) Ltd. gave loan of ₹ 6 crores on 01.07.2018 to its associated concern in Australia without charging interest. For giving the said advance, Democrat (P) Ltd. mobilized funds by issuing 8% Debentures on 01.06.2018.

Kite Inc. of Portugal entered into an agreement for supply of electronic goods to Democrat (P) Ltd. of Chennai on regular basis. As per agreement, it supplied goods worth ₹ 10 crore every month from April, 2018 onwards and the supply is to be made for 42 months continuously.

Democrat (P) Ltd. permitted yet another of its associated enterprise by name Maxwell (P) Ltd. registered in South Africa to use the hired machineries for exploration of mineral oil in Kenya. Democrat (P) Ltd. paid ₹ 5 crores to Dusseldorf Inc. of Germany towards hire charges of plant and machinery for the previous year 2018-19. The usage of Maxwell (P) Ltd. is equal to 55% of the total hire charges paid and the balance was for the use by Democrat (P) Ltd. Maxwell (P) Ltd. did not share or pay any hire charges and the entire amount was paid by Democrat (P) Ltd.

During the Previous Year 2018-19, Democrat (P) Ltd. sponsored a football tournament in India. Mr. Dickie Bird, a citizen of UK but resident of India (for Assessment Year 2019-20), a famous international referee received ₹ 4,50,000 for acting as referee in the tournament from Democrat (P) Ltd.

Income-tax assessment of Democrat (P) Ltd.

The income-tax return of the Assessment Year 2018-19 was filed by Democrat (P) Ltd on 20.12.2018 declaring total income of ₹ 52.50 crores. The assessee obtained report in respect of international transactions from the 'Accountant' (as mentioned in the *Explanation* below section 288(2) and the report contained information about the international transactions of the assessee. The Assessing Officer referred the international transactions to Transfer Pricing Officer (TPO) for determination of arm's length price without providing an opportunity of hearing to Democrat (P) Ltd. The TPO wanted the documents and information in respect of the international transactions and the assessee could not furnish information and documents for the transactions of the value of ₹ 4.50 crores. The Assessing Officer passed the order of assessment based on the TPO report subsequently. (**Note:** The law as regards scope of work and power of TPO are the same for the Assessment Years 2018-19 and 2019-20. There is no change in legal provision.)

Proposed joint venture between Democrat (P) Ltd and Good Day Inc.

The Democrat (P) Ltd jointly with Good Day Inc. bid for a turnkey project worth ₹ 500 crores in India. It was Democrat (P) Ltd who solicited the association of Good Day Inc. in executing the turnkey project. The parties have agreed to enter into an agreement to specifically allot the scope of work between them and to bear the profits and losses arising thereon respectively. There would be no common risk sharing in the arrangement between the companies. However, they apprehend that they could be assessed as an AOP during the income-tax assessment.

Whereabouts of Ashok Chatterjee

Ashok Chatterjee, one of the directors of Democrat (P) Ltd., left India on 05.06.2015 and his

whereabouts were unknown. There is income-tax arrears of ₹ 40 lakhs relating to his personal assessment of the Assessment Years 2012-13 to 2015-16. Only in December, 2018, it came to light that Ashok Chatterjee has settled in Canada. He has properties in Canada and one vacant land at Siliguri, West Bengal whose value as per State stamp valuation authority is ₹ 10 lakhs.

Purchase of land from non-resident

Democrat (P) Ltd acquired a vacant site at Mysore from Ms. Kousalya, a non-resident settled in Germany, for expansion of its manufacturing activity. The land was acquired by Ms. Kousalya in April, 2005, when she was a resident of India. Now, Democrat (P) Ltd acquired the said land for ₹ 48 lakhs on 10th March, 2019. Ms. Kousalya does not have permanent account number and has also not furnished tax residency certificate. The tax was deducted at source out of the purchase price and was remitted to the exchequer on 20th March, 2019. The balance amount of purchase price has not yet been remitted to Ms. Kousalya as the approval for remittance is pending from RBI.

Activity profile of Dr. Deepak Mitra

Dr. Deepak Mitra (age 50), yet another director of Democrat (P) Ltd residing at Palghat, Kerala, earned royalty income of ₹ 50 lakhs from Gobar Gas Inc. of Canada for the year ended 31.03.2019. However, he received only ₹ 20 lakhs during the previous year 2018-19, and the balance is outstanding as on 31.03.2019. Dr. Deepak Mitra maintains cash system of accounting of royalty income and hence, admitted only ₹ 20 lakhs for the assessment year 2019-20. The DTAA between India and Canada provides for tax@15% in Canada without prejudice to taxation of the same income in India. The other income of Dr. Deepak Mitra is by way of income from house property (computed) ₹ 4.5 lakhs and dividend income from Democrat (P) Ltd of ₹ 8 lakhs. He paid premium to LIC of India of ₹ 1.5 lakhs in respect of a life insurance policy of his son who is studying in Australia.

Rajesh Mitra son of Dr. Deepak Mitra, shareholder in Democrat (P) Ltd

Rajesh Mitra son of Dr. Deepak Mitra born and brought up in India acquired 10,000 equity shares of Democrat (P) Ltd on 10.06.2010 for ₹ 9 lakhs. He left India for employment in USA in January, 2011 and settled there. He has never visited India subsequently. His entire shareholdings in Democrat (P) Ltd were sold for ₹ 28.80 lakhs on 10.01.2019. The amounts were repatriated to his bank account in USA subsequently.

The exchange rates are given below:

On 10.06.2010 1$= ₹ 45;

On 10.01.2019 1$ = ₹ 72.

Cost inflation index P.Y.2010-11 = 167; P.Y. 2018-19 = 280.

Fair Market Value (FMV) of each equity share as on 31.01.2018 = ₹ 300

Activity profile of director Mithun Banerjee

Director Mithun Banerjee is a renowned technocrat, and is one of the directors of the company

Democrat (P) Ltd since 01.06.2014. He is a partner in Lilly LLP, New York. A notice for assessment of his income under Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 was served on 01.05.2018 for the alleged undisclosed income / assets held in USA. The initial capital contribution in the firm was made in the previous year 2005-06 was his only contribution and the accumulations are by way of profits which were not disclosed by him for income-tax assessment, in India. He has not withdrawn any amount from the firm at any time.

The Balance Sheet of Lilly LLP is given below:

	01.04.2018	01.10.2018	31.03.2019
	In US$		
Cash on hand (as per books)	10,000	12,000	15,000
Cash at Bank (as per books)	20,000	18,000	15,000
Stock in trade (as per books)	30,000	30,000	30,000
Vacant site FMV as on 1.4.2018 $ 40,000	20,000	50,000 (FMV)	60,000 (FMV)
Plant and machinery	75,000 (As per books)	50,000 (FMV	40,000 (FMV)
Bullion FMV as on 01.04.2018 $ 25,000	15,000	30,000 (FMV)	35,000 (FMV)
	1,90,000	**1,90,000**	**1,95,000**
Liabilities			
Sundry Creditors (as per books)	50,000	55,000	60,000
Partners' Capital			
Mithun Banerjee (25%)	30,000	No fresh capital introduction.	
Bimal (50%)	50,000	No fresh capital introduction.	
Senthil (25%)	60,000	No fresh capital introduction.	
	1,90,000		

The partnership agreement provides that in the event of dissolution, the net worth exceeding the capital of the partners is to be shared in the profit sharing ratio.

The reference rate of RBI of 1 US $ as against Indian Rupee on various dates are as under:

01.04.2018 = ₹ 65; 01.05.2018 = ₹ 68; 31.03.2019 = ₹ 72

Celebrity for annual function of the company

Democrat (P) Ltd celebrated its anniversary by inviting Mr. Ricky Ponting, a famous Australian cricketer who is not a citizen of India. He came to India for the first time in April, 2018 on the invitation of Democrat (P) Ltd. He was paid ₹ 25 lakhs for his presence in the anniversary celebrations of Democrat (P) Ltd.

Choose the most appropriate alternative for the following MCQs: (2 x 10 = 20 Marks)

1.1 What is the 'due date' within which the liaison office of Good Day Inc. has to submit the annual statement to the Income-tax authority for the year ended 31st March, 2019?

(A) 30-05-2019

(B) 31-07-2019

(C) 30-09-2019

(D) 31-03-2020

1.2 Compute the amount of capital gain/loss in the hands of Rajesh Mitra on sale of shares of Democrat (P) Ltd.

(A) Long-term capital loss ₹ 1,20,000

(B) Long-term capital gain ₹ 13,71,020

(C) Long-term capital gain ₹ 19,80,000

(D) Long-term capital gain ₹ 2,70,000

1.3 Under what section tax is deductible at source on the payments made to Mr. Dickie Bird who acted as referee in the football tournament for the amounts received from Democrat (P) Ltd ?

