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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 assumptions made or views taken.

PAPER 6C: INTERNATIONAL TAXATION

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

All questions relate to Assessment Year 2023-24, unless otherwise stated in the questions/case studies.

Case Study 1

I Co, an Indian company is engaged in the business of manufacture of packaging material having its manufacturing facility in India. I Co is a wholly owned subsidiary of Sing Co, a company incorporated in Singapore. Donald and Joe, citizens and residents of the United States of America, each of them hold 50% of the share capital of Sing Co. Donald and Joe, each had invested USD equivalent to INR 100 crores in Sing Co in April 2015.

Sing Co is set-up as a holding company for all the investments to be made by Donald and Joe in the region of Asia-Pacific. Sing Co, has following investments:

(i) 100% of Share Capital of J Co, a company in Japan.

(ii) 76% of Share Capital of T Co, a company in Thailand. Balance share capital of T Co is held by another resident and citizen of Thailand.

J Co and T Co are also engaged in the business of manufacture of packaging material.

Joe had also set-up an entity in Germany, G Co, in order to provide a loan to I Co. Joe holds 100% shar capital of G Co. At the time the loan was to be provided by G Co, there was some ambiguity under the exchange control laws in India as to whether such loan could be given. Therefore, G Co invested in fully Compulsorily Convertible Debentures ('CCD') of I Co, which is considered as equity investment under the exchange control laws in India. The amount of investment by G Co in the CCD of I Co in December 2005 is INR 0.50 crores. The terms of the CCD state that the CCDs shall be compulsorily converted into equity shares of I Co in December 2025 at the fair value at that time. Further, the terms of the CCD also state that till such time they are not converted, I Co would be required to pay the holder of the CCDs an interest at the rate of 5.4% p.a., every calendar year. The interest is due and payable on 31st December every year.

During FY 2021-22, in order to gain competitive advantage and to capture the global market, I Co had availed the assistance of UK Co to prepare its marketing campaign. UK Co is wholly owned by Rishi, a UK resident. Rishi is not related to Donald or Joe.

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, 2022.

As the preparation of the marketing campaign requires the team of UK Co as well as the in house marketing team of I Co to work closely, the marketing service agreement between I Co and UK Co requires employees of UK Co to visit India twice in a financial year, for 20-30 days each. For the said services, UK Co is paid GBP 300,000 for each visit. The number of days spent by the employees of UK Co during FY 2021-22 and FY 2022-23 in India under the marketing service agreement:

Month of visit	***Number of days of visit***
April 2021	*27*
December 2021	*30*
July 2022	*20*
March 2023	*25*

On 1st June 2022, Donald and Joe, having received an offer which they believe was fair, sold their entire stake in Sing Co to Rishi for USD equivalent to INR 350 crores each. In the same month, G Co sold the CCD of I Co to UK Co for INR 0.6 crores.

For the calendar year 2022, I Co in December 2022, paid interest of INR 0.27 crores on the CCDs to UK Co.

The accounting period of Sing Co is January to December, the relevant extract of the balance sheet of Sing Co as on 31st December 2021,1st June 2022 and 31st December 2022 are as follows:

Particulars	***As on 31st December 2021 (in INR crores)***	***As on 1st June 2022 (in INR crores)***	***As on 31st December 2022 (in crores)***
Details regarding Sing Co			
Book value of assets	*1,000*	*1,300*	*1,500*
Liabilities	*300*	*250*	*350*
Fair Market Value of assets	*800*	*850*	*950*
Details regarding investment in I Co			
Cost of acquisition	*150*	*150*	*150*
Book value of assets in balance sheet of I Co	*350*	*450*	*480*
Liabilities	*150*	*200*	*250*
Fair market value of assets	*350*	*400*	*600*

Notes:

1. *Exchange Control laws in India would mean the Foreign Exchange Management Act, 1999 read along with the Rules, Regulations and Master Directions issued thereunder from time to time.*

2. *Rule 2(k) of the Foreign Exchange Management (Non- debt Instruments) Rules, 2019 defines the turn equity instruments:*

   *"**equity instruments**" means equity shares, convertible debentures, preference shares and share warrants issued by an Indian company.*

   Explanation:

   (i) Equity shares issued by an Indian Company in accordance with the provisions of the Companies Act,2013 or any other applicable law, shall include equity shares that have been partly paid. "Convertible debentures" means fully and mandatorily convertible debentures which are fully paid. "Preference shares" means-_____

   (ii) _____

   (iii) _____

3. *Reference to the Act would mean the Income-tax Act,1961.*

4. *Reference to the Rule would mean the Income-tax Rules,1962.*

5. *Donald has complied with the applicable rules under the Income tax Rules.*

6. *For the purposes of this case study if required, consider that the concept and meaning of associated enterprises as provided under the Act and that under the Indo – USA DTAA is similar.*

Reference Material

(a) Relevant extracts of India – Germany DTAA

ARTICLE 3

GENERAL DEFINITIONS

1. _____

2. As regards the application of this Agreement by a Contracting Sate any term not defined therein shall, unless the context otherwise requires, have the meaning which it has under the law of that State concerning the taxes to which this Agreement applies.

ARTICLE 11

INTEREST

1. *Interest arising in a Contracting Sate and paid to a resident of the other Contracting Sate may be taxed in that other Sate.*
2. *However, such interest may also be taxed in Contracting Sate in which it arises and according to the laws of that State, but if the recipient is the beneficial owner of the interest the tax so charged shall not exceed 10 per cent of the gross amount of the interest.*

ARTICLE 13

CAPITAL GAINS

1. *Gains derived by a resident of a Contracting State form alienation of immovable property situated in the other Contracting State may be taxed in that other State.*
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 with the whole enterprise) or of such fixed base, may be taxed in that other State.*
3. *Gains from the alienation of ships or aircraft operated in international traffic or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated.*
4. *Gains from the alienation of shares in a company which is a resident of a Contracting State may be taxed in that State.*
5. *Gains from the alienation of any property other than that referred to in paragraphs 1 to 4 shall be taxable only in the Contracting State of which the alienator is a resident.*

(b) Relevant extracts of India – USA DTAA

ARTICLE 1

PERSONS COVERED

1. *This Convention shall apply to persons who are residents of one or both of the Contracting States except as provided in the Convention.*
2. _____
3. _____
4. _____

ARTICLE 4

RESIDENCE

1. *For the purposes of this Convention, the term "resident of a Contracting Sate" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, citizenship, place of management, place of incorporation or any other criterion of a similar nature, provided, however, that _____.*

   (a) *this term does not include any person who is liable to tax in that State in respect only of income from source in that State; and _____*

   (b) *_____*

2. *Whereby reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, _____*

3. *Where, by reason of paragraph 1, a company is a resident of both the Contracting State, such company shall be considered to be outside the scope of this convention except for the purposes of paragraph 2 of Article 10 (Dividends), Article 26 (Non-Discrimination), Article 27 (Mutual Agreement Procedure), Article 28 (Exchange of Information or Administrative Assistance) and Article 30 (Entry into Force).*

4. *_____*

ARTICLE 13

GAINS

Except as provided in Article 8 (Shipping and Air Transport) of this convention, each Contracting State may tax capital gains in accordance with the provisions of its domestic law.

(c) Relevant extracts of India – Singapore DTAA

ARTICLE 11

INTEREST

1. *Interest arising in a Contracting State and paid to a resident of the other Contracting Sate may be taxed in that other State.*

2. *However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed:*

   (a) *10 per cent of the gross amount of the interest if such interest is paid on a loan granted by a bank carrying on a bona fide banking business or by a similar financial institution (including an insurance company);*

(b) 15 per cent of the gross amount of the interest in all other cases.

3. _____

6. _____

ARTICLE 13

CATPTAL GAINS

1. Gains derived by a resident of a Contracting State form the alienation of immovable property, referred to in Article 6, and situated in the other Contracting State may be taxed in that other State.

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 fixed base, may be taxed in that other State.

3. Gains form the alienation of ships or aircraft operated in international traffic or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the Contracting State of which the alienator is a resident.

4A. Gains form the alienation of shares acquired before 1 April,2017 in a company which is a resident of a Contracting State shall be taxable only in the Contracting State in which the alienator is a resident.

4B. Gains form the alienation of shares acquired on or after 1 April,2017 in a company which is a resident of a Contracting State may be taxed in that State.

4C. However, the gains referred to in paragraph 4B of this Article which arise during the period beginning on 1 April,2017 and ending on 31 March,2019 may be taxed in the State of which the company whose shares are being alienated is a resident at a tax rate that shall not exceed 50% of the tax rate applicable on such gains in that State.

5. Gains form the alienation of any property other than that referred to in paragraphs 1, 2, 3, 4A and 4B of this Article shall be taxable only in the Contracting State of which the alienator is a resident.

(d) Relevant extracts of India – UK DTAA

ARTICLE 5

PERMANENT ESTABLISHMENT

1. For the purposes of this Convention, the term "permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term "permanent establishment" shall include especially:

(a) a place of management;

(b) a branch;

(c) an office;

(d) a factory;

(e) a workshop;

(f) premises used as a sales outlet or for receiving or soliciting orders;

(g) a warehouse in relation to a person providing store facilities for other;

(h) a mine, an oil or gas well, quarry on other place of extraction of natural resources;

(i) an installation or structure used for the exploration or exploitation of natural resources;

(j) a building site or construction, installation or assembly project or supervisory activity in connection therewith , where such site, project or supervisory activity continues for a period of more than six months, or where such project or supervisory activity, being incidental to the sale or machinery or equipment, continues for a period not exceeding six months and the charges payable for the project or supervisory activity exceed 10 per cent of the sale price of the machinery and equipment;

(k) the furnishing of services including managerial services, other than those taxable under Article 13 (Royalties and fees for technical services), within a Contracting State by an enterprise through employees or other personnel, but only if:

(i) activities of that nature continue within that State for a period or periods aggregating more than 90 days within any twelve-month period; or

(ii) services are performed within that State for an enterprise within the meaning of paragraph 1 of Article 10 (Associated enterprises) and continue

for a period or periods aggregating more than 30 days within any twelve-month period:

Provided that for the purposes of this paragraph 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 provides services or facilities in connection with, or supplies plant and machinery on hire used or to be used in, the prospecting for, or extraction or production of, mineral oils in that State.

