FINAL

Paper 15

DIRECT TAX LAWS AND INTERNATIONAL TAXATION

Study Notes

SYLLABUS 2022

The Institute of Cost Accountants of India

CMA Bhawan, 12, Sudder Street, Kolkata - 700 016

www.icmai.in

First Edition	:	August 2022
Reprint	:	January 2023
Reprint	:	March 2023
Reprint	:	May 2023
Reprint	:	August 2023
Revised Edition	:	February 2024

Price: ₹ 700.00

Published by :

Directorate of Studies
The Institute of Cost Accountants of India
CMA Bhawan, 12, Sudder Street, Kolkata - 700 016
studies@icmai.in

Printed at :

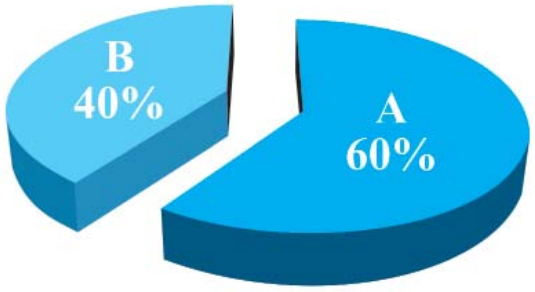
M/s. Print Plus Pvt. Ltd.
212, Swastik Chambers
S. T. Road, Chembur
Mumbai - 400 071

PAPER 15 : DIRECT TAX LAWS AND INTERNATIONAL TAXATION

Syllabus Structure:

The syllabus in this paper comprises the following topics and study weightage:

Module No.	Module Description	Weight
	Section A : Direct Tax Laws	**60%**
1	Assessment of Income and Computation of Tax Liability of Various Entities	60%
2	Tax Management, Return and Assessment Procedure	
3	Grievance Redressal	
4	Penalties and Prosecutions	
5	Business Restructuring	
6	Different Aspects of Tax Planning	
7	CBDT and Other Authorities	
8	E-commerce Transaction and Liability in Special Cases	
9	Income Computation and Disclosure Standards (ICDS)	
10	Black Money Act, 2015	
11	Case Study	
	Section B: International Taxation	**40%**
12	Double Taxation and Avoidance Agreements (DTAA) [Sec.90. 90A and 91]	40%
13	Transfer Pricing	
14	GAAR	



Learning Environment

Subject Title	**DIRECT TAX LAWS AND INTERNATIONAL TAXATION**
Subject Code	**DIT**
Paper No.	**15**
Course Description	The subject primarily focuses on various provisions of direct taxation laws to guide assessment of income and computation of tax liability of different assessees and also on application of such provisions in arriving at tax efficient decisions. The subject further includes a detail discussion on provisions relating to compliance along with necessary coverage of Income Computation and Disclosure Standards. In addition to the above, the subject highlights international taxation laws including DTAA, GAAR and transfer pricing.
CMA Course Learning Objectives (CMLOs)	1. Interpret and appreciate emerging national and global concerns affecting organizations and be in a state of readiness for business management. a. Identify emerging national and global forces responsible for enhanced/varied business challenges. b. Assess how far these forces pose threats to the status-quo and creating new opportunities. c. Find out ways and means to convert challenges into opportunities 2. Acquire skill sets for critical thinking, analyses and evaluations, comprehension, syntheses, and applications for optimization of sustainable goals. a. Be equipped with the appropriate tools for analyses of business risks and hurdles. b. Learn to apply tools and systems for evaluation of decision alternatives with a 360-degree approach. c. Develop solutions through critical thinking to optimize sustainable goals. 3. Develop an understanding of strategic, financial, cost and risk-enabled performance management in a dynamic business environment. a. Study the impacts of dynamic business environment on existing business strategies. b. Learn to adopt, adapt and innovate financial, cost and operating strategies to cope up with the dynamic business environment. c. Come up with strategies and tactics that create sustainable competitive advantages. 4. Learn to design the optimal approach for management of legal, institutional, regulatory and ESG frameworks, stakeholders' dynamics; monitoring, control, and reporting with application-oriented knowledge. a. Develop an understanding of the legal, institutional and regulatory and ESG frameworks within which a firm operates. b. Learn to articulate optimal responses to the changes in the above frameworks. c. Appreciate stakeholders' dynamics and expectations, and develop appropriate reporting mechanisms to address their concerns.

	5. Prepare to adopt an integrated cross functional approach for decision management and execution with cost leadership, optimized value creations and deliveries. a. Acquire knowledge of cross functional tools for decision management. b. Take an industry specific approach towards cost optimization, and control to achieve sustainable cost leadership. c. Attain exclusive knowledge of data science and engineering to analyze and create value.

Subject Learning Objectives [SLOB(s)]	1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc. (CMLO 4 a, b) 2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof. (CMLO 3a, b and 5a) 3. To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure. (CMLO 4 c) 4. To acquire knowledge on various provisions and processes available as per taxation laws that offers for redressal of taxpayers' grievances. (CMLO 4c)
Subject Learning Outcomes (SLOC) and Application Skills (APS)	**SLOC(s)** 1. Students will develop understanding of legal provisions and analyse, interpret, and apply the same in day-to-day business transactions. 2. They will acquire knowledge and application skills required to compute income and tax liabilities, and be able to apply those for helping management to take tax efficient business decisions. 3. Students would learn about ways and means for identifying various compliance requirements as well as processes. 4. Students will attain abilities to help management in identifying statutory forum for redressal of grievances and process to be followed for the same. **APS** 1. Students will analyse and interpret various legal provisions and rules while computing taxable income and tax liabilities of various types of assessees. 2. Students will participate in various types of business decision making process for both optimisation of tax cost and avoidance of exposures to risks of non-compliance. 3. Students will identify the concerned legal and regulatory provisions and will follow systems and processes for redressal of grievances as well as compliance management.

Module wise Mapping of SLOB(s)

Module No.	Topics and Sub-topics	Additional Resources (Research articles, case studies, blogs)	SLOB Mapped
Section A: Direct Tax Laws			
1	Assessment of Income and Computation of Tax Liability of Various Entities	Common for all Modules: Income-tax Act, 1961 (Bare Act) and the Income-tax Rules www.incometaxindia.gov.in For this module, refer Chapter IV, XII of the Income-tax Act, 1961	To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
2	Tax Management, Return and Assessment Procedure	Refer Chapter XIV of the Income-tax Act, 1961	To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure.
3	Grievance Redressal	Refer Chapter XX of the Income-tax Act, 1961	To acquire knowledge on various provisions and processes available as per taxation laws that offers for redressal of taxpayers' grievances.
4	Penalties and Prosecutions	Refer Chapter XXI of the Income-tax Act, 1961	To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure.
5	Business Restructuring	Refer Chapter XV of the Income-tax Act, 1961	To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.
6	Different Aspects of Tax Planning	Refer www.incometaxindia.gov.in for Bare Acts & Rules	
7	CBDT and other authorities	Refer Chapter XIII of the Income-tax Act, 1961	To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
8	E-commerce Transaction and Liability in Special Cases	Refer Chapter XV of the Income-tax Act, 1961	To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.

9	Income Computation and Disclosure Standards (ICDS)	Refer Chapter IV of the Income-tax Act, 1961	1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc. 2. To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure.
10	Black Money Act,2015	Refer Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015.	To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
11	Case Study	For RTI Case Laws, refer https://www.incometaxindia.gov.in/Pages/right-to-information/case-laws.aspx	1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc. 2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.
Section B: International Taxation			
12	Double Taxation and Avoidance Agreements (DTAA)	Refer Chapter IX of the Income-tax Act, 1961	1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc. 2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.
13	Transfer Pricing	Refer Chapter X of the Income-tax Act, 1961	
14	GAAR	Refer Chapter XA of the Income-tax Act, 1961	

Contents as per Syllabus

Contents as per Syllabus

SECTION - A

DIRECT TAX LAWS

Assessment of Income and Computation of Tax Liability of Various Entities

1

This Module includes:

Assessment of Income and Computation of Tax Liability of Various Entities

SLOB Mapped against the Module:

To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.

Module Learning Objectives:

After studying this module, the students will be able to -

- Understand the provisions of taxation in respect of various person
- Understand the provisions of alternative taxation scheme applicable in respect of various person
- Compute and examine the tax payable by various person.

Introduction

1

In the earlier stage of the course, we learned about various categories of person and provisions relating to computation of income under different heads of income. In general, provisions relating to computation of income are applicable to all assessee unless and until mentioned otherwise. Few of the provisions are applicable in case of specific type of person like company, trust, etc.

In this chapter, we will discuss the various provisions relating to specific person like:

a. Company

b. Business Trust

c. Securitisation Trust

d. Investment Fund

e. Religious or Charitable Trust

f. Local Authority

g. Mutual Concerns

In the chapter, apart from learning of computation of income of aforesaid persons, we will also learn about alternative tax regime, if any, available in respect of such person.

Individual including Non-resident

1.1

Individual

Computation of Total Income requires the complete knowledge of all heads of income and deduction under Chapter VIA.

Computation of Total Income of…….. for the A.Y. 2024-25

Particulars	Amount
Salaries	***
Income from house property	***
Profits and gains of business or profession	***
Capital gains	***
Income from other sources	***
Gross Total Income	****
Less: Deductions u/s 80C to 80U (subject to Max. of GTI before casual income, STCG covered u/s 111A & LTCG)	***
Total Income / Taxable Income (Rounded off u/s 288A)	****

Computation of Tax Liability of Mr. X …….. for the A.Y. 2024-25

Particulars	Rate	Details	Amount
Total Income other than STCG u/s 111A, LTCG & casual income [as per regime]			***
Add: Tax on casual income	30%		***
Add: Tax on LTCG	20%/10%/0%		***
Add: Tax on STCG covered u/s 111A	15%		***
Total tax liability before rebate and cess			PQR
Less: Rebate u/s 87A			**
			STY
Add: Surcharge			**
			ABC
Add: Health and Education cess @ 4%			**
Tax liability after cess			***

Particulars	Rate	Details	Amount
Less: Relief u/s 86, 89, 90 & 91			**
Tax liability			***
Less: Advance Tax		***	
Less: Tax Deducted / Collected at Source		***	
Less: Any other prepaid tax		***	***
Tax Payable (if **+ ve) or Refundable (**if **– ve)** (Rounded of u/s 288B)			***

Non-resident

"Non-resident" means a person who is not a "resident", and for the purposes of sections 92, 93 and 168, includes a person who is not ordinarily resident within the meaning of sec. 6(6) - [Sec. 2(30)]

Residential Status

Assessee	Condition to be a Resident	Condition to be an Ordinarily resident
Individual	Assessee satisfies any one condition of sec. 6(1) i.e. (a) He is in India in the previous year for a period of 182 days or more; **or** (b) He is in India for a period of 60 days or more during the previous year and 365 days or more during 4 previous years immediately preceding the relevant previous year. **Exceptions** A. In the following cases, condition (ii) of sec. 6(1) [i.e. sec. 6(1)(c)] is irrelevant: 1. An Indian citizen, who leaves India during the previous year for employment purpose. 2. An Indian citizen, who leaves India during the previous year as a member of crew of an Indian ship. B. An individual shall be deemed to be resident in India, if following conditions are satisfied a. He is a citizen of India b. His total income, other than the income from foreign sources, exceeds ₹15 lakhs during the previous year;	Assessee satisfies both the conditions of sec. 6(6) (a) He has been resident in India in at least 2 out of 10 previous years immediately preceding the relevant previous year; **and** (b) He has resided in India for a period of 730 days or more during 7 previous years immediately preceding the relevant previous year. **Exceptions** A. An individual shall be **deemed to be resident but not ordinarily resident** in India, if following conditions are satisfied: a. He is a citizen of India b. His total income, other than the income from foreign sources, exceeds ₹15 lakhs during the previous year; and

<table>
<tr><th>Assessee</th><th>Condition to be a Resident</th><th>Condition to be an Ordinarily resident</th></tr>
<tr><td></td><td>c. He is not satisfying any of the basic conditions given u/s 6(1) [i.e., 182 days or 60 days + 365 days]; and
d. He is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature. [Sec. 6(1A)]
C. In case of an Indian citizen or a person of Indian origin comes on a visit to India during the previous year, modified condition (ii) of sec. 6(1) is applicable:
<table>
<tr><th>Case</th><th>Modified condition (ii) of sec. 6(1)</th></tr>
<tr><td>His total income, other than the income from foreign sources[1], exceeds ₹15 lakhs during the previous year</td><td>He is in India for a period of 120 days or more (but less than 182 days) during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year</td></tr>
<tr><td>His total income, other than the income from foreign sources, does not exceed ₹ 15 lakhs during the previous year</td><td>He is in India for a period of 182 days or more during the previous year</td></tr>
</table></td><td>c. He is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.
d. He is deemed to be resident in India u/s 6(1A).
B. An individual shall be deemed to be resident but not ordinarily resident in India, if following conditions are satisfied:
a. He is an Indian citizen or a person of Indian origin.
b. He comes on a visit to India during the previous year
c. His total income, other than the income from foreign sources, exceeds ₹15 lakhs during the previous year
d. He is in India for a period of 120 days or more (but less than 182 days) during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year</td></tr>
<tr><td>HUF</td><td>Management is wholly or partly situated in India</td><td>Karta satisfies all conditions of sec. 6(6)</td></tr>
<tr><td>Company</td><td></td><td></td></tr>
<tr><td>a) Indian Co.</td><td>Always resident</td><td rowspan="5">Not applicable</td></tr>
<tr><td>b) Other Co.</td><td>Place of effective management is in India</td></tr>
<tr><td>Firm</td><td rowspan="4">Management is wholly or partly situated in India</td></tr>
<tr><td>AOP</td></tr>
<tr><td>BOI</td></tr>
<tr><td>Other person</td></tr>
</table>

Place of effective management

Place of effective management" means a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole, are in substance made.' Circular 6/2017 dated 24-01-2017 provides that the process of determination of POEM would be primarily based on the fact as to whether or not the company is engaged in active business outside India (ABOI).

Particulars	POEM
Company is engaged in active business outside India	
– If the majority meetings of the board of directors of the company are held outside India	Outside India
– If Board of directors of the company are standing aside and not exercising their powers of management and such powers are being exercised by either the holding company or any other person (s) resident in India	In India
Company is not engaged in active business outside India then the following are required to be ascertained: 1. The person(s) who actually make the key management and commercial decision for the conduct of the company's business as a whole 2. Place where these decisions are in fact being made[1]	
If such place is in India	In India

Taxpoint

- A company shall be said to be engaged in "active business outside India" if:
  a) the passive income is not more than 50% of its total income; and
  b) less than 50% of its total assets are situated in India; and
  c) less than 50% of total number of employees are situated in India or are resident in India; and
  d) the payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.
- Passive income of a company shall be aggregate of:
  i. income from the transactions where both the purchase and sale of goods is from / to its associated enterprises; and
  ii. income by way of royalty, dividend, capital gains, interest (except for banking company or public financial institution) or rental income;

Clarification related to guidelines for establishing 'Place of Effective Management' (PoEM) in India [Circular 25/2017 dated 23-10-2017]

Guiding Principles for determination of POEM of a company were issued on 24th January, 2017 vide Circular No. 06 of 2017. Further, vide Circular No. 08 of 2017 dated 23rd February, 2017, it has been clarified that the POEM provisions shall not apply to a company having turnover or gross receipts of ₹ 50 crore or less in a financial year[2].

The stakeholders have been raised concern that as per the extant guidelines, POEM may be triggered in cases of certain multinational companies with regional headquarter structure merely on the ground that certain employees having multi-country responsibility or oversight over the operations in other countries of the region are working from India, and consequently, their income from operations outside India may be taxed in India.

1 The place where management decisions are taken would be more important than the place where such decisions are implemented.

2 In other words, a foreign company whose annual turnover / gross receipts is ₹ 50 crores or less cannot be resident in India.

In this regard, it may be mentioned that Para 7 of the guidelines provides that the place of effective management in case of a company engaged in active business outside India (ABOI) shall be presumed to be outside India if the majority meetings of the board of directors (BoD) of the company are held outside India.

However, Para 7.1 of the guidelines provides that if on the basis of facts and circumstances it is established that the Board of directors of the company are standing aside and not exercising their powers of management and such powers are being exercised by either the holding company or any other person(s) resident in India, then the POEM shall be considered to be in India.

It has also been provided that for this purpose, merely because the BoD follows general and objective principles of global policy of the group laid down by the parent entity which may be in the field of Pay roll functions, Accounting, Human resource (HR) functions, IT infrastructure and network platforms, Supply chain functions, Routine banking Operational procedures, and not being specific to any entity or group of entities per se; would not constitute a case of BoD of companies standing aside.

In view of the above, it is clarified that so long as the Regional Headquarter Operates for subsidiaries/ group companies in a region within the general and objective principles of global policy of the group laid down by the parent entity in the field of Pay roll functions, Accounting, HR functions, IT infrastructure and network platforms, Supply chain functions, Routine banking operational procedures, and not being specific to any entity or group of entities per se; it would, in itself, not constitute a case of BoD of companies standing aside and such activities of Regional Headquarter in India alone will not be a basis for establishment of PoEM for such subsidiaries/ group companies.

It is further clarified that the provisions of General Anti-Avoidance Rule contained in Chapter X-A of the Income-tax Act, 1961 may get triggered in such cases where the above clarification is found to be used for abusive/ aggressive tax planning.

Clarification on applicability of section 9(1)(i) relating to indirect transfer in case of redemption of share or interest outside India [Circular No. 28/2017, dated 07-11-2017]

As per sec. 9(1)(i), all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India or through the transfer of a capital asset situate in India, shall be deemed to accrue or arise in India.

Explanation 5 to section 9(1)(i) provides that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India.

Concerns were raised by investment funds, including private equity funds and venture capital funds that on account of the extant indirect transfer provisions in the Act, non-resident investment funds investing in India, which are set up as multi-tier investment structures, suffer multiple taxation of the same income at the time of subsequent redemption or buyback. Such taxability arises firstly at the level of the fund in India on its short term capital gain/business income and then at every upper level of investment in the fund chain on subsequent redemption or buyback.

Vide Finance Act, 2017, Category I and Category II FPIs have already been exempted from indirect transfer provisions of the Act through insertion of proviso to Explanation 5 to section 9(1)(i) of the Act, with effect from 01.04.2015.

There could be situations in multi-tiered investment structures, where interest or share held indirectly by a non-resident in an Investment Fund or a Venture Capital Company or a Venture Capital Fund (hereinafter referred to as 'specified funds'), is redeemed in an upstream entity outside India in consequence of transfer of shares or

securities held in India by the specified funds, the income of which have been subject to tax in India. In such cases, application of indirect transfer provisions on redemption of share or interest in the upstream entity may lead to multiple taxation of the same income. In respect of Category I and Category II FPIs though, such multiple taxation will not take place on account of the insertion of proviso to Explanation 5 to section 9(1)(i) of the Act, vide Finance Act, 2017.

The CBDT has received representations to exclude investors above the level of the direct investor who is already chargeable to tax in India on such income from the ambit of indirect transfer provisions of the Act.

In order to address this concern, the CBDT has clarified that the provisions of section 9(1)(i) read with *Explanation 5*, shall not apply in respect of income accruing or arising to a non-resident on account of redemption or buyback of its share or interest held indirectly (i.e. through upstream entities registered or incorporated outside India) in the specified funds (namely, investment funds, venture capital company and venture capital funds) if such income accrues or arises from or in consequence of transfer of shares or securities held in India by the specified funds and such income is chargeable to tax in India.

However, the above benefit shall be applicable only in those cases where the proceeds of redemption or buyback arising to the non-resident do not exceed the pro-rata share of the non-resident in the total consideration realized by the specified funds from the said transfer of shares or securities in India. It is further clarified that a non-resident investing directly in the specified funds shall continue to be taxed as per the extant provisions of the Act.

Foreign company said to be resident in India [Sec. 115JH]

Where,

i. a foreign company is said to be resident in India in any previous year; and

ii. such foreign company has not been resident in India in any of the previous years preceding the said previous year,

then, the provisions relating to the computation of total income, treatment of unabsorbed depreciation, set off or carry forward and set off of losses, collection and recovery and special provisions relating to avoidance of tax shall apply with such exceptions, modifications and adaptations as may be specified in notification[3] issued by the Government for the said previous year.

Consequences when such company fails to comply with the conditions

- Where, in a previous year, any benefit, exemption or relief has been claimed and granted to the foreign company and, subsequently, there is failure to comply with any of the conditions specified in the notification, then,:
  - i. such benefit, exemption or relief shall be deemed to have been wrongly allowed;
  - ii. the Assessing Officer may, notwithstanding anything contained in this Act, re-compute the total income of the assessee for the said previous year and make the necessary amendment as if the exceptions, modifications and adaptations did not apply; and
  - iii. the provisions of sec. 154 shall, so far as may be, apply thereto and the period of 4 years specified therein being reckoned from the end of the previous year in which the failure to comply with the conditions takes place.

Other Point

- Where the determination regarding foreign company to be resident in India has been made in the assessment proceedings relevant to any previous year, then the provisions shall also apply in respect of any other previous year, succeeding such previous year, if the foreign company is resident in India in that previous year and the previous year ends on or before the date on which such assessment proceeding is completed.