(A) under section 194E

(B) under section 194J

(C) under section 115BBA

(D) under section 195

1.4 Kite Inc of Portugal in December, 2018, after the monthly supply of goods, applied for advance ruling. How much fee would it need to pay for obtaining the advance ruling?

(A) ₹ 10 lakhs

(B) ₹ 5 lakhs

(C) ₹ 2 lakhs

(D) ₹ 10,000

1.5 At what rate Democrat (P) Ltd must deduct tax at source on the amount paid to Ms. Kousalya for purchase of vacant land?

(A) 20.8%

(B) 31.2%

(C) 30.9%

(D) 20.6%

1.6 For Democrat (P) Ltd, the GAAR provisions will apply as the value of transactions made with two of its associated enterprises was

(A) ₹ 11 crores in aggregate

(B) ₹ 3.11 crores in aggregate

(C) ₹ 2.75 crore in respect of transaction with Maxwell P Ltd.

(D) ₹ 36 lakhs by way of interest from associate concern in Australia

1.7 How much is the penalty payable by Democrat (P) Ltd for non-maintenance of documents and information relating to international transaction?

(A) ₹ 1,00,000

(B) ₹ 9,00,000

(C) ₹ 22,50,000

(D) ₹ 1,50,000

1.8 For the assessment year 2019-20, at what rate and under what section, tax is deductible at source on the interest payment made by Manna Dey (P) Ltd to Becker Inc?

(A) At 10% under section 194A

(B) At 20% under section 195

(C) At 30% under section 195

(D) None of the above

1.9 How much of interest paid by Manna Dey (P) Ltd. to its associated enterprise, Jimmy Connors Ltd of United Kingdom, is liable for disallowance taking note of its income from business ?

(A) ₹108 lakhs

(B) ₹ 90 lakhs

(C) ₹ 31.50 lakhs

(D) ₹ 49.50 lakhs

1.10 The time limit for assessment of Mithun Banerjee under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 is

(A) 31.03.2019

(B) 31.3.2020

(C) 31.12.2020

(D) 31.03.2021

You are required to answer the following issues:

1.11 Compute the income of Good Day Inc. in respect of providing plant and machinery on hire for extraction of mineral oils as per the applicable presumptive provisions of the Income-tax Act, 1961. ***(3 marks)***

1.12 Will your answer be different if Good Day Inc. spent only ₹ 1.50 crore out of ₹ 2 crore mobilization advance received for movement of rigs to offshore site at Mumbai? ***(2 marks)***

1.13 State the legal correctness of the action of the Assessing Officer as regards making reference to the Transfer Pricing Officer without providing an opportunity of hearing to the assessee i.e., Democrat (P) Ltd. ***(3 marks)***

1.14 Is the passing of assessment order by the Assessing Officer based on TPO's report without passing draft assessment order, tenable in law? ***(3 marks)***

1.15 As Chartered Accountant, what would be your advise as regards joint venture between Good Day Inc. and Democrat (P) Ltd. with specific allocation of work between them and the possibility of assessment as AOP. ***(3 marks)***

1.16 State the procedure to be followed by the Tax Recovery Officer for recovery of tax arrears of non-resident Ashok Chatterjee. ***(2 marks)***

1.17 Can the Assessing Officer treat Democrat (P) Ltd as agent of non-resident Ms. Kousalya, if there are any tax arrears pending against her name? Will your answer be different, if Ms. Kousalya opts for Chapter XII-A of the Act? ***(3 marks)***

1.18 Compute the undisclosed income / asset of Mithun Banerjee under Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015. Also, compute the tax liability of Mithun Banerjee. ***(4 marks)***

1.19 Compute the tax liability of Dr. Deepak Mitra and the amount of eligible foreign tax credit and the amount of foreign tax credit to be carried forward to future assessment years. ***(4 marks)***

1.20 At what rate, tax is deductible at source on the payment made to Mr. Ricky Ponting? Is Mr. Ricky Ponting liable to file his income-tax return in India? In case he has no PAN, at what rate tax is deductible at source and what would be the consequences of filing or non-filing of income tax return? ***(3 marks)***

Solution to Case Study 1

Q. No.	Answer
1.1	(A)
1.2	(C)
1.3	(B)
1.4	(A)
1.5	(A)

Q. No.	Answer
1.6	(B)
1.7	(B)
1.8	(D)
1.9	-[1]
1.10	(D)

[1] The correct answer is nil, since interest payable to non-resident associated enterprise does not exceed ₹ 1 crore.

Answer to Q. 1.11

The presumptive provisions applicable in this case are those contained in section 44BB.

As per this section, the profits and gains shall be deemed to be equal to 10% of the following amounts:

- paid or payable to the taxpayer on account of the provision of such services or facilities or supply of plant & machinery for the aforesaid purposes in India; and
- received or deemed to be received in India by the assessee on account of such service or facilities or supply of plant and machinery used or to be used in prospecting for, or extraction or production of mineral oils outside India

Computation of income of Good Day Inc. as per section 44BB

Particulars	Amt (₹ in crore)
Amount received for movement of rigs from foreign country to an offshore site at Mumbai	2
Amount received by way of hire charges towards provision of plant and machinery in India	5
Amount to be considered for purposes of section 44BB	7

Income from business under section 44BB at 10% of ₹ 7,00,00,000 is ₹ 70,00,000, which is the income of Good day Inc. chargeable to tax in India under the head "Profits and gains of business or profession" for the A.Y. 2019-20

Note - The mobilization fee of ₹ 2 crore received by Good Day Inc. is also includible in the gross receipts for the purpose of computing the income chargeable under section 44BB [*Sedco Forex International Inc vs. CIT (2017) 399 ITR 1 (SC)].*

Answer to Q.1.12

No, the answer would be the same. The mobilization fee received by Good Day Inc. is liable to tax under section 44BB regardless of the actual amount of expenditure incurred for movement of rigs to the offshore site.

The quantum of expenditure incurred in relation to mobilization fee is immaterial and regardless of the amount of expenditure incurred, the entire fee of ₹ 2 crore is to be included for the purposes of section 44BB. Hence, the answer will not change.

Answer to Q.1.13

As per section 92CA(1), where an assessee has entered into an international transaction in any previous year, and the Assessing Officer considers it necessary or expedient so to do, then, he

may refer the computation of the arm's length price in relation to the said international transaction to the Transfer Pricing Officer.

The Assessing Officer has to take the prior approval of the Principal Commissioner of Income-tax (PCIT)/Commissioner of Income-tax (CIT) before making such a reference.

There is no requirement under the Act to provide an opportunity of being heard to the assessee before making reference to the Transfer Pricing Officer.

Therefore, the action of Assessing Officer to refer the international transaction to Transfer Pricing Officer for determination of arm's length price without providing an opportunity of hearing to Democrat (P) Ltd. is **correct.**

Note *– The CBDT has, vide Instruction No.3/2016 dated 10.3.2016, stipulated that the Assessing Officer must, before making reference to the TPO, provide an opportunity of being heard to the assessee before recording his satisfaction or otherwise, in the following cases:*

(i) The assessee has not filed accountant's report u/s 92E but has undertaken an international transaction which comes to the notice of the Assessing Officer;

(ii) The assessee has not declared one or more international transaction(s) in the accountant's report filed u/s 92E and the said transaction(s) come to the notice of the Assessing Officer; and

(iii) Where the assessee has declared international transaction in the accountant's report filed u/s 92E but certain qualifying remarks were made to the effect that the said transactions are not international transactions or they do not impact the income of the taxpayer.

In respect of other cases, such opportunity of hearing need not be given before making reference to the TPO.

Answer to Q.1.14

As per section 144C(1), the Assessing Officer is required to forward a draft order of assessment to the eligible assessee if he proposes to make any variation in the income or loss returned which is prejudicial to the interest of such assessee.

Eligible assessee means, *inter alia*, any person in whose case variation arises on account of order of Transfer Pricing Officer.

In the present case, Democrat (P) Ltd. is an eligible assessee and the Assessing Officer is required to forward a draft assessment order to Democrat (P) Ltd.

Therefore, the action of Assessing Officer in passing an assessment order without forwarding a draft assessment order to Democrat (P) Ltd. is not tenable in law.