3. _____

7. _____

ARTICLE 7

BUSINESS PROFITS

1. 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. _____

_____

9. _____

ARTICLE 12

INTEREST

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such interest may also be taxed in the Contracting State in which it arises and accordingly to the law of that State, provided that where the resident of the other Contracting State is the beneficial owner of the interest the tax so charged shall not exceed 15 per cent of the gross amount of the interest.

3. _____

_____

11. _____

Required:

Choose the most appropriate option for the following MCQs:

1.1 Based on the above facts, with regards to transactions between I Co and UK Co undertaken during the year, which of the following statement is correct?

(A) The marketing services rendered by UK Co after 1 June 2022 and interest paid to UK Co would be considered as transactions between associated enterprises under the Act.

(B) The marketing services rendered by UK Co throughout the financial year as well as interest paid to UK Co would be considered as transactions between associated enterprises under the Act.

(C) Only the marketing services rendered by UK Co would be considered as a transaction between associated enterprises under the Act.

(D) Only the interest paid to UK Co would be considered as a transaction between associated enterprises under the Act. ***(2 Marks)***

1.2 At what rate would G Co be taxed in India on the sale of CCDs assuming all relevant documents and approvals are in place?

(A) At the rate of 5% (plus applicable surcharge and education cess) under the Act.

(B) At the rate of 20% (plus applicable surcharge and education cess) under section 112 of the Act.

(C) At the rate of 10% under Article 11 of the India - Germany DTAA

(D) Nil under Article 13 of the India - Germany DTAA ***(2 Marks)***

1.3 At what rate is the interest paid by I Co to UK Co taxable in India assuming all relevant documents and approvals are in place?

(A) At the rate of 5% (plus applicable surcharge and education cess) under the Act.

(B) At the rate of 20% (plus applicable surcharge and education cess) under the Act.

(C) At the rate of 40% (plus applicable surcharge and education cess) under the Act.

(D) At the rate of 15% under Article 12 of the India - UK DTAA ***(2 Marks)***

1.4 If the Place of Effective Management of I Co is considered to be in the USA, which of the following statement is correct?

(A) I Co will be considered as a resident of India under the Act but a resident of USA under the India - USA DTAA

(B) I Co will be considered as a resident of India under the Act as well as under the India - USA DTAA

(C) *I Co will be considered as a non-resident under the Act and a resident of India under the India-USA DTAA*

(D) *I Co will be considered as a non-resident under the Act and a resident of USA under the India USA DTAA* ***(2 Marks)***

1.5 *With regards to the transfer of shares of Sing Co by Donald to Rishi, which DTAA would be relevant to examine for taxability in India?*

(A) *India-Singapore DTAA*

(B) *India-USA DTAA*

(C) *India-UK DTAA*

(D) *Singapore-USA DTAA* ***(2 Marks)***

Descriptive Questions:

You are required to answer the following descriptive questions:

1.6 *Compute the taxable income of Donald in India for AY 2023-24, if any. You may assume that the Cost Inflation Index for FY 2015-16 is 254 and for FY 2022-23 is 331. You may also assume that documents required for availing benefits of the DTAA, if any, would be available. Would your answer be different if half of the assets owned by I Co were located outside India?* ***(8 Marks)***

1.7 *Compute the tax payable by UK Co for AY 2023-24. For the purposes of this question the following assumptions to be considered:*

(a) *Applicable exchange rate of 1 USD[1] = INR 75.*

(b) *UK Co will be able to provide documents required for availing the benefits under the DTAA, if any.*

(c) *All transactions are at an arm's length price.*

(d) *The services rendered by UK Co to I Co would not be considered as Royalties or Fees for Technical Services under Article 13 of the India- UK DTAA.*

(e) *No attributable expenses have been incurred by UK Co for rendering the marketing services.* ***(7 Marks)***

Solution to Case Study 1

Answers to Q.1.1 to Q.1.5

MCQ No.	Correct Option
1.1	(B)
1.2	(D)

[1] *to be read as 'GBP'*

1.3	(D)
1.4	(B)
1.5	(B)

Answer to Q.1.6

Capital gain arising in the hands of Donald from transfer of a capital asset situated in India would be deemed to accrue or arise in India. Shares of Sing Co., Singapore, shall be deemed to be situated in India if those shares derive directly or indirectly, its value substantially from assets located in India.

Shares of Sing Co. would be deemed to derive its value substantially from the assets located in India, if on the specified date, the fair market value of Indian assets (without reduction of liabilities) i.e., fair market value of assets of I Co. –

- exceeds ₹ 10 crores; and
- represents at least 50% of the value of all the assets owned by the Sing Co.

Specified date would be the date of transfer i.e., 1.6.2022 since book value of the assets of Sing Co. on the date of transfer i.e., ₹ 1,300 crores exceeds the book value of the assets as on the last balance sheet date preceding the date of transfer i.e., ₹ 1,000 crores by at least 15%.

Shares of Sing Co. does not derive its value substantially from assets located in India since the fair market value of assets located in India (without reduction of liabilities) on 1.6.2022, being the specified date i.e., ₹ 400 crores exceeds ₹10 crores but does not represent at least 50% of the fair market value of assets of Sing Co. i.e., 850 crores.

Hence, the shares of Sing Co. would not be deemed to be a capital asset situated in India and the capital gains from the transfer of shares of Sing Co. by Donald would not be deemed to accrue or arise in India. Accordingly, the gains would not be taxable in the hands of Donald in India as per Income-tax Act, 1961. Donald does not have any income chargeable to tax in India and hence his total income will be **NIL.**

No, the answer would be the same, if half of the assets owned by I Co. were located outside India, since Rule 11UB(8) provides that for determining FMV of the Indian company**,** all assets of the company shall be taken into account irrespective of the location of the asset.

Note for Alternate answer –

As per Explanation 5 and 6 of section 9(1)(i), an asset or capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be situated in India, if the share or interest derives, directly or indirectly, derive its value substantially from the assets located in India, if on the specified date, the value of such assets exceeds ₹ 10 crores and representing at least 50% of the value of all the assets owned by the company or entity, as the case may be.

As per clause (b) of Explanation 6 of section 9(1)(i), the value of an asset shall be the ***fair market value as on the specified date, of such asset without reduction of liabilities, if any.*** *In the facts given on page no (4), liabilities and fair market value of assets of Sing Co. and I Co. are separately given in table on different dates. However, in the facts it is not clear whether the fair market value of assets of Sing Co. and I Co. is without reduction of liabilities or after reduction of liabilities. An alternate solution has been worked out assuming that fair market value of assets Sing Co. and I Co. is given after reduction of liabilities. Accordingly, the taxable income of Donald in India would be determined in the following manner:*

Capital gain arising in the hands of Donald from transfer of a capital asset situated in India would be deemed to accrue or arise in India. Shares of Sing Co., Singapore, shall be deemed to be situated in India if those shares derive directly or indirectly, its value substantially from assets located in India.

Shares of Sing Co. would be deemed to derive its value substantially from the assets located in India, if on the specified date, the fair market value of Indian assets (without reduction of liabilities) i.e., fair market value of assets of I Co. –

- exceeds ₹ 10 crores; and
- represents at least 50% of the value of all the assets owned by the Sing Co.

Specified date would be the date of transfer i.e., 1.6.2022 since book value of the assets of Sing Co. on the date of transfer i.e., ₹ 1,300 crores exceed the book value of the assets as on the last balance sheet date preceding the date of transfer i.e., ₹ 1,000 crores by at least 15%.

Shares of Sing Co. derives its value substantially from assets located in India since the fair market value of assets located in India (without reduction of liabilities) on 1.6.2022, being the specified date i.e., ₹ 600 crores (₹ 400 crores + ₹ 200 crores) exceeds ₹10 crores and represents more than 50% i.e., 54.545% of the fair market value of assets of Sing Co. i.e., ₹ 1,100 crores (₹ 850 crores + ₹ 250 crores).

Hence, the shares of Sing Co. would be deemed to be a capital asset situated in India and the capital gains from the transfer of shares of Sing Co. by Donald would be deemed to accrue or arise in India. Accordingly, the gains would be taxable in the hands of Donald in India as per Income-tax Act, 1961.

As per Article 13 of India-USA DTAA, each Contracting State may tax capital gains in accordance with the provisions of its domestic law. Hence, capital gains is taxable in India as per DTAA.

Taxable income of Donald in India for the A.Y. 2023-24	
Particulars	**₹ (in crores)**
Full value of consideration	350
Less: Cost of acquisition	100
Long term capital gains [Since shares held for more than 24 months]	**250**

Fair Market Value of all the assets of the Sing Co. as on the specified date (1.6.2022) (₹ 850 crores + ₹ 250 crores)	1,100
Fair Market Value of assets of the Sing Co located in India as on the specified date (1.6.2022), i.e., Fair value of I Co as held by Sing Co. (₹ 400 crores + ₹ 200 crores)	600
Long-term capital gains (income) attributed to assets located in India [250 x 600/1100]/ **Taxable income**	**136.36**
No, the answer would be the same, if half of the assets owned by I Co. were located outside India. The same is since Rule 11UB(8) provides that for determining FMV of the Indian company**, all assets of the company shall be taken into account irrespective of the location of the asset**.	

Answer to Q.1.7

UK Co. and I Co. are associated enterprises as per section 92A(b) or even under the India-UK DTAA, since Rishi participates directly in the control or capital of UK Co. (wholly owned by Rishi) and indirectly, through intermediary i.e., Sing Co., in the control or capital of I Co. (wholly owned subsidiary of Sing Co.).

Computation of tax payable by UK Co for A.Y. 2023-24	
Particulars	**Amount per unit (in ₹)**
I. Profits and gains of business or profession	
Marketing services to I Co. (GBP 3,00,000 per visit x 2 visits in F.Y. 2022-23 x 75)	4,50,00,000
[As per Article 5(2)(k) of India-UK DTAA, furnishing of marketing services by UK Co. to I Co. in India would constitute a PE in India as • these services are performed for an associated enterprises and • it continues for a period or periods aggregating more than 30 days within any 12 months period i.e., 45 days in this case. As per Article 7 of India-UK DTAA, profits attributable to PE in India may be taxed in India.]	
II. Income from Other Sources	
Interest on CCDs from I Co. [As per Article 12 of India-UK DTAA, interest may also be taxed in India i.e., arising Country. As per section 9(1)(v), interest payable by a I Co. resident in India to UK Co. non-resident would be deemed to accrue or arise in India. Hence, such interest would be chargeable to tax in India]	27,00,000
Total Income	**4,77,00,000**

Tax Payable	
Tax on business income of ₹ 4,50,00,000 @ 40%	1,80,00,000
Add: Surcharge @ 2% [Since total income > ₹ 1 crores but ≤ ₹ 10 crores	3,60,000
	1,83,60,000
Add: HEC @ 4%	7,34,400
	1,90,94,400
Tax on interest of ₹ 27,00,000 @15% [Taxable at lower of tax rate @ 40% plus surcharge @ 2% and HEC @4% as per Income-tax Act and tax rate @ 15% as per Article 12(2) of India-UK DTAA]	**4,05,000**
Tax Payable	**1,94,99,400**

Case Study 2

Mr. Sunny, a citizen of India is a renowned Indian scientist and is an employee for Indian Research Centre (IRC) in India.