3 Notification No. 29/2018 dated 22/06/2018

1.1.1 Computation of income on presumptive basis

Shipping Business in the case of Non-residents [Sec. 44B]

Applicable to	All non-resident assesse
Condition	Assessee must be engaged in the business of operation of ships.
Estimated income	Income taxable under the head "Profits & gains of business or profession" from such business shall be estimated at 7.5% of the amount being aggregate of the following: 1. The amount paid or payable (whether in or out of India) to the assessee (or to any person on his behalf) on account of the carriage of passengers, livestock, mail or goods shipped at any port in India; and 2. The amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods shipped at any port outside India.
Notes: The amount paid or payable or received or deemed to be received, as the case may be, shall also include demurrage charges or handling charges or any other amount of similar nature.	

Special procedure for Shipping Business of Non-residents [Sec. 172]

Applicable to

The section is applicable for the purpose of the levy and recovery of tax in the case of any ship, belonging to or chartered by a non-resident, which carries passengers, livestock, mail or goods shipped at a port in India.

Deemed Income

Where such a ship carries passengers, livestock, mail or goods shipped at a port in India, $7^{1}/_{2}$% of the amount paid or payable on account of such carriage to the owner or the charterer or to any person on his behalf, whether that amount is paid or payable in or out of India, shall be deemed to be income accruing in India to the owner or charterer on account of such carriage.

Computation of Tax

- Before the departure from any port in India of any such ship, the master of the ship shall prepare and furnish to the Assessing Officer a return of the full amount paid or payable to the owner or charterer or any person on his behalf, on account of the carriage of all passengers, livestock, mail or goods shipped at that port since the last arrival of the ship thereat.
- However, where the AO is satisfied that it is not possible for the master of the ship to furnish such return before the departure of the ship from the port and provided the master of the ship has made satisfactory arrangements for the filing of the return and payment of the tax by any other person on his behalf, the Assessing Officer may, if the return is filed within 30 days of the departure of the ship, deem the filing of the return by the person so authorised by the master as sufficient compliance.
- On receipt of the return, the Assessing Officer shall assess such income and determine the sum payable as tax thereon at the rate or rates in force applicable to the total income of a company which has not made the arrangements referred to in sec. 194 (i.e. foreign company) and such sum shall be payable by the master of the ship.
- For this purpose, the Assessing Officer may call for such accounts or documents as he may require.
- No order assessing the income and determining the sum of tax payable thereon shall be made after the expiry of 9 months from the end of the financial year in which the return is furnished.

Other Provisions

- **Option to claim that assessment shall be made***:* The owner or charterer of a ship has option to claim before the expiry of the assessment year relevant to the previous year in which the date of departure of the ship from the Indian port falls, that an assessment be made of his total income of the previous year and the tax payable on the basis thereof be determined in accordance with the other provisions of this Act. If he so claims, any payment made u/s 172 shall be treated as advance tax and the difference between the sum so paid and the amount of tax found payable by him on such assessment shall be paid by him or refunded to him, as the case may be [Sec. 172(7)]
- The ship which leaves the Indian port and only casually visits the Indian port is covered by sec. 172 and those who do regular shipping business are covered by sec. 44B [*V.M. Salgaocar & Brother Ltd. -vs.- Deputy Controller [1991] 187 ITR 381 (Kar.)*]

Profits & Gains in connection with the Business of Exploration, etc. of Mineral Oils [Sec. 44BB]

Applicable to	Non-resident assessee
Conditions	Assessee must be engaged in the business of - ➢ Providing services or facilities in connection with; or ➢ Supplying plant[1] and machinery on hire, used or to be used in, – the prospecting for, or extraction or production of, mineral oils[2]. 1. Plant includes ships, aircraft, vehicles, drilling units, scientific apparatus and equipment, used for the purpose of the said business 2. Mineral oil includes petroleum and natural gas.
Estimated income	A sum equal to 10% of the aggregate of the following amount shall be deemed to be the profits and gains of such business chargeable to tax - ➢ The amount paid or payable (whether in or out of India) to the assessee (or to any person on his behalf) on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils in India; and ➢ The amount received or deemed to be received in India by or on behalf of the assessee on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils outside India.
Assessee may claim lower profit	An assessee may claim lower profits and gains if he keeps and maintains books of account as per sec. 44AA and gets his accounts audited and furnishes the report u/s 44AB and thereupon the Assessing Officer shall proceed to make an assessment of the total income of the assessee u/s 143(3) & determine the sum payable by, or refundable to, the assessee
Taxpoint	Benefit of unabsorbed depreciation and brought forward loss shall not be allowed to the assessee for such previous year

Profits and Gains of the Business of Operation of Aircraft [Sec. 44BBA]

Applicable to	All non-resident assessee.
Condition	Assessee must be engaged in the business of operation of aircraft.

Estimated income	Income of such business shall be estimated at 5% of the aggregate of the following - ➢ The amount paid or payable (whether in or out of India) to the assessee (or to any person on his behalf) on account of the carriage of passengers, livestock, mail or goods from any place in India; and ➢ The amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods from any place outside India.

Illustration 1:

USA Airlines incorporated as a company in USA operates its flights to India and vice versa during the year 2023-24 and collects charges of ₹ 150 lakh for carriage of passengers and cargo out of which ₹ 90 lakh were received in US Dollars for the passenger fare booked from New York to Mumbai. The total expenses for the year on operation of such flights were ₹ 195 lakh. Income chargeable to tax of the foreign airlines may please be computed.

Solution:

Computation of income of USA Airlines

Particulars	Fare booked from Mumbai to New York whether paid in India or outside India	Fare booked from New York to Mumbai	
		If paid in India (or deemed to be received in India)	If paid outside India
Fare	₹ 60 lakh [₹ 150–₹ 90]	₹ 90 lakh	₹ 90 lakh
Taxable Income @ 5% of the above	₹ 3,00,000	₹ 4,50,000	-

Profits and Gains of Foreign Companies engaged in the Business of Civil Construction, etc. in certain Turnkey Power Projects [Sec. 44BBB]

Applicable to	A foreign company
Condition	The assessee must be engaged in the business of - ➢ civil construction; or ➢ erection of plant or machinery or testing or commissioning thereof, – in connection with a turnkey power project approved by the Central Government in this behalf.
	Approval issued by the Department of Power in the Ministry of Energy shall be deemed to be the approval of the Central Government for this section.
Estimated income	Income of such business shall be estimated at 10% of the amount paid or payable (whether in or out of India) to the said assessee (or to any person on his behalf) on account of such civil construction, erection, testing or commissioning.
Assessee may claim lower profit	An assessee may claim lower profits and gains if he keeps and maintain books of account as per sec. 44AA and gets his accounts audited and furnishes the report u/s 44AB and thereupon the Assessing Officer shall proceed to make an assessment of the total income of the assessee u/s 143(3) and determine the sum payable by, or refundable to, the assessee.
Taxpoint	Benefit of unabsorbed depreciation and brought forward loss shall not be allowed to the assessee for such previous year

Special Provision for Computing Income by way of Royalties, etc. in case of Non-resident [Sec. 44DA]

Applicable to	A non-resident (not being a company) or a foreign company
Conditions	1. Assessee has earned income by way of royalty or fees for technical services received from the Government or an Indian concern in pursuance of an agreement made with the Government or the Indian concern; 2. Assessee carries on business in India through a permanent establishment situated therein, or performs professional services from a fixed place of profession situated therein; and 3. Right, property or contract in respect of which royalties or fees for technical services are paid is effectively connected with such permanent establishment or fixed place of profession, as the case may be.
Agreement date	After 31/3/2003
Tax Treatment	Income shall be computed under the head "Profits and gains of business or profession" in accordance with the provisions of this Act:
Deduction not permissible	No deduction shall be allowed in respect of - ➢ any expenditure or allowance which is not wholly and exclusively incurred for the business of such permanent establishment or fixed place of profession in India; or ➢ amounts paid (otherwise than towards reimbursement of actual expenses) by the permanent establishment to its head office or to any of its other offices.

Note: Assessee shall keep and maintain books of account and other documents as per sec. 44AA and get his accounts audited u/s 44AB and upload one month prior to the due date of filing of the return of income, the report of such audit in Form 3CE duly signed and verified by chartered accountant.

Deduction of Head Office Expenditure in the case of Non-residents [Sec. 44C]

In case of a non-resident assessee, head office expenditure shall not be allowed (in computing the income chargeable under the head "Profits and gains of business or profession") in excess of the higher of the following amount:

(i) an amount equal to 5% of the adjusted total income; or

(ii) the amount of so much of the expenditure in the nature of head office expenditure incurred by the assessee as is attributable to the business or profession of the assessee in India,

Other Points

- Adjusted total income means the total income without giving effect to:
  a) Head-office expenditure u/s 44C; or
  b) Unabsorbed depreciation u/s 32(2); or
  c) The first proviso to sec. 36(1)(ix) i.e. capital expenditure on family planning; or
  d) Any loss carried forward u/s 72 or 73 or 74 or 74A; or
  e) The deductions under Chapter VIA;
- Where the adjusted total income of the assessee is a loss, then (i) shall be computed at the rate of 5% of the average adjusted total income of the assessee.

- Average adjusted total income means average of adjusted total income of 3 assessment years immediately preceding the relevant assessment year. However, where the total income of the assessee is assessable only for last 2 or 1 year(s), then average of last 2 or 1 year(s) shall be considered.
- Head office expenditure means executive and general administration expenditure incurred by the assessee outside India, including expenditure incurred in respect of:

  (a) rent, rates, taxes, repairs or insurance of any premises outside India used for the purposes of the business or profession;

  (b) salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;

  (c) travelling by any employee or other person employed in, or managing the affairs of, any office outside India; and

  (d) such other matters connected with executive and general administration as may be prescribed.

1.1.2 Capital gain on transfer of shares / debentures by a non-resident [First proviso to Sec. 48 and rule 115A]

Applicable on

A *non-resident* assessee (not being an assessee covered u/s 115AC and 115AD)

Nature of asset

Capital assets whether long-term or short term being shares in, or debentures of *an Indian company* acquired by utilizing foreign currency

Taxpoint:

- The provision shall also be applicable in respect of capital gains accruing or arising on transfer of shares in, or debentures of, an Indian company, acquired through reinvestment.
- The asset may be a short-term or long-term capital asset.
- The above provision is not applicable to units of UTI and Mutual Funds.

Procedure

Capital gain on transfer of above asset shall be computed as under:

- Cost of acquisition, expenditure on transfer and the sale consideration shall be converted into the same foreign currency as was initially utilized in the purchase of the shares or debentures; and
- Capital gains (computed in such foreign currency) shall be reconverted into Indian currency.

Taxpoint:

- Benefit of indexation shall not be available in case of above transfer.
- The method of computation is mandatory and not optional.
- Capital gain shall be determined as under:

Step	Conversion of	Particulars	Conversion rate
1	Sale consideration	Find sale consideration in Indian currency and convert it into foreign currency	At average exchange rate[1] on the date of transfer
2	Expenditure on transfer	Find expenditure on transfer in Indian currency and convert it into foreign currency	At average exchange rate on the date of transfer (not on the date when expenditure was incurred)
3	Cost of acquisition	Find cost of acquisition in Indian currency and convert it into foreign currency	At average exchange rate on the date of acquisition.
4	Capital gain in foreign currency	Step 1 – Step 2 – Step 3	Not applicable
5	Taxable Capital gain	Capital gain so calculated (in step 4) will be reconverted into Indian currency	At buying rate[2] on the date of transfer

1. **Average exchange rate:** It is the average of the telegraphic transfer buying rate and telegraphic transfer selling rate.
2. **Buying Rate:** It is telegraphic transfer buying rate of such currency.

   Telegraphic transfer buying/selling rate in relation to a foreign currency is a rate of exchange adopted by the State Bank of India for purchasing/selling such currency where such currency is made available by that bank through telegraphic transfer.

Illustration 2:

Anthony, a non-resident Indian, acquired 1,000 shares in A Ltd. (an Indian Company) for ₹ 20,000 by utilizing foreign currency (SGP $) on 18/08/2023. On 16/09/2023, Anthony sold such shares for ₹ 45,000 and utilized the proceeds in acquisition of 500 shares of B Ltd. (an Indian Company) after paying expenditure on transfer on 13/9/2023 ₹ 5,000. Compute capital gain liability in the previous year 2023-24.

Date	Buying rate	Selling rate
18/08/2023	45	46
13/09/2023	48	50
16/09/2023	46	48

Solution:

Since the assessee is a non-resident and shares of an Indian company were acquired by utilizing foreign currency, hence, first proviso to sec. 48 and Rule 115A shall be applicable on above transactions.

Computation of capital gain for the A.Y. 2024-25

Particulars	Working	Rate applied	Amount	Amount
Sale consideration	₹ 45,000/₹ 47	Av. rate as on 16/09/2023		$957.4
Less: Expenditure on transfer	₹ 5,000/₹ 47	Av. rate as on 16/09/2023		$106.4
Net Sale consideration				$851.0
Less: Cost of acquisition	₹ 20,000/₹ 45.5	Av rate as on 18/08/2023	$439.6	
Less: Cost of improvement			Nil	$439.6
Short term Capital Gain				$411.4
Short term capital gain	**$411.4 × ₹ 46**	Buying rate as on 16/09/2023		**₹ 18,924**

Special Tax Rate for Long Term Capital Gain in Some Cases [Sec. 112(1)(c)]

Applicable on

Non-resident (not being a company) or a foreign company

Conditions to be satisfied

1. Long-term capital gains shall be arising from the transfer of a capital asset, being unlisted securities or shares of a company in which the public are substantially interested.
2. Capital gain in respect of such asset shall be computed without giving effect to the
   - first proviso to sec. 48 (computation of capital gain in foreign currency) and
   - second proviso to sec. 48 (index benefit).

Special Tax Rate

Such long term capital gain shall be taxable @ 10% (+ surcharge and cess, as applicable).

Special Provisions in relation to certain income of Non-residents [Sec. 115A to Sec.115AC]

Following table enumerated the provisions relating to sec.115A to 115AC

Sec. Particulars	115A(1)(a)	115A(1)(b)	115AB	115AC
Applicable on	Non-resident	Non-resident	Overseas financial organization[$]	Non-resident
Income covered	a) Dividends; or b) Interest received from notified infrastructure bonds or Govt. or an Indian concern on money borrowed in foreign currency; or c) Interest of the nature and extent referred to in sec. 194LC/194LD/ 194LBA(2)	Royalty or fees for technical services (other than income covered u/s 44DA) received as per agreement entered with Government or an Indian concern[2] on or after 1-4-1976	Long-term capital gains arising from the transfer of units of UTI or mutual fund specified u/s 10(23D) purchased in foreign currency	a) Interest on notified foreign currency bonds of Indian / public sector company b) Dividend on GDR c) LTCG arising on transfer of such bonds or Global Depository Receipts (GDR)
Special tax rate	10% (Dividend received from a unit in IFSC) or 5% or 4% or 10% (respective rates referred to in sec. 194LC or 194LD or 194LBA)/ 20% (other cases)	20%	10%	10%
Allowability of expenditure u/s 28 to 44C & sec. 57	No	No	Not Applicable	No

4 Where such agreement is with an Indian concern, the agreement is approved by the Central Government or where it relates to a matter included in the industrial policy, for the time being in force, of the Government of India, the agreement is in accordance with that policy

Sec. Particulars	115A(1)(a)	115A(1)(b)	115AB	115AC
Deduction under Chapter VIA	Not available **Exception** Deduction u/s 80LA can be claimed by a Unit of an International Financial Services Centre	Available	Not available	Not available
Index benefit	Not Applicable	Not Applicable	Not Available	Not Available
Requirement to furnish return#	No	Yes	Yes	No

If total income consists of such income only and appropriate tax has been deducted from such income

$Overseas financial organisation means any fund, institution, association or body, whether incorporated or not, established under the laws of a country outside India, which has entered into an arrangement for investment in India with any public sector bank or public financial institution or a mutual fund specified u/s 10(23D) and such arrangement is approved by the Securities and Exchange Board of India.

Special Provisions in relation to certain Income of Non-residents [Sec. 115ACA to Sec.115BBA]

The following table enumerated the provisions relating to sec.115ACA to 115BBA

Sec. Particulars	115ACA	115AD	115BBA(1)(a)	115BBA(1)(b)
Applicable on	Resident individual	Specified Fund[3] or Foreign Institutional Investor	Non-resident sportsman or entertainer being foreign citizen	Non-resident sports association
Income covered	a) Dividend on GDR$ of an Indian company engaged in specified knowledge based industry or service* issued as ESOP b) Long-term capital gains on transfer of such GDR	a) Income on securities (other than unit referred to in sec. 115AB) b) STCG or LTCG on transfer of such securities	Income by way of: a) participation in India in any game or sport; or b) advertisement; or c) contribution of articles relating to any game or sport in India in newspapers, magazines or journals. In case of entertainer, any income received or receivable from his performance in India, **Taxpoint:** Match Referee is not considered as sportsmen.	Any amount guaranteed to be paid or payable to such association for any game or sport played in India

5 In case of specified fund, the provision of sec. 115AD shall apply only to the extent of income that is attributable to units held by non-resident (not being a permanent establishment of a non-resident in India) calculated in the prescribed manner.

Sec. Particulars	115ACA	115AD		115BBA(1)(a)	115BBA(1)(b)
Special tax rate	10%	Interest u/s 194LD	5%	20%	20%
		STCG u/s 111A	15%		
		Other STCG	30%		
		LTCG[@]	10%		
		Other Income	20% (10% in case of specified fund)		
Allowability of expenditure u/s 28 to 44C & sec. 57	No	No		No	No
Deduction u/ch VIA	Not available	Not available		Not available	Not available
Index benefit	Not Available	Not Available		Not Applicable	Not Applicable
Requirement to furnish return#	Yes	Yes		No	No
Others	Assessee must be an employee of such company or its subsidiary			Winning from lottery, cross-word puzzles etc. is taxable @ 30% u/s 115BB	

[@] In case of long-term capital asset referred to in section 112A, income-tax @ 10% shall be calculated on such income exceeding ₹ 1 lakh.

[#] Specified knowledge based industry or service means:

a. information technology software;
b. information technology service;
c. entertainment service;
d. pharmaceutical industry;
e. bio-technology industry; and
f. any other specified industry or service

[$]Global Depository Receipts means any instrument in the form of a depository receipt or certificate (by whatever name called) created by the Overseas Depository Bank outside India or in an International Financial Services Centre and issued to investors against the issue of:

i. ordinary shares of issuing company, being a company listed on a recognised stock exchange in India; or
ii. foreign currency convertible bonds of issuing company
iii. ordinary shares of issuing company, being a company incorporated outside India, if such depository receipt or certificate is listed and traded on any International Financial Services Centre

⊙ Where the specified fund is investment division of an offshore banking unit, the provisions of sec. 115AD shall apply to the extent of income that is attributable to the investment division of such banking units, referred to in clause (c)(ii) to the Explanation to sec. 10(4D), as a Category-I portfolio investor under the Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2019 made under the Securities and Exchange Board of India Act, 1992, calculated in such manner as may be prescribed.

Special Provision in case of Non-resident Indian [Sec.115C to 115-I]

Applicable on

Non-resident Indians deriving –

(a) Income from investment in foreign exchange asset; or

(b) Long-term capital gain on foreign exchange asset.

Taxpoint

- Foreign exchange asset means any specified asset, which the assessee has acquired or purchased with, or subscribed to, in convertible foreign exchange.
- Specified asset means any of the following –
  - Shares in Indian company;
  - Debenture issued by an Indian company which is not a private company;
  - Deposit with an Indian company, which is not a private company;
  - Any security of the Central Government; or
  - Any notified asset.
- Investment income means any income derived from a foreign exchange asset.
- Long-term capital gain means income chargeable under the head Capital gains relating to a capital asset, being a foreign exchange asset, which is not a short-term capital asset.
- Non-resident Indian means an individual, being a citizen of India or a person of Indian origin who is not a resident.

Special Provision [Sec. 115D]

1. No deduction in respect of any expenditure or allowance is allowed under any provision of this Act in computing the investment income.
2. No deduction shall be allowed to the assessee u/s 80C to 80U

Tax on Investment Income and Long-term Capital Gain [Sec. 115E]

Nature of income	Rate of tax
Income from investment	20%
Long term capital gain	10%

Exempted Capital Gain [Sec. 115F]

Applicable to

Non-resident Indian (i.e. an individual being a citizen of India or a person of Indian origin who is a non-resident)

Conditions

1. Assessee has transferred any of the following long term capital asset, acquired in convertible foreign exchange:
   - Shares in an Indian company; or
   - Debentures of an Indian public limited company; or
   - Deposits with an Indian public limited company; or
   - Central Government securities.

   (hereinafter referred to as *original asset*)

2. Within 6 months of transfer of original asset, the taxpayer has invested the whole or any part of net consideration in any of the following assets (hereinafter referred to as *new asset*)
   a) Shares in an Indian company; or
   b) Debentures of an Indian public limited company; or
   c) Deposit with an Indian public limited company; or
   d) Central Government securities; or
   e) National Savings Certificate VI and VII issues.