Note - *In Asstt. CIT vs. Vijay Television P Ltd (2018) 407 ITR 642 (Mad) (decision rendered on 23.04.2018) it was held that the passing of assessment order without forwarding the draft assessment order to the assessee is an incurable illegality and that such illegality could not be protected by section 292B.*

Answer to Q.1.15

As per the Circular[2] issued by the CBDT, it has been clarified that consortium arrangement for executing Turnkey project which has the following attributes may not be treated as an AOP –

1. Each member is independently responsible for executing its part of work through its own resources and also bear the risk of its scope of work
2. Each member earns profits or incurs losses, based on performance of the contract falling strictly within its scope of work.
3. Each member is responsible for the men and material used in their area of work.
4. The control and management of the consortium is not unified and common management is only for the *inter-se* coordination between the consortium and members for administrative convenience.

The benefit of this circular cannot be availed, if the members of the Consortium are associated enterprises, as per section 92A.

In the present case, Democrat (P) Ltd. and Good Day Inc., which are not associated enterprises, form a joint venture for turnkey project. They entered into an agreement to specifically allot the scope of work between them and to bear the profits and losses arising thereon, respectively. Also, there would be no common risk sharing in the arrangement between the two. They are not associated enterprises, at present. Hence, the joint venture between Good Day Inc. and Democrat (P) Ltd. may not be treated as an AOP.

My advice as a CA would be that:

(i) till the completion of the turnkey project, it must be ensured that Good Day Inc. and Democrat (P) Ltd., do not become associated enterprises;

(ii) the conditions stated in the Circular are strictly complied with, during the entire duration of the turnkey project.

Answer to Q.1.16

In the present case, Ashok Chatterjee has one vacant land in India of stamp duty value of ₹10 lakhs and income-tax arrears of ₹ 40 lakhs. As per section 173, the Tax Recovery Officer can recover income-tax arrears of ₹10 lakhs from such land in India.

Since India has a DTAA with Canada and Ashok Chatterjee has properties in Canada, Tax Recovery Officer may forward to the CBDT a certificate drawn up by him under section 222 for balance income-tax arrears of ₹ 30 lakhs and the CBDT may take such action thereon as it may deem appropriate having regard to the terms of the agreement with such country.

Answer to Q.1.17

As per section 163(1), "agent" in relation to a non-resident includes, *inter alia,* any person in India from or through whom the non-resident is in receipt of any income, whether directly or indirectly.

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[2] **Circular F.No.225/2/2016/ITA.II dated 7.3.2016**

In the present case, Kausalya, a non-resident, is in receipt of income (in the nature of capital gains) from Democrat (P) Ltd. Democrat (P) Ltd. can be treated as an agent of non-resident, Ms. Kousalya, for any tax arrears pending against her name provided it has been given an opportunity of being heard as to its liability to be treated as such.

Alternative Answer

As per section 163(1), "agent" also includes any other person, who, whether a resident or a non-resident, has acquired by means of a transfer, a capital asset in India.

In the present case, since, Democrat (P) Ltd. has purchased a vacant site at Mysore from Ms. Kousalya, for which it is yet to remit the purchase price to her, it can be treated as an agent of non-resident, Ms. Kousalya, for any tax arrears pending against her name provided it has been provided an opportunity of being heard as to its liability to be treated as such.

Ms. Kousalya cannot opt for the provisions of Chapter XII-A, and hence there is no possibility of change in view.

Answer to Q.1.18

Value of interest of Mithun Banerjee in Lilly LLP is chargeable to tax in India under the Black Money Act in the A.Y.2019-20, since these assets came to the notice of the Assessing Officer in the P.Y.2018-19.

For computing the value of interest in Lilly LLP, market value as on valuation date, being value on 1st April of the previous year i.e., on 01.04.2018 is to be considered.

Computation of undisclosed income/asset of Mithun Banerjee

Particulars	Amount (In US $)
Cash in hand (as per books)	10,000
Cash at bank (as per books)	20,000
Stock-in-trade (as per books)	30,000
Plant and machinery (as per books)	75,000
Total of book value of above assets (A)	**1,35,000**
Vacant site (FMV as on 1.4.2018)	40,000
Bullion (FMV as on 1.4.2018)	25,000
Total of FMV of above assets (B)	**65,000**
Sundry creditors (as per books) (C)	50,000
Net worth of Lilly LLP (A+B – C)	**1,50,000**
Value of interest in Lilly LLP	
Net worth portion equal to capital contribution (D)	30,000

Balance Net worth portion after capital contribution as per partnership deed in profit sharing ratio [10,000 (1,50,000 – 1,40,000) x 25%] (E)	2,500
Value of interest of Mithun Banerjee in Lilly LLP (D + E)	**32,500**
Value of interest of Mithun Banerjee in Lilly LLP in ₹[32,500 x 65, being exchange rate as on 1st April of the previous year i.e., on 1.4.2018]	**21,12,500**

As per section 3(1) of Black Money (Undisclosed Foreign Income and Assets) 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.

Tax liability of Mithun Banerjee would be ₹ 6,33,750, being 30% of ₹ 21,12,500.

Answer to Q.1.19

Since Dr. Deepak Mitra is resident in India for the P.Y.2018-19, his global income would be subject to tax in India. Therefore, income earned by him in Canada would be taxable in India. He is, however, entitled to deduction under section 90, since India has a DTAA with Canada.

Computation of tax liability of Dr. Deepak Mitra for A.Y.2019-20		
Particulars	**₹**	**₹**
Profits and gains from business or profession		
Royalty income (following cash system of accounting)		20,00,000
Income from house property (computed)		4,50,000
Income from other Sources		
Dividend income from Democrat (P) Ltd.	8,00,000	
Less: Exempt under section 10(34)	8,00,000	-
Gross Total income		**24,50,000**
Less: Deduction under Chapter VI-A		
Section 80C – LIC premium of his son		1,50,000
Total income		**23,00,000**
Computation of tax liability		
Upto ₹ 2,50,000	Nil	
₹ 2,50,001 – ₹ 5,00,000	12,500	
₹ 5,00,001 – ₹ 10,00,000	1,00,000	
₹ 10,00,001 – ₹ 23,00,000	3,90,000	
		5,02,500
Add: Health and education cess@4%		20,100
Tax liability		**5,22,600**
Less: Foreign tax credit **[See Working Note below]**		3,00,000
Net Tax liability		**2,22,600**

Working Note: Computation of Foreign Tax Credit		
Particulars		
Doubly taxed income	₹ 20,00,000	
Rate of tax in Canada	15%	
Average rate of tax in India [5,22,600/23,00,000 x 100]	22.72%	
Lower of Indian rate of tax and rate of tax in Canada		15%
Deduction u/s 90 = 15% x ₹ 20,00,000		₹ 3,00,000
Foreign tax credit allowed to be carried forward is ₹ 4,50,000 [₹ 30,00,000, being royalty income not received x 15%]		

***Note** – Sub-rule 5(ii) of Rule 128 provides that Foreign Tax Credit shall be determined by conversion of the currency of payment of foreign tax at the telegraphic transfer buying rate on the last day of the month immediately preceding the month in which such tax has been paid or deducted. However, in this case, in the absence of relevant information in the question, Foreign Tax Credit has been computed applying the provisions of Rule 128 other than sub-rule 5(ii) thereof.*

Answer to Q. 1.20

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 advertisement.

Payment of ₹ 25 lakh by Democrat (P) Ltd. to Mr. Ricky Ponting, a non-resident, for advertisement is income referred to in section 115BBA, hence, Democrat (P) Ltd. is liable to deduct tax at source on such payment @20% under section 194E. Since Mr. Ricky Ponting is a non-resident, the amount of tax to be deducted would be increased by health and education cess @4%. Therefore, the effective rate of tax to be deducted by Democrat (P) Ltd. is 20.8%

Section 115BBA provides that if the total income of the non-resident sportsman comprises of only income referred to in that section and tax deductible at source has been fully deducted, it shall not be necessary for him to file his return of income. Accordingly, Mr. Ricky Ponting is not liable to file his income-tax return in India if tax has been fully deducted on advertisement charges by Democrat (P) Ltd.

If Mr. Ricky Ponting has no PAN, in such a case also, tax shall be deducted @20.8%, being the rate higher of the following rates

(i) Rate specified in the relevant provisions of the Act i.e., 20%

(ii) At the rate in force

(iii) At the rate of 20%

There would be no consequence of filing or non-filing of income-tax return as he is not required to file his return of income as per section 115BBA.

PAPER – 6C: INTERNATIONAL TAXATION

Case Study 2

Introductory

Harivallabh Pvt. Ltd., (HPL) is a private limited company, incorporated in India in 1990. It is engaged in several activities, important one being manufacture of accessories for mobile phones.

This company is a part of a group called Dow Group. A company called DAS Martin, which is also a part of the Dow group, has acquired 10 lakh shares of ₹ 100 each in HPL, 18 years ago, for a consideration of ₹ 50.3 crores. The investment made in HPL was with the prior approval of Department of Industrial Policy & Promotion (DIPP) and RBI permission was also obtained.