IRC has offered to sponsor his research in Country U as he is being one of the finest young talents in his organization. Mr. Sunny has consented to the same. He is very enthusiastic about it as this is his first ever visit outside India.

Activities in Country U:

(1) IRC sent him on sponsorship basis for a special research program in CASA Foundation in Country U for an initial period from November 1, 2020 - March 31, 2022. Later on, it got extended as referred to in point (3) below.

He visited India on Diwali break for a 15-day period from November 1, 2021-November 15, 2021. Rest of the period he was in Country U itself.

(2) During his research period in Country U, he received stipend from CASA Foundation @ USD 5,000.00 per month which was directly credited to his overseas bank account in Country U. TDS @ 30% was done by CASA Foundation as per the applicable laws, on 31.03.2022. As per terms of contract the stipend would fall due at the time of completion of the research or at the time of payment, whichever is earlier.

IRC paid USD 50 per day as per diem allowance during his stay in Country U which was directly transferred to his overseas account in Country U. No TDS was deducted on the same. He was paid per diem allowance for 22 days for each month. Out of the total per diem allowance received, he could only spend USD 40 against each receipt.

(3) Since, his training got extended from April 1, 2022 to September 25, 2022 therefore, he could return to India only on September 26, 2022. The emolument terms continued to be the same till his extended stay in Country U. He was paid stipend for the complete month of September irrespective of his early departure in September.

The stipend for the extended period (from 01.04.2022 - 25.09.2022) was paid together on 30.09.2022. TDS as per the applicable laws was also deducted @ 30% on 30.09.2022. The per diem allowance for September, 2022 was for 20 days only.

(4) He became a visiting faculty in the StanC University in Country U since Jan 1, 2022 till his return to India. He used to visit University over the weekend as a visiting faculty.

He received an honorarium from the University StanC by way of Bank transfer - USD 500 per week in his overseas bank account held in Country U. Payment made & TDS deducted @ 30% on 30.09.2022, for the period Jan 1, 2022 - Sept 30, 2022. He managed to visit for 35 weeks to StanC during his stay in Country U. Out of the same, 22 weeks were visited in FY 22-23.

Activities in Country I:

(5) Mr. Sunny, while on training in Country U developed a Special Space Software Module which could be customized as per each country's requirements and could be used accordingly. Mr. Sunny registered his Intellectual Property (IP) rights in Country I in September 2022.

He earned Royalty income of EURO 10,000.00 from all over the world in his overseas bank account in Country I for FY 22-23. He incurred EURO 500 to register IP in Country I. The tax rate of Country I is 20%. The Royalty is paid to him as on 31.03.2023 after deduction of TDS. TDS is deducted on gross basis.

(6) He was also a visiting faculty in Country I and use to deliver lectures on Space and Aeronautical Activities in AleX University in Country I. He earned Honorarium of EURO 5,000.00 during FY 2022-23. No tax was deducted by Country I on this.

Activities in India:

(7) Mr. Sunny resumed back his scientific research in India in IRC from Oct 1, 2022, itself. He was paid a fixed salary of INR 5,00,000.00 per month since his rejoining. The salary is directly credited to his Indian bank account.

(8) He continued to take virtual sessions once he was back to India for the remaining sessions. The university continued to pay him same amount of Honorarium as before for next 24 weeks for FY 22-23. But, he refused to accept the sum directly in his hand and instead instructed them to transfer the same to Research Centre of IRC (RCI) as a voluntary contribution. The contributions made to RCI are 100% eligible for 80G exemption.

The StanC University in Country U deducted taxes on the honorarium @30% on 31.03.2023 and transferred rest of the amount to RCI on his behalf.

Additional information:

(A) Both his overseas bank balances (Country U and Country I) during FY 22-23 did not have an aggregate balance of more than USD 5,000.00 anytime during the year.

(B) As per terms of contract the emoluments from overseas would fall due at the time of completion of the research/activity or at the time of payment, whichever is earlier.

(C) Mrs. Sunny, an Indian Citizen but is a tax resident of Country I, is a lawyer by profession. She has not visited India during the year. Her income during AY 2023-24 is as follows:

Sl. No.	Details of income	Amount in INR
(a)	Gift form Mr. Sunny received in bank account in India	50,00,000.00
(b)	Sale of shares of I Co, an unlisted Indian Company	50,00,000.00
(c)	Gift from Mrs. Gonda, an Indian resident friend, received in her bank account in Country I	2,50,000.00
(d)	Fees for consultancy services rendered from Country I to I Co, an Indian company.	10,00,000.00

(D) Consider SBI Telegraphic Transfer Bank Rate (TTBR) conversion rate as follows:

Name of the Country	Currency	As on (in INR)			
		28.02.2023	31.03.2023	30.09.2022	31.08.2022
Country U	USD	80	85	80	80
Country I	EURO	95	100	-	-

(E) Mr. Sunny does not want to opt for the provisions of Section 115BAC of the Act

(F) Ignore interest liability for the purpose of computing tax liability.

Notes:

(a) Reference to the Act would mean the Income-tax Act, 1961.

(b) Reference to the Rule would mean the Income-tax Rules, 1962.

(c) Assume that all the provisions of Foreign Exchange Management Act, 1999 wherever required has been complied with.

(d) The DTAA of India with Country U and Country I are in line with OECD Model Convention, 2017 and UN Model Convention, 2017 respectively.

(e) The proportionate credit method is being followed by India to provide relief for taxes paid outside India.

(f) Consider the exchange rate as on 31.3.23 for the purpose of Black Money Act.

Required:

Choose the most appropriate alternative for the following MCQs:

2.1 What is the quantum of the penalty under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015, if Mr. Sunny is a resident and ordinarily

Resident (ROR) for the previous year 2022-23 and if he fails to furnish information about his Bank Accounts in the return of his income for AY 2023-24?

(A) NIL

(B) INR 10 lakhs

(C) INR 5 Lakhs

(D) Amount equivalent to non-disclosure ***(2 Marks)***

2.2 What would be the tax consequence of the Honorarium refused by Mr. Sunny in India, which of the statement is correct in this respect?

(A) The amount received by RCI will be treated as income and chargeable to tax only in the hands of RCI.

(B) The amount received by RCI will be treated as application of income and chargeable to tax only in the hands of Mr. Sunny and he will also be entitled to exemption u/s 80G.

(C) No amount will be chargeable to tax in the hands of Mr. Sunny as there is a diversion of income at source itself by overriding title.

(D) The amount received by RCI is chargeable to tax both in the hands of Mr. Sunny and RCI. ***(2 Marks)***

2.3 With regards to the taxability under the provisions of the Act (ignoring provisions of the DTAA, if any), of gift received by Mrs. Sunny in her Country I account from Mrs. Gonda, which of the following statement is correct?

(A) The gift is not taxable in India as it is not received in India.

(B) The gift is taxable in India as it is deemed to accrue or arise in India.

(C) The gift is not taxable in India as Mrs. A[2] does not have a business connection in India.

(D) The gift is not taxable in India as Mrs. A[2] is a non-resident. ***(2 Marks)***

2.4 As per the DTAA between India and Country I, royalty arising in Country I to Mr. Sunny will be taxable according to which statement below?

(A) Royalties arising to Mr. Sunny may be taxed only in India.

(B) Royalty arising to Mr. Sunny may be taxed either in India or in Country I under Royalties Article under India-Country I DTAA.

(C) Royalty arising to Mr. Sunny may be taxed both in India and in Country I under Royalties Article under India-Country I DTAA.

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[2] *to be read as Mrs. Sunny*

(D) Royalties arising to Mr. Sunny may be taxed only in Country I. ***(2 Marks)***

2.5 What will be the doubly taxed Income of Mr. Sunny in respect of Income earned in Country U and Country I to claim Foreign Tax Credit in India under section 91 of ITA[3] for AY 2023-24, assumingly there is no DTAA with both the countries for the purpose of this question?

(A) INR 33,84,000.00 and INR 15,00,000.00 respectively

(B) INR 43,20,000.00 and INR 13,50,000.00 respectively

(C) INR 38,00,000.00 and INR 14,50,000.00 respectively

(D) INR 32,80,000.00 and INR 9,50,000.00 respectively ***(2 Marks)***

Descriptive Questions:

2.6 Determine the Residential status of Mr. Sunny and compute his tax liability in India for FY 2022-23. ***(3 + 4 Marks)***

2.7 What are the implications on non-disclosure of Foreign Assets under Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015, if while filing the Income Tax Return, Mr. Sunny fails to disclose his Foreign Income and Overseas Assets in India? ***(8 Marks)***

Solution to Case Study 2

Answers to Q.2.1 to Q.2.5

MCQ No.	Correct Option
2.1	(A)
2.2	(D)
2.3	(B)
2.4	(C)
2.5	-

Answer to Q.2.6

Mr. Sunny is a citizen of India, who being outside India, returned to India permanently during P.Y. 2022-23. He would be resident in India during the P.Y. 2022-23 since Mr. Sunny stayed in India for **187 days** [5+31+30+31+31+28+31].

Since, Mr. Sunny leaves India for the first time in November 2020, he would have been resident in India in P.Y. 2020-21 and earlier previous years and his stay in India during last 7 PYs would be more than 729 days. Accordingly, Mr. Sunny is a **resident and ordinarily resident** in India during P.Y. 2022-23.

[3] *to be read as 'Income-tax Act'*

Since Mr. Sunny is a resident and ordinarily resident in India, **his global income is taxable in India during the P.Y. 2022-23**.