Amount of exemption

Exemption is available to the minimum of the following –

- Long term capital gain; or
- $\frac{\text{Long term capial gain} \times \text{Amount invested in the new asset}}{\text{Net sale consideration on transfer of original asset}}$

Withdrawal of exemption

When the new asset acquired by the assessee is transferred or converted into money within 3 years from the date of its acquisition, the capital gains exempted earlier shall be revoked.

On revocation of exemption, benefit availed earlier under this section shall be taxed as long-term capital gain in the previous year in which such new asset is transferred or converted into money.

Note: Sec. 115F is optional in nature and not mandatory, i.e. an assessee may or may not opt for sec. 115F by giving a declaration in return of income to this effect. [Sec. 115-I]

Return of Income not to be Filed in certain cases [Sec. 115G]

It is not necessary to file return if during the previous year there is no other income and tax has been deducted at source.

Applicability of Provisions after Becoming Resident [Sec. 115H]

Where a person become assessable as resident in India in any subsequent previous year, he may assessed as above provisions for that income provided he file a declaration in writing along with his return of income of subsequent year in this regard.

Non-applicability of Provisions [Sec. 115I]

An assessee may elect not to be governed by this provision for any assessment year by furnishing return of income for that assessment year u/s 139 declaring therein that the provision of this chapter shall not apply on him for that assessment year and if he does so, the provisions of this chapter shall not apply on him.

Conversion of an Indian branch of Foreign Company into Subsidiary Indian Company [Sec. 115JG]

Where a foreign company is engaged in the business of banking in India through its branch situated in India and such branch is converted into a subsidiary company thereof, being an Indian company (hereafter referred to as an Indian subsidiary company) in accordance with the scheme framed by the Reserve Bank of India (and subject to the conditions as may be notified by the Central Government), then,

(a) The capital gains arising from such conversion shall not be chargeable to tax in the assessment year relevant to the previous year in which such conversion takes place.

(b) The provisions of this Act relating to treatment of unabsorbed depreciation, set off or carry forward and set off of losses, tax credit in respect of tax paid on deemed income relating to certain companies and the computation of income in the case of the foreign company and the Indian subsidiary company shall apply with such exceptions, modifications and adaptations as may be specified in that notification.

Consequence of failure to Comply with any of the Conditions

In case of failure to comply with any of the conditions specified in the scheme or in the notification, all the provisions of this Act shall apply to the foreign company and the said Indian subsidiary company without aforesaid benefit, exemption or relief.

Consequence of failure to Comply with any of the conditions after Claiming Benefit

Where, in a previous year, any benefit, exemption or relief has been claimed and granted to the foreign company or the Indian subsidiary company and, subsequently, there is failure to comply with any of the conditions specified in the scheme or in the notification, then:

(a) Such benefit, exemption or relief shall be deemed to have been wrongly allowed;

(b) The Assessing Officer may, notwithstanding anything contained in this Act, re-compute the total income of the assessee for the said previous year and make the necessary amendment; and

(c) The provisions of sec. 154 shall, so far as may be, apply thereto and the period of 4 years specified in that section being reckoned from the end of the previous year in which the failure to comply with the condition takes place.

Submission of Statement by a Non-resident having Liaison Office [Sec.285]

Every person, being a non-resident having a liaison office in India set up in accordance with the guidelines issued by the Reserve Bank of India under the Foreign Exchange Management Act, 1999, shall, in respect of its activities in a financial year, prepare and deliver to the Assessing Officer having jurisdiction, within 60 days from the end of such financial year, a statement in such form (Form 49C) and containing such particulars as may be prescribed.

Furnishing of the report in respect of international group [Sec. 286]

- Every constituent entity resident in India, shall, if it is constituent of an international group, the parent entity of which is not resident in India, notify the prescribed income-tax authority (herein referred to as prescribed authority) in the form and manner, on or before such date, as may be prescribed:

  a) whether it is the alternate reporting entity of the international group; or

  b) the details of the parent entity or the alternate reporting entity, if any, of the international group, and the country or territory of which the said entities are resident. [Sec. 286(1)]

- Every parent entity or the alternate reporting entity, resident in India, shall, for every reporting accounting year, in respect of the international group of which it is a constituent, furnish a report[6], to the prescribed authority[7] within a period of 12 months from the end of the said reporting accounting year, in the form and manner as may be prescribed [Sec. 286(2)]

- The report in respect of an international group shall include:

  a. the aggregate information in respect of the amount of revenue, profit or loss before income-tax, amount of income-tax paid, amount of income-tax accrued, stated capital, accumulated earnings, number of employees and tangible assets not being cash or cash equivalents, with regard to each country or territory in which the group operates;

  b. the details of each constituent entity of the group including the country or territory in which such constituent entity is incorporated or organised or established and the country or territory where it is resident;

6 Rule 10DB: Form Nos. 3CEAC to 3CEAE

7 Director General of Income-tax (Risk Assessment)

c. the nature and details of the main business activity or activities of each constituent entity; and

d. any other information as may be prescribed.

- A constituent entity of an international group, resident in India, other than the entity referred to sec. 286(2), shall furnish the report, in respect of the international group for a reporting accounting year within prescribed period, if the parent entity is resident of a country or territory,—

  a. where the parent entity is not obligated to file such report;

  b. with which India does not have an agreement providing for exchange of such report; or

  c. there has been a systemic failure of the country or territory and the said failure has been intimated by the prescribed authority to such constituent entity.

- However, if there are more than one such constituent entities of the group, resident in India, the report shall be furnished by any one constituent entity, if,—

  a. the international group has designated such entity to furnish such report on behalf of all the constituent entities resident in India; and

  b. the information has been conveyed in writing on behalf of the group to the prescribed authority.

- If, an alternate reporting entity of the international group has furnished such report with the tax authority of the country or territory in which such entity is resident, on or before the date specified by that country or territory and the following conditions are satisfied then separate report is not required to be furnished:

  a. the report is required to be furnished under the law for the time being in force in the said country or territory;

  b. the said country or territory has entered into an agreement with India providing for exchange of the said report;

  c. the prescribed authority has not conveyed any systemic failure in respect of the said country or territory to any constituent entity of the group that is resident in India;

  d. the said country or territory has been informed in writing by the constituent entity that it is the alternate reporting entity on behalf of the international group; and

  e. the prescribed authority has been informed by such entity.

- The prescribed authority may, for the purposes of determining the accuracy of the report furnished by any reporting entity, by issue of a notice in writing, require the entity to produce such information and document as may be specified in the notice within 30 days of the date of receipt of the notice.

- The prescribed authority may, on an application made by such entity, extend the period of thirty days by a further period not exceeding 30 days.

- The provisions of this section shall not apply in respect of an international group for an accounting year, if the total consolidated group revenue, as reflected in the consolidated financial statement for the accounting year preceding such accounting year does not exceed prescribed amount[8].

[8] Rule 10DB(6) provides that for the purposes of sec. 286(7), the total consolidated group revenue of the international group shall be ₹ 5,500 crores

- "Accounting Year" means:

  a. a previous year, in a case where the parent entity is resident in India; or

  b. an annual accounting period, with respect to which the parent entity of the international group prepares its financial statements under any law for the time being in force or the applicable accounting standards of the country or territory of which such entity is resident, in any other case.

- "Agreement" means a combination of all of the following agreements:

  i. an agreement entered into u/s 90 or u/s 90A; and

  ii. an agreement for exchange of the report referred to in sec. 286(2) and notified by the Central Government.

- "Alternate Reporting Entity" means any constituent entity of the international group that has been designated by such group, in the place of the parent entity, to furnish the report in the country or territory in which the said constituent entity is resident on behalf of such group.

- "Constituent Entity" means:

  i. any separate entity of an international group that is included in the consolidated financial statement of the said group for financial reporting purposes, or may be so included for the said purpose, if the equity share of any entity of the international group were to be listed on a stock exchange;

  ii. any such entity that is excluded from the consolidated financial statement of the international group solely on the basis of size or materiality; or

  iii. any permanent establishment of any separate business entity of the international group included in (i) or (ii) [*supra*], if such business unit prepares a separate financial statement for such permanent establishment for financial reporting, regulatory, tax reporting or internal management control purposes;

- "Group" includes a parent entity and all the entities in respect of which, for the reason of ownership or control, a consolidated financial statement for financial reporting purposes,—

  i. is required to be prepared under any law for the time being in force or the accounting standards of the country or territory of which the parent entity is resident; or

  ii. would have been required to be prepared had the equity shares of any of the enterprises were listed on a stock exchange in the country or territory of which the parent entity is resident;

- "Consolidated Financial Statement" means the financial statement of an international group in which the assets, liabilities, income, expenses and cash flows of the parent entity and the constituent entities are presented as those of a single economic entity.

- "International Group" means any group that includes,—

  i. two or more enterprises which are resident of different countries or territories; or

  ii. an enterprise, being a resident of one country or territory, which carries on any business through a permanent establishment in other countries or territories;

- "Parent Entity" means a constituent entity, of an international group holding, directly or indirectly, an interest in one or more of the other constituent entities of the international group, such that:

  i. it is required to prepare a consolidated financial statement under any law for the time being in force or the accounting standards of the country or territory of which the entity is resident; or

ii. it would have been required to prepare a consolidated financial statement had the equity shares of any of the enterprises were listed on a stock exchange,

and, there is no other constituent entity of such group which, due to ownership of any interest, directly or indirectly, in the first mentioned constituent entity, is required to prepare a consolidated financial statement, under the circumstances referred to in (i) or (ii) [*supra*], that includes the separate financial statement of the first mentioned constituent entity;

- "Reporting Accounting Year" means the accounting year in respect of which the financial and operational results are required to be reflected in the report
- "Reporting Entity" means the constituent entity including the parent entity or the alternate reporting entity, that is required to furnish a report.
- "Systemic Failure" with respect to a country or territory means that the country or territory has an agreement with India providing for exchange of such report, but—

i. in violation of the said agreement, it has suspended automatic exchange; or

ii. has persistently failed to automatically provide to India the report in its possession in respect of any international group having a constituent entity resident in India.

Withholding Tax for Non-Resident

1.1.3 TDS on payment to non-resident sportsman or sports associations [Sec. 194E]

Who is responsible to deduct tax: Any person who is responsible to pay the following income –

Payee	Income by way of
Sportsman (including an athlete) or an entertainer being non-resident foreign citizen	1. Participation in India in any game (excluding card game or gambling) or sport
	2. Advertising
	3. Contribution of articles relating to any game or sports in any newspaper, magazine or journal.
Sports association being non- resident	Any game (other than card game) or sports organised in India

Rate of TDS: 20% (+ Surcharge + Health & Education Cess)

When tax shall be deducted: At the time of payment or crediting the party whichever is earlier.

1.1.4 TDS on interest from Infrastructure Debt Fund [Sec. 194LB]

Who is responsible to deduct tax: Any person responsible for paying income by way of interest by an infrastructure debt fund referred to in sec. 10(47) to a non-resident or a foreign company.

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: 5% (+ SC + HEC)

1.1.5 TDS on interest to non-resident [Sec. 194LC]

Who is responsible to deduct tax: Any Indian company or a business trust[4] responsible for paying income by way of interest to a non-resident or a foreign company. Such interest is payable in respect of

1. in respect of monies borrowed by it in foreign currency from a source outside India:
   a. under a loan agreement at any time on or after 01-07-2012 but before 01-07-2023; or
   b. by way of issue of long-term infrastructure bonds at any time 01-07-2012 but before 01-10-2014; or
   c. by way of issue of any long-term bond including long-term infrastructure bond at 01-10-2014 but before 01-07-2023,

   as approved by the Central Government in this behalf; or
2. in respect of monies borrowed by it from a source outside India by way of issue of rupee denominated bond before 01-07-2023; or
3. in respect of monies borrowed by it from a source outside India by way of issue of any long-term bond or rupee denominated bond on or after 01-04-2020 but before 01-07-2023, which is listed only on a recognised stock exchange located in any International Financial Services Centre,
4. in respect of money borrowed by it from a source outside India by way of issuance of any long-term bond or rupee denominated bond on or after 01-07-2023, which is listed only on a recognised stock exchange located in an International Financial Services Centre
5. to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf, having regard to the terms of the loan or the bond and its repayment.

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: 5% (+ SC + Health & Education Cess) [in case of interest mentioned in point 3 above rate of TDS is 4%] [Further, in case of interest mentioned in point 4 above rate of TDS is 9%]

Note: W.e.f. 01-06-2013, the provisions of section 206AA (i.e. rate of TDS will be 20% in absence of PAN) shall not apply in respect of payment of interest, on long-term bonds including long term infrastructure bonds (being referred to in sec. 194LC) to a non-resident, not being a company, or to a foreign company.

1.1.6 Income by way of interest on certain bonds, Govt. securities [Sec. 194LD]

Who is responsible to deduct tax: Any person who is responsible for paying interest (at the rate notified by the Central Government) to a person being a Foreign Institutional Investor or a Qualified Foreign Investor[9]. Such interest shall be payable:

a. on or after 01-06-2013 but before 01-07-2023 in respect of the investment made by the payee in:
   i. a rupee denominated bond of an Indian company [provided rate of interest shall not exceed the notified rate]; or
   ii. a Government security;
b. on or after 01-04-2020 but before 01-07-2023 in respect of the investment made by the payee in municipal debt securities.

9 "Qualified Foreign Investor" shall have the meaning assigned to it in the Circular No. Cir/IMD/DF/14/2011, dated the 9th August, 2011, as amended from time to time, issued by the Securities and Exchange Board of India, under section 11 of the Securities and Exchange Board of India Act, 1992.

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: 5% (+ SC + Health & Education Cess)

1.1.7 TDS on other sums payable to non-resident [Sec. 195]

Who is responsible to deduct tax: Any person (resident or non-resident[10]) responsible for paying any sum chargeable under this Act (excluding income chargeable under the head "Salaries") to a non-resident.

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: At the rate in force during the financial year

Exemption or relaxation from the provision

When the recipient applies to the Assessing Officer in Form 13 and gets a certificate authorising the payer to deduct tax at lower rate or deduct no tax [Refer sec. 197]

Note: In case, payer is a Government or Public sector bank or a financial institution [within the meaning of 10(23D)], tax shall be deducted only at the time of payment.

Other Points

Provision for furnishing information: The person responsible for paying to a non-resident, not being a company, or to a foreign company, any sum, whether or not chargeable under the provisions of this Act, shall furnish the information relating to payment of such sum, in such form and manner, as may be prescribed.

If a person fails to furnish such information or furnishes inaccurate information, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of ₹ 1,00,000/- [Sec. 271-I]

Application to the Assessing Officer: The Board may notify a class of persons or cases, where the person responsible for paying to a non-resident, any sum, whether or not chargeable under the provisions of this Act, shall make an application to the Assessing Officer to determine, by general or special order, the appropriate proportion of sum chargeable, and upon such determination, tax shall be deducted on that proportion of the sum which is so chargeable.

1.1.8 TDS on income in respect of units of non-residents [Sec. 196A]

Who is responsible to deduct tax: Any person responsible for paying any income in respect of units of a Mutual Fund specified u/s 10(23D) or of the Unit Trust of India to a foreign company or to any non corporate non resident assessee.

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: 20% + SC + HEC

Exemption or relaxation from the provision:

Tax shall not be deducted from any income payable in respect of units of the Unit Trust of India to a non-resident Indian or a non-resident HUF, if the following conditions are satisfied –

- The units have been acquired from the Unit Trust of India out of the funds in a Non-resident (External) Account maintained with any bank in India; or
- The units have been acquired from the Unit Trust of India by remittance of funds in foreign currency

[10] whether or not such non-resident person has: (i) a residence or place of business or business connection in India; or (ii) any other presence in any manner whatsoever in India

Other Points

"Non-resident Indian" means an individual, being a citizen of India or a person of Indian origin who is not a "resident".

1.1.9 TDS on income from units [Sec. 196B]

Who is responsible to deduct tax: Any person responsible for paying any income in respect of units referred to in sec. 115AB or by way of long-term capital gains arising from the transfer of such units to an Offshore Fund.

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: 10% + Surcharge + Health & Education Cess

Note: Since income on units is exempted from 1-4-2003, hence, the section is applicable only in the case of long term capital gain arising on transfer of such units.

1.1.10 TDS on income from foreign currency bonds or GDR [Sec. 196C]

Who is responsible to deduct tax: Any person responsible for paying any income by way of interest or dividends in respect of bonds or Global Depository Receipts referred to in section 115AC or by way of long-term capital gains arising from the transfer of such bonds or Global Depository Receipts to a non-resident

When tax shall be deducted: At the time of payment (by any mode) or crediting the payee, whichever is earlier.

Rate of TDS: 10% + Surcharge + Health & Education Cess

1.1.11 TDS on income of FII from securities [Sec. 196D]

Who is responsible to deduct tax: Any person responsible for paying any income in respect of securities referred to in section 115AD (1)(a) [not being interest referred to in sec. 194LD] to Foreign Institutional Investor or specified fund [referred to in sec. 10(4D)].

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS: 20% (10% in case payee is specified fund) + Surcharge + Health & Education Cess

Notes

- Tax shall not be deducted from any capital gains arising from the transfer of securities referred to in section 115AD, payable to a Foreign Institutional Investor. Similarly, tax shall not be deducted if such income is exempted u/s 10(4D).
- Further, where DTAA agreement applies to the payee and if the payee has furnished a certificate referred to sec. 90 or 90A, as the case may be, then, tax shall be deducted at the rate of 20% or at the rate provided in such agreement for such income, whichever is lower.

1.1.12 Recovery of Tax

As per section 160, agent of the non-resident, including a person who is treated as an agent u/s 163 is considered as a representative assessee in respect of the income of a non-resident specified in sec. 9(1).

As per sec. 161, every representative assessee, as regards the income in respect of which he is a representative assessee, shall be subject to the same duties, responsibilities and liabilities as if the income were income received by or accruing to or in favour of him beneficially, and shall be liable to assessment in his own name in respect of that income; but any such assessment shall be deemed to be made upon him in his representative capacity only, and the tax shall, subject to the other provisions contained in this Chapter, be levied upon and recovered from him in like manner and to the same extent as it would be leviable upon and recoverable from the person represented by him.

Agent of a Non-resident [Sec. 163]

Where the person liable to tax under this Act resides outside India, then tax may be levied upon and recovered from his agent. The agent shall be deemed to be the assessee in respect of such tax. The Assessing Officer may serve a notice on the persons for his intention of treating him as the agent of non resident. No person shall be treated as the agent of a non-resident unless he has had an opportunity of being heard by the Assessing Officer as to his liability to be treated as such.

Who may be treated as an Agent

"Agent", in relation to a non-resident, includes any person in India:

(a) who is employed by or on behalf of the non-resident; or

(b) who has any business connection with the non-resident; or

(c) from or through whom the non-resident is in receipt of any income, whether directly or indirectly; or

(d) who is the trustee of the non-resident;

and includes also any other person who, whether a resident or non-resident, has acquired by means of a transfer, a capital asset in India.

Exception

A broker in India who, in respect of any transactions, does not deal directly with or on behalf of a non-resident principal but deals with or through a non-resident broker shall not be deemed to be an agent under this section in respect of such transactions, if the following conditions are fulfilled:

(i) the transactions are carried on in the ordinary course of business through the first-mentioned broker; and

(ii) the non-resident broker is carrying on such transactions in the ordinary course of his business and not as a principal.

Taxpoint

- An agent shall be entitled to -
  a) recover any sum paid by him from the person on whose behalf it is paid; or
  b) to retain out of any moneys that may be in his possession; or
  c) to retain out of any moneys that may come to him in his capacity as such agent
- Any agent or any person, who apprehends that he may be assessed as an agent, may retain (equal to estimated liability) out of any money payable by him to the person residing outside India on whose behalf he is liable to pay tax (hereinafter in this section referred to as the principal).
- However, where there is any disagreement between the principal and such agent or person, regarding amount to be so retained, such agent or person may secure from the Assessing Officer a certificate stating the amount to be so retained pending final settlement of the liability.

- The amount recoverable from such agent or person at the time of final settlement shall not exceed the amount specified in such certificate, except to the extent to which such agent or person may at such time have in his hands additional assets of the principal.

Recovery of tax in respect of non-resident from his assets [Sec. 173]

Where the person entitled to the income referred to in sec. 9(1)(i) is a non-resident, the tax chargeable thereon, whether in his name or in the name of his agent who is liable as a representative assessee, may be recovered by deduction under any of the provisions of Chapter XVII-B and any arrears of tax may also be recovered from any assets of the non-resident which are, or may at any time come, within India.

Recovery of tax in pursuance of agreements with foreign countries [Sec. 228A]

Where an assessee is in default or is deemed to be in default in making a payment of tax, the Tax Recovery Officer may, if the assessee has property in a country outside India (being a country with which the Central Government has entered into an agreement for the recovery of income-tax under this Act and the corresponding law in force in that country), forward to the Board a certificate drawn up by him u/s 222 and the Board may take such action thereon as it may deem appropriate having regard to the terms of the agreement with such country.

Illustration 3:

Smart (a non resident) has computed his tax liability as under – ₹ in lakhs

Particulars	Details	Amount
Income from business A		2,80,000
Long term capital gain	10,000	
Less: Income from business B u/s 71	(10,000)	Nil
Income from other sources		30,000
Total Income		3,10,000
Tax liability (after rebate u/s 87A)		520

Comment on the above computation.