About DAS Martin

DAS Martin holds 70% of the share capital of HPL.

DAS Martin does not have an office, or employee or agent in India and hence, no Permanent Establishment (PE) in India as per Article 5 of the India Nation L Double Taxation Avoidance Agreement (called India Nation L DTAA). As far as Indian taxation is concerned, it is a non-resident, as it is not covered under the provisions of section 6(3) of the Income-tax Act, 1961. DAS Martin is a resident of Nation L and is engaged in trading activities for the last two decades, with annual turnover of 2 million USD.

DAS Martin proposes to transfer in February, 2019, above 70% of the shareholding to another Singapore company called DAS Singapore, which is part of the Dow group, pursuant to Group reorganisation. Assume that this Case Study is being given to you for your opinion in January, 2019.

Objectives of transfer of shares in HPL by Dow Group

(i) Dow Group is a large and complex group having presence in several countries across the world. In order to reduce complexities, improve efficiency and reduce costs in group companies worldwide, Dow Group is transforming its holding model. The group reorganization will change the business model of the group giving the capability to support more diverse, growing business that is also expected to be more profitable in the long-term.

(ii) Prior to 2019, Dow group was divided in the following 5 areas depending on its geographical locations

- North America
- South America
- Europe
- Asia Pacific
- India, Middle East and Africa (Dow IMEA group)

(iii) In the beginning of year 2019, the IMEA group was dismantled and countries in IMEA group were realigned to other regions as per geographical convenience. The Asia pacific region now consists of countries like India, China and other South East Asian countries. The

Europe region, *inter alia*, consists of Mauritius, United Kingdom, Germany and other European countries.

(iv) In order to achieve objective of operational excellence and administrative convenience, it became necessary for the Dow groups to re-align the holding model of HPL.

(v) It is contemplated that the holding company of HPL would be shifted to Singapore, to achieve better control. Singapore is one of the upcoming countries in the Asia Pacific region. Keeping in view the above facts, Dow group is contemplating to shift the shareholding of HPL from Nation L to Singapore.

(vi) The Group believes that such re-alignment would help the Group to focus on customer service including support for new product launches, strong compliance culture, commitment to health, safety and the environment, and commitment to developing people that deliver strong results for the Group even as the external environment has become more demanding.

Related facts and aftermath of proposed transfer of shares

(i) Dow group proposes to achieve the above objective through its entity in Singapore i.e., DAS Singapore. DAS Singapore will be a 70% subsidiary of DAS Martin.

(ii) DAS Martin proposes to contribute shares held in HPL as its capital in DAS Singapore. By virtue of this, HPL India would become 70% subsidiary of DAS Singapore.

(iii) In view of above, DAS Martin proposes to transfer the shareholding (10 lakh shares) of HPL to DAS Singapore by way of capital contribution.

(iv) The value of DAS Singapore's shares recorded in the books of DAS Martin (equivalent amount in INR being 182.3 crores) would be considered as the sales consideration for transfer of shares of HPL.

(v) The cost at which DAS Martin has obtained the shares of HPL would be the cost of acquisition.

Payments made by HPL for advertisements

HPL has made the following payments to DAS Martin from April 2018 to December 2019:

(i) ₹ 43 lakhs for advertisements in foreign web sites;

(ii) ₹ 8 lakhs for space booking in foreign newspapers.

Installation projects undertaken by KTS Singapore in India

Another group company of DOW group, KTS Singapore, a company incorporated in Singapore 10 years back and having its tax residency there, has carried out four installation projects in India during the P.Y.2018-19.

These four projects are independent of each other and secured through four independent work orders. These are installation projects and executed using its two cranes which were imported from Singapore in November, 2017. To carry out the installation work, four to five

key personnel from Singapore are deployed, along with the local manpower. Prior to the present installation projects, the cranes were used for executing installation projects for XYZ Pvt. Ltd., India, in the Godavari basin.

The scope of work under these projects is similar and requires the Singapore entity to provide ground preparation details for the movement of cranes and obtain approval to the scheme under which erection is to be executed. The Load Movement Test on the crane is required to be organized. The holding of the equipments after erection before completion of welding of the column sections is required to be carried out. Setting up, fitting, placing, positioning of the fabricated equipments at the site is, thus, required to be carried out.

One of these four projects was from 1st April, 2018 and was for a period of 173 days. Another project, undertaken for some other client, was from 1st August, 2018 and was for 170 days. The other two projects were for a period of 90 days each, falling within the above periods only.

Exhibit 1

Article 13 of the India Nation L DTAA which deals with the taxation of capital gains arising to the resident of contracting state, reads thus:

"ARTICLE 13 - Capital Gains -

1. Gains from the alienation of immovable property, as defined in paragraph (2) of article 6, may be taxed in the Contracting State in which such property is situated.
2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State or of movable property pertaining to a fixed base available to a resident of a Contracting State in the other Contracting State for the purpose of performing independent personal services, including such gains from the alienation of such a permanent establishment (alone or together with the whole enterprise) or of such a fixed base, may be taxed in that other State.
3. Notwithstanding the provisions of paragraph (2) of this article, gains from the alienation of ships and aircraft operated in international traffic and movable property pertaining to the operation of such ships and aircraft, shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.
4. Gains derived by a resident of a Contracting State from the alienation of any property other than those mentioned in paragraphs (1), (2) and (3) of this article shall be taxable only in that State.

For the purposes of this article, the term "alienation" means the sale, exchange, transfer, or relinquishment of the property or the extinguishment of any right therein or the compulsory acquisition thereof under any law in force in the respective Contracting States."

Exhibit 2

India Singapore DTAA

ARTICLE 5: "PERMANENT ESTABLISHMENT:

1. For the purposes of this Agreement, the term "permanent establishment" means a fixed place of business through which the business of the enterprise is wholly or partly carried on.
2. The term "permanent establishment" includes especially: .....
3. A building site or construction, installation or assembly project constitutes a permanent establishment only if it continues for a period of more than 183 days in any fiscal year.
4. An enterprise shall be deemed to have a permanent establishment in a Contracting State and to carry on business through that permanent establishment if it carries on supervisory activities in that Contracting State for a period of more than 183 days in any fiscal year in connection with a building site or construction, installation or assembly project which is being undertaken in that Contracting State.
5. Notwithstanding the provisions of paragraphs 3 and 4, and enterprise shall be deemed to have a permanent establishment in a Contracting State and to carry on business through that permanent establishment if it provides services or facilities in that Contracting State for a period of more than 183 days in any fiscal year in connection with the exploration, exploitation or extraction of mineral oils in that Contracting State."

ARTICLE 7: BUSINESS PROFITS:

"The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is directly or indirectly attributable to that permanent establishment."

2. (a) **Multiple choice questions** ***(10 x 2 = 20 Marks)***

Choose the most appropriate alternative for the following:

(Alternative to be given only in capital letters A, B, C or D):

(i) In respect of payments effected by HPL to DAS Martin, the total withholding tax (ignoring DTAA provisions) required to be made is

(A) ₹ 5,07,600

(B) ₹ 5,17,920

(C) ₹ 4,24,400

(D) Insufficient data/information to compute

(ii) Relating to the installation projects, KTS Singapore offered payment of ₹ 1,20,000 to CA Akash Kumar, who did not receive it, but directed the company

to give it to Children India, an unregistered entity engaged in charitable' activities. The said amount of ₹ 1,20,000 is

(A) Taxable in the hands of CA Akash Kumar only;

(B) Taxable in the hands of CA Akash Kumar as well as Children India;

(C) Taxable only in the hands of Children India;

(D) Taxable neither in the hands of CA Akash Kumar nor Children India.

(iii) The provisions relating to taxation of indirect transfer of shares of an Indian company were introduced vide Finance Act, 2012, as an aftermath of the decision of the Apex Court in

(A) McDowell & Co. Ltd. *vs.* CTO;

(B) Union of India *vs.* Azadi Bachao Andolan;

(C) Vodafone International Holdings B.V. *vs.* UOI;

(D) CIT *vs.* Yokogawa India Ltd.

(iv) If, in the given Case Study, DAS Singapore happens to be a subsidiary of DSA USA (A US company), the transfer of shares in HPL to DAS Singapore will be governed by the provisions of

(A) India US DTAA;

(B) India Nation LDTAA;

(C) India Singapore DTAA;

(D) USA Singapore DTAA.

(v) If it is held that the transfer of shares in HPL by DAS Martin to DAS Singapore is chargeable to tax in India, ignoring the DTAA provisions, the rate of tax applicable (without surcharge or cess) is

(A) 30%;

(B) 10%;

(C) 20%;

(D) None of the above

(vi) Assuming that the FMV of the shareholding in HPL in the hands of DAS Martin is ₹ 192.3 crores, regardless of the taxability of the capital gain in India.