Computation of tax liability of Mr. Sunny for A.Y. 2023-24		
Particulars		**₹**
Salary		
Salary from IRC [₹ 5,00,000/month x 6]		30,00,000
Per diem allowance [USD 50 per day x 130 (22 days x 5 months + 20 days for September)]	6,500	
Less: Actually spent [USD 40 x 130 days]	5,200	
USD 1,300 x 80, being foreign exchange rate on 31.8.2022		1,04,000
Gross salary		31,04,000
Less: Standard deduction under section 16(ia)		50,000
		30,54,000
Income from Other Sources		
Country U		
Stipend from CASA Foundation [USD 5,000 x 6 x 85[4]]		25,50,000
Honorarium from Stanc University [USD 500 per week x 46 weeks (22+24) x 85[5]]		19,55,000
Country I		
Royalty from all over world but received in Country I's bank account	10,000	
Less: Expenses for registration of IP	500	
EURO 9,500 x 100[6]]		9,50,000
Honorarium from AleX University [EURO 5,000 x 100[7]]		5,00,000
Gross Total Income		**90,09,000**
Less: Deduction under section 80G [12,000 (500 x 24) – 3,600 (30% of 12,000) x 85]		7,14,000
Total Income		82,95,000
Tax on ₹ 82,95,000 [30% of ₹ 72,95,000 + ₹ 1,12,500]		23,01,000
Add: Surcharge@10%		2,30,100
		25,31,100
Add: HEC@4%		1,01,244

[4] being foreign exchange rate on the last day of the P.Y. i.e., 31.3.2023 as per Rule 115
[5] being foreign exchange rate on the last day of the P.Y. i.e., 31.3.2023 as per Rule 115
[6] being foreign exchange rate on the last day of the P.Y. i.e., 31.3.2023 as per Rule 115
[7] being foreign exchange rate on the last day of the P.Y. i.e., 31.3.2023 as per Rule 115

Tax liability		**26,32,344**
Less: Relief for tax paid in Country U and Country I [₹ 12,03,036 + ₹ 1,90,000] [Refer note below]		13,93,036
Tax liability		12,39,308
Tax liability (Rounded off)		**12,39,310**
Note -		
Average rate of tax in India [i.e., ₹ 26,32,344 / ₹ 82,95,000 x 100]	31.734%	
Tax paid in India in respect of income earned in Country U [37,91,000 (25,50,000 + 19,55,000 – 7,14,000) x 31.734%]	12,03,036	
Tax paid in Country U [USD 30,000 x 30% x 80[8] + USD 11,000 x 30% x 80 + USD 12,000 x 30% x 80]	12,72,000	
Relief for tax paid in Country U [Tax paid in Country U but restricted to tax paid in India]	**12,03,036**	
Tax paid in India in respect of income earned in Country I [9,50,000 x 31.734%]	3,01,473	
Tax paid in Country U [USD 10,000 x 20% x 95[9]]	1,90,000	
Relief for tax paid in Country I	**1,90,000**	

Note - *Mr. Sunny is an employee of IRC in India. IRC has sent Mr. Sunny on sponsorship basis in Country U for research programme. The training got extended upto 25.9.2022. IRC paid USD 50 per day as per diem allowance to Mr. Sunny for 22 days for each month during his stay in Country U and 20 days for the month of September 2022. Mr. Sunny is a resident and ordinarily resident and his global income is taxable in India during the P.Y. 2022-23. As per Rule 115, for conversion of per day per diem allowance which is taxable under the head "salaries" in Indian currency, TTBR conversion rate on the last day of the month immediately preceding the month in which the salary is due, or is paid in advance or in arrears is to be taken. It means for April, 2022, TTBR conversion rate on 31.3.2022, for May, on 30.4.2022, for June, on 31.5.2022, for July, on 30.6.2022, for August, on 31.7.2022 and for September, on 31.8.2022 is to be considered.*

In point (D) of additional information, TTBR conversion rate only on 31.8.2022, 30.9.2022, 28.2.2023 and 31.3.2023 are given. TTBR conversion rates on 31.3.2022, 30.4.2022, 31.5.2022, 30.6.2022 and 31.7.2022 are not provided in the facts of the case study. Accordingly, in the solution TTBR conversion rate as on 31.8.2022 is taken for converting per day per diem allowance of all the months.

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[8] *TTBR on the last day of the month immediately preceding the month in which such tax has been paid or deducted*

[9] *TTBR on the last day of the month immediately preceding the month in which such tax has been paid or deducted*

Answer to Q.2.7

As per section 3(1) of the 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.

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

Penalty is leviable under section 43 of the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 for non-disclosure of foreign assets,

If Mr. Sunny, being a resident and ordinarily resident, who has furnished the return of income for any previous year under section 139, fails to furnish any information or furnishes inaccurate particulars in such return relating to any asset (including financial interest in any entity) located outside India, held by him as a beneficial owner or otherwise, or in respect of which he was a beneficiary, or relating to any income from a source located outside India, at any time during such previous year, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of ₹ 10 lakhs.

Such penalty would, however, not apply in respect of an asset, being one or more bank accounts having an aggregate balance which does not exceed a value equivalent to ₹5 lakh at any time during the previous year.

Offence and Prosecution under section 50 of Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 will also ensue for non-disclosure of foreign assets.

If Mr. Sunny, being a resident and ordinarily resident, who has furnished the return of income for any previous year under section 139, willfully fails to furnish in such return any information relating to an asset (including financial interest in any entity) located outside India, held by him, as a beneficial owner or otherwise or in which he was a beneficiary, at any time during such previous year, or disclose any income from a source outside India, he shall be punishable with rigorous imprisonment for a term which shall not be less than six months but which may extend to seven years and with fine.

Case Study 3

SAAIRA India Bridge Constructions Private Limited (SAAIRA INDIA) is in the trading business of equipment, machinery and accessories used for infrastructure. It also caters services to onsite construction activities and provides installation and assembly services for the use of machinery and equipment.

SAAIRA INDIA is engaged in Assembly Projects in Country K, which is carrying construction activities and providing installation services of the machinery in collaboration with Country K - Government. The project started on December 1, 2021, and will last till April 30, 2023. For the purpose it has set up a project office in Country K.

ANAIRA AS is a Company from Country N which is into the business of providing designs, drawings and in manufacturing and trading of equipment, machinery and accessories. ANAIRA

AS works on ERP (Enterprise Resource Planning system) software. Any person placing orders with ANAIRA AS must place through the web-based app only. ANAIRA has no PE in India.

SAAIRA INDIA has entered into following agreement with ANAIRA AS:

Indian Activities:

An agreement for regular supply of equipment from ANAIRA AS to all its onsite locations across the globe including India. The total contract value amounts to INR 250 Crores spread in different locations as follows:

Location of Business	***Amount (In Crores)***
India	*100*
Country K	*50*
Others	*100*
Total	***250***

In pursuance of the agreement, SAAIRA INDIA has been provided a login ID to place an order on the ANAIRA's app. Payment is to be made in advance or during the time of placing the order.

Country K Project Activities:

(a) ***ANAIRA*** *made direct supplies of the equipment / machinery to the tune of INR 50 Crores to Country K onsite project based on "Ship to, Bill to Basis". The invoice is raised on Indian entity and the equipment is directly shipped at the Country K Project site without touching the Indian port.*

Modus Operandi*: The order is placed by SAAIRA INDIA through its login ID on ANAIRA's App. On confirmation of the order by ANAIRA AS, the products get directly delivered from its warehouse to Country K Project site on F.O.B. basis.*

(b) ***SAAIRA INDIA*** *deployed its supervisory team in FY 22-23 to oversee this project. The supervisory team mainly assist in supervision of activities and assists in installation of machinery.*

The supervisory teams consist of following personnel:

- ***An Expatriate****: Mr. Rolex is a Singapore tax resident till March 2022. To render administrative and managerial services on the project, he is sent from SAAIRA's Singapore subsidiary to SAAIRA INDIA. His stay in India will be from September 29, 2022-March 31st, 2023. For the same, the Singapore subsidiary is paid a total sum of INR 5 lakhs by SAAIRA INDIA at the end of the assignment.*
- ***Two specialist technicians****: Mr. Ram and Mr. Rahim, both as Resident and Ordinarily Resident (ROR) in India will render technical consultancy in installation of machinery and equipment for the Country K project. They are on a fixed salary basis and are on the payrolls of SAAIRA INDIA @ INR 1,00,000.00 per month. The SAAIRA INDIA cross*

charges half of their salary to the Country K project office since October 1, 2021, as they spent half of their time on the Project in Country K. They will continue to do so till the project lasts.

- ***An independent renowned engineer:*** *Mr. Lalu Meena, an Indian Citizen, is an expert and specialises into equipment installation. He has stayed for 120 days in UAE for FY 22-23. He was a resident of UAE for previous 2 financial years. The SAAIRA INDIA has entered into a contractual agreement for a period of 6 months. He is paid INR 24 lakhs for the services in India, and he is physically present for 135 days in India and the balance he manages from virtual meetings. The amount is directly credited to his UAE overseas account. SAAIRA INDIA has involved him in the Country K project also. He will stay for 61 days in Country K for the project. He will be paid AED 100,000 directly from Country K to his UAE bank account as a Professional Fees. He spends balance 49 days of the year in Switzerland as a vacation.*

  In addition to the above supervisory team, ***a Locum Doctor*:*** *Dr. Vidyut was hired on a retainership fee from India and was sent to Country K as a substitute for a medical officer (who was working in-house in the project office of Country K). Dr. Vidyut stays for a period of 8 months in Country K from August 1, 2022 till March 31, 2023. Dr. Vidyut has always been a tax resident of India till FY 21-22. He runs his own clinic in India and earned INR 28 lakhs as gross receipts in FY 22-23, The project office in Country K paid Dr. Vidyut INR 2.5 lakh per month for the services rendered in Country K. He was additionally made a payment of INR 10 lakhs in lieu of foregoing his Indian practice during that period by Country K project office. The project office in Country K deducts TDS @ 20% on the entire amount paid to Dr. Vidyut.*

Additional information:

(i) In the case of SAAIRA INDIA, the draft assessment order was passed for AY 2021-22 by the Assessing Officer (AO) under Section 143(3) read with Section 144C of the Act on 30.09.2022. In the draft assessment order, the AO proposed an adjustment of INR 20 Crores based on the arm's length price of international transactions determined under Section 92CA(3) of the Act. The total income for FY 2020-21 is INR 50 Crores. The Income Tax Return (ITR) for FY 20-21 was filed on 20.11.2021.

The draft assessment order was received by SAAIRA INDIA as on 01.10.2022.