Solution:

Computation made by Smart is incorrect, as because first intra head set-off shall be made, thereafter inter head set-off can be made. The correct computation is shown below -

Computation of total income and tax liability of Smart for the A.Y. 2024-25

₹ in lakhs

Particulars	Details	Amount
Profits & Gains of Business or Profession		
Income from business A	2,80,000	
Income from business B u/s 70	(10,000)	2,70,000
Capital Gains		
Long term capital gain		10,000
Income from other sources		30,000
Gross Total Income		3,10,000
Tax liability [(₹ 10,000 × 20%) × 104%]		2,080

In case of non-resident individual, rebate u/s 87A is not available.

Illustration 4:

Mr. Crown, a non-resident, gives you the following information for the year ended 31-3-2024

Interest on Government securities (gross)	21,000
Dividend on shares of foreign companies received aboard	52,000
Interest from deposits in Indian companies (gross)	30,000
Income from horse races in India	20,000

He has donated a sum of ₹ 10,000 to Municipal Corporation of Delhi for promotion of family planning. He has paid ₹ 2,000 by cheque to New India Assurance Co. for mediclaim for himself. He has also spent ₹ 16,000 on medical treatment of his minor son who is physically handicapped.

Compute total income of Mr. Crown for the assessment year 2024-25 assuming that he has opted for old regime

Solution:

Computation of Total Income of Mr. Crown, a non-resident, for the A.Y.2024-25

Particulars	Working	Amount	Amount
Income from other sources			
Dividend from			
Foreign company	Non-resident	Nil	
Interest from			
Government securities		21,000	
Indian company deposits		30,000	51,000
Casual income			
Winning from horse races			20,000
Gross Total Income			71,000
Less: Deduction			
U/s 80D (Medical insurance)		2,000	
U/s 80DD (Handicapped son)	Non-resident	Nil	
U/s 80G (Donation)	Note	6,900	8,900
Total Income			62,100

Note: Computation of Deduction u/s 80G

Computation of Adjusted GTI:

Adj. GTI = GTI – Deduction u/s 80CCC to 80U other than 80G

= ₹ 71,000 – ₹ 2,000 = ₹ 69,000

Qualifying amount for donation = 10% of Adjusted GTI = 10% of ₹ 69,000 = ₹ 6,900

Deduction: In case of donation to Municipal Corporation for family planning, rate of deduction is 100% of qualifying amount. Hence, deduction u/s 80G shall be ₹ 6,900 (being 100% of ₹ 6,900).

Illustration 5:

Roger, a foreign national, furnishes the following data for the previous year ended 31st March, 2024:

(i) Royalty from Indian concern under an agreement made on 15-09-1996 approved by the Central Government ₹ 3,00,000.

(ii) Expenditure as per section 28 to 44C for earning such income ₹ 2,00,000.

(iii) Interest from an Indian company on money lent in foreign currency ₹ 11,00,000.

(iv) Expenditure on collection of above interest ₹ 90,000.

(v) Gross sale of business in India ₹ 30,00,000.

(vi) Expenditure as per sections 28 to 44C for above business ₹ 28,00,000.

Determine the total income of Roger for the assessment year 2024-25.

Solution:

Computation of Total income of Roger for the A.Y. 2024-25

Particulars	Amount	Amount	Amount
Profits and gains of business or profession			
Sale	30,00,000		
Less: Expenditure	28,00,000	2,00,000	
Royalty income	3,00,000		
Less: Expenditure (Not allowed u/s 115A)	Nil	3,00,000	5,00,000
Income from other sources			
Interest income		11,00,000	
Less: Expenses (Not allowed u/s 115A)		Nil	11,00,000
Total Income			**16,00,000**

Note: As per sec. 115A, no expenses shall be allowed from royalty and interest income.

Illustration 6:

The total income of a non-resident Indian includes:

- Investment income (net) ₹ 50,000
- Long term capital gain ₹ 25,000
- Other income ₹ 2,65,000

What will be the tax payable by him (old regime) in respect of A.Y. 2024-25 on the above income under chapter XIIA (special provisions relating to certain income of non-residents) of the I.T. Act, 1961?

Solution:

Since the assessee is non-resident hence income shall be taxable as per provision of sec. 115E as under –

Particulars	Income	Rate	Tax liability
Investment income (Net)	50,000	20%	10,000
Long term capital gain	25,000	10%	2,500
Other income	2,65,000	[(2,50,000×Nil) + (15,000×5%)]	750
Tax before surcharge			13,250
Add: Health & Education cess @ 4%			530
Tax liability (Rounded off)			13,780

Illustration 7:

Mr. Q, a non-resident, operates an aircraft between Singapore and Chennai. He received the following amounts in the course of the business of operation of aircraft during the previous year:

(i) ₹ 2 crores in India on account of carriage of passengers from Chennai.

(ii) ₹ 1 crore in India on account of carriage of goods from Chennai.

(iii) ₹ 3 crores in India on account of carriage of passengers from Singapore.

(iv) ₹ 1 crore in Singapore on account of carriage of passengers from Chennai.

(v) The total expenditure incurred by Mr. Q for the purposes of the business during the year was ₹ 6.75 crores.

Compute income chargeable to tax of the foreign airlines

Solution:

Computation of income of Mr. Q for the A.Y. 2024-25

Particulars	Amount
Amount received in India on account of carriage of passengers from Chennai	2,00,00,000
Amount received in India on account of carriage of goods from Chennai	1,00,00,000
Amount received in India on account of carriage of passengers from Singapore	3,00,00,000
Amount received in Singapore on account of carriage of passengers from Chennai	1,00,00,000
Total	**7,00,00,000**
Total Income (as per sec. 44BBA being 5% of above)	**35,00,000**

Illustration 8:

The net result of the business carried on by a branch of foreign company in India for the year ended 31.03.2024 was a loss of ₹ 50 lacs after charge of head office expenses of ₹ 100 lacs allocated to the branch. Compute income of the branch for the assessment year 2024-25.

Solution:

Computation of income of the branch for the A.Y. 2024-25

Particulars	Amount	Amount
Net Income for the year ended on 31-03-2024		(50,00,000)
Add: Head office expenses (to be considered separately)		1,00,00,000
Adjusted Total Income		50,00,000
Less: Head office expenses allowable u/s 44C being lower of the following:		
- 5% of ₹ 50,00,000	2,50,000	
- Actual Expenses	1,00,00,000	2,50,000
Total Income		**47,50,000**

Illustration 9:

Roger Federer, a tennis professional and a non-Indian citizen participated in India in a tennis Tournament and won the prize money of ₹ 15 lakh. He contributed articles on the tournament in a local newspaper for which he was paid ₹ 1 lakh. He was also paid ₹ 4 lakh by a Soft Drink Company for appearance in a T.V. advertisement. Although his expenses in India were met by the sponsors, he had to incur ₹ 1,30,000 towards his travel cost to India. He was a non-resident for tax purposes in India. What would be his tax liability in India for A.Y. 2024-25. Is he required to file his return of income u/s 139(1).

Solution:

U/s 115BBA, where a sportsman who is not a citizen of India receives any income by way of i) participating in any game in India; or ii) advertisement; or iii) contributing articles relating to any game or sport in India in newspapers, magazines or journals, then such income shall be chargeable to tax @ 20% + cess @ 4% on the tax.

Accordingly, his income for the A.Y. 2024-25 are as under:

Particulars	Amount
Tennis tournament prize	15,00,000
Amount received on contributing articles in the newspaper	1,00,000
Amount received on advertisement	4,00,000
Total Income	**20,00,000**
Tax on above [₹ 20,00,000 × 20% × 104%]	**4,16,000**

Notes:

a. While computing income, no deduction in respect of any expenditure or allowance shall be allowed

b. It shall not be necessary for the assessee to furnish return of his income if:

(i) his total income consisted only of income referred to in sec. 115BBA; and

(ii) the tax deductible at source has been deducted from such income

Illustration 10.

Compute the income-tax in the following cases:

(a) Royalty of ₹ 10 lakh received by a foreign company from an Indian concern in pursuance of an agreement approved by the Central Government in the previous year 2023-24.

(b) ₹ 10 lakh long-term capital gains received by an overseas financial organisation on transfer of unit purchased in foreign currency.

Solution:

(a) As per Section 115A(i)(b), the rate of income tax applicable on royalty is 20%.

Therefore, Income tax = 20% of ₹ 10,00,000 = ₹ 2,00,000

Health & Education cess = 4% of ₹ 2,00,000 = ₹ 8,000

Total tax payable = ₹ 2,00,000 + ₹ 8,000 = ₹ 2,08,000

(b) Long term Capital Gain = ₹ 10,00,000

Income-tax u/s 115AB = 10% of ₹ 10,00,000 = ₹ 1,00,000

Health & Education cess = 4% of ₹ 1,00,000 = ₹ 4,000

Total tax payable = ₹ 1,00,000 + ₹ 4,000 = ₹ 1,04,000

Illustration 11.

A non-resident foreign company has a permanent establishment (PE) in India, in respect of which royalty ₹ 101 lakh was earned from an Indian company in pursuance of an agreement dated 10th June, 2016 (expenditure incurred on PE in India ₹ 12,37,600). Compute the gross tax liability of foreign company ignoring TDS/advance tax for the assessment year 2024-25, assuming that there is no other income of the company for the year.

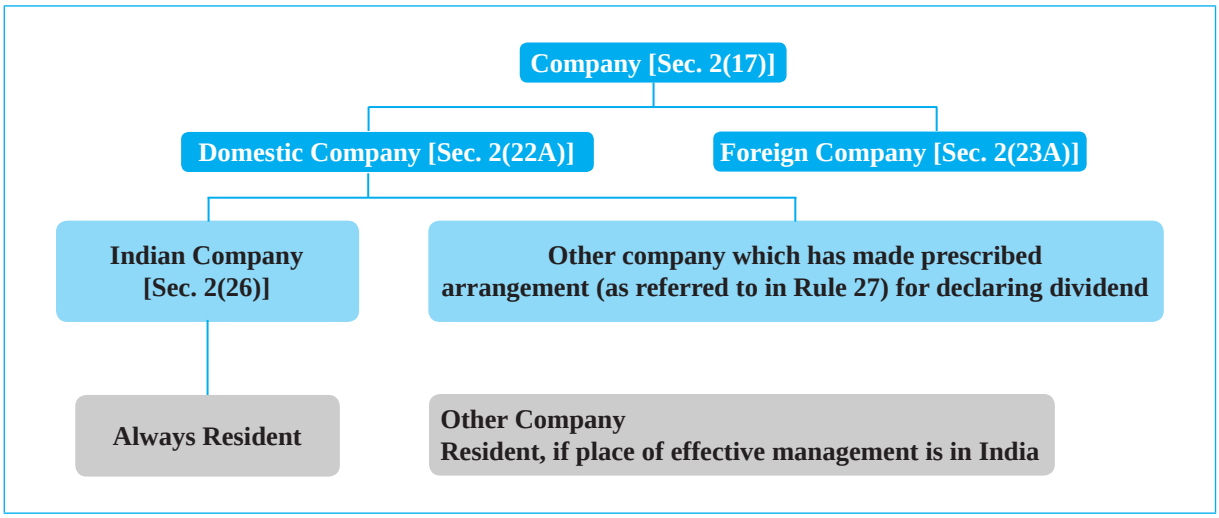
Solution:

Computation of Total Income and Tax Liability

Particulars	Amount
Royalty covered u/s 44DA	1,01,00,000
Less: Expenses	12,37,600
Income	88,62,400
Tax on above [104% {₹ 88,62,400 * 40%} [Rounded off]	36,86,760

Company

1.2



Company [Sec. 2(17)]

Company means:

a. any Indian company; or

b. any body corporate, incorporated under the laws of a foreign country; or

c. any institution, association or body which is or was assessable or was assessed as a company for any assessment year on or before April 1, 1970; or

d. any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the Central Board of Direct Taxes to be a company.

Indian Company [Sec. 2(26)]

An Indian company means a company formed & registered under the Companies Act, 1956 & includes

a. a company formed and registered under any law relating to companies formerly in force in any part of India other than the state of Jammu & Kashmir and the Union territories specified in (c) infra;

b. a company formed and registered under any law for the time being in force in the State of Jammu & Kashmir;

c. a company formed and registered under any law for the time being in force in the Union territories of Dadar & Nagar Haveli, Goa, Daman & Diu and Pondicherry;

d. a corporation established by or under a Central, State or Provincial Act;

e. any institution, association or body which is declared by the Central Board of Direct Taxes (CBDT) to be a company u/s 2(17).

In the aforesaid cases, a company, corporation, institution, association or body will be treated as an Indian company only if its registered office or principal office, as the case may be, is in India.

Domestic Company [Sec. 2(22A)]

Domestic company means:

i) an Indian company; or

ii) any other company, which in respect of its income liable to tax under the Act, has made prescribed arrangements for the declaration and payment of dividends (including dividend on preference share), payable out of such income, within India.

Prescribed arrangements for declaration and payment of dividends within India [Rule 27]

The arrangements to be made by a company for the declaration and payment of dividends (including dividends on preference shares) within India shall be as follows:

a. The share-register of the company for all shareholders shall be regularly maintained at its principal place of business within India.

b. The general meeting for passing the accounts of the previous year relevant to the assessment year and for declaring any dividends in respect thereof shall be held only at a place within India.

c. The dividends declared, if any, shall be payable only within India to all shareholders.

Foreign Company [Sec. 2(23A)]

Foreign company means a company which is not a domestic company.

Company in which public are substantially interested [Sec. 2(18)]

A company is said to be a company in which the public are substantially interested (also known as widely held company):

1. **Government company:** A company owned by the Government or the Reserve Bank of India or in which not less than 40% of the shares are held (whether singly or taken together) by the Government or the Reserve Bank of India or a corporation owned by that bank; or
2. **A company u/s 8:** A company which is registered u/s 8 of the Companies Act, 2013; or
3. **Mutual benefit finance company:** A company
   a. which carries on, as its principal business, the business of acceptance of deposits from its members; &
   b. which is declared by the Central Government u/s 620A of the Companies Act, 1956, to be a *Nidhi* or *Mutual Benefit Society*; or

4. **Company in which shares are held by co-operative societies:** A company whose equity shares carrying not less than 50% of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant previous year beneficially held by, one or more co-operative societies;

5. **Listed company:** A company which is not a private company as defined in the Companies Act, 1956, and the conditions specified either in item (A) or in item (B) are fulfilled, namely:—

   A) equity shares in the company were, as on the last day of the relevant previous year, listed in a recognised stock exchange in India;

   B) equity shares in the company carrying not less than 50% (40% in case of an Indian company whose business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power i.e. industrial company) of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant previous year beneficially held by:

   (a) the Government; or

   (b) a corporation established by a Central, State or Provincial Act; or

   (c) any company to which this clause applies or any subsidiary company of such company if the whole of the share capital of such subsidiary company has been held by the parent company or by its nominees throughout the previous year.

6. **Company which is prescribed by Board:** A company having no share capital and if, having regard to its objects, the nature and composition of its membership and other relevant considerations, it is declared by order of the Board to be a company in which the public are substantially interested. [Such company shall be deemed to be a company in which the public are substantially interested only for such assessment year or assessment years as may be specified in the declaration]; or

Rate of Tax for Company Assessee

The income of a company is taxable as under:

Short term capital gain covered u/s 111A	15%
Long term capital gain covered u/s 112A	10%
Other Long term capital gain	20%
Winnings from lottery, cross-word puzzles, etc.	30%
Other Income	
– In the case of a domestic company	
➢ Where its total turnover or gross receipts during the previous year 2021-22 does not exceed ₹ 400 crores	25%
➢ In other case	30%
– In the case of a foreign company:	
➢ Royalty received from Government or an Indian concern in pursuance of an agreement made by it with the Indian concern after March 31, 1961, but before April 1, 1976, or fees for rendering technical services in pursuance of an agreement made by it after February 29, 1964, but before April 1, 1976, and where such agreement has in either case been approved by Central Government	50%
➢ Other incomes	40%

Surcharge: The amount of tax computed as above shall be further increased by a surcharge as per the following table:

Total Income	Surcharge as a % of Income Tax	
	Domestic Company	Foreign Company
Income less than or equal to ₹ 1,00,00,000	Nil	Nil
Income exceeds ₹ 1 crore but does not exceed ₹ 10 crores	7%	2%
Income exceeds ₹ 10 crores	12%	5%

Health & Education Cess: 4% of 'Tax liability after surcharge' is also levied on every company.

Marginal Relief

Condition: Total income exceeds ₹ 1,00,00,000

Relief: Marginal relief is provided to ensure that the additional income tax payable including surcharge on excess of income over ₹ 1,00,00,000 is limited to the amount by which the income is more than ₹ 1,00,00,000

Similar relief is also available if income exceeds ₹ 10 crores. In that case, in the above, ₹ 1 crore shall be replaced with ₹ 10 crores

Tax on income of certain manufacturing domestic companies [Sec. 115BA]

Applicable to: Domestic Company

Conditions:

1. The company has been set-up and registered on or after the 01-03-2016.
2. The company is not engaged in any business other than the business of manufacture or production of any article or thing and research in relation to, or distribution of, such article or thing manufactured or produced by it; and
3. The total income of the company has been computed:
   (a) Without any deduction u/s 10AA or 32(1)(iia) or 32AC or 32AD or 33AB or 33ABA or 35(1)(ii) or 35(1)(iia) or 35(1)(iii) or 35(2AB) or 35(2AA) or 35AC or 35AD or 35CCC or 35CCD or under any provisions of Chapter VI-A under the heading "C.—Deductions in respect of certain incomes" other than the provisions of sec. 80JJAA;
   (b) Without set off of any loss carried forward from any earlier assessment year if such loss is attributable to any of the deductions referred above; and
   (c) Depreciation u/s 32 [other than 32(1)(iia)], is determined in the manner as may be prescribed.
      - Depreciation u/s 32(1)(ii) of any block of assets entitled to more than 40% shall be restricted to 40% on the written down value of such block of assets [Rule 5]

Rate of Tax: 25% + SC + Cess

Other Points

- Income taxable at special rate shall be taxable at special rate of tax applicable on that income. E.g., short term capital gain covered u/s 111A is taxable @ 15%.
- The loss referred to in the conditions shall be deemed to have been already given full effect to and no further deduction for such loss shall be allowed for any subsequent year.

- The scheme is optional. The option is exercised by the person in the prescribed manner[11] on or before the due date specified u/s 139(1) for furnishing the first of the returns of income which the person is required to furnish under the provisions of this Act. Further, once the option has been exercised for any previous year, it cannot be subsequently withdrawn for the same or any other previous year.
- Where the person exercises option u/s 115BAA, the option under this section may be withdrawn.

Tax on income of certain domestic companies [Sec. 15BAA]

Applicable to: Domestic Company

Conditions:

The total income of the company shall be computed:

a. without any deduction u/s 10AA or 32(1)(iia) or 32AD or 33AB or 33ABA or 35(1)(ii) or 35(1)(iia) or 35(1)(iii) or 35(2AA) or 35(2AB) or 35AD or 35CCC or 35CCD or under any provisions of Chapter VI-A under the heading "C.—Deductions in respect of certain incomes" other than the provisions of sec. 80JJAA or sec. 80M.

   Exception

   In case of unit in the International Financial Services Centre, the deduction u/s 80LA shall be available to such Unit subject to fulfilment of the conditions contained in sec. 80LA.

b. Without set off of any loss carried forward from any earlier assessment year if such loss is attributable to any of the deductions referred above; and

c. Depreciation u/s 32 [other than 32(1)(iia)], is determined in the manner as may be prescribed.

Rate of Tax: 22% + SC @ 10% + Cess

Other Points

- Income taxable at special rate shall be taxable at special rate of tax applicable on that income. E.g., short term capital gain covered u/s 111A is taxable @ 15%.
- The loss referred to in the conditions shall be deemed to have been already given full effect to and no further deduction for such loss shall be allowed for any subsequent year.
- The scheme is optional. The option is exercised by the person in the prescribed manner[12] on or before the due date specified u/s 139(1) for furnishing the first of the returns of income which the person is required to furnish under the provisions of this Act. Further, once the option has been exercised for any previous year, it cannot be subsequently withdrawn for the same or any other previous year.
- Where the person fails to satisfy the conditions in any previous year, the option shall become invalid in respect of the assessment year relevant to that previous year and subsequent assessment years and other provisions of the Act shall apply, as if the option had not been exercised for the assessment year relevant to that previous year and subsequent assessment years.
- Where a person has exercised the option u/s 115BAA, the provision of sec. 115JB (i.e. MAT) is not applicable.
- In case of a person, where the option exercised by it, u/s 115BAB has been rendered invalid due to violation of conditions contained in that section, such person may exercise option under this section.

[11] Uploading Form 10-IB
[12] Uploading Form 10-IB

Tax on income of new manufacturing domestic companies [Sec. 115BAB]

Applicable to: Domestic Company

Conditions:

a) The company has been set-up and registered on or after 01-10-2019, and has commenced manufacturing or production of an article or thing on or before 31-03-2024.

b) The business is not formed by splitting up, or the reconstruction, of a business already in existence.