(A) DAS Singapore alone will be liable to tax in India for ₹ 10 crore u/s 56(2) in respect of the difference between FMV and the consideration given to DAS Martin;

(B) DAS Martin alone will be liable to tax u/s 56(2) in India for ₹ 10 crore in respect of the difference between FMV and the consideration received by DAS Martin;

(C) DAS Singapore will not be liable to tax in India u/s 56(2) for ₹ 10 crore in respect of the difference between FMV and the consideration given to DAS Martin;

(D) Neither DAS Martin nor DAS Singapore will be liable to tax in India under section 56(2).

(vii) HPL is bound to report details with respect to transfer of shares by DAS Martin to DAS Singapore in the following Form:

(A) Form 49D;

(B) Form 3CT;

(C) Form 3CTA;

(D) There is no reporting requirement on HPL to report the transfer of the shareholding.

(viii) If DAS Martin happens to be a resident of two Contracting States, namely, Nation L being the place of effective management and also Nation M being the place of incorporation, then, it will be treated as resident of Country L as per the

(A) US Model Convention;

(B) OECD Model Convention;

(C) UN Model Convention;

(D) Both options (B) as well as (C)

(ix) In order to determine the residence of an individual, the following factor is not taken cognizance of under the OECD Model Convention:

(A) Centre of vital interests;

(B) Habitual abode;

(C) Own house in Chennai given on rent for the past twelve years;

(D) Flat taken on rent in Noida where the individual is living for the last twelve years.

(x) If DAS Martin happens to be a resident of two Contracting States, namely, Nation L, being the place of effective management, and also Nation M, being the place of incorporation, then, it will be treated as resident of either Nation L or Nation M, as per the -

(A) US Model Convention only

(B) OECD Model Convention

(C) UN Model Convention

(D) Both options (B) and (C)

(b) Descriptive questions:

(i) The management of DAS Martin wishes to know whether the proposed transfer of shares in HPL to Das Singapore can be regarded as a device or scheme to avoid income-tax in India and whether GAAR can be invoked. ***(5 marks)***

(ii) Examine whether the gains arising from the transfer will be taxable in India, when the former does not have a PE in India, per Article 13 - India Nation L DTAA (Exhibit 1) and in light of the provisions of Article 13 of the said Treaty. ***(4 marks)***

(iii) State whether the provisions of section 92 to section 92F of the Income-tax Act, 1961 ("the Act") relating to transfer pricing would still be applicable in respect of the transfer of shares by DSA Mauritius to DSA Singapore[3]. ***(3 marks)***

(iv) Examine whether the sale consideration receivable by DAS Martin should suffer any withholding tax in India as per section 195 of the Act. ***(3 marks)***

(v) Is DAS Martin required to file return of income in India under section 139(1) of the Act? ***(4 marks)***

(c) In respect of the payments made by HPL to DAS Martin, discuss the applicability of equalization levy. ***(5 marks)***

(d) Can KTS Singapore be considered to have a PE in India, in terms of the India Singapore DTAA and can the profits from the installation projects undertaken in India be taxed in India ? ***(6 marks)***

Solution to Case Study 2

Answer to Q.(a)

Q. No.	Answer
(i)	(D)
(ii)	(B)
(iii)	(C)
(iv)	(B)
(v)	(B)

Q. No.	Answer
(vi)	(A)
(vii)	(D)
(viii)	-[4]
(ix)	(C)
(x)	(D)

[3] To be read as DAS Martin to DAS Singapore

[4] As per para 3 of Article 4 of the OECD and UN Model Convention, 2017, if DAS Martin happens to be a resident of two contracting states, the competent authorities of the Contracting States, i.e., Nation M and Nation L shall endeavour to determine by mutual agreement the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention, having regard to its place of effective management, the place where it is incorporated and any other relevant factor. As per para 4 of Article 4 of the US Model Convention 2016, where by reason of the provisions of paragraph 1 of this Article, a company is a resident of both Contracting States, such company shall not be treated as a resident of either Contracting State for purposes of its claiming the benefits provided by this Convention. Therefore, none of the options are correct.

Answer to Q.(b)

(i) As per section 95, an arrangement entered into by an assessee may be declared to be an impermissible avoidance arrangement and the consequence in relation to tax arising therefrom may be determined subject to the provisions of GAAR, if the main purpose or one of the main purposes of which is to obtain a tax benefit and which satisfies any of the following tests:

- creates rights, or obligations, which are not ordinarily created between persons dealing at arm's length;
- results, directly or indirectly, in the misuse, or abuse, of the provisions of this Act;
- lacks commercial substance or is deemed to lack commercial substance under section 97, in whole or in part or
- is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for bona fide purposes

In the present case, in the absence of the DTAA between India and nation L, the capital gains arising in the hands of DAS Martin would be chargeable to tax in India, since such income would be deemed to accrue or arise in India on account of capital assets (70% shares in HPL), being situated in India.

Moreover, the transfer of shares in HPL by DAS Martin to another Singapore company i.e., DAS Singapore is pursuant to group reorganisation and to achieve the objectives like reducing complexities, achieving operational excellence, etc.

The shares were acquired 18 years back for a substantial cost of about ₹ 50.3 crores. The investment made in the HPL was with the prior approval of Department of Industrial Policy & Promotion (DIPP) and RBI permission was also obtained.

From the above facts, it is evident that the arrangement of transferring the shares held in HPL, an Indian company, to DAS Singapore by way of capital contribution is not for the purpose of obtaining any tax benefit, since such capital gains are chargeable to tax in India, in the absence of beneficial provisions of the DTAA.

Further, the purpose of entering into such arrangement does not satisfy any of the objectives due to which arrangement would be deemed as impermissible avoidance arrangement.

Thus, in the present case, the proposed transfer of shares in HPL to DAS Singapore cannot be regarded as device or scheme to avoid income-tax in India and hence, GAAR cannot be invoked.

(ii) The capital gains arising in the hands of DAS Martin would be chargeable to tax in India, since such income would be deemed to accrue or arise in India on account of capital assets (70% shares in HPL), being situated in India.

Article 13(4) of the India-Nation L DTAA provides that gains derived by a resident of a contracting State (DAS Martin, resident of Nation L) from the alienation of any property (Shares in HPL) would be taxable only in that State i.e., Nation L.

Section 90(2) provides that where a double taxation avoidance treaty is entered into by the Government, the provisions of the Income-tax Act, 1961 would apply to the extent they are more beneficial to the assessee. In other words, if the DTAA provisions are more beneficial, the same will apply.

Thus, applying Article 13(4) of the tax treaty between India and Nation L, capital gains arising in the hands of DAS Martin would be taxable only in Nation L and hence, such capital gains would not be taxable in India.

(iii) Unless the transaction is taxable in India, there would be no application of transfer pricing provisions under sections 92 to 95. Section 92 is not an independent charging section and would be applicable only if there is any chargeable income arising from the international transaction.

Since by virtue of Article 13(4) of the DTAA between Nation L and India, the capital gains arising from transfer of shares of HPL by DAS Martin to DAS Singapore are taxable only in Nation L, the same would not be subject to tax in India. Accordingly, the transfer pricing provisions contained under sections 92 to section 95 would not apply.

Hence, the transfer pricing provisions contained in sections 92 to 95 would not be applicable in respect of transfer of shares of HPL by DAS Martin to DAS Singapore.

Note: *The aforesaid view has been taken in Dana Corporation [2010] 321 ITR 178 (AAR), Praxair Pacific Limited 326 ITR 276 and Vanenburg Group B.V. vs. CIT 289 ITR 464.*

(iv) Under section 195(1), the obligation to deduct tax at source from interest and other payments to a non-resident, which are chargeable to tax in India, is on "any person responsible for paying to a non-resident or to a foreign company".

For section 195 to apply, there should be income chargeable to tax in India, in the given situation.

Explanation 2 to Section 195(1)clarifies that the obligation to comply with section 195(1) and to make deduction thereunder applies and shall be deemed to have always applied and extends and shall be deemed to have always extended to all persons, resident or non-resident, whether or not the non-resident has:

(a) a residence or place of business or business connection in India; or

(b) any other presence in any manner whatsoever in India.

However, by virtue of the DTAA between India and Country L, in this case, the capital gains would be chargeable to tax only in Country L. The same would not be taxable in India.

Thus, in the present case, DAS Singapore, being a non-resident foreign company is not required to withhold tax on the sale consideration payable to DAS Martin, since capital gains is not taxable in India as per the DTAA between India and Country L.