SAAIRA INDIA did not agree with adjustment and decided to challenge the addition of INR 20 Crores to the appropriate authorities. SAAIRA INDIA fought upto the Income Tax Appellate Tribunal (ITAT) level. The ITAT also upheld the addition of INR 20 Crores made by the AO which was finally accepted by SAAIRA INDIA. The date of issue of ITAT Order is 15.01.2023.

*(ii) *A locum doctor is a medical professional who substitutes for a practice of a regular doctor for a period of time.*

(iii) 1 AED = INR 25

(iv) The DTAA between India and Country K and Country N are in line with UN Model Convention 2017 and OECD Model Convention, respectively.

(v) Article 6(b) of the India-Singapore DTAA refers to Article 9 of the DTAA. A related enterprise within the meaning of Article 9 of the DTAA, for the purposes of this question is understood as similar to an associated enterprise under section 92A of the Act. Therefore, to identify related enterprises for the purposes of Article 6(b) the principles as laid down in Section 92A of the Act may be used.

(vi) Reference to the Act would mean the Income-tax Act, 1961.

(vii) Reference to the Rule would mean the Income-tax Rules, 1962.

Reference Material

The relevant extract of India-UAE DTAA

ARTICLE 4-RESIDENT

1. For the purposes of this Agreement the term 'resident of a Contracting State' means:

(a) in the case of India: any person who, under the laws of India, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature. This term, however, does not include any person who is liable to tax in India in respect only of income from sources in India; and

(b) in the case of the United Arab Emirates: an individual who is present in the UAE for a period or periods totalling in the aggregate at least 183 days in the calendar year concerned, and a company which is incorporated in the UAE, and which is managed and controlled wholly in UAE.

2. _____

_____

4. _____

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 an enterprise is wholly or partly carried on.

2. The term "permanent establishment" includes especially:

(a) _____

(g) _____

(h) *building site or construction or assembly project or supervisory activities in connection therewith, but only where such site, project or activity continues for a period of more than 9 months;*

(i) *the furnishing of services including consultancy services by an enterprise of a Contracting State through employees or other personnel in the other Contracting State, provided that such activities continue for the same project or connected project for a period or periods aggregating more than 9 months within any twelve-month period.*

3. _____

_____

5. _____

The relevant extract of 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. *xxxxxxxx*

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.*

6. *An enterprise shall be deemed to have a permanent establishment in a Contracting State if it furnishes services, other than services referred to in paragraphs 4 and 5 of this Article and technical services as defined in Article 12, within a Contracting State through employees or other personnel, but only if :*

(a) *activities of that nature continue within that Contracting State for a period or periods aggregating more than 90 days in any fiscal year, or*

(b) activities are performed for a related enterprise (within the meaning of Article 9 of this Agreement) for a period or periods aggregating more than 30 days in any fiscal year.

7. _____

_____

10. _____

Required:

Choose the most appropriate alternative for the following MCQs:

3.1 Mr. Lalu Meena would be considered as Resident of which country under India-UAE DTAA?

(A) Resident of India

(B) Resident of UAE

(C) Resident of India as well as UAE

(D) Resident of neither India nor UAE ***(2 Marks)***

3.2 Whether Mr. Rolex stay in India will constitute PE and if yes, under which clause of Permanent Establishment Article of India-Singapore DTAA will it constitute the same?

(A) Yes, it constitutes PE under Article 5(3)

(B) Yes, it constitutes PE under Article 5(4)

(C) Yes, it constitutes PE under Article 5(6)

(D) No, there is no PE ***(2 Marks)***

3.3 Which of the statement is correct preposition for the Indian Technicians - Mr. Ram and Mr. Rahim?

(A) They will constitute service PE as they are working for the Country K Project in a separate capacity.

(B) The income paid to the technicians will be considered as Salary income for them and reimbursement received by the SAAIRA INDIA will be considered as Fees for Technical Services.

(C) The income earned by the Indian Technicians from Country K Project is Fees for Technical Services under India-Country K DTAA and should be dealt accordingly.

(D) There is no PE and the technical service rendered to the Country K project office is in the regular course of employment. Hence, it is salary income due to the employer-employee relationship with SAAIRA INDIA. ***(2 Marks)***

3.4 What is the amount of Primary Adjustment in case of SAAIRA INDIA and what is the time limit to repatriate 'Excess money' without any interest in India for such Primary Adjustment in the given case?

(A) INR 50 Crores; on or before 90 days from date of passing of draft order by Transfer Pricing Officer.

(B) INR 20 Crores; within 90 days from the date of order by ITAT

(C) INR 20 Crores; on or before 90 days from date of order by Transfer Pricing Officer.

(D) INR 50 Crores; on or before such time as permitted by the Assessing Officer on application. ***(2 Marks)***

3.5 How much of the total income received by Dr. Vidyut in Country K is taxable in terms of the India-Country K DTAA. For the purposes of this question consider India-Country K DTAA as based on UN Model and assuming Dr. Vidyut is a tax resident of India?

(A) INR 20 lakhs as Independent Personal Services (IPS)

(B) Entire Income taxable as Business Profits

(C) Entire Income taxable as other income

(D) INR 20 lakhs as Business Income and INR 10 lakhs as other income. ***(2 Marks)***

Descriptive Questions:

3.6 Examine the taxability in India of various receipts of ANAIRA AS in context of the case study, under the various provisions of the Income-tax Act and DTAA. ***(7 Marks)***

3.7 (a) Whether the Project office set-up by SAAIRA INDIA will constitute PE in Country K and if yes, since when will it constitute PE and which type of PE will it constitute?

(4 Marks)

(b) Evaluate the possibilities of each personnel deputed by SAAIRA INDIA as a part of the supervisory team constituting various types of PE in Country K on standalone basis. ***(4 Marks)***

Solution to Case Study 3

Answers to Q.3.1 to Q.3.5

MCQ No.	Correct Option
3.1	(A)
3.2	(C)
3.3	(D)
3.4	(B)
3.5	(A)

Answer to Q.3.6

Taxability in India of various receipts of ANAIRA AS

As per **section 10(50)** of the Income-tax Act, 1961, any income arising *inter alia* from any e-commerce supply or services made or provided or facilitated and chargeable to equalisation levy under Chapter VIII of the Finance Act, 2016 would be exempt from income-tax.

In the present case, ANAIRA AS, being a foreign company would be an e-commerce operator since it owns, operates or manages a web based app for online sale of equipment.

Therefore, **euqlisation levy @ 2%** under section 165A of the Finance Act, 2016 would be **chargeable on ₹ 250 crores** received by ANAIRA AS, being an e-commerce operator from online sale of goods owned by it to SAAIRA India, resident in India.

Therefore, ANAIRA AS is required to pay euqlisation levy of ₹ 5 crores in respect of supply of equipment to SAAIRA India. Consequently, income from such transaction would be exempt from Income-tax.

As per Article 7 of the DTAA between India and Country N, which is in line with OECD Model Convention, 2017, business profits of ANAIRA AS cannot be taxed in India, unless it has a permanent establishment in India, in which case, the profits that are attributable to the PE can be taxed in India.

Since there is no fixed place PE in India for supply of equipment's, no part of the profits can be taxed in India, by virtue of India's DTAA with Country N.

Accordingly, the receipts of ANAIRA AS would not be taxable in India neither under the Income-tax Act nor as per DTAA.

Note for Alternate Answer *– The question requires to examine the taxability in India of various receipts of ANAIRA AS under the various provisions of Income-tax Act and DTAA. Based on facts given in the case study, the provisions of equalization levy under section 165A of the Finance Act, 2016 and section 10(50) of the Income-tax Act are attracted. The main answer is given based on the provisions of equalization levy and section 10(50) of the Income-tax Act.*

However, due to the specific reference to "under the various provisions of the Income-tax Act" and DTAA an alternate answer applying Explanation 2A to section 9(1)(i) of the Income-tax Act, relating to significant economic presence is given below ignoring the provisions of equalisation levy, since the levy itself is through Chapter VIII of the Finance Act, 2016 and not through the Income-tax Act, 1961:

Alternate answer

Explanation 2A to section 9(1)(i) provides that significant economic presence of a non-resident shall constitute business connection in India in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if aggregate of payments arising from such transaction exceeds the prescribed threshold of ₹ 2 crores whether or not the non-resident has place of business in India or the non-resident renders services in India.

In the present case, since ANAIRA AS from Country N, being a foreign company has entered into a transaction with SAAIRA INDIA for supply of equipment for consideration of ₹ 250 crores, the ANAIRA AS would be considered to have significant economic presence in India, which would constitute business connection in India by virtue of *Explanation 2A* to section 9(1)(i) of the Income-tax Act, 1961.

Therefore, income attributable to the transaction with SAAIRA INDIA for supply of equipment for consideration of ₹ 250 crores would be deemed to accrue or arise in India.

The same shall be irrespective of the fact that equipment to the tune of ₹ 50 crores and ₹ 100 crores are directly supplied to Country K or other locations, respectively.

However, as per Article 7 of the DTAA between India and Country N, which is in line with OECD Model Convention, 2017, business profits of ANAIRA AS cannot be taxed in India, unless it has a permanent establishment in India, in which case, the profits that are attributable to the PE can be taxed in India.

Since there is no fixed place PE in India for supply of equipment's, no part of the profits can be taxed in India, by virtue of India's DTAA with Country N.

Accordingly, the receipts of ANAIRA AS would not be taxable in India as per DTAA.

Answer to Q.3.7(a)

As per Article 5(3) of the UN Model Convention the term "permanent establishment" include a building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only if such site, project or activities last more than six months.

In the present case, since SAAIRA INDIA is engaged in Assembly Projects in Country K, which is carrying on construction activities and providing installation services of machinery in Country K from 1st December 2021 and last till 30th April 2023 (which is more than 6 months), is squarely covered by the above Article.

The project of SAAIRA INDIA would constitute construction PE with effect from F.Y. 2021-22 itself.

Answer to Q.3.7(b)

The UN Model Convention, 2017 incorporates the concept of service PE. To constitute a PE, the activities carried on through employees or other personnel engaged by the enterprise for furnishing services, including consultancy services should continue within a Contracting State for a period of periods aggregating more than 183 days in any 12 months period commencing or ending in the fiscal year concerned.

Mr. Rolex

Mr. Rolex was present in India during 20-9-22 to 31-3-2023 i.e., more than 183 days for the project in India. In his case, India-Singapore DTAA would be applicable. Hence, he will not constitute a PE in country K.