Exception

i. Where business is formed as a result of the re-establishment, reconstruction or revival by the person of the business of any such undertaking as is referred to in sec. 33B, in the circumstances and within the period specified in that section.

c) The company does not use any machinery or plant previously used for any purpose.

- Any machinery or plant which was used outside India by any other person shall not be regarded as machinery or plant previously used for any purpose, if the following conditions are fulfilled:

  A. such machinery or plant was not, at any time previous to the date of the installation used in India;

  B. such machinery or plant is imported into India from any country outside India; and

  C. no deduction on account of depreciation in respect of such machinery or plant has been allowed or is allowable under the provisions of this Act in computing the total income of any person for any period prior to the date of the installation of machinery or plant by the person.

- Where in the case of a person, any machinery or plant or any part thereof previously used for any purpose is put to use by the company and the total value of such machinery or plant or part thereof does not exceed 20% of the total value of the machinery or plant used by the company, then, this condition shall be deemed to have been complied with.

d) The company does not use any building previously used as a hotel or a convention centre, as the case may be, in respect of which deduction u/s 80-ID has been claimed and allowed.

e) The company is not engaged in any business other than the business of manufacture or production of any article or thing (*it includes the business of generation of electricity*) and research in relation to, or distribution of, such article or thing manufactured or produced by it.

Exception

The business of manufacture or production of any article or thing shall not include business of:

i. development of computer software in any form or in any media;

ii. mining;

iii. conversion of marble blocks or similar items into slabs;

iv. bottling of gas into cylinder;

v. printing of books or production of cinematograph film; or

vi. any other business as may be notified by the Central Government in this behalf; and

f) The total income of the company has been computed:

A. without any deduction u/s 10AA or 32(1)(iia) or 32AD or 33AB or 33ABA or 35(1)(ii) or 35(1)(iia) or 35(1)(iii) or 35(2AA) or 35(2AB) or 35AD or 35CCC or 35CCD or under any provisions of Chapter VI-A under the heading "C.—Deductions in respect of certain incomes" other than the provisions of sec. 80JJAA or 80M.

B. Without set off of any loss carried forward from any earlier assessment year if such loss is attributable to any of the deductions referred above; and

C. Depreciation u/s 32 [other than 32(1)(iia)], is determined in the manner as may be prescribed.

Rate of Tax: 15% + SC @ 10% + Cess

Other Points

- Income taxable at special rate shall be taxable at special rate of tax applicable on that income. E.g., short term capital gain covered u/s 111A is taxable @ 15%.
- Where the total income of the person, includes any income, which has neither been derived from nor is incidental to manufacturing or production of an article or thing and in respect of which no specific rate of tax has been provided separately under this Chapter, such income shall be taxed @ 22% and no deduction or allowance in respect of any expenditure or allowance shall be allowed in computing such income.
- The income-tax payable in respect of income being short term capital gains derived from transfer of a capital asset on which no depreciation is allowable under the Act shall be computed @ 22%
- Where the person fails to satisfy the conditions in any previous year, the option shall become invalid in respect of the assessment year relevant to that previous year and subsequent assessment years and other provisions of the Act shall apply to the person as if the option had not been exercised for the assessment year relevant to that previous year and subsequent assessment years.
- The loss referred to in the conditions shall be deemed to have been already given full effect to and no further deduction for such loss shall be allowed for any subsequent year.
- The scheme is optional. The option is exercised by the person in the prescribed manner[13] on or before the due date specified u/s 139(1) for furnishing the first of the returns of income which the person is required to furnish under the provisions of this Act. Further, once the option has been exercised for any previous year, it cannot be subsequently withdrawn for the same or any other previous year.
- Where a person has exercised the option u/s 115BAB, the provision of sec. 115JB (i.e. MAT) is not applicable.
- If any difficulty arises regarding fulfilment of the conditions, the Board may, with the approval of the Central Government, issue guidelines for the purpose of removing the difficulty and to promote manufacturing or production of article or thing using new plant and machinery. Every guideline issued by the Board shall be laid before each House of Parliament, and shall be binding on the person, and the income-tax authorities subordinate to it.
- Where it appears to the Assessing Officer that, owing to the close connection between the person to which this section applies and any other person, or for any other reason, the course of business between them is so arranged that the business transacted between them produces to the person more than the ordinary profits which might be expected to arise in such business, the Assessing Officer shall, in computing the profits and gains of such business for the purposes of this section, take the amount of profits as may be reasonably deemed to have been derived therefrom:

[13] Uploading Form 10-IB

Taxpoint:

- In case the aforesaid arrangement involves a specified domestic transaction referred to in sec. 92BA, the amount of profits from such transaction shall be determined having regard to arm's length price as defined in sec. 92F(ii).
- The amount, being profits in excess of the amount of the profits determined by the Assessing Officer, shall be deemed to be the income of the person. Such income is computed @ 30%

Illustration 12.

Compute gross total income of Minakshi Ltd. under the head Profits & gains of business or profession for the assessment year 2024-25

Profit & Loss A/c for the year ended 31/3/2024

Particulars	Amount	Particulars	Amount
To Opening stock	4,00,000	By Sales	17,80,000
To Purchase of raw material	5,00,000	By Closing Stock	5,00,000
To Conversion cost	4,00,000	By Interest on debenture	10,000
To Customs duty	1,70,000	By Bad debt recovery	25,000
To Salary and wages	80,000	(Previously allowed)	
To Bonus to employee	15,000	By Interest on income tax Refund	6,000
To Carriage inward	20,000	By Rent from house property	40,000
To Advertisement	30,000		
To Interest	2,000		
To Carriage outward	38,000		
To Depreciation	50,000		
To Provision for income tax	20,000		
To Compensation paid to director	1,00,000		
To Provision for bad debt	10,000		
To Audit fees	20,000		
To Bad debt	30,000		
To Traveling expenses	25,000		
To Municipal tax	5,000		
To Net profit	4,46,000		
	23,61,000		23,61,000

Additional information

(a) Minakshi, holder of 21% share, sold goods to the company for ₹ 40,000 though market value is lower by ₹ 10,000. Payment to her was made by way of bearer cheque.

(b) Advertisement expenses relate to the purchase of a machinery for advertisement. Depreciation allowed on such machinery is ₹ 2,250.

(c) Ritu, holder of 21% share, purchased goods from the company for ₹ 30,000 though market value is ₹ 35,000. She made payment by way of bearer cheque.

(d) Purav, who supplies more than 25% of goods, sold goods to company for ₹ 10,000 however, market value of such goods was ₹ 8,000.

(e) Outstanding salary ₹ 20,000 was paid on 30-12-2024.

(f) Bonus is not paid till due date of furnishing return.

(g) Provision for bad debts is in excess of ₹ 1,000.

(h) Salary paid in excess of requirement to non-relative ₹ 2,000 and to relative of director ₹ 6,000.

(i) Traveling expenses is on traveling of Minakshi for 10 days out of which she used 8 days for acquiring a new machine from Jaipur for company and 2 days for meeting her relative. However, Minakshi agreed to refund proportionate cost.

(j) On 31-7-2023, company purchased a machine from Jaipur costing ₹ 5,00,000.

(k) Customs duty paid on 30-11-2024. However, company paid ₹ 5,000 on 30-7-2023 outstanding customs duty of earlier year

(l) Company incurred capital expenditure of ₹ 1,00,000 for promoting family planning among its workers.

(m) Carriage inward shows the expenditure incurred for acquiring machine from Jaipur.

(n) Interest paid is related to loan taken for purchasing debenture.

(o) As on 1-4-2023, company holds following assets –

Assets	Rate	Value
Plant & Machinery	15%	6,00,000
Furniture	10%	1,00,000

Compute gross total income for assessment year 2024-25. Ignore provision of sec. 115JB.

Solution:

Computation of gross total income of Minakshi Ltd. for the A.Y. 2024-25

Particulars	Notes	Details	Amount	Amount
Income from house property				
Gross Annual value (Rent received)			40,000	
Less: Municipal tax			5,000	
Net annual value (NAV)			35,000	
Less: Standard deduction u/s 24(a) [30% of NAV]			10,500	24,500
Profits & gains of business or profession				
Net profit as per Profit and Loss A/c			4,46,000	
Add: Expenditure disallowed but debited in P/L A/c				
Depreciation	1	50,000		
Provision for income tax	2	20,000		
Provision for bad debt	3	10,000		
Municipal tax	4	5,000		
Excessive payment to Minakshi	5	10,000		

Particulars	Notes	Details	Amount	Amount
Cash payment to Minakshi in excess of ₹ 10,000	6	30,000		
Advertisement expenditure	7	30,000		
Bonus	8	15,000		
Excess payment of salary to relative of director	9	6,000		
Travelling expenses	10	25,000		
Customs duty	11	1,70,000		
Carriage inward	10	20,000		
Interest	12	2,000	3,93,000	
			8,39,000	
Less: Expenditure allowed but not debited to P/L A/c				
Customs duty of earlier years	11	5,000		
Expenditure on promoting family planning among employees	13	20,000		
Depreciation u/s 32	1	2,91,250		
Less: Income taxable under other head but credited in P/L A/c				
Rent from house property	14	40,000		
Interest on debenture	14	10,000		
Interest on refund of income tax	14	6,000	3,72,250	4,66,750
Income from other sources				
Interest on debenture		10,000		
Less: Interest on borrowed capital	12	2,000	8,000	
Interest on refund of income tax			6,000	14,000
Gross Total Income				**5,05,250**

Notes

1. Depreciation is allowed as per Income tax Act being calculated as under -

Particulars	Details	Amount
Block 1: Plant and Machinery @ 15%		
W.D.V. as on 1/4/2023	6,00,000	
Add: Purchase during the year	5,40,000[#]	
	11,40,000	
Less: Sale during the year	-	
	11,40,000	
Depreciation @ 15% [₹ 11,40,000 × 15%]	1,71,000	
Additional depreciation @ 20% [₹ 5,40,000 × 20%]	1,08,000	2,79,000
Block 2: Furniture @ 10%		
W.D.V. as on 1/4/2023	1,00,000	
Add: Purchase during the year	-	

Particulars	Details	Amount
	1,00,000	
Less: Sale during the year	-	
	1,00,000	
Depreciation @ 10% [₹ 1,00,000 x 10%]		10,000
On machinery for advertisement		2,250
Depreciation allowed u/s 32		2,91,250

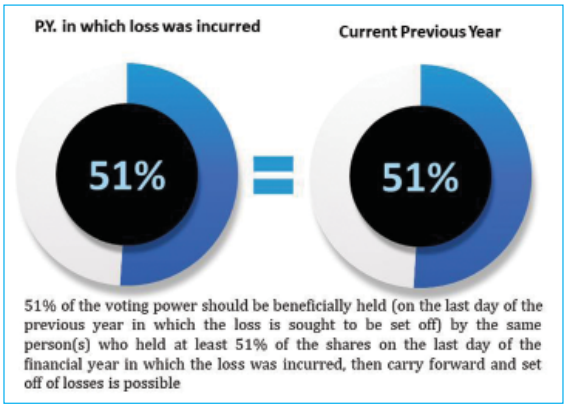
Computation of actual cost of machinery purchased during the year -

Particulars	Amount
Purchase cost	5,00,000
Carriage inward	20,000
Traveling cost *	20,000
Actual cost of purchased machinery	5,40,000

* Since traveling cost for 10 days was ₹ 25,000. Hence cost for 8 days (used for acquiring the new machine) is ₹ 20,000.

2. Income tax is not allowed u/s 40(a).
3. Any anticipatory loss is not allowed.
4. Municipal tax is not allowed as deduction from business income but allowed from Income from house property.
5. Since Minakshi has a substantial interest in the company, hence, excessive payment is disallowed u/s 40A(2).
6. Payment of allowed expenditure otherwise than by account payee cheque or demand draft in excess of ₹ 10,000 shall be disallowed u/s 40A(3).
7. Any capital expenditure is not allowed.
8. By virtue of sec. 43B, bonus to employees is allowed as deduction on payment basis.
9. Excessive payment to relative of director is disallowed [Sec. 40A(2)].
10. Since traveling expenditure and carriage inward is related to acquisition of machine, hence the same should be added with the cost of machine. Further, personal expenditure of Minakshi being refundable shall not be treated as expenditure.
11. As per sec. 43B, customs duty is allowed as deduction on payment basis.
12. Interest on loan taken for acquisition of debenture is deductible from income from debenture.
13. Any capital expenditure on promoting family planning among employees by a company is allowed in 5 equal installments [Sec. 36(1)(ix)].
14. Rent from house property is taxable under the head Income from house property, whereas interest income (including interest on income tax refund) is taxable under the head Income from other sources.
15. Any excessive payment received from a person who has substantial interest is not governed by sec. 40A(2).
16. A person supplying 25% of raw material is not treated as person who holds substantial interest. Hence excessive payment to Purav is allowed.
17. Compensation paid to director shall be allowed u/s 37(1).
18. Sec. 43B covers bonus and commission paid to employee but does not cover salary paid to employee.

1.2.1 Carry Forward and Set-off of Losses in the case of Closely Held Companies [Sec. 79]



In case of a company in which public are not substantially interested (other than eligible start-up company referred below), no loss shall be carried forward and set off against the income of the previous year, unless at least 51% of the voting power of the company are beneficially held (on the last day of the previous year in which the loss is sought to be set off) by the same person(s) who held at least 51% of the shares on the last day of the financial year in which the loss was incurred.

Taxpoint

a) **Losses under the head 'Capital gains':** Sec. 79 applies to all losses, including losses under the head Capital gains.

b) **Unabsorbed depreciation:** The above provision is not applicable on unabsorbed depreciation, such unabsorbed depreciation shall be allowed to be carried forward.

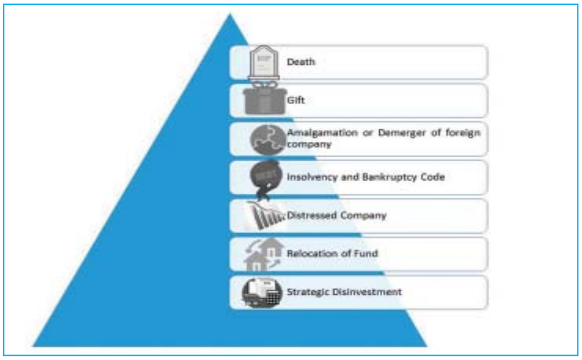
Option for eligible start-up company[14]

In the case of eligible start-up company, not being a company in which the public are substantially interested, the loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year, if:

- All the shareholders of such company who held shares carrying voting power on the last day of the year or years in which the loss was incurred continue to hold those shares on the last day of such previous year; and
- Such loss has been incurred during the period of 10 years beginning from the year in which such company is incorporated

Exceptions: However, change in the share holding due to following reasons shall not be considered-

1. **Transfer due to death:** Where a change in the said voting power takes place in a previous year consequent upon the death of a shareholder
2. **Transfer by way of gift:** Where a change in the said voting power takes place in a previous year on account of transfer of shares by way of *gift to any relative* of the shareholder making such gift.
3. **Amalgamation or demerger of foreign company:** Any change in the shareholding of an Indian company which is a subsidiary of a foreign company as a result of amalgamation or demerger of a foreign company subject to the condition that 51% shareholders of the amalgamating or demerged foreign company continues to be the shareholder of the amalgamated or the resulting foreign company.



[14] As defined in sec. 80-IAC

4. **Insolvency and Bankruptcy Code**: Where change in the shareholding is taken place pursuant to a resolution plan approved under the Insolvency and Bankruptcy Code, 2016, after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner.

5. **Relocation of Fund**: The section is not applicable to a case to the extent that a change in the shareholding has taken place during the previous year on account of relocation referred to in the Explanation to sec. 47(viiac) and (viiad).

6. **Distressed Company:** The provision is not applicable to a company, and its subsidiary and the subsidiary of such subsidiary, where:

   i. the National Company Law Tribunal (NCLT), on an application moved by the Central Government u/s 241 of the Companies Act, 2013, has suspended the Board of Directors of such company and has appointed new directors nominated by the Central Government, u/s 242 of the said Act; and

   ii. a change in shareholding of such company, and its subsidiary and the subsidiary of such subsidiary, has taken place in a previous year pursuant to a resolution plan approved by the Tribunal u/s 242 of the Companies Act, 2013 after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner.

7. **Strategic Disinvestment**: The provision is not applicable to an erstwhile public sector company (as defined u/s 72A) provided that the ultimate holding company of such company, immediately after the completion of strategic disinvestment (as defined u/s 72A), continues to hold, directly or through its subsidiary or subsidiaries, at least 51% of the voting power of such company in aggregate.

   Taxpoint: Where the condition of 51% is not complied with in any previous year after the completion of strategic disinvestment, the provision of sec. 79 shall apply for such previous year and subsequent previous years.

Illustration 13.

Following are the details of X Pvt Ltd, determine the brought forward loss available for set off during the previous year 2023-24 relevant to the assessment year 2024-25:

Previous Year 2022-23	Previous Year 2023-24
Business Loss = ₹ 12 lakh	Business Profit = ₹ 25 lakh
Unabsorbed depreciation: ₹ 2 lakh	(before adjusting brought forward loss and unabsorbed depreciation)
Details of Shareholders as on 31-03-2023	Details of Shareholders as on 31-03-2024
A = 30%	E = 30%
B = 25%	F = 25%
C = 20%	C = 20%
D = 25%	D = 25%

How shall your view will differ, if Mr. B had gifted the shares to Mr. F, a relative of Mr. B.

Solution:

As per sec. 79, in case of a company in which public are not substantially interested, no loss shall be carried forward and set off against the income of the previous year, unless at least 51% of the voting power of the company are beneficially held (on the last day of the previous year in which the loss is sought to be set off) by the same person(s) who held at least 51% of the shares on the last day of the financial year in which the loss was incurred. However, the said provision is not applicable in case of unabsorbed depreciation.

Since, in the given case, shareholders holding 51% shares as on 31-03-2023 (the last day of the previous year in which loss has been incurred) and 31-03-2024 are not beneficially held by the same persons hence such loss shall not be available for set off with the income of the previous year 2023-24. Thus, no brought forward business loss is available for set off during the previous year 2023-24 relevant to the assessment year 2024-25. However, unabsorbed depreciation of ₹ 2 lakh shall be available for adjustment from the business income of the previous year 2023-24. Thus, business income for the assessment year 2024-25 is ₹ 23 lakhs.

If Mr. B had gifted the shares to Mr. F

Transfer of shares by way of gift to a relative is not considered as change in shareholding for the purpose of sec. 79. Hence, the loss of ₹ 12 lakh of previous year 2022-23 shall be available for set off with income of the previous year 2023-24.

Illustration 14.

A private limited company has share capital in the form of equity share capital. The shares were held until 31st March, 2022 by 4 members A, B, C and D equally. The company made losses/profits for the past three assessment years are as follow:

Asst. Year	Business Loss	Unabsorbed depreciation	Total
2020-21	Nil	₹ 15,00,000	₹ 15,00,000
2021-22	Nil	₹ 12,00,000	₹ 12,00,000
2022-23	₹ 9,00,000	₹ 9,00,000	₹ 18,00,000

The above figures have been accepted by the tax department.

During the previous year 31-3-2023, A sold his shares to Y and during the previous year 31-3-2024, B sold his shares to Z. The profits for the past two years are as follows:

31-3-2023 ₹ 18,00,000 (before charging depreciation ₹ 9,00,000)

31-3-2024 ₹ 45,00,000 (before charging depreciation ₹ 7,50,000)

Compute taxable income for A.Y. 2024-25

Solution:

According to sec. 79, loss sustained by the closely held company shall not allowed to be set off unless in the year of such set off the shareholders holding not less than 51% of beneficial interest in share capital of the company in the year of sustaining the loss shall continue to be the shareholders of the company. Accordingly, the taxable income of the company for the A.Y. 2023-24 shall be nil as detailed here below:

Particulars	₹ in lacs
Income before depreciation	18
Less: Depreciation of the current year	9
Income after depreciation	9
Less: Unabsorbed business loss b/f	9
Taxable income	**Nil**

However, the abovementioned condition of beneficial ownership shall not be applied for carry forward and set off of unabsorbed depreciation therefore, the company can carry forward and set off the unabsorbed depreciation, even if there is a change in the shareholding pattern between the year in which the loss was suffered and the year

in which it seeks to set off such loss. Thus, the taxable income of the company for A.Y. 2024-25 is worked out as follow:

₹ in lacs

Particulars	Amount	Amount
Income before depreciation		45
Less: Depreciation of the current year		7.5
Income after current depreciation		37.50
Less: Unabsorbed Depreciation		
A.Y. 2020-21	15	
A.Y. 2021-22	12	
A.Y. 2022-23	9	36
Taxable income		**1.50**

1.2.2 No set off of losses consequent to search, requisition and survey [Sec. 79A]

Set off of loss (**including unabsorbed depreciation**) shall not be allowed from the undisclosed income while computing total income for the previous year if following conditions are satisfied:

a. Total income of the assessee includes undisclosed income

b. Such undisclosed income is consequent to a search u/s 132 or a requisition u/s 132A or a survey u/s 133A [other than u/s 133A(2A)].