(v) As per section 139(1), every person*, inter alia*, being a company, is required to furnish a return of income of his income during the previous year, in the prescribed form and verified

in the prescribed manner and setting forth such other particulars as may be prescribed, on or before the due date specified thereunder.

Unlike individuals, in the case of firms/companies, there is no stipulation that such obligation will arise only where the total income exceeds the maximum amount not chargeable to tax. Even if the total income is nil, a company, including foreign company, will have to furnish the return of income.

By virtue of section 9(1)(i), capital gain arising on transfer of shares held in HPL, an Indian company, would be deemed to accrue or arise in India in the hands of DAS Martin during the previous year 2018-19.

There is no specific exemption provided under any provisions of the Income-tax Act, 1961 in respect of such income or allowing a foreign company from not filing the return of income under certain circumstances like the present situation where the income is not chargeable to tax in India due to DTAA provisions.

Hence, it is required to furnish return of income on or before the due date, even though DAS Martin is non-resident in India.

The aspect that such income is not taxed in India in the hands of DAS Martin by virtue of the India Country L DTAA does not remove the obligation of DAS Martin to file its return of income in India. In fact, for claiming the benefit of section 90, DAS Martin has to file its return of income in India.

Answer to Q.(c)

Chapter VIII of the Finance Act, 2016, "Equalisation Levy", provides for an equalisation levy of 6% of the amount of consideration for specified services received or receivable by -

- a non-resident not having permanent establishment in India: here, DAS Martin is a non-resident which does not have a PE in India;
- from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India: here, HPL is a resident in India carrying on business.

"Specified Service" means

(1) online advertisement;

(2) any provision for digital advertising space or any other facility or service for the purpose of online advertisement and

(3) any other service as may be notified by the Central Government.

Since only online advertisement or any provision for digital advertising space for the purpose of online advertisement included within the meaning of specified services, the equalisation levy @6% would be applicable only on the amount of ₹ 43,00,000, paid for advertisements in foreign websites, to DAS Martin, a non-resident not having a PE in India.

Hence, equalisation levy would not apply on the payment of ₹ 8 lakhs made by HPL to DAS Martin for space booking in foreign newspapers.

Answer to Q.(d)

As per Article 5(3) of India Singapore DTAA, a building site or construction, installation or assembly project constitutes a PE only if continues for a period of more than 183 days in any fiscal year.

Further, as per Article 7, the profits of an enterprise of a Contracting State (Singapore, in the present case) shall be taxable only in that State i.e., Singapore, unless the enterprise carries on business through PE situated therein in the other Contracting State (India, in the present case).

The nature and purpose of the activities undertaken in the four projects relates to installation and assembly projects and are covered under Article 5.3 of the DTAA. The controversy whether Article 5.3 or 5.4 will apply does not exist, as it is clear that the activities of KTS Singapore relates to installation and assembly projects.

During the previous year 2018-19, KTS Singapore has carried out four independent installation projects in India. One of these projects was continued for a period of 173 days, another project continued for 170 days and other two projects were continued for a period of 90 days each.

All these are independent projects and there is no inter-connection and inter-dependence amongst them. None of them appears to be an extension of another. Therefore, the duration test for installation and assembly projects provided under Article 5.3 of the DTAA cannot be construed to be read for all the projects that do not pass the test of cohesiveness, inter-connection and inter-dependence.

Since none of the installation projects undertaken by KTS Singapore continued for a period of more than 183 days, such projects cannot constitute PE for KTS Singapore.

Consequently, profits from such installation projects undertaken in India would not be taxed in India and will only be taxed in Singapore.

Case Study 3

FMG Associates is a firm of Chartered Accountants at Jaipur. It has received queries from its clients and for which it has to provide solutions. All the facts relate to A.Y.2019-20.

Resident Ramji with income outside India

Mr. Ramji an individual resident in India furnished details of his global income for the previous year 2018-19.

Income from business carried on in India ₹ 8,00,000

Agricultural income in Sri Lanka (in Sri Lanka Rupee) 1,00,000

Dividend income from a company incorporated in USA (declared on 10.1.2019) US $ 20,000

Royalty income from a detective novel published in country Sri Lanka (in Sri Lanka Rupee) 7,00,000

Income from house property in the country USA US $ 10,000 Business income from Sri Lanka (in Sri Lanka Rupee) 4,00,000

***Note**: All the foreign incomes were repatriated to his bank account in India in April, 2019 except business income earned outside India. Assume the accounting year is uniform for all the countries and tax payable in foreign country was paid, wherever it was taxable.*

The **synopsis** of the relevant Article of the **DTAA between India and USA** regards taxation of property income and dividend income is given below:

(1) Income derived by a resident of a Contracting State from immovable property, situated in the other Contracting State may be taxed in that other State.

Assume rate of tax in USA 30% and in India at slab rate.

(2) Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident.

Assume rate of tax in USA@25% and in India at slab rate.

The **synopsis** of the relevant Article of the **DTAA between India and Sri Lanka** as regards taxation of agricultural income, business income and royalty income are given below :

(1) Income derived by a resident of a Contracting State from immovable property (including income from agricultural land) situated in the other Contracting State may be taxed in that other Contracting State.

(2) The profits of an enterprise of a 'Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profit of the enterprise may be taxed in the other State but only so much as is attributable to that permanent establishment.

Assume rate of tax in Sri Lanka @20% and in India @ slab rate.

(3) Royalties arising in a Contracting State and paid to resident of the other Contracting State may be taxed in that other State. However, such royalties may also be taxed in the Contracting State at a rate not exceeding 10% of the gross amount of royalty.

Assume rate of tax in Sri Lanka @10% and in India @10% for non-residents and regular rate for residents.

Exchange rates

TT Buying Rate	Sri Lanka Rupee	US Dollars
31.03.2019	INR 1 = 2.54 LKR	1 US dollar = 70 INR
31.12.2018		1 US dollar = 71 INR

Ramji's son Pramod (age 23) is employed in ESS Softwares Ltd, Bengaluru. He was sent on deputation to USA on 10.01.2017 to attend to onsite duties and he returned to India on 05.01.2019. He was paid per diem allowance at USA which was adequate enough to meet his living expenses there. His salary of ₹ 27 lakhs after deducting his PF contribution of ₹ 1,80,000, was credited to his bank account at Bengaluru during the previous year 2018-19.

Non-Resident company seeking AAR

PQR Inc. of Germany is supplying technical know-how to be used by Mayur Co Ltd, Mumbai for manufacture of combustion engine at Nagpur. The agreement for supply of technical know-how is in return for royalty and was signed on 10.05.2017. The royalty exceeded ₹ 10 crore for the assessment year 2017-18. Mayur Co Ltd filed its return of income on 30th August, 2018 and approached AAR in September, 2018 as regards withholding tax on royalties paid to PQR Inc., Germany. The application of Mayur Co Ltd was admitted by AAR in November, 2018. The Assessing Officer issued a notice under section 143(2) on 10.01.2019. The foreign company PQR Inc. also applied for advance ruling on 20.01.2019 to know its tax liability in respect of its royalty income received from Mayur Co Ltd.

Mayur Co Ltd has a branch office in Sri Lanka. It exported goods worth ₹ 5 crores by raising invoice for ₹ 4.40 crores. It gave advance of ₹ 1 crore to its branch in Sri Lanka out of the loan obtained by it from State Bank of India. It did not charge any interest though the borrowing cost attributable for the advance is ascertained at ₹ 7,40,000 for the year ended 31.03.2019.

PQR Inc. has the following incomes in India for the year ended 31st March, 2019:

(i) Dividend income from Indian listed companies ₹ 12,50,000;

(ii) Royalty income from Roger Moore (P) Ltd, Cochin ₹ 8,40,000. The royalty agreement was made in accordance with the policy of the Government of India. The DTAA between India and Germany provides for taxing the royalty at 10%;

(iii) Interest ₹ 5,50,000 received on global depository receipts purchased in foreign currency from ABC Ltd; and

(iv) Interest ₹ 3,20,000 received from an infrastructure debt fund referred to in section 10(47).

Mayur Co Ltd. has 30% shareholding by way of 3 lakh equity shares of € 10 each in Botham Ltd of Spain. In December, 2018, Botham Ltd. declared dividend at 10% on the face value of shares. Mayur Co Ltd. received ₹ 22 lakhs on repatriation of the dividend amount to its bank account in India.

Mayur Co Ltd. is contemplating to transfer the shareholding in Botham Ltd. to a subsidiary company to be incorporated in yet another country and by virtue of the DTAA between that country and Spain, such dividend income will become tax-free. Presently, such dividend income is taxable in India as per DTAA between India and Spain. This plan of transferring the shares by forming the subsidiary company in foreign country is in nascent stage.