Mr. Ram and Mr. Rahim

In this case, Mr. Ram and Mr. Rahim spent only half of their time i.e., less than 183 days on the project in Country K in the P.Y.2022-23, service PE of SAAIRA India would not be constituted.

Mr. Lalu Meena

Stay of Mr. Lalu Meena in Country K for the project for 61 days would also **not constitute Service PE** for SAAIRA India, since his stay in India is not for more than 183 days.

Case Study 4

Marvel Ltd, Mumbai

Marvel Ltd, Mumbai is engaged in manufacture of mobile phones in India. It borrowed INR 100 crores on 1st July, 2022 from Reid Inc. of USA for which interest is payable @ 6% per annum. Mike Inc. of USA who holds 30% shareholding in Marvel Ltd. guaranteed the loan given by Reid Inc. to Marvel Ltd. For securing the guarantee, Mike Inc. deposited INR 100 crores with Reid Inc.

The net profit of Marvel Ltd was INR 4 crores as per Statement of Profit and Loss for the year ended 31st March, 2023. Marvel Ltd has claimed interest on loan, depreciation of INR 3 crores (which includes additional depreciation of INR 85 lakhs) and provision for income-tax of INR 1 crore. It also claimed guarantee fee paid to Mike Inc. @ 2% of the loan and whereas in the case of unrelated parties, it was found that the guarantee fee payable is 1% of the loan.

Kevin Ltd of Country S

Kevin Ltd of Country S is an associated enterprise of Mike Inc. of USA. Kevin Ltd has a branch in India since 2010. It was selling the goods to Indian customers by importing from various countries besides sale in India of goods manufactured by it in Country S. A survey under section 133A of the Act was conducted in its branch premises in January, 2022 and undisclosed assets of INR 90 lakhs were found. Assessment for the assessment year 2022-23 was completed by making addition of the entire undisclosed asset of INR 90 lakhs. The assessee preferred appeal before CIT (Appeals) who gave complete relief to the assessee. The Income-tax Department wants to file an appeal before ITAT.

The adjusted total income of the Indian branch of Kevin Ltd for the year ended 31st March, 2023 is INR 80 lakhs. The branch incurred INR 12 lakhs by way of executive and general administrative expenditure during the financial year 2022-23. The head office has allocated INR 18 lakhs as the branch's share of head office expenditure including the expenditure of INR 12 lakhs incurred by the branch.

Gayle, Director of Kevin Ltd

Gayle (age 58) one of the directors of Kevin Ltd is a citizen of Country S. He joined the Indian branch of Kevin Ltd on 1st July, 2018 after remaining in Country S since his birth. He has been in India since he joined the branch of Kevin Ltd. He reports the following transactions for the financial year 2022-23:

(a) *Interest on securities held in Country S fetching interest annually. Credited USD 1,000 to his bank account in India on 31st July, 2022. Interest is due on 30th June, 2022. There is no DTAA between India and Country S.*

(b) *He has rubber estate in Country M. Agricultural income from rubber estate USD 5,000 representing total sale proceeds of rubber less cultivation expenses remitted by his rubber estate manager on 26th March, 2023. It is to be treated as business income of Gayle. There is a DTAA between India and Country M and as per DTAA the said income is taxable in both the countries and the resident Country would give tax credit. The relevant Article in DTAA is similar to that of rule 128 of the Income-tax Rules, 1962.*

(c) *Has let out a property in Country K from which he gets monthly rental income of USD 1,000 credited to his bank account in India in the first week of every subsequent calendar month. There is no DTAA between India and Country K.*

(d) *Invested in equity shares of a listed company in Country K who declared dividend on 23rd January,2023 but it was not received till 31st March, 2023. The amount of dividend is USD 500 (gross).*

(e) *During the financial year 2022-23, Gayle went on deputation to Country A for 3 months (i.e from 1st May to 31 July,2022) and was paid USD 10,000 per month as salary by the branch in Country A. This amount was credited to his bank account in India. As per the employment agreement the salary is due on the first day of the succeeding calendar month. There is a DTAA between India and Country A and as per DTAA the salary income is taxable in both the countries with no tax credit thereof.*

Trio (P) Ltd, Jaipur a wholly owned subsidiary of Marvel Ltd

Trio (P) Ltd, Jaipur is a wholly owned subsidiary of Marvel Ltd. It paid INR 60 lakhs to Jones Inc. of USA as fee for technical services. Services were rendered by the employees of the branch of Jones Inc. in Mumbai. There is DTAA between India and USA which provides for tax withholding @ 10% in respect of fee for technical services.

Trio (P) Ltd invested in MM (P) Ltd of country X and received dividend of ₹600 lakhs during the financial year 2022-23. It declared and distributed interim dividend of INR 200 lakhs in October, 2022 and a final dividend of INR 300 lakhs in October, 2023.

Trio (P) Ltd availed online digital advertisement service provided by Marshall Inc. of USA. It paid INR 10 lakhs and the amount outstanding as on 31st March, 2023 was INR 2 lakhs for the said online digital advertisement service. Marshall Inc. is also an e-commerce operator who sold its goods to customers resident in India for INR 180 lakhs during the financial year 2022-23. Also,

during the same year, Marshall Inc. sold goods for INR 70 lakhs to customers outside India but has used IP address in India for the purchase of those goods.

Additional information:

(a) Maria (age 55) wife of Gayle a foreign citizen came to India and remained with Gayle since July, 2018. She has total income in India of INR 11 lakhs and income of INR 3 lakhs in Country S for the financial year 2022-23.

(b) Consider SBI Telegraphic Transfer Bank Rate (TTBR) conversion rate as follows:

Date	***Ex Rate in INR FOR 1 USD***
30.4.2022	*78*
31.5.2022	*79*
30.6.2022	*80*
31.7.2022	*76*
31.8.2022	*80*
30.9.2022	*77*
31.10.2022	*79*
30.11.2022	*80*
31.12.2022	*81*
31.1.2023 to 31.3.2023	*82*

(c) Reference to the Act would mean the Income-tax Act, 1961.

(d) Reference to the Rule would mean the Income-tax Rules, 1962.

Required:

Choose the most appropriate alternative for the following MCQs:

4.1 How much must be the tax deductible at source by Trio (P) Ltd on the fee for technical services paid to Jones Inc.?

(A) INR 24,96,000

(B) INR 24,00,000

(C) INR 6,00,000

(D) INR 6,24,000 ***(2 Marks)***

4.2 Can the Income-tax Department prefer appeal before ITAT in respect of the complete relief obtained by Kevin Ltd from CIT (Appeals)?

(A) No, as the tax liability is less than INR 50 lakhs.

(B) Yes, as the tax liability is more than INR 25 lakhs.

(C) *Yes, as the tax liability is more than INR 50 lakhs.*

(D) *No, as the undisclosed asset is less than INR 100 lakhs.* **(2 Marks)**

4.3 *Assuming Maria has opted for section 115BAC, how much is her tax liability for the assessment year 2023-24?*

(A) *INR 1,69,000*

(B) *INR 1,32,790*

(C) *INR 2,41,800*

(D) *INR 1,89,990* **(2 Marks)**

4.4 *How much of dividend received by Trio (P) Ltd would be liable to tax for the assessment year 2023-24?*

(A) *INR 100 lakhs*

(B) *INR 200 lakhs*

(C) *INR 400 lakhs*

(D) *INR 500 lakhs* **(2 Marks)**

4.5 *How much of head office expenditure could be claimed by the Indian branch of Kevin Ltd for the assessment year 2023-24?*

(A) *INR 4,00,000*

(B) *INR 6,00,000*

(C) *INR 12,00,000*

(D) *INR 18,00,000* **(2 Marks)**

Descriptive Questions:

4.6 *Marvel Ltd wants to know how much of interest is deductible in computing its income for the assessment year 2023-24. Also calculate the tax payable by Marvel Ltd if it had opted for section 115BAA of the Act.* **(5 Marks)**

4.7 *Compute the total income of Gayle for the assessment year 2023-24.* **(5 Marks)**

4.8 *Discuss the tax consequence in the hands of Trio Ltd and Marshall Inc, in respect of online digital advertisement. Will your answer be different in case Marshall Inc. has a branch in India which was actively engaged in providing digital advertisement service for Trio Ltd and was an e-commerce operator for sale of its goods?* **(5 Marks)**

Solution to Case Study 4

Answers to Q.4.1 to Q.4.5

MCQ No.	Correct Option
4.1	(A)
4.2	(C)
4.3	(A)
4.4	(C)
4.5	(A)

Answer to Q.4.6

In the present case, since Mike Inc. USA holds 30% of voting power i.e., not less than 26% of voting power in Marvel Ltd., Mike Inc. and Marvel Ltd. are deemed to be associated enterprises.

Since loan of ₹ 100 crores taken by Marvel Ltd., an Indian company from Reid Inc, is guaranteed by Mike Inc, an associated enterprise of Marvel Ltd., such debt shall be deemed to have been issued by an associated enterprise and interest payable to Reid Inc, being in excess of ₹ 1 crore, shall be considered for the purpose of limitation of interest deduction under section 94B.

Computation of amount of interest deductible in computing income of Marvel Ltd. A.Y. 2023-24		
Particulars		**₹ in crores**
Net Profit		4.0
Add: Interest (already debited ₹ 100 crores x 6% x 9/12)		4.5
Add: Guarantee Fees (2% of ₹ 100 crores)[10]		2.0
Add: Depreciation including additional depreciation		3.0
Add: Provision of Income-tax		1.0
EBITDA		**14.5**
Interest paid or payable by Marvel Ltd. including guarantee fee of ₹ 1 crore after TP adjustment of ₹ 1 crore		5.5
Less: Excess interest – Lower of		1.15
Interest paid or payable in excess of 30% of EBITDA [₹ 5.5 – 4.35]	1.15 crores	
Interest paid or payable to non-resident AE	5.5 crores	
Interest allowable as deduction		**4.35**

[10] *guarantee fee can be classified as interest as defined in section 2(28A) of the Act.*

Computation of Tax Payable by Marvel Ltd. A.Y. 2023-24	
Particulars	**₹ in crores**
EBITDA	14.5
Less: Interest allowable u/s 94B	4.35
Less: Depreciation [Additional depreciation of ₹ 85 lakhs not allowable since company is opting for section 115BAA]	2.15
Total Income	**8.0**
Tax Payable [₹ 8 crores x 25.168% (22% plus Surcharge @10% plus Health and Education Cess @4%]	**2.01344**

Answer to Q.4.7

During the P.Y. 2022-23, Gayle stayed in India for 273 days in India. Since he stayed in India for 182 days or more during the P.Y. 2022-23, he would be resident in India for the A.Y. 2023-24.