Taxpoint:

- Loss may be current year loss or brought forward loss
- Undisclosed income means:

  i. any income of the previous year represented, either wholly or partly, by any money, bullion, jewellery or other valuable article or thing or any entry in the books of account or other documents or transactions found in the course of a search u/s 132 or a requisition u/s 132A or a survey u/s 133A [other than u/s 133A(2A)], which has,—

     a. not been recorded on or before the date of search or requisition or survey, as the case may be, in the books of account or other documents maintained in the normal course relating to such previous year; or

     b. not been disclosed to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner before the date of search or requisition or survey, as the case may be; or

  ii. any income of the previous year represented, either wholly or partly, by any entry in respect of an expense recorded in the books of account or other documents maintained in the normal course relating to the previous year which is found to be false and which would not have been found to be so, had the search not been initiated or the survey not been conducted or the requisition not been made.

1.2.3 Minimum Alternate Tax (MAT) or Tax on Book Profit [Sec. 115JB]

At times it may happen that a taxpayer, being a company, may have generated income during the year, but by taking the advantage of various provisions of Income-tax Law (like exemptions, deductions, depreciation, etc.), it may have reduced its tax liability or may not have paid any tax at all. Due to increase in the number of zero tax paying companies, MAT was introduced by the Finance Act, 1987 with effect from assessment year 1988-89. Later on, it was withdrawn by the Finance Act, 1990 and then reintroduced by Finance (No. 2) Act, 1996, w.e.f. 1-4-1997.

The objective of introduction of MAT is to bring into the tax net "zero tax companies" which in spite of having earned substantial book profits and having paid handsome dividends, do not pay any tax due to various tax concessions and incentives provided under the Income-tax Law.

Applicable to

Any company (whether Indian or Foreign, resident or non-resident, closely held or widely held company)

Circumstance in which MAT is applicable: Where the income-tax, payable on the total income (being computed under this Act in respect of any previous year) is less than 15% of its book profit

Treatment:

- Such book profit shall be deemed to be the total income of the assessee; and
- The tax payable by the assessee on such total income shall be the amount of income-tax at the rate of 15% (plus surcharge, Health & Education cess)

Other Points

- **Unit in IFSC:** Where the assessee is a unit located in an International Financial Services Centre and derives its income solely in convertible foreign exchange, the rate of MAT shall be 9%
- **Book Profit should be as per Schedule III to the Companies Act, 2013:** Every company shall prepare its Statement of Profit and Loss for the relevant previous year in accordance with the provisions of Schedule III to the Companies Act, 2013. However, in case of banking, insurance or electricity company, such statement should be prepared as per provisions of the Act which governs such company.

➢ While preparing the annual accounts:

a. the accounting policies;

b. the accounting standards followed for preparing such accounts;

c. the method and rates adopted for calculating the depreciation,

shall be the same as have been adopted for the purpose of preparing such accounts and laid before the company at its annual general meeting.

- **When assessing officer has power to alter profit:** Where the statement of profit and loss has been prepared in accordance with Schedule III to the Companies Act, 2013 and which has been scrutinised and certified by the statutory auditors and relevant authorities, the Assessing Officer has no power to scrutinise net profit in the statement of profit and loss except to the extent provided in Explanation [**Apollo Tyres Ltd. -vs.- CIT (SC)**]

- **Report from Accountant:** Every company to which this section applies, shall upload a report in the prescribed form [Form 29B] from an accountant, certifying that the book profit has been computed in accordance with the provisions of this section one month prior to the due date of the filing of the return of income u/s 139 or along with the return of income furnished in response to a notice u/s 142(1)
- **Life Insurance Business:** The provision of this section shall not apply to any income accruing or arising to a company from life insurance business referred to in sec. 115B.
- **Companies opting for sec. 115BAA and sec. 115BAB:** The provision of this section shall not apply to a person who has exercised the option referred to u/s 115BAA and u/s 115BAB.
- **Advance Pricing agreement & Secondary Adjustment:** In case of a company, where there is an increase in book profit of the previous year due to income of past year (or years) included in the book profit on account of an advance pricing agreement entered into by the assessee u/s 92CC or on account of secondary adjustment required to be made u/s 92CE, the Assessing Officer shall, on an application made to him in this behalf by the assessee, recompute the book profit of the past year (or years) and tax payable, if any, by the assessee during the previous year. In this situation, the provisions of sec. 154 shall apply and the period of 4 years shall be reckoned from the end of the financial year in which the said application is received by the Assessing Officer. This provision shall apply only if the assessee has not utilised the credit of tax paid under this section in any subsequent assessment year u/s 115JAA.
- **Foreign Company:** The provisions of this section shall not be applicable and shall be deemed never to have been applicable to an assessee, being a foreign company, if:

  i. The assessee is a resident of a country or a specified territory with which India has an agreement referred to in sec. 90 or the Central Government has adopted any agreement u/s 90A and the assessee does not have a permanent establishment in India in accordance with the provisions of such agreement; or

  ii. the assessee is a resident of a country with which India does not have an agreement of the nature referred above and the assessee is not required to seek registration under any law for the time being in force relating to companies.

  Taxpoint: The MAT provision is not applicable to an assessee, being a foreign company, where its total income comprises solely of profits and gains from business referred to in section 44B or 44BB or 44BBA or 44BBB and such income has been offered to tax at the rates specified in those sections.
- **No impact of MAT on losses:** Nothing shall affect the determination of the amounts in relation to the relevant previous year to be carried forward to the subsequent year or years under the provisions of sec. 32(2) or 72(1)(ii) or 73 or 74 or 74A(3).
- **Other provision will apply:** All other provisions of this Act like Advance Tax, interest, etc. shall apply to every company, mentioned in this section.

Illustration 15.

Business income (before adjusting brought forward losses) & Book Profit of X Ltd. for various years are as follow:

	Year 1	Year 2	Year 3
Business Income as per other provisions of the Act	(-) ₹ 2,00,000	₹ 1,50,000	₹ 1,50,000
Book Profit	₹ 1,00,000	₹ 60,000	₹ 2,50,000

In the aforesaid case, tax shall be computed as under:

Particulars	Year 1	Year 2	Year 3
Business Income after set off	(-) ₹ 2,00,000	Nil	₹ 1,00,000
Tax on above @ 30% **[A]**	**Nil**	**Nil**	**₹ 30,000**
Book Profit	₹ 1,00,000	₹ 60,000	₹ 2,50,000
15% of Book Profit **[B]**	**₹ 15,000**	**₹ 9,000**	**₹ 37,500**
Tax [Higher[15] of A & B]	**₹ 15,000**	**₹ 9,000**	**₹ 37,500**
Add: Surcharge*	Nil	Nil	Nil
Tax & Surcharge	₹ 15,000	₹ 9,000	₹ 37,500
Add: Health & Education Cess	₹ 600	₹ 360	₹ 1,500
Tax Liability (R/off)	**₹ 15,600**	**₹ 9,360**	**₹ 39,000**

*As total income of the company does not exceed ₹ 1 crore, hence surcharge is not applicable.

It is to be noted that when a company is liable to pay tax u/s 115JB, book profit of the company shall be considered as total income of the company.

Computation and Meaning of Book Profit [Explanation 1 to sec. 115JB]

Book profit means the profit as shown in the statement of profit and loss for the relevant previous year:

As **increased** by (if following amount is debited in the Statement of Profit & Loss):

(a) the amount of income-tax paid or payable, and the provision therefore;

- It includes:
  - Any interest under Income Tax Act;
  - Surcharge and cess on income-tax.
- It does not include:
  - Penalty paid or payable under this Act
  - Any tax, interest or penalty paid or payable under Wealth Tax Act or other Act;
  - Securities Transaction Tax;

(b) the amounts carried to any reserves, by whatever name called;

(c) the amount set aside to provisions made for meeting liabilities, other than ascertained liabilities;

- Any provision made to meet unascertained liabilities like provision for gratuity or future losses, etc. should be added back. However, if the provision for gratuity has been made on the basis of actuarial valuation, it becomes ascertained liability, hence should not be added back [Shree Sajjan Mills Ltd. -vs.- CIT (SC)]

(d) the amount by way of provision for losses of subsidiary companies;

(e) the amount or amounts of dividends paid or proposed;

(f) the amount or amounts of expenditure relatable to any income to which sec. 10 or sec. 11 or sec. 12 apply.

(g) the amount or amounts of expenditure relatable to income being share of profit from AOP, if such share is exempt u/s 86

[15] There is another view. As per that view, comparison shall be made after applying surcharge and cess in respective tax.

(h) expenditure relating to following income of a foreign company if tax payable on such income under normal provision is less than 15%:

(A) the capital gains arising on transactions in securities; or

(B) the interest, dividend, royalty or fees for technical services chargeable to tax u/s 115A to 115BBG

(i) notional loss on transfer of a capital asset, being share or a special purpose vehicle to a business trust in exchange of units allotted by the trust referred to in sec. 47(xvii) or the amount representing notional loss resulting from any change in carrying amount of said units or the amount of loss on transfer of units referred to in sec. 47(xvii)

(j) the amounts of expenditure relatable to income by way of royalty in respect of patent chargeable to tax u/s 115BBF

(k) the amount of depreciation

(l) the amount of deferred tax and provision thereof

(m) the amount set aside as provision for diminution in the value of any asset (like asset written-off, etc.)

(n) the amount standing in revaluation reserve relating to revalued asset on the retirement or disposal of such asset (if not credited to the statement of Profit and Loss)

(o) gain on transfer of units referred to in sec.47(xvii) computed by taking into account the cost of the shares exchanged with units referred to in the said clause or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through statement of profit or loss, as the case may be;

As reduced by:

(i) the amount withdrawn from any reserve or provision if any such amount is credited to the statement of profit and loss.

- An amount withdrawn from reserve being created before 1-4-1997 otherwise than by way of a debit to the statement of profit and loss shall not be reduced.
- An amount withdrawn from reserves created or provisions made on or after 1-4-1997 shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) in that year.

(i) the amount of income to which any of the provisions of sec. 10 or sec. 11 or sec. 12 apply, if any such amount is credited to the statement of profit and loss.

(ii) share of profit from AOP, if such share is exempt u/s 86

(iii) following income of a foreign company if tax payable on such income under normal provision is less than 15%:

a. the capital gains arising on transactions in securities; or

b. the interest, dividend, royalty or fees for technical services chargeable to tax u/s 115A to 115BBG

(v) the amount representing,—

a. notional gain on transfer of a capital asset, being share of a special purpose vehicle to a business trust in exchange of units allotted by that trust referred to in sec.47(xvii); or

b. notional gain resulting from any change in carrying amount of said units; or

c. gain on transfer of units referred to in sec.47(xvii),

if any, credited to the statement of profit and loss; or

(vi) the amount of loss on transfer of units referred to in sec.47(xvii) computed by taking into account the cost of the shares exchanged with units referred to in the said clause or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through statement of profit or loss, as the case may be;

(vii) the amount of income by way of royalty in respect of patent chargeable to tax u/s 115BBF;

(viii) the amount of depreciation debited to the statement of profit and loss (excluding the depreciation on account of revaluation of assets);

(ix) the amount withdrawn from revaluation reserve and credited to the statement of profit and loss, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred above;

(x) the amount of brought forward loss or unabsorbed depreciation, whichever is less as per books of account.

- the loss shall not include depreciation;
- the provisions of this clause shall not apply if the amount of loss brought forward or unabsorbed depreciation, is nil;

Exception:

The **aggregate** (not lower) amount of unabsorbed depreciation & loss brought forward shall be reduced, in case of a:

a. company, and its subsidiary and the subsidiary of such subsidiary, where, the Tribunal, on an application moved by the Central Government u/s 241 of the Companies Act, 2013 has suspended the Board of Directors of such company and has appointed new directors who are nominated by the Central Government u/s 242 of the said Act;

b. company against whom an application for corporate insolvency resolution process has been admitted by the Adjudicating Authority under Insolvency and Bankruptcy Code, 2016

(xi) the amount of deferred tax, if any such amount is credited to the statement of profit and loss

(xii) the amount of profits of sick industrial company for the assessment year commencing on and from the assessment year relevant to the previous year in which the said company has become a sick industrial company and ending with the assessment year during which the entire net worth of such company becomes equal to or exceeds the accumulated losses.

Net worth means paid up capital + free reserve

Illustration 16.

Apple Industries Ltd. provides the following information for the financial year 2023-24:

Net profit as per statement of profit and loss after debiting/crediting the following:	₹ 120 lakh
Proposed dividend	₹ 30 lakh
Profit from unit established in SEZ	₹ 20 lakh
Provision for income-tax	₹ 18 lakh

Provision for deferred tax	₹ 10 lakh
Provision for permanent diminution in value of investments	₹ 3 lakh
Depreciation debited to statement of profit and loss ₹ 10 lakh includes	
depreciation on revaluation of assets to the tune of	₹ 1 lakh

Bought forward losses and unabsorbed depreciation as per books of the company are as follows :

(₹ in lakh)

Previous Year	Brought Forward Losses	Unabsorbed Depreciation
2020 – 21	1	4
2021 – 22	1	1
2022 – 23	10	5

Compute the book profit of the company as per section 115JB for the assessment year 2024-25.

Solution:

Computation of Book Profit of Apple Industries Ltd. for the A.Y.2024-25 (₹ In lakhs)

Particulars	Details	Amount
Net profit as per books of accounts		120
Add:		
Proposed Dividend	30	
Provision for income tax	18	
Provision for deferred-tax	10	
Provision for permanent diminution in value of investments	3	
Depreciation	10	71
		191
Less:		
Depreciation (ignoring depreciation on revaluation)	9	
Lower of brought forward loss and unabsorbed depreciation	10	19
Book Profit		172

Illustration 17.

The book profits of a company in the previous year 2023-24 computed in accordance with section 115JB are ₹60,00,000. If the total income for the same period computed as per the provisions of the Income-tax Act, 1961 is ₹12,00,000 calculate the tax payable by the company in the assessment year 2024-25 and also indicate whether the company is eligible for any tax credit.

Solution:

Computation of Tax Liability of …… for the A.Y. 2024-25

Particulars	Amount
Total Income	12,00,000
Tax on above [A]	3,60,000
Book Profit	60,00,000
Tax on above [B]	9,00,000
Tax liability [Higher of (A) and (B)]	9,00,000
Add: Health & Education Cess	36,000
Tax & Cess payable u/s 115JB [B]	9,36,000

Illustration 18.

X Ltd. charged depreciation on its fixed assets at the rate prescribed in the income tax rules. However, the Assessing Officer disallowed the same and allowed the rate as prescribed in the Companies Act, 2013 for the purpose of computation of book profit under section 115JB for the previous year 2023-24. Examine the legality of action taken by the Assessing Authority.

Solution:

This issue was settled by the Supreme Court in *Malayala Manorama Co. Ltd. -vs.- CIT*. The Apex Court observed that for the purpose of computation of book profit under section 115JB, the Assessing Officer's power is restricted to examining whether the books of account are certified by the authorities under the Companies Act as having been properly maintained in accordance with the Companies Act. Thereafter, he only has the limited power of making additions and deductions as provided for in Explanation 1 to section 115JB. The Assessing Officer does not have the jurisdiction to go behind the net profit shown in the profit and loss account except to the extent provided in Explanation 1 to section 115JB. Where an assessee is consistently charging depreciation in its books of account at the rates prescribed in Income-tax Rules and the accounts of the assessee have been prepared and certified as per the provisions of the Companies Act, the Assessing Officer does not have any jurisdiction under section 115JB to rework the net profit of the assessee by substituting the rates of depreciation prescribed under the Companies Act. Applying the ratio of the Supreme Court decision to this case, it may be concluded that the action of the Assessing Officer is not correct.

Illustration 19.

The net profit of Renuka Ltd. an Indian company, as per its profit and loss account prepared as per the Income-tax Act, 1961 is ₹ 90,00,000 after debiting and crediting following items:

	₹
Provision for income-tax	5,00,000
Provisions for deferred tax	3,00,000
Proposed dividend	7,50,000
Depreciation including depreciation on revaluation of assets ₹ 20,00,000 debited to profit and loss account	60,00,000
Profit from industrial unit in SEZ area	80,000
Provision for permanent diminution in the value of investments	70,000

Compute tax liability under section 115JB for the assessment year 2024-25.

Solution:

Computation of Book Profit for the purpose of Sec. 115JB

Particulars	Details	Amount
Net profit as per books of accounts		90,00,000
Add:		
Provision for income tax	5,00,000	
Provisions for deferred tax	3,00,000	
Provision for permanent diminution in the value of investments	70,000	
Proposed dividend	7,50,000	
Depreciation	60,00,000	76,20,000
		1,66,20,000
Less:		
Depreciation (without considering depreciation on revaluation)	40,00,000	
Profit from industrial unit in SEZ area	Nil	40,00,000
Book Profit		1,26,20,000

Computation of Tax Liability under section 115JB

Particulars	Amount
Book profit u/s 115JB	1,26,20,000
15% of book profit	18,93,000
Add: Surcharge [As total income exceeds ₹ 1,00,00,000/-]	1,32,510
Tax & Surcharge	20,25,510
Add: Health & Education Cess @ 4%	81,020
Tax Liability u/s 115JB	21,06,530

The tax liability u/s 115JB is required to be compared with tax liability calculated on income calculated as per other provisions of the Act.

Illustration 20.

Sun bright Ltd., an Indian company furnished following particulars of its income for the previous year 2023-24. Calculate its total income and income tax liability for the assessment year 2024-25:

	₹
Income from business	5,00,000
Dividend received during the year:	
— from Indian company	20,000
— from foreign company	5,000
Gains from transfer of capital assets:	
— short term capital gains	25,000
— long term capital gains	50,000
Agricultural income in India	35,000

Additional information:

(i) Business expenses already charged from business income include ₹ 10,000 revenue expenditure and ₹ 30,000 capital expenditure on family planning programme for employees.

(ii) Company has debited following donations in the profit and loss account of the business of company.

- PM Care Fund: ₹ 50,000.

Solution

Computation of Total Income of Sun Bright Ltd. for the Assessment Year 2024-25

Particulars	Amount	Amount
Income from Business		
Profit as per Profit & Loss A/c		5,00,000
Add: Disallowed Expenditure		
(i) Donation	75,000	
(ii) Capital Expenditure on Family Planning (₹ 30,000 - ₹ 6,000)	24,000	99,000
		5,99,000
Capital Gain		
- Long term	50,000	
- Short term	25,000	75,000
Income from Other Sources		
Dividend from:		
- Indian Company	20,000	
- foreign Company*	5,000	
Agricultural Income	Exempt	25,000
Gross Total Income		6,99,000
Less: Deduction u/s		
- 80G (Donation)		50,000
Total Income		6,49,000

Computation of Tax Liability

Particulars	Tax on LTCG	Other Income
Total Income	50,000	5,99,000
Rate	20%	30%
Tax	10,000	1,79,700
Total tax		1,89,700
Surcharge		Nil
Tax including surcharge		1,89,700
Health & Education Cess @ 4%		7,588
Total tax (Rounded Off)		1,97,290

***** It is assumed that foreign company is not a specified foreign company u/s 115BBD.

Illustration 21.

Following is the profit and loss account of Z Ltd. for the year ended on 31-3-2024

Particulars	Amount	Particulars	Amount
To Raw material consumed	20,00,000	By Sale	
To Rent	5,00,000	Export	50,00,000
To Salary & Wages	10,00,000	Domestic	30,00,000
To Depreciation	5,00,000	By Closing Stock	10,00,000
To Provision for contingencies	75,000		
To Wealth Tax of earlier year	50,000		
To Loss of subsidiary co.	50,000		
To Custom Duty	40,000		
To Proposed dividend	1,00,000		
To Provision for Income tax	1,05,000		
To Net Profit	45,80,000		
	90,00,000		90,00,000

Additional Information

1. Interest on bank loan relating to year 2021-22 has been paid during the previous year ₹ 1,00,000.
2. Whole of Custom duty is unpaid.
3. Company is entitled to get deduction u/s 80G ₹ 1,00,000
4. For the purpose of Income tax, depreciation is ₹ 4,00,000.
5. Turnover of the company during the previous year was ₹ 65 crores and it is life time highest turnover achieved by the company.
6. In past few years, company had suffered losses, following balances are still unabsorbed:

	As per Income tax Act	As per books of Accounts
Depreciation	--	₹ 3,50,000
Losses	₹ 42,50,000	₹ 4,00,000

Compute tax liability of the company.

Solution:

Computation of total income of Z Ltd. for the A.Y.2024-25 (as per other provisions of the Act)

Particulars	Details	Amount
Net profit as per books of accounts		45,80,000
Add: Expenditure disallowed but debited in P/L A/c		
Excess Depreciation	1,00,000	
Provisions for Contingencies	75,000	
Wealth Tax	50,000	

Particulars	Details	Amount
Loss of subsidiary company	50,000	
Proposed Dividend	1,00,000	
Provision for income tax	1,05,000	
Unpaid customs duty	40,000	5,20,000
		51,00,000
Less: Expenditure allowed but not debited in P/L A/c		
Interest on bank loan of earlier years		1,00,000
		50,00,000
Less: Brought forward business loss		42,50,000
Gross Total Income		7,50,000
Less: Deduction u/s 80G		1,00,000
Total Income		**6,50,000**

Computation of Book Profit of Z Ltd. for the A.Y.2024-25

Particulars	Details	Amount
Net profit as per books of accounts		45,80,000
Add:		
Provision for contingencies	75,000	
Loss of subsidiary company	50,000	
Proposed Dividend	1,00,000	
Provision for income tax	1,05,000	
Depreciation	5,00,000	8,30,000
		54,10,000
Less:		
Depreciation (as assets are not revalued)	5,00,000	
Lower of unabsorbed depreciation and brought forward loss (as per books of account)	3,50,000	8,50,000
Book Profit		**45,60,000**

Computation of tax liability of Z Ltd.