Tax dispute of Vijay Jain

Vijay Jain, a resident of India, exported goods to foreign country by under invoicing the sale consideration and accumulated wealth outside India. Based on Tax Information Exchange Agreement between India and Bermuda, a notice for assessment of the undisclosed foreign income under The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 was issued in March, 2017. The assessee disputed the issue of notice. The Assessing Officer called for details and proceeded with the assessments. There was change in incumbent and the successor continued the assessment proceedings without issuing a fresh notice to the assessee. Vijay Jain moved writ before the High Court in March, 2018 for quashing the proceedings. The Court, vide its order dated 31.03.2018, stayed the proceedings up to 31.12.2018. Vijay Jain had to pay ₹ 8 lakhs towards tuition fees and hostel expenses of his son studying in USA.

Proposal for e-sale of books in India

XY Co Publishers Ltd, United Kingdom, is a reputed scientific book publisher with global presence. The company decided to penetrate the Indian market by procuring orders online. The company anticipates the online booking to pick up in due course of time. It is planning to dispatch goods from the warehouse in Kolkata based on the orders received. There would be no direct sale to any of the customers in India from the warehouse in Kolkata. The amounts have to be paid online by the buyers directly to the bank account of XY Co Publishers Ltd maintained in London. It is contemplating to have a website and server in India owned by it or avail the same of an outside entity for its online business in India.

Advertisement expenditure of Chetan Ltd

Chetan Ltd, Mysore is a 100% subsidiary of Beijing Ltd of Chicago, USA. It acted as the distributor of world famous mobile handsets by brand name "Chicago" manufactured by parent company viz. Beijing Ltd. During the previous year 2018-19, Chetan Ltd remitted the amounts due to Beijing Ltd in settlement of the invoices by furnishing necessary forms prescribed under Income-tax Rules, 1962. The agreement between the companies envisages that 5% of the sale consideration realized by Chetan Ltd. must be spent towards advertisement of "Chicago", being the brand name of the mobile handsets.

Each handset was invoiced @ ₹ 15,000 for Chetan Ltd. and whereas it was invoiced at ₹ 13,000 to unrelated parties. Chetan Ltd. sold 40,000 handsets in the previous year 2018-19 at the average price of ₹ 16,000 per handset. The credit period allowed by Beijing Ltd was 3 months for Chetan Ltd and whereas for other dealers, it was given against full payment. The cost of capital may be taken as 12% per annum and the purchases as uniform throughout the year. Beijing Ltd. charged ₹ 1500 per handset as warranty charges and whereas for unrelated parties it charged ₹ 2000. The assessee selected Beijing Ltd as tested party for comparing controlled and uncontrolled transactions.

Chetan Ltd spent ₹ 3 crores towards advertisement expenses in India. The Assessing Officer applied "Bright Line Test" and wants to add back 50% of the expenditure as towards brand

building of parent company's product while determining the arm's length price.

BB Co Ltd. of Chennai is an associated enterprise of Chetan Ltd. It exported the semi-finished textile goods to Pick Inc, Singapore. The goods were further processed and sold to yet another 100% subsidiary of BB Co Ltd viz. Sea Ltd. at Sydney, Australia for reaching the customers therein. BB Co Ltd wants to apply for advance pricing agreement to" protect itself and its subsidiaries.

Choose the most appropriate alternative for the following MCQs : ***(10 x 2 = 20 Marks)***

3.1 The objective of Tax Information Exchange Agreements entered into by the Central Government with various countries is to enable -

(A) certainty in tax levy between countries

(B) concessional levy of tax for the same income between them

(C) investigation of cases of tax evasion or avoidance

(D) mobilization of tax from non-residents

3.2 What is the time limit within which the assessment of Vijay Jain has to be completed under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 from the facts given?

(A) 31.03.2019

(B) 31.12.2019

(C) 31.12.2020

(D) 31.03.2021

3.3 The amount of dividend income earned by Mayur Co Ltd. from Botham Ltd. of Spain is chargeable to tax in India @_____ and it is covered by action plan of BEPS.

(A) 10% and 4

(B) 15% and 4

(C) 15% and 3

(D) 20% and not covered

3.4 How will DTAAs prevent treaty shopping / abuse such as the one contemplated by Mayur Co Ltd.?

(A) Protocols in DTAA

(B) Provision in domestic law

(C) Limitation of Benefit clause in DTAA

(D) Conduit rulings

3.5 The APA that would be applicable to BB Co Ltd for protecting itself and its two subsidiaries in Singapore and Australia for avoiding litigation in transfer pricing regulations, would be

(A) Multi-lateral APA

(B) Bilateral APA

(C) Unilateral APA

(D) None, as it is not possible

3.6 The selection and rejection of comparable in India is carried out through

(A) Deductive approach

(B) Detective approach

(C) Additive approach

(D) Primitive approach

3.7 How much is the penalty payable by Vijay Jain for failure to furnish the prescribed form for remittance of tuition fees to his son?

(A) Nil

(B) ₹10,000

(C) ₹ 50,000

(D) ₹1,00,000

3.8 What is the residential status of Pramod for the assessment year 2019-20?

(A) Non-resident

(B) Resident and ordinarily resident

(C) Resident but not ordinarily resident

(D) None of the above

3.9 How much is to be adjusted to the total income of the Mayur Co Ltd. by applying transfer pricing regulations for the transactions carried out with its Sri Lanka branch office?

(A) ₹ 60,00,000

(B) ₹ 7,40,000

(C) ₹ 67,40,000

(D) Nil

3.10 Which part of Form No.15CA is to be filled up and filed by Chetan Ltd for import of handsets from Beijing Ltd.?

(A) Part A and B

(B) Part B and C

(C) Part A and C

(D) Part D

You are required to answer the following issues:

3.11 Compute the total income of resident Ramji for the assessment year 2019-20 by allowing foreign tax credit wherever applicable in the light of DTAA provisions. ***(6 marks)***

3.12 Pramod claims the salary income earned outside India up to 05.01.2019 is not chargeable to tax in India. Decide the validity of his contention. ***(2 marks)***

3.13 Is the application filed by Mayur Co Ltd seeking advance ruling permissible in law ? Also, decide whether the foreign company PQR Inc. can seek advance ruling when the application of Mayur Co Ltd is pending ? ***(4 marks)***

3.14 With brief reasons for treatment of the items, you are requested to compute the tax liability of PQR Inc. for the assessment year 2019-20. ***(4 marks)***

3.15 The assessee wants to know the forms to be obtained from the Chartered Accountant and filing of the same before the income-tax authorities. In respect of tuition fee paid by Vijay Jain for his son. Advise him suitably. ***(4 marks)***

3.16 Advise whether XY Co Publishers Ltd should have a website and server owned by it or avail the same from an outsider in the context of Income-tax Act, 1961. ***(4 marks)***

3.17 Compute the arm's length price adjustment for Chetan Ltd ignoring any adjustment towards advertisement expenditure. ***(4 marks)***

3.18 Is the Assessing Officer justified in applying "Bright Line Test" for disallowing or adjusting the advertisement expenditure in computing arm's length price ? ***(2 marks)***

Solution to Case Study 3

Answer to Q.3.1 to 3.10

Q. No.	Answer
3.1	(C)
3.2	(B)
3.3	(C)
3.4	(C)
3.5	(A)

Q. No.	Answer
3.6	(A)
3.7	(A)
3.8	(B)
3.9	(D)
3.10	(B)

Answer to Q.3.11

Computation of total income of resident Ramji for the A.Y.2019-20		
Particulars	₹	₹
Income from house property		
Annual Value of house in USA = $ 10,000 x 70	7,00,000	
Less: Deduction@30%	2,10,000	
		4,90,000
Profits and gains of business or profession		
Income from business carried on in India	8,00,000	
Business income in Sri Lanka (4,00,000 LKR/2.54) [Taxable only in Sri Lanka – Hence, not included in computation of total income][5]	Nil	
Income chargeable under this head		8,00,000
Income from Other Sources		
Agricultural income in Sri Lanka (1,00,000 LKR/2.54)	39,370	
Dividend income from a company incorporated in the USA ($ 20,000 x 71) – Since dividend was declared on 10.1.2019, the rate as on 31.12.2018 has to be considered for conversion.	14,20,000	
Royalty income from a detective novel published in Sri Lanka (7,00,000 LKR/2.54)	2,75,591	
Income chargeable under this head		17,34,961
Gross Total Income		**30,24,961**
Less: **Deductions under Chapter VI-A**		
Section 80QQB [Royalty income from detective novel[6]]		2,75,591
Total Income		**27,49,370**

Answer to Q.3.12

Mr. Pramod has stayed in India for 86 days [27 days (January) +28 days (February) + 31 days (March)] in the P.Y.2018-19. During the four preceding previous years, i.e., from P.Y.2014-15 to P.Y.2017-18, he has been in India for 1015 days [i.e., 365 days in P.Y.2014-15, 365 days in P.Y.2015-16, 285 days in P.Y.2016-17 and 0 days in P.Y.2017-18]. Mr. Pramod is a resident in

[5] Alternatively, the income can first be included in total income to determine the rate of tax on remaining income as per Article 23(2) of the India-Sri Lanka DTAA.