Gayle remained in India since July, 2018, he would have been resident in India in P.Y. 2018-19 and thereafter and his stay in India during last 7 PYs would be more than 729 days. Accordingly, Gayle is a resident and ordinarily resident in India during P.Y. 2022-23.

Accordingly, global income would be taxable in his hands.

Computation of Total Income of Gayle for the A.Y. 2023-24

Particulars		₹
Salary from branch in Country A [USD 10,000 x 79[11] + USD 10,000 x 80 + USD 10,000 x 76]	23,50,000	
Less: Standard Deduction u/s 16	50,000[12]	23,00,000
Income from house property		
Income from house property in Country K (USD 1000 x 12 x 82[13])	9,84,000	
Less: Deduction u/s 24 – 30% of NAV	2,95,200	
		6,88,800
Profits and gains of business or profession		
Agricultural income from rubber estate in Country M (USD 5,000 x 82[14])		4,10,000

[11] *the last day of the month immediately preceding the month in which the salary is due*

[12] *In the absence of information whether the Gayle is opting for section 115BAC or not, it is assumed that he is not opting of section 115BAC. Accordingly, standard deduction of Rs. 50,000 is provided. However, if it is assumed that Gayle is opting for section 115BAC, standard deduction would not be available.*

[13] *the last day of the previous year*

[14] *the last day of the previous year*

Income from other Sources	
Interest on securities held in Country S [USD 1,000 x 79[15]]	79,000
Dividend on listed shares in Country K [USD 500 x 81[16]]	40,500
Gross total income/Total income	**35,18,300**

Answer to Q 4.8

I. Tax consequences in respect of online digital advertisement where Marshall Inc. has no PE in India

In the hands of Trio Ltd.:

Trio Ltd. is required to deduct equalisation levy of ₹ 72,000 @ 6% of ₹ 12 lakhs, being the amount paid or payable towards online advertisement services provided by Marshall Inc., a non-resident not having permanent establishment in India.

Non-deduction of equalisation levy would attract disallowance under section 40(a)(ib) of 100% of the amount paid while computing business income.

In the hands of Marshall Inc.:

Section 10(50) provides that any income arising from providing any specified service on or after the date on which the provisions of Chapter VIII of the Finance Act, 2016 comes into force, and chargeable to equalisation levy under that Chapter would be exempt from income-tax. Therefore, ₹ 12 lakhs would be exempt from income-tax in the hands of Marshall Inc.

II. Tax consequences in respect of online digital advertisement where Marshall Inc. has a PE in India and was an e-commerce operator

In the hands of Trio Ltd.:

Equalisation levy would not be attracted where the non-resident service provider (Marshall Inc., in this case) has a permanent establishment in India and the service is effectively connected to the permanent establishment in India.

Tax has to be deducted by Trio Ltd. at the rates in force under section 195 in respect of such payment to Marshall Inc.

Non-deduction of tax at source under section 195 would attract disallowance under section 40(a)(i) of 100% of the amount paid while computing business income.

In the hands of Marshall Inc.:

₹ 12 lakhs would not be exempted from income-tax in the hands of Marshall Inc. under section 10(50). Since Marshall Inc. has a PE in India and advertisement services are

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[15] last day of the month immediately preceding the month in which the income is due

[16] the last day of the month immediately preceding the month in which the dividend is declared, distributed or paid by the company

effectively connected with the PE in India, such advertisement income would be deemed to accrue or arise in India in the hands of Marshall Inc. under section 9(1)(i) and be taxable in the hands of Marshall Inc. under the Income-tax Act, 1961.

Case Study 5

Sachin, a citizen and resident of India, holds 50% shares of NL Co, a company in the Netherlands, which is engaged in the business of facilitating sale of specialised industrial equipment and licensed proprietary software for total automation of such specialised industrial equipment. The balance shares of NL held by Aagam, Sachin's son who is an Indian Citizen but resident of Netherlands, Sachin also owns 75% of the shares of I Co, an Indian company, which renders research and development services to NL Co. The balance 25% of the shares of I Co is held by Kajal, Sachin's wife. Kajal is a citizen and resident of India.

NL Co has subsidiaries in different countries as under:

(a) *In Country B, a wholly owned subsidiary, B Co, it identifies and promotes manufactures who are willing to sell products through Chemo.com.*

(b) *In France, a wholly owned subsidiary, F Co, it purchases the industrial equipment from NL Co and sells them in Paris.*

(c) *Similarly, another wholly owned subsidiary, HK Co in Hong Kong, which purchases the industrial equipment from NL Co and sells them to buyers located in Hong Kong.*

The directors of NL Co are Sachin, Kajal and Aagam. The meeting of the Board of Directors takes place in the Netherlands, wherein Sachin and Kajal travel to the Netherlands, Aagam is the person who takes the critical decisions in the Netherlands and such decisions are generally ratified by the Board.

The industrial equipment is sold by placing orders on the portal Chemo.com, a website, owned and operated by NL Co. The website is an e-commerce platform wherein products tangible such as goods as well as intangibles such as software (which are to be downloaded with a key received after purchase) are sold. The licensed proprietary software used to be sold off-the-shelf in CD disks earlier. However, now, such software can be downloaded from the 'Chemo.com". The terms of use of the proprietary software clearly specify that the person who has downloaded the software is licensed to use the software but cannot make copies of the same. NL Co has also appointed a 3rd party in India, D Co, as its exclusive distributer for sale of software in India, D Co distributes other softwares as well.

The total value of goods (including software) sold on Chemo.com to Indian residents during F Y 22-23 is INR 125 crores.

In order to fulfil the orders at the earliest, NL Co has a dedicated space in a warehouse in India. NL Co is considering shutting down its warehouse operations in India and sale its goods in India through the website of Aus Co, a third party in Australia, which only runs the e-commerce platform and does not have any warehouse or storage space in India.

Details of receipts of NL Co during AY 2023-24 is as follows:

NL Co had acquired 5% of the shares in List Co, an Indian Company, listed on the National Stock Exchange in India. During the financial year relevant to the AY 2023-24, List Co has declared and paid dividends.

(a) Dividend income received from investments in Europe INR 30 crores

(b) Rental income from properties INR 40 crores

(c) Income from sale of goods INR 100 crores

Further, NL Co has 8 employees on its payroll. 5 employees are working from home and are based in India. 3 employees are working from the Netherlands.

The net worth of NL Co is as follows:

Particulars	***Amount (in INR crores)***
Share capital	*50*
Reserve and Surplus (Profit and Loss Account)	*150*
Net worth	*200*

I Co is undertaking some ground-breaking research, for which a substantial amount of capital outlay was required. In order to provide a short-term funding, during AY 2023-24, NL Co and Sachin provided a loan of INR 40 crores and INR 10,00,000, respectively to I Co. The interest payable on the loan provided by NL Co is 5% p.a., whereas the interest payable on the loan provided by Sachin is 12% p.a. Accordingly, for the relevant AY 2023-24, I Co paid INR 2 crores as interest on the loan to NL Co and INR 1,20,000 as interest to Sachin.

I Co has a branch in Country A and another branch in Country B, carrying out R&D activities for customers of that country. I Co has opted for the new regime of taxation under section 115BAA of the Act and accordingly, its income is taxed at the rate of 22% plus applicable surcharge and education cess.

During the year, I Co has rendered research and development services to all the subsidiaries of NL Co. i.e. B Co, F Co and HK Co and charged management fees for the services rendered. For the purpose of determining the price to be charged to the entities, the proportionate costs incurred by I Co towards rendering of the services are cross-charged with a 15% mark-up.

The details of foreign receipts of I Co during AY 2023-24 is as follows:

Nature of income	***Amount (in INR crores)***	***Taxes paid/ withheld in the respective country (other than India) (in INR crores)***	***Rate of tax at which taxes paid in respective country***
Profits (loss) of branch in Country A	*100*	*30*	*30%*

Profit /(loss) of branch in Country B	*(150)*	*0*	*NA*
Management fees from B Co	*120*	*12*	*10%*
Management fees from F Co	*180*	*0*	*0%*
Management fees from HK Co	*80*	*0*	*0%*
Receipts from conduct of R&D for other parties	*1,000*	*0*	*NA*

The profit & loss of I Co. for AY 2023-24 is as follows:

Particulars	***Amount (in INR crores)***
Receipts from operations (gross)	*1,500*
Management Fees earned (gross)	*380*
Total Gross Receipt	*1,880*
Expenses & Disallowances (including incurred at branch and those disallowable under the Act)	*1,560*
Net before tax	*320*
Income tax payable in India before tax credit	*80.54*
Taxes paid outside India	*42*

For the purpose of benchmarking management services fees under the Transactional Net Margin Method, the Profit Level Indicator (ratio of operating profit to operating costs) of comparable companies is as follows:

Name of comparable company	***Profit level indicator***
Company P	*21%*
Company Q	*28%*
Company R	*26.5%*
Company S	*23.5%*
Company T	*18%*
Company U	*14%*
Company V	*32%*
Company W	*17.5%*
Company X	*19%*
Company Y	*23%*
Company Z	*20%*

The income earned by Sachin during the year is as follows:

Sl. No.	Details of income	Amount
a.	Salary from NL Co	INR 25,00,000
b.	Interest on loan to I Co	INR 1,20,000
c.	Consideration on sale of shares of U Co, a US company listed on NASDAQ. The sale was undertaken on 15th October 2022	USD 1,50,000
d.	Dividend form U Co, a US company listed on NASDAQ, on 1st October 2022	USD 12,000

The shares of U Co were acquired by Sachin on 1 January 2017 for USD 1,00,000. The fair market value of the shares on 31 January 2018 was USD 1,20,000.

Sachin had acquired an immovable property in France for INR 7.5 crores on 1 January 2018. The same was not disclosed in the return of income of Sachin. During AY 2023-24, a notice was issued by the Assessing Officer alleging that the foreign assets were not adequately disclosed by Sachin. The fair market value of the property during AY 2023-24 is INR 8 crores. During the course of proceedings, Sachin was able to substantiate that income to the extent of INR 5 crores out of the INR 7.5 crores was duly assessed to tax in India.