Particulars	Amount
Total income as per other provisions of the Act	6,50,000
Tax on above @ 25% **[A]**	1,62,500
Book profit u/s 115JB	45,60,000
15% of book profit **[B]**	6,84,000
Tax [Higher of A & B]	6,84,000
Add: Surcharge [As total income is only ₹ 45,60,000/-, thus, surcharge is not applicable]	Nil
Tax & Surcharge	6,84,000
Add: Health & Education Cess @ 4%	27,360
Tax Liability (Rounded off)	7,11,360

Illustration 22.

Following is the profit and loss account of Z Ltd. for the year ended on 31-3-2024

Particulars	Amount	Particulars	Amount
To Raw material consumed	23,25,000	By Sale	1,60,00,000
To Rent	3,50,000	By Closing Stock	10,00,000
To Salary & Wages	12,00,000	By Revaluation Reserve	25,000
To Depreciation	5,00,000	By General Reserve	1,00,000
To Provision for contingencies	75,000		
To Wealth Tax	50,000		
To Provision for bad debts	40,000		
To Proposed dividend	1,00,000		
To Provision for Income tax	1,05,000		
To Net Profit	1,23,80,000		
	1,71,25,000		1,71,25,000

Additional Information

1. The amount of depreciation includes depreciation on revaluation of assets ₹ 50,000. Further, for the purpose of Income tax, depreciation is ₹ 4,00,000.
2. Turnover of the company during the previous year was ₹ 530 crores. However, during the financial year 2021-22, turnover of the company was ₹ 250 crores only.
3. In past few years, company had suffered losses, following balances are still unabsorbed:

	As per Income tax Act	As per books of Accounts
Depreciation	₹ 66,00,000	Nil
Losses	₹ 35,50,000	Nil

Compute tax liability of the company.

Solution:

Computation of total income of Z Ltd. for the A.Y.2024-25 (as per other provisions of the Act)

Particulars	Details	Amount
Net profit as per books of accounts		1,23,80,000
Add: Expenditure disallowed but debited in P/L A/c		
Excess Depreciation	1,00,000	
Provisions for Contingencies	75,000	
Wealth Tax	50,000	
Provision for bad debts	40,000	
Proposed Dividend	1,00,000	
Provision for income tax	1,05,000	4,70,000
		1,28,50,000

Particulars	Details	Amount
Less: Amount credited to P/L A/c		
Revaluation Reserve	25,000	
General Reserve	1,00,000	1,25,000
		1,27,25,000
Less: Brought forward business loss		35,50,000
		91,75,000
Less: Unabsorbed Depreciation		66,00,000
Total Income		**25,75,000**

Computation of Book Profit of Z Ltd. for the A.Y.2024-25

Particulars	Details	Amount
Net profit as per books of accounts		1,23,80,000
Add:		
Provision for contingencies	75,000	
Proposed Dividend	1,00,000	
Provision for income tax	1,05,000	
Provision for Bad Debts	40,000	
Depreciation	5,00,000	8,20,000
		1,32,00,000
Less:		
Depreciation (ignoring depreciation on revaluation)	4,50,000	
Amount transferred from Revaluation Reserve	25,000	
Amount transferred from General Reserve	1,00,000	5,75,000
Book Profit		**1,26,25,000**

Computation of tax liability of Z Ltd.

Particulars	Amount
Total income as per other provisions of the Act	25,75,000
Tax on above @ 25% **[A]**	6,43,750
Book profit u/s 115JB	1,26,25,000
15% of book profit **[B]**	18,93,750
Tax [Higher of A & B]	18,93,750
Add: Surcharge [As total income is ₹ 1,26,25,000]	1,32,563
Tax & Surcharge	20,26,313
Add: Health & Education Cess @ 4%	81,053
Tax Liability (Rounded off u/s 288B)	**21,07,370**

Tax Credit in respect of Tax Paid on Deemed Income [Sec. 115JAA]

- Where any amount of tax is paid u/s 115JB by an assessee, being a company, then, credit in respect of tax so paid shall be allowed to him in accordance with the provisions of this section. [Sec. 115JAA(1A)]
- The tax credit to be allowed as above shall be the difference of the tax paid for any assessment year u/s 115JB and the amount of tax payable by the assessee on his total income computed in accordance with the other provisions of this Act. However, no interest shall be payable on the tax credit allowed.
- Mathematically, tax credit available = Tax paid u/s 115JB - Tax payable as per other provisions of the Act
- The amount of tax credit determined shall be carried forward and set off but such carry forward shall not be allowed beyond the 15 assessment years immediately succeeding the assessment year in which tax credit becomes allowable.
- The tax credit shall be allowed set-off in a year when tax becomes payable on the total income computed in accordance with the provisions of this Act other than sec. 115JB.
- Set off in respect of brought forward tax credit shall be allowed for any assessment year to the extent of the difference between the tax on his total income and the tax which would have been payable under the provisions of sec. 115JB for that assessment year. In other words, after setting off of MAT credit, tax liability of the year cannot be less than tax would have been payable u/s 115JB for that year.
- The amount of tax credit in respect of any income-tax paid in any country or specified territory outside India u/s 90 or 90A or 91, allowed against the minimum alternate tax, exceeds the amount of the tax credit admissible against the regular income-tax payable by the assessee, then, while computing the amount of credit, such excess amount shall be ignored.

Example

a. Tax paid in foreign country: ₹ 70/-

b. Tax payable u/s 115JB: ₹ 75/-

c. Tax payable under other provisions of the Act: ₹ 10/-

Then,

Foreign tax credit to the extent of ₹ 70/- is available for discharging tax liability u/s 115JB.

While calculating credit u/s 115JAA for subsequent year, ₹ 60/- shall be ignored and credit of ₹ 5 is available as shown below:

Tax payable under other provisions of the Act	A	₹ 10
Less: Foreign Tax Credit	B	₹ 10
Tax Payable after adjustment	C	Nil
Tax payable u/s 115JB	D	₹ 75
Less: Foreign Tax Credit	E	₹ 70
Tax Payable after adjustment	F	₹ 5
MAT Credit available without considering aforesaid provision	D – A	₹ 65
Credit not available due to aforesaid provision	E – B	₹ 60
Credit available in the subsequent year(s)	F – C	₹ 5

- Where as a result of an order, the amount of tax payable is reduced or increased, the amount of tax credit allowed under this section shall also be increased or reduced accordingly.
- Aforesaid provisions do not apply to a limited liability partnership which has been converted from a private company or unlisted public company.
- The provisions of this section shall not apply to a person who has exercised the option u/s 115BAA.

MAT on Ind AS compliant Financial Statement [Sec. 115JB(2A)]

A company whose financial statements are drawn up in compliance to the Indian Accounting Standards specified in Annexure to the Companies (Indian Accounting Standards) Rules, 2015, the book profit (as computed above) shall be further:

a) increased by all amounts credited to other comprehensive income in the statement of profit and loss under the head "Items that will not be re-classified to profit or loss";

b) decreased by all amounts debited to other comprehensive income in the statement of profit and loss under the head "Items that will not be re-classified to profit or loss";

- No adjustment shall be made for the amount credited or debited to other comprehensive income under the head "Items that will not be re-classified to profit or loss" in respect of—

(i) revaluation surplus for assets in accordance with the Indian Accounting Standards 16 and Indian Accounting Standards 38; or

(ii) gains or losses from investments in equity instruments designated at fair value through other comprehensive income in accordance with the Indian Accounting Standards 109:

- However, the book profit of the previous year in which the asset or investment referred above is retired, disposed, realised or otherwise transferred shall be increased or decreased, as the case may be, by the amount or the aggregate of the amounts referred above for the previous year or any of the preceding previous years and relatable to such asset or investment.

c) increased by amounts or aggregate of the amounts debited to the statement of profit and loss on distribution of non-cash assets to shareholders in a demerger in accordance with Appendix A of the Indian Accounting Standards 10;

d) decreased by all amounts or aggregate of the amounts credited to the statement of profit and loss on distribution of non-cash assets to shareholders in a demerger in accordance with Appendix A of the Indian Accounting Standards 10.

MAT in case of demerger [Sec. 115JB(2B)]

In the case of a resulting company, where the property and the liabilities of the undertaking being received by it are recorded at values different from values appearing in the books of account of the demerged company immediately before the demerger, any change in such value shall be ignored for the purpose of computation of book profit of the resulting company.

First time adoption of Ind AS [Sec. 115JB(2C)]

In case of Ind AS compliant company, the book profit of the year of convergence and each of the following 4 previous years, shall be further increased or decreased, as the case may be, by 1/5th of the transition amount.

- "Transition Amount" means the amount or the aggregate of the amounts adjusted in the other equity (excluding capital reserve, and securities premium reserve) on the convergence date but not including the following:

  A. Aggregate of the amounts adjusted in the other comprehensive income on the convergence date which shall be subsequently re-classified to the profit or loss;

  B. Revaluation surplus for assets in accordance with the Indian Accounting Standards 16 and Indian Accounting Standards 38 adjusted on the convergence date;

  C. Gains or losses from investments in equity instruments designated at fair value through other comprehensive income in accordance with the Indian Accounting Standards 109 adjusted on the convergence date;

  D. Adjustments relating to items of property, plant and equipment and intangible assets recorded at fair value as deemed cost in accordance with paragraphs D5 and D7 of the Indian Accounting Standards 101 on the convergence date;

  E. Adjustments relating to investments in subsidiaries, joint ventures and associates recorded at fair value as deemed cost in accordance with paragraph D15 of the Indian Accounting Standards 101 on the convergence date; and

  F. Adjustments relating to cumulative translation differences of a foreign operation in accordance with paragraph D13 of the Indian Accounting Standards 101 on the convergence date.

- The book profit of the previous year in which the asset or investment referred to in (B) to (E) (*supra*) is retired, disposed, realised or otherwise transferred, shall be increased or decreased, as the case may be, by the aggregate of the amounts relatable to such asset or investment.
- The book profit of the previous year in which the foreign operation referred to in (F) is disposed or otherwise transferred, shall be increased or decreased, as the case may be, by the aggregate of the amounts relatable to such foreign operations.
- "Year of Convergence" means the previous year within which the convergence date falls;
- "Convergence Date" means the first day of the first Indian Accounting Standards reporting period as defined in the Indian Accounting Standards 101.

1.2.4 Tax on Distributed Income to Shareholders [Sec. 115QA]

The provisions are enumerated here-in-below:

1. The asseessee is a Domestic company
2. The assessee-company has distributed income on buy back of its own shares from its shareholders
   - "Buy-back" means purchase by a company of its own shares in accordance with the provisions of any law for the time being in force relating to companies
   - "Distributed income" means the consideration paid by the company on buy-back of shares as reduced by the amount, which was received by the company for issue of such shares, determined in the manner as may be prescribed.
3. Such company shall be liable to pay additional income-tax @ 20% (+ surcharge + cess) on the distributed income. Such tax is irrespective of the fact that the company is not liable for paying income tax on its income.
4. The principal officer of the domestic company and the company shall be liable to pay the tax to the credit of

the Central Government within 14 days from the date of payment of any consideration to the shareholder on buy-back of shares.

5. The tax on the distributed income by the company shall be treated as the final payment of tax in respect of the said income and no further credit therefor shall be claimed by the company or by any other person in respect of the amount of tax so paid.

6. No deduction under any other provision of this Act shall be allowed to the company or a shareholder in respect of the income which has been charged to tax under this section or the tax thereon.

Interest Payable for Non-payment of Tax by Company [Sec. 115QB]

Where the principal officer of the domestic company and the company fails to pay the tax on the aforesaid distributed income within 14 days, he or it shall be liable to pay simple interest @ 1% for every month or part thereof on the amount of such tax for the period beginning on the date immediately after the last date on which such tax was payable and ending with the date on which the tax is actually paid.

When Company is Deemed to be Assessee in Default [Sec. 115QC]

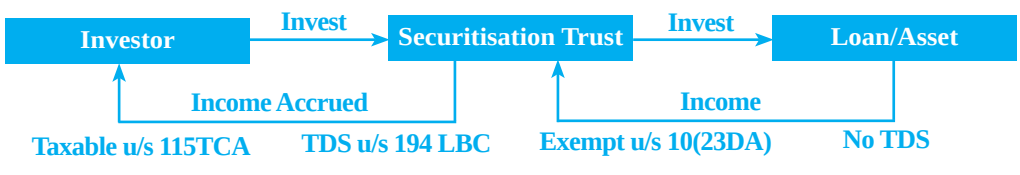
If any principal officer of a domestic company and the company does not pay tax on distributed income in accordance with the provisions of section 115QA, then, he or it shall be deemed to be an assessee in default in respect of the amount of tax payable by him or it and all the provisions of this Act for the collection and recovery of income-tax shall apply.

1.2.5 Tax on income from Securitisation Trusts [Sec. 115TCA]

Meaning

Securitisation Trust means a trust (which fulfils such conditions, as may be prescribed), being a:

Special purpose distinct entity	As per regulation 2(1)(u) of the SEBI (Public Offer and Listing of Securitised Debt Instruments) Regulations, 2008 made under the SEBI Act, 1992 and the Securities Contracts (Regulation) Act, 1956, and regulated under the said regulations
Special Purpose Vehicle	Regulated by the guidelines on securitisation of standard assets issued by the RBI
Trust	Set-up by a securitisation company or a reconstruction company formed, for the purposes of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act), or in pursuance of any guidelines or directions issued by the RBI

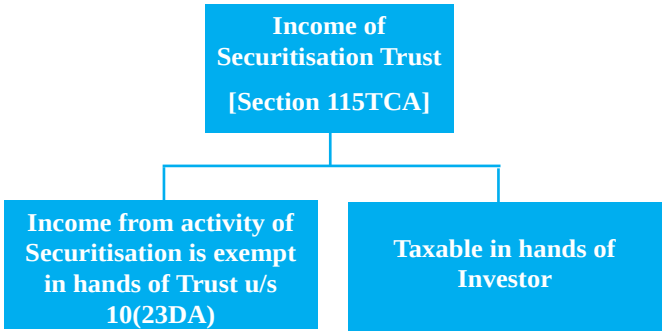


Tax Treatment in hands of investor

- Income of an investor of a securitisation trust, out of investments made in the securitisation trust, shall be chargeable to income-tax in the same manner as if it were the income accruing or arising to, or received by, such person, had the investments by the securitisation trust been made directly by him.

a. Investor means a person who is holder of any securitised debt instrument or securities or security receipt issued by the securitisation trust.

b. Securities means debt securities issued by a Special Purpose Vehicle as referred to in the guidelines on securitisation of standard assets issued by the RBI.



- **Nature of income:** The income paid or credited by the securitisation trust shall be deemed to be of the same nature and in the same proportion in the hands of the investor, as if it had been received by, or had accrued or arisen to, the securitisation trust during the previous year.
- **Deemed Credit:** The income accruing or arising to, or received by, the securitisation trust, during a previous year, if not paid or credited to the investor, shall be deemed to have been credited to the account of the investor on the last day of the previous year in the same proportion in which such investor would have been entitled to receive the income had it been paid in the previous year.
- **Statement specifying nature of income:** The person responsible for crediting or making payment of the income on behalf of securitisation trust and the securitisation trust shall furnish, within 30th June of the financial year following the previous year during which the income is distributed, to the investor who is liable to tax in respect of such income and to the prescribed income-tax authority (30th November of the financial year following the previous year during which the income is distributed) , a statement in such form (Form 64E) and verified in such manner, giving details of the nature of the income paid or credited during the previous year and such other relevant details, as may be prescribed.
- **Double taxation:** Any income which has been included in the total income of the investor, in a previous year, on account of it having accrued or arisen in the said previous year, shall not be included in the total income of such person in the previous year in which such income is actually paid to him by the securitisation trust.

Tax treatment in hands Securitisation Trust

Any income of a securitisation trust from the activity of securitisation is exempt u/s 10(23DA).

TDS on income from Investment in Securitization Fund [Sec. 194LBC]

Who is responsible to deduct tax: The person responsible for making the payment to an investor in respect of an investment in a securitisation trust, being referred to in sec. 115TCA

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS:

Payee	Rate of TDS
Resident	
– Individual or HUF	25%
– Other resident	30%
Non-Resident	
– Foreign Company	40%
– Other than foreign company	30%

Exemption or relaxation from the provision

When the recipient applies to the Assessing Officer in Form 13 and gets a certificate authorising the payer to deduct tax at lower rate or deduct no tax

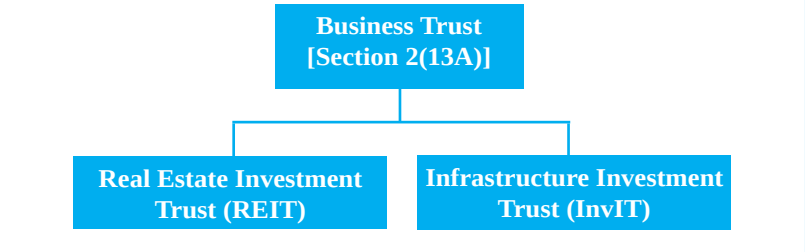
1.2.6 Tax on income of unit holder and business trust [Sec. 115UA]

Meaning [Sec. 2(13A)]

Business Trust means a trust registered as:

i. an Infrastructure Investment Trust under the SEBI (Infrastructure Investment Trusts) Regulations, 2014; or

ii. a Real Estate Investment Trust under the SEBI (Real Estate Investment Trusts) Regulations, 2014



Tax treatment in hands of Business Trust

1. **Following income are exempt:**

A. Income of Business Trust [Sec 10(23FC)]

Any income of a business trust by way of

a. interest received or receivable from a special purpose vehicle; or

b. dividend received or receivable from a special purpose vehicle

- "Special purpose vehicle" means an Indian company in which the business trust holds controlling interest and any specific percentage of shareholding or interest, as may be required by the regulations under which such trust is granted registration
- Special purpose vehicle is not required to deduct tax at source on interest paid to the business trust [Sec. 194A(3)(xi)]. However, business trust is required to deduct tax at source @ 10% (5% in case of non-corporate non-resident or foreign company) on interest component of income distributed to the unitholders [Sec. 194LBA]

B. Income of Real Estate Investment Trust [Sec. 10(23FCA)]

Any income of a business trust, being a real estate investment trust, by way of renting or leasing or letting out any real estate asset owned directly by such business trust.

Taxpoint: Where rent is credited or paid to a business trust, being a real estate investment trust, in respect of any real estate asset, referred to in sec. 10(23FCA), owned directly by such business trust, TDS u/s 194-I is not required to be deducted. Business trust is required to deduct tax at source @ 10% (30% in case of non-corporate non-resident and 40% in case of foreign company) on distribution of such rental income to the unit holders [Sec. 194LBA]

2. **Other Income of Business Trust**

Subject to the provisions of sec. 111A and sec. 112, the total income of a business trust shall be charged to tax at the maximum marginal rate.

Tax treatment in hands of unit holders

A. **Distributed Income to unit holder of a Business Trust [Sec 10(23FD)]**

Any distributed income, referred to in section 115UA, received by a unit holder from the business trust, not being that proportion of the income which is of the same nature as the income referred to in 10(23FC)(a) [i.e., proportionate interest income] or 10(23FC)(b)

Case	REIT	InvIT	Unitholders
Dividend from SPV (SPV not opted for Sec. 115BAA)	Exempt	Exempt	Exempt
Dividend from SPV (SPV opted for Sec. 115BAA)	Exempt	Exempt	Taxable
Dividend other than dividend from SPV	Taxable	Taxable	Exempt
Interest from SPV	Exempt	Exempt	Taxable
Interest other than above	Taxable	Taxable	Exempt
Rental income from SPV	Taxable	Taxable	Exempt
Rental income from property owned by REIT	Exempt	Taxable	From REIT: Taxable From InvIT: Exempt
Capital Gain	Taxable @ sp rate, if any else MMR	Taxable @ sp rate, if any else MMR	Exempt

[i.e., proportionate dividend income where the special purpose vehicle has exercised the option u/s 115BAA] or 10(23FCA) [i.e., proportionate rental income] is exempt

B. Any income distributed by a business trust to its unit holders shall be deemed to be of the same nature and in the same proportion in the hands of the unit holder as it had been received by, or accrued to, the business trust.

If in any previous year, the distributed income, received by a unit holder from the business trust is of the nature as referred to in sec. 10(23FC) or 10(23FCA)], then, such distributed income shall be deemed to be income of such unit holder and shall be charged to tax as income of the previous year.

Taxpoint: Unitholder, being non-corporate non-resident or foreign company, may be liable to tax u/s 115A.

Other Provisions

- Any person responsible for making payment of the income distributed on behalf of a business trust to a unit holder shall furnish a statement to the unit holder (within 30th June of the financial year following the previous year during which the income is distributed) and the prescribed authority (within 30th November of the financial year following the previous year during which the income is distributed), in such form and manner as may be prescribed, giving the details of the nature of the income paid during the previous year and such other details as may be prescribed.
- The provision is not applicable in respect of any sum referred to in sec. 56(2)(xii), received by a unit holder from a business trust.

- Any transfer of a capital asset, being share of a special purpose vehicle to a business trust in exchange of units allotted by that trust to the transferor is not regarded as transfer for the purpose of computation of capital gain.
- Income referred to in sec. 10(23FC) or 10(23FCA) is not taxable in hands of business trust but taxation of such income is passed to the unit holder. On the other hand, all other income of the business trust is taxable in hands of the business trust and distribution thereof to the unit holders is not taxable again in hands of the unitholders.

1.2.7 TDS on certain income from units of a Business Trust [Sec. 194LBA]

Who is responsible to deduct tax: Any business trust distributing income referred to in sec. 115UA [being of the nature referred to in sec. 10(23FC) or 10(23FCA)] to its unit holder

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS:

Payee	Rate of TDS	
	Payment referred to in sec. 10(23FC)	Payment referred to in sec. 10(23FCA)
If payment is made to a resident unit holder	10%	10%
If payment is made to a unit holder being non-resident (not being a company)	Dividend income: 10% Other Income: 5%	30% + SC + Health & Education Cess
If payment is made to a unit holder being a foreign company	Dividend income: 10% Other Income: 5%	40% + SC + Health & Education Cess

Other Point

The provision is not applicable in respect of income of the nature referred to in sec. 10(23FC)(b) [i.e., dividend], if the special purpose vehicle has not exercised the option u/s 115BAA.

Illustration 23.

DEF is a real estate investment trust (REIT). It owns house properties in different parts of Maharashtra. Besides, it holds controlling interest in A Ltd. (A Ltd., an Indian company, is SPV created by DEF for the purpose of owning commercial properties). Annual income of DEF for the previous year 2023-24 are calculated as under:

	₹ in crore
Rental income from properties directly owned by DEF (computed)	7
Long-term capital gain on sale of land and buildings directly owned by DEF (computed)	20
Short term capital gain on sale of listed shares of A Ltd.	2
Short term capital gain on sale of land and buildings directly owned by DEF (computed)	8
Interest from A Ltd.	13
Total	50

DEF distributes ₹ 50 crore to its unitholders. X is one of the unitholders. He holds 10% units in DEF. Compute income in hands of DEF and X

Solution:

Computation of total income and tax liability of DEF for the A.Y. 2024-25

Particulars	₹ in crore
Rental income from properties directly owned by DEF [Exempt u/s 10(23FCA)]	Nil
Long-term capital gain on sale of land and buildings directly owned by DEF	20
Short term capital gain on sale of listed shares of A Ltd.	2
Short term capital gain on sale of land and buildings directly owned by DEF	8
Interest from A Ltd. [Exempt u/s 10(23FC)]	Nil
Total Income	**30**

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

Particulars	₹ in crore
Rental income from properties [₹ 5 crore x 7 / 50]	0.70
Long-term capital gain on sale of land and buildings [Exempt u/s 10(23FD)]	Exempt
Short term capital gain on sale of listed shares of A Ltd. [Exempt u/s 10(23FD)]	Exempt
Short term capital gain on sale of land and buildings [Exempt u/s 10(23FD)]	Exempt
Interest from A Ltd. [₹ 5 crore x 13 / 50]	1.30
Total Income	**2.00**

1.2.8 Tax on income of investment fund and its unit holders [Sec. 115UB]

Meaning

Investment fund means any fund established or incorporated in India in the form of a trust or a company or a limited liability partnership or a body corporate which has been granted a certificate of registration as a Category I or a Category II Alternative Investment Fund and is regulated under the SEBI (Alternative Investment Funds) Regulations, 2012, made under the SEBI Act, 1992 or regulated under the International Financial Services Centres Authority (Fund Management) Regulations, 2022 made under the International Financial Services Centres Authority Act, 2019

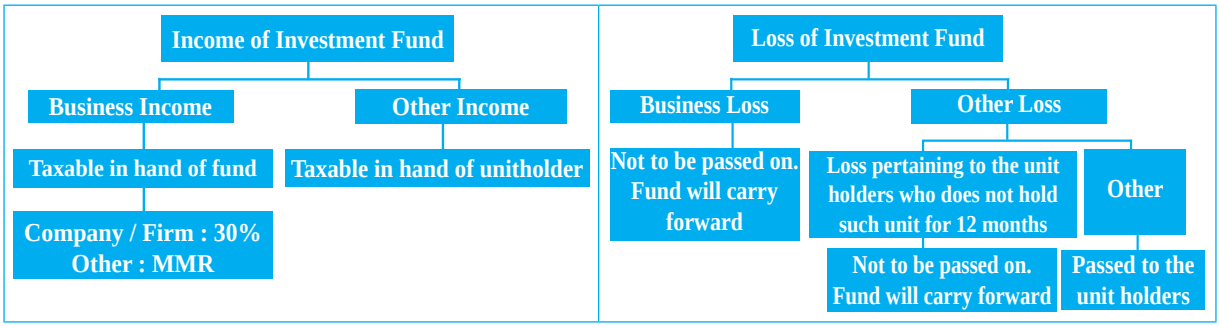
Tax treatment in hands of Investment Fund

A. Non-business income of Investment Fund

Any income of an investment fund other than the income chargeable under the head "Profits and gains of business or profession" is exempt u/s 10(23FBA)].

B. The total income of the investment fund shall be charged to tax as follow:

Where such fund is a company or a firm	Taxable at the rate specified in the Finance Act
In any other case	Taxable at maximum marginal rate



Other Provisions

- **Statement specifying nature of income:** The person responsible for crediting or making payment of the income on behalf of an investment fund and the investment fund shall furnish, within 30th June of the financial year following the previous year during which the income is distributed, to the person who is liable to tax in respect of such income and to the prescribed income-tax authority (within 30th November of the financial year following the previous year during which the income is distributed), a statement in the prescribed form and verified in such manner, giving details of the nature of the income paid or credited during the previous year and such other relevant details, as may be prescribed.

Tax treatment in hands of unitholders

A. Income, being that proportion of income which is of the same nature as income chargeable under the head "Profits and gains of business or profession" in hands of the investment fund is exempt in hands of the unit holders [Sec. 10(23FBB)].

B. Any income accruing or arising to, or received by, a person, being a unit holder of an investment fund, out of investments made in the investment fund, shall be chargeable to income-tax in the same manner as if it were the income accruing or arising to, or received by, such person had the investments made by the investment fund been made directly by him.

Taxpoint:

- **Carry forward of Loss:** Where in any previous year, the net result of computation of total income of the investment fund [without giving effect to the provisions of sec. 10(23FBA)] is a loss under any head of income and such loss cannot be or is not wholly set-off against income under any other head of income of the said previous year, then:

  i. out of such loss, the loss arising to the investment fund as a result of the computation under the head "Profits and gains of business or profession", if any, shall be:

     - allowed to be carried forward and it shall be set off by the investment fund in accordance with the provisions of Chapter VI; and
     - Such loss shall not be passed through to the unit holders.

  ii. the other loss, if any, shall not be passed through to the unit holders, if such loss has arisen in respect of a unit which has not been held by the unit holder for a period of atleast 12 months.

- The loss other than the loss under the head "Profits and gains of business or profession", if any, accumulated at the level of investment fund as on 31-03-2019, shall be:

i. deemed to be the loss of a unit holder who held the unit on the 31-03-2019 in respect of the investments made by him in the investment fund; and

ii. allowed to be carried forward by such unit holder for the remaining period calculated from the year in which the loss had occurred for the first time taking that year as the first year and shall be set off by him in accordance with the provisions of Chapter VI:

Taxpoint: Such loss shall not be available to the investment fund on or after 01-04-2019.

- **Nature of income:** The income paid or credited by the investment fund shall be deemed to be of the same nature and in the same proportion in the hands of the unitholders, as if it had been received by, or had accrued or arisen to, the investment fund during the previous year (subject to adjustment of losses).
- **Deemed Credit:** The income of the investment fund, if not paid or credited to the unit holders, shall be deemed to have been credited to the account of the said person on the last day of the previous year in the same proportion in which such person would have been entitled to receive the income had it been paid in the previous year.
- **Double Taxation:** Any income which has been included in total income of the unitholder in a previous year, on account of it having accrued or arisen in the said previous year, shall not be included in the total income of such person in the previous year in which such income is actually paid to him by the investment fund.

1.2.9 TDS on income of units of Investment Fund [Sec. 194LBB]

Who is responsible to deduct tax: The person responsible for making the payment of any income, other than that proportion of income which is of the same nature as income referred to in sec. 10(23FBB), to a unit holder in respect of units of an investment fund specified in clause (a) of the Explanation 1 to sec. 115UB

When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.

Rate of TDS:

Payee	Rate of TDS
Resident	10%
Non-resident (not being a company)	30%
Foreign Company	40%

Note: Where the payee is a non-resident (not being a company) or a foreign company, deduction shall not be made in respect of any income that is not chargeable to tax.

Exemption or relaxation from the provision

When the recipient applies to the Assessing Officer in Form 13 and gets a certificate authorising the payer to deduct tax at lower rate or deduct no tax

Illustration 24.

Compute total income of each investment fund for A.Y. 2024-25 from the following details:

Income	Fund A (₹)	Fund B (₹)	Fund C (₹)
Business Income	Nil	5,00,000	(2,00,000)
Capital Gains	20,00,000	15,00,000	(5,00,000)
Income from Other Sources	5,00,000	3,00,000	10,00,000

Further, it is also given that there are 20 unit-holders each holding one unit. You are also requested to compute income of unit holder assuming that income from investment fund is the only income of unit holder.

SolutionL

Computation of total income of the investment fund for the A.Y. 2024-25

Particulars	Fund A (₹)	Fund B (₹)	Fund C (₹)
Business Income	Nil	5,00,000	Nil
Total Income	Nil	5,00,000	Nil

Such income is taxable at the rate @ 30% if the fund is a company or firm else at maximum marginal rate of tax.

Computation of total income of the unit holder for the A.Y. 2024-25

Particulars	Fund A (₹)	Fund B (₹)	Fund C (₹)
Capital Gains [Income / 20]	1,00,000	75,000	
Income from Other Sources [Income / 20] [#(₹ 10 lakh – ₹ 2 lakh) / 20]	25,000	15,000	40,000#
Total Income	**1,25,000**	**90,000**	**40,000**

Illustration 25.

In case of case C of the aforesaid illustration, if Fund C has earned following income during the previous year 2024-25, compute total income for the assessment year 2025-26

- Business Income: ₹ 2,00,000
- Capital Gains: ₹ 8,00,000
- Income from Other Sources: ₹ 9,00,000

Solution:

Computation of total income of the investment fund for the A.Y. 2024-25

Particulars	Amount (₹)
Business Income	2,00,000
Total Income	**2,00,000**

Computation of total income of the unit holder for the A.Y. 2025-26

Particulars	Amount (₹)
Capital Gains [(₹ 8 lakh – ₹ 5 lakh i.e., b/f loss) / 20]	15,000
Income from Other Sources [Income / 20]	45,000
Total Income	**60,000**

1.2.10 Tax on income from Patent [Sec. 115BBF]

Where the total income of an eligible assessee includes any income by way of royalty in respect of a patent developed and registered in India, tax @ 10% shall be payable on such royalty income.

- Eligible Assessee means a person resident in India and who is a patentee;
- Patentee means the person, being the true and first inventor of the invention, whose name is entered on the patent register as the patentee, in accordance with the Patents Act, and includes every such person, being the true and first inventor of the invention, where more than one person is registered as patentee under that Act in respect of that patent.
- Developed means at least 75% of the expenditure incurred in India by the eligible assessee for any invention in respect of which patent is granted under the Patents Act, 1970
- Royalty, in respect of a patent, means consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head "Capital gains" or consideration for sale of product manufactured with the use of patented process or the patented article for commercial use) for the:
  - i. transfer of all or any rights (including the granting of a licence) in respect of a patent; or
  - ii. imparting of any information concerning the working of, or the use of, a patent; or
  - iii. use of any patent; or
  - iv. rendering of any services in connection with the activities referred above
- Lump sum includes an advance payment on account of such royalties which is not returnable.

Other Provisions

- **No deduction for expenditure:** No deduction in respect of any expenditure or allowance shall be allowed to the eligible assessee in computing his royalty income.
- **Option to the assessee:** The eligible assessee is required to exercise the option for taxation of such royalty income in accordance with the provisions of this section, in the prescribed manner, on or before the due date for furnishing the return of income for the relevant previous year.
- **Concessional Rate is not applicable:** Where an eligible assessee opts for taxation of his royalty income in accordance with the provision of this section and he offers the royalty income for any of the 5 assessment years relevant to the previous year succeeding the previous year not in accordance with the provisions this section, then, the assessee shall not be eligible to claim the benefit of this section for 5 assessment years subsequent to the assessment year relevant to the previous year in which such income has not been offered to tax in accordance with this section.

1.2.11 Tax on income from transfer of carbon credits [Sec. 115BBG]

Where the total income of an assessee includes any income by way of transfer of carbon credits, tax @ 10% shall be payable on the income by way of transfer of carbon credits.

- Carbon credit in respect of one unit shall mean reduction of one tonne of carbon dioxide emissions or emissions of its equivalent gases which is validated by the United Nations Framework on Climate Change and which can be traded in market at its prevailing market price.
- No deduction for expenditure: No deduction in respect of any expenditure or allowance shall be allowed to the assessee while computing his income by way of transfer of carbon credit

Trust

1.3

'Charity begins at home but should not end there.' – Francis Bacon

The essence of the above quote has been fully captured in the definition of the expression "charitable purpose" as envisaged in the Income Tax Act, 1961. Under the Indian Income Taxation Laws, a trust is considered as charitable, if its objects are directed to the benefit of the society at large and not for an individual or group of individuals. Various deductions or exemptions are available under the law to the charitable trust.

Now a days, business trust, securitization trust, etc., are also formed. The Act provides special code in respect of computation of income of these trusts.

1.3.1 Religious or Charitable Trust

Income of a religious or charitable trust or institution is exempt from tax u/s 11. Trust must be created in accordance with law for charitable purposes.

Meaning of Certain Terms

Trust	It is an obligation annexed to the ownership; ➢ arising out of a confidence reposed by the owner; ➢ declared and accepted by him (owner); ➢ for the benefit of another (or of another and the owner). **Note:** For the purpose of the Income Tax Act, the word trust includes "any other legal obligation"
Author of the trust	The person who reposes or declares the confidence and creates trust.
Beneficiary	The person for whose benefit the trust is created.
Trustee	The person who accepts the confidence and who is authorised to manage the trust property and to look after the interest of the beneficiary.
Trust property	The property set aside by the trust, for the benefit of the beneficiary, being the subject matter of the trust.
Instrument of trust	The deed or instrument by which the trust is created. **Note:** No trust in relation to immovable property can be framed unless and until a non-testamentary instrument in writing is signed by the author of the trust or by the will of the author of the trust. However, such an instrument is not required in the case of a movable property when such property is transferred to the trustee.

Charitable purpose	As per Sec. 2(15), it includes relief of the poor, education, yoga, medical relief, preservation of the environment (including watersheds, forests, and wildlife), and preservation of monuments or places or objects of artistic or historic interest and the advancement of any other object of general public utility. (discussed in detail later in this chapter)
Public trust	A trust in which beneficiaries are the general public or a class thereof.
Private trust	A trust in which the beneficiary is the specific person(s).

Contents

Sec.11	Exemption of income from property held in trust or other legal obligation for religious or charitable purpose(s) wholly.
Sec.12	Exemption of income derived by such a trust from voluntary contribution
Sec.12A/12AB	Conditions relating to registration of trust
Sec.13	Withdrawal of exemptions u/s 11 and 12

Conditions for Exemption [Sec. 11]

A. Property must be held under a trust

The income-yielding property must be held under a trust or other legal obligations.

Taxpoint:

- There must be a trust: If there is neither trust nor any legal obligation, exemption will not be available even if the entire income of the property is applied to charitable or religious purpose.
- There must be a property: A mere creation of a trust for generating income is not sufficient. There must be a property held under a trust for generating income.

B. Purpose of the trust

Trust must be created wholly for charitable/religious and lawful purposes. (discussed in detail later in this chapter).

C. Registration of the trust

The trust must be a registered trust. (The procedure of registration is discussed later in this chapter).

D. Audit of Accounts

Where the total income of the trust or institution without giving effect to the provisions of sec. 11 and 12 exceeds the maximum amount which is not chargeable to income-tax in any previous year,—

i. the books of account and other documents have been kept and maintained in such form and manner and at such place, as may be prescribed; and

ii. Such accounts of the trust must be audited. Audit report must be uploaded one month prior to the due date of filing of return.

E. Application of Income

Income must be applied for the purpose of the trust. (a detailed discussion is made later in this chapter)

- While computing income of the trust, the provisions of sec. 40(a)(ia), sec. 40A(3) and sec. 40A(3A) shall apply as they apply in computing the income chargeable under the head "Profits and gains of business or profession.

F. Return of Income

Income-tax return required to furnished u/s 139(4A) should be furnished within the due date of filing return of income.

G. Additional condition for charitable trust created on or after 1/4/1962

A charitable trust created on or after 1/4/1962 should satisfy further following conditions:

a. It should not be created for the benefit of any particular religious community or caste.

b. No part of its income should be applied directly or indirectly for the benefit of the settlor or other specified persons.

c. Its property should be held wholly for charitable purposes.

Trust must be created wholly for charitable/religious and lawful purposes

Meaning of Charitable trust

1. As per Sec. 2(15), charitable purpose includes relief of the poor, education, yoga, medical relief, preservation of environment (including watersheds, forests and wildlife) and preservation of monuments or places or objects of artistic or historic interest and the advancement of any other object of general public utility.

   Exception: The advancement of any other object of general public utility shall not be a charitable purpose, if it involves the carrying on of:

   a) any activity in the nature of trade, commerce or business, or

   b) any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration,

   - irrespective of the nature of use or application, or retention, of the income from such activity, unless:

     i. such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility; and

     ii. the aggregate receipts from such activity or activities during the previous year, do not exceed 20% of the total receipts, of the trust or institution undertaking such activity or activities, of that previous year.

2. In this regard it is to be noted that -

   Sec. 10(21) exempts, subject to certain conditions, income of an approved scientific research association, which is applied fully for the purpose of such association.

   Sec. 10(23C) exempts, subject to certain conditions, income of a University and other educational institutions or hospital or other institutions existing fully for educational or philanthropic purposes respectively.

3. If the object is not intended to give relief to the poor or for the advancement of medical or educational field, it may be treated as charitable purpose if it causes the advancement of object of **general public utility**. As per Bar council of Maharastra -vs.- CIT meaning of –

General	**:**	Pertaining to a whole class
Public	**:**	The body of people at large
Utility	**:**	Usefulness

4. The expression "object of general public utility" is not restricted to 'the object beneficial to whole of mankind'. An object beneficial to a particular section shall also be deemed as "object of general public utility". However, it must not be beneficial, only to a particular caste or religious community.
5. Charitable purpose includes Promotion of Sports and Games. Therefore, an association engaged in the promotion of games and sports can claim exemption u/s 11.
6. A trust or institution meant for the benefit of Scheduled Castes, Scheduled Tribes, Backward Classes, etc. is eligible for exemption u/s 11.
7. Trust created for charitable or religious purposes, which promotes international welfare in which India is interested, shall be eligible for exemption provided a general or special order has been received from CBDT in this regard.

Meaning of Religious Purpose

- Sec.11 provides exemption to income of the trust held for charitable or religious purpose. Religious purpose is different from charitable purpose. A private trust held for religious purpose is not eligible for exemption u/s 11, however, a public trust held for religious purpose can claim exemption u/s 11. A charitable trust created on or after 1/4/1962, should not be created for the benefit of any particular religious community or caste.
- As per explanation 3A to sec. 11(1), where the property held under a trust or institution includes any temple, mosque, gurdwara, church or other place notified u/s 80G(2)(b), any sum received by such trust or institution as voluntary contribution for the purpose of renovation or repair of such temple, mosque, gurdwara, church or other place, may, at its option, be treated by such trust or institution as forming part of the corpus of the trust or the institution, subject to the condition that the trust or the institution,—
  a. applies such corpus only for the purpose for which the voluntary contribution was made;
  b. does not apply such corpus for making contribution or donation to any person;
  c. maintains such corpus as separately identifiable; and
  d. invests or deposits such corpus in the forms and modes specified u/s 11(5).
- Further, as per Explanation 3B, where any trust or institution has treated any sum received by it as forming part of the corpus, and subsequently any of the aforesaid conditions is violated, such sum shall be deemed to be the income of such trust or institution of the previous year during which the violation takes place

Meaning of lawful purpose

The trust shall not be treated as lawful if the purpose -

- for which it is created is forbidden by law.
- is fraudulent
- is regarded as immoral or opposed to public policy
- causes injury to others.

Where a trust has two objects one of which in unlawful