[6] Assuming that the same is in the nature of literary work

India for A.Y.2019-20, since his stay in India is for more than 60 days in the P.Y.2018-19 and more than 365 days in the four preceding previous years.

Also, he is resident and ordinarily resident in India since his stay in India has exceeded 730 days in the seven immediately preceding previous years and he has been resident in 2 or more previous years out of 10 immediately preceding previous years.

In case of a resident and ordinarily resident, global income would be taxable in India. Hence income from salary earned in USA (including per diem allowance) would be taxable in India under the provisions of the Income-tax Act, 1961.

Note *– (1) The second condition of 60 days in the P.Y.2018-19 + 365 days in the 4 preceding previous years for determining his residential status will apply to him since he is an Indian citizen who, being outside India, has returned to India during the P.Y.2018-19. Only if he is visiting India, will the second condition not apply.*

(2) This answer is based on the provisions of the Income-tax Act, 1961. Since the relevant extract of the India-US DTAA is not given in the question, the same has not been considered for the purpose of answering this question.

Answer to Q.3.13

A resident applicant can make an application for advance ruling for determining the tax liability of a non-resident arising out of a transaction which has been undertaken or is proposed to be undertaken by the resident applicant with such non-resident.

Therefore, Mayur Co. Ltd., a resident, can file an application for advance ruling for determining the rate of withholding tax on royalties paid to a non-resident, PQR Inc. Germany.

Even though it has filed its return of income on 30.8.2018, since notice under section 143(2) has been issued on 10.1.2019 only after the application for advance ruling was made in September, 2018, it would not be treated as a case where an application is pending before the income-tax authority. This is because the application was not pending before the income-tax authority on the date of making the application for advance ruling. It was so held in *Sin Oceanic Shipping ASA vs. AAR (2013) 357 ITR 102 (Delhi)*.

Therefore, the application filed by Mayur Co. Ltd. seeking advance ruling is permissible in law.

Permissibility of PQR Inc., a foreign company, seeking advance ruling when application filed by Mayur Co. Ltd. is pending before the AAR

The application filed by Mayur Co. Ltd. is pending before the AAR for ruling. The issue in respect of which PQR Inc. wants to file an application is the same issue for which Mayur Co. Ltd. has already made an application.

The Income-tax Act, 1961 does not contain any specific provision debarring the non-resident from making an application to the AAR where the application by the resident is pending before

the AAR. However, there is no requirement for filing the same, since the said issue has already been raised by the resident applicant for the same transaction.

Therefore, it is advisable that PQR Inc. does not file an application in respect of the same transaction to the AAR.

Answer to Q.3.14

Computation of tax liability of PQR Inc., a German Company, in India for A.Y.2019-20

	Particulars of Income	Tax treatment	Tax liability (₹)
(i)	Dividend income of ₹12,50,000 from Indian listed companies	Exempt u/s 10(34), since the same is subject to dividend distribution tax u/s 115-O. Section 115BBDA is not attracted in case of a foreign company which is non-resident in India.	Nil
(ii)	Royalty of ₹ 8,40,000 from Roger Moore (P) Ltd., Cochin	Subject to tax@10% as per India-Germany DTAA (DTAA rate is inclusive of cess)	84,000
(iii)	Interest of ₹ 5,50,000 on GDRs purchased in foreign currency from ABC Ltd.	Subject to tax@10.4% [i.e., 10% as per section 115AC plus cess@4%]	57,200
(iv)	Interest of ₹ 3,20,000 received from infrastructure debt fund referred to in section 10(47)	Subject to tax@5.2% [i.e., 5% as per section 115A plus cess@4%]	16,640
		Total tax liability	**1,57,840**

Answer to Q. 3.15

Section 195(6) requires the person responsible for paying to a non-corporate non-resident or a foreign company, any sum, whether or not chargeable under the provisions of the Income-tax Act, 1961, to furnish the information relating to payment of such sum in Form 15CA and 15CB.

As per Rule 37BB(2), the person responsible for paying to a non-corporate non-resident, or to a foreign company, any sum which is not chargeable under the provisions of the Income-tax Act, 1961, shall furnish the information in Part D of Form No.15CA.

Rule 37BB(3), however, provides that no information is required to be furnished for any sum which is not chargeable under the provisions of the Act, if, *inter alia*, the remittance is of the nature specified in the specified list given thereunder.

Payment of tuition fees by Vijay Jain for his son studying abroad is not income chargeable to tax in the hands of his son. Further, since the remittance is in the nature finding place in the specified list given in Rule 37BB(3)(ii), no information is required to be furnished in respect thereof in Part D of Form No.15CA or Form 15CB.

Hence, there is no form is required to be obtained from Chartered Accountant and filed before income-tax authorities.

Answer to Q.3.16

The concept of "business connection" assumes significant importance in the context of the Income-tax Act, 1961. The scope of business connection has now been expanded to include "significant economic presence" in India.

"Significant economic presence" means systematic and continuous soliciting of business activities or engaging in interaction with such number of users in India through digital means, *inter alia*, through websites with the help of servers owned by the assessee or a third person. The Rules in this regard are yet to be notified.

It is possible that transacting business in India by availing the services of website and server, irrespective of its location, would fall within the meaning of "significant economic presence" and hence, constitute business connection, in which case, the income would be taxable in India. However, since the number of users in India are yet to be prescribed, business connection would be established only if users are of the prescribed number.

***Note [Alternate Answer]** : As per section 92F(iiia), "permanent establishment" includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.*

Existence of website by itself would not constitute a PE. Where the website is being used as a virtual office for transacting orders of purchases or sales, then, it could be regarded as a permanent establishment, if the server supporting the website is located in India.

In this case, since XY Co. Publishers Ltd., UK, wants to procure online orders from Indian customers, for which payment has to be made online by them, the website and server owned by them in India would constitute a permanent establishment. A warehouse set up in India may not constitute a PE in this case, since only delivery of goods is being effected through the warehouse and there is no direct sale of goods by the warehouse.

Therefore, XY Co. Publishers Ltd. should avail the services of website and server from an outsider.

Answer to Q.3.17

Arms' length adjustment for Chetan Ltd.	
Particulars	**₹**
Price charged by Beijing Ltd. to unrelated parties	13,000

Add: Excess billing to Chetan Ltd. attributable to 3 months credit provided [₹ 15,000 x 3/12 x12/100]	450
	13,450
Less: Difference in warranty charges [₹ 2,000 – ₹ 1,500] to be deducted, since the warranty charges were lower for Chetan Ltd.	500
Arm's length adjustment to be made in the price of each handset	12,950
Price charged from Chetan Ltd.	15,000
Arm's length adjustment for each handset	2,050

Arm's length adjustment for 40,000 handsets[7] = 40,000 x ₹ 2,050 = ₹ 8,20,00,000

Answer to Q.3.18

The issue under consideration is whether bright line test can be used by the Assessing Officer to determine the excess/non-routine advertising, marketing and promotion (AMP) expenditure incurred by the taxpayer for building brand of its associated enterprises in India.

The Delhi High Court, in *Bausch & Lomb Eyecare (India) (P.) Ltd. v. Addl. CIT [2016] 381 ITR 227, held that a*dvertisement expense is not an international transaction and there is no machinery provision for computation of AMP expense adjustment.

In *Sony Ericsson Mobile Communications India (P) Ltd v. CIT (2015) 374 ITR 118,* the Delhi High Court held that bright line test has no statutory mandate and a broad-brush approach is not mandated or prescribed. It further opined that the exercise to separate "routine" and "non-routine" advertising, marketing and promotion or brand building exercise by applying the bright line test of non-comparables should not be sanctioned

Hence, applying the rationale of the above rulings of the High Court, the Assessing Officer is not justified in adopting the "Bright Line Test" for disallowing or adjusting the advertisement expenditure in computing arm's length price.

Note *– There are other court rulings on this issue, and the question can be answered on the basis of any such ruling(s).*

[7] In the absence of information in the question, it is assumed that the handsets supplied by Beijing Ltd. is 40,000, being the number of handsets sold by Chetan Ltd. in the P.Y.2018-19