Additional information:

(1) India-Netherlands and India-Australia have a DTAA in existence and both the countries are signatory to the Multilateral Instrument (MLI) and both the countries have notified the DTAA as Covered Tax Agreement (CTA) in its MLI deposit note to the Organisation for Economic Cooperation and Development (OECD). Also Article 2 of the DTAA's of both the countries is matched.

(2) Reference to the Act would mean the Income-tax Act, 1961.

(3) Reference to the Rule would mean the Income-tax Rules, 1962.

(4) Consider SBI Telegraphic Transfer Bank Rate (TTBR) conversion rate as follows:

Date	Exchange Rate for 1 USD (in INR)
1 January 2017	65
31 January 2018	67
1 April 2022	72
30 September 2022	74
1 October 2022	75
15 October 2022	76

Required:

Choose the most appropriate alternative for the following MCQs:

5.1 Would the transactions between NL Co and D Co be subject to transfer pricing in India?

(A) Yes, as NL Co and D Co are associated enterprises under the Act.

(B) No, as NL Co and D Co are not associated enterprises under the Act.

(C) No, provided appropriate tax has been withheld in Netherlands.

(D) Yes, if the value of the transactions between NL Co and D Co exceed INR 1 crore during the previous year. ***(2 Marks)***

5.2 The tax and penalty payable by Sachin under the Black Money Act in AY 2023-24 (ignore surcharge and education cess) is:

(A) 4.9 Crores

(B) 1.7 Crores

(C) 1.6 Crores

(D) 3 times the tax on value of immovable property ***(2 Marks)***

5.3 Assuming that the Place of Effective Management of NL Co is held to be in India, at what rate is the tax to be deducted by List Co on the dividends paid by it?

(A) 10% under section 194

(B) 20% (plus applicable surcharge and education cess) under section 195

(C) Nil

(D) 40% (plus applicable surcharge and education cess) under section 195 ***(2 Marks)***

5.4 For the management fees received by I Co, for determining the arm's length price, the transfer pricing adjustment required to be undertaken is:

(A) Upward increase by 19%

(B) Upward increase by 23.5%

(C) Upward increase by 19.11%

(D) No adjustment required ***(2 Marks)***

5.5 Taxable income of Sachin for the AY 23-24 is

(A) 40,72,08,000

(B) 20,72,08,000

(C) 10,72,08,000

(D) 72,08,000 ***(2 Marks)***

Descriptive Questions:

5.6 Compute the eligible foreign tax credit which can be claimed by I Co in respect of its income earned during AY 2023-24. You may assume that India does not have a DTAA with Country A and Country B. ***(7 Marks)***

5.7 Determine whether the income earned by NL Co would be taxable in India. Determine the taxability of Aus Co if the goods of NL Co were sold on the website of Aus Co. You may assume that the India-Netherlands and India- Australia DTAA is based on the OECD Model and are Covered Tax Agreements under the OECD MLI. ***(8 Marks)***

Solution to Case Study 5

Answers to Q.5.1 to Q.5.5

MCQ No.	Correct Option
5.1	(B)
5.2	-
5.3	(B)
5.4	-
5.5	(A)

Answer to Q.5.6

Computation of Foreign Tax Credit which can claimed by I Co. on income earned during A.Y. 2023-24

Particulars	Income taxable in India (₹ in crores)	Tax paid in India [@ 25.168%] (₹ in crores) [A]	Tax paid in Other Country (₹ in crores) [B]	Foreign Tax Credit [A or B, whichever is lower] (₹ in crores)
Country A				
Profits of branch in Country A	100 .00	25.168	30	25.168
Country B				
Loss of branch in Country B	(150)	0	0	0
Management fees from B Co. **(Refer Note 2 below)**	21.91	5.514	12	5.514
France				
Management fees from F Co. **(Refer Note 2 below)**	32.87	8.273	0	0

Hong Kong				
Management fees from HK Co. **(Refer Note 2 below)**	14.61	3.677	0	0
Total Foreign Tax Credit				**30.682**

Note 1

Since Sachin holds 75% shares directly in I Co. and 50% shares indirectly in each B Co., F Co. and HK Co. through NL Co. (50% of 100%), I Co. is associated enterprise to B Co., F Co. and HK Co. Accordingly, the transaction between I Co. and B Co., F Co. and HK Co for providing management services would be international transaction. Therefore, management fees received by I Co. from B Co., F Co. and HK Co. has to be computed at arm length price.

Since I Co. has more than 6 comparables and TNMM is the most appropriate method, range concept would be applicable. Dataset of comparables in ascending order would be as 14%, 17.5%, 18%, 19%, 20%, 21%, 23%, 23.5%, 26.5%, 28% and 32%.

Percentile	Value of to be selected	Range
35th	Total no. of data in dataset x 35% = 11x 35% = 3.85 means 4th value	19%
65th	Total no. of data in dataset x 65% = 11x 65% = 7.15 means 8th value	23.5%
Median	Total no. of data in dataset x 50% = 11x 50% = 5.50 means 6th value	21%

Since I Co. charged cost plus 15% mark up, which is outside the range of 19% to 23.5%, 21% would be the ALP.

Note 2:

Determination of ALP for management fees and profits chargeable to tax

Particulars		₹
Management fees from B Co.		120.00
Cost of management fees from B Co. [120/115 x 100]	(A)	104.35
ALP [Cost plus 21%] [104.35 + 21% of 104.35]	(B)	126.26
Profits on management fees from B Co.	**[B – A]**	**21.91**
Management fees from F Co.		180
Cost of management fees from F Co. [180/115 x 100]	(C)	156.52
ALP [Cost plus 21%] [156.52 + 21% of 156.52]	(D)	189.39
Profits on management fees from F Co.	**[D – C]**	**32.87**

Management fees from HK Co.		80
Cost of management fees from HK Co. [80/115 x 100]	(L)	69.57
ALP [Cost plus 21%] [69.57 + 21% of 69.57]	(M)	84.18
Profits on management fees from HK Co.	**[M – L]**	**14.61**

Note 3 - It would be beneficial for I Co. to set-off the loss from branch in Country B against Indian income as shown in the case study. In such case the amount of foreign tax credit would increase. Consequently, tax liability would decrease.

Answer to Q. 5.7

1. Taxability of Income earned by NL Co.

In the given case, NL Co. is a Netherlands based company and hence, resident of Netherlands. It is a foreign company under the Income-tax Act, 1961. However, the said company shall be considered to be resident in India if its place of effective management is in India. In this case, the company does not satisfy the active business test outside India, since 62.5% (5/8) of its employees out of total employees are based in India.

It has failed the active business test outside India, on account of 50% or more of its employees are based in India, the persons who take key management and commercial decisions for conduct of the company's business as a whole and the place where the decisions are made are the key factors in determining whether the POEM of the company is in India.

The facts of the case state that the key management decisions and commercial decisions for conduct of the company's business as a whole are made by Aggam who takes the critical decisions in the Netherlands, and such decisions ratified by the Board meetings takes place in Netherlands. Therefore, the POEM of NL Co. is not in India in the P.Y.2022-23 and hence, NL Co. will not be resident in India for the A.Y. 2023-24.

Accordingly, the income which accrues or arises or deemed to accrue or arise in India, received or deemed to be received in India would be taxable in the hands of NL Co. Thus, taxability of income earned by NL Co. would be determined in the following manner:

Income from sale of industrial equipment (including software) on Chemo.com to Indian resident: As per *Explanation 2* below section 9(1)(vi) of the Income-tax Act, the consideration received for use or right to use any industrial, commercial or scientific equipment (including software) would be considered as royalty.

As per Article 12(2) of India-Netherlands (based on OECD Model), the term "royalty" means consideration for the use of or right to use or for information concerning industrial, commercial or scientific experience. However, use or right to use any industrial equipment are not considered as royalty. As such payment is not considered as royalty, the payment would be

covered under Article 7 Business Profits read with Article 5 PE of the DTAA. The payment towards purchase of industrial equipment would be taxable as business profits only if NL Co. has a PE in India.

As per Article 4(a) of the OECD Model Convention, 2017, the term "permanent establishment" shall be deemed not to include use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise.

In the present case, warehouse for delivery of goods would not constitute PE in India for NL Co., Netherlands. Though income from sale of industrial equipment (including software) would be taxable in India under the Income-tax Act considering it as royalty but since DTAA provisions are more beneficial to NL Co., such income would not be taxable in India.

Note – *Alternatively, considering that warehouse for delivery of goods is not in the nature of preparatory or auxiliary activity, the PE would be constituted. In such a case, the profit attributable to the PE from sale industrial equipment (including software) would be taxable as per India-Netherlands DTAA.*

NL Co. a foreign company would be an e-commerce operator since it owns, operates or manages a portal Cheemo.com for sale of industrial equipment. However, NL Co. has a warehouse in India which would fall within the definition of PE defined under section 164(g) Chapter VIII of the Finance Act, 2016.

Accordingly, NL Co. is not required to pay euqlisation levy.

Dividend income received from investments in Europe of ₹ 30 crores: Dividend income received from investments in Europe would not be taxable in India in the hands of NL Co.

However, dividend received from List Co. would be deemed to accrue or arise in India and would be taxable in India.

Rental income from properties of ₹ 40 crores: Rental income properties would not be taxable in the hands of NL Co. (if it is assumed that properties are located outside India).

Note – *Alternatively, if it is assumed that properties are located in India, rental income from such properties would be deemed to accrue or arise in India and hence, would be taxable in India.*

Interest on loan provided to I Co., an Indian company

As per section 9(1)(v), interest payable by a I Co. resident in India to NL Co. non-resident would be deemed to accrue or arise in India. Hence, such interest would be chargeable to tax in India.

As per the OECD Model Convention, interest is taxed in both the States, the Source State as well as the Residence State.

However, in the source state (in the present case, India) tax rate should not exceed 10% of the gross amount of the interest. Overall tax rate in India, inclusive of surcharge and HEC cess will be 10% on the gross amount.

2. Taxability in the hands of Aus Co.

In respect of industrial equipment (including software) sold on its website: Since, the consideration for sale of industrial equipment (including software) is not royalty, Aus Co. being an e-commerce operator, not having a PE in India is liable to pay equalization levy @ 2% on consideration received for online sale of goods to residents in India.

As per India-Netherlands DTAA income from sale of goods would not be taxable in India, since Aus Co. does not have PE in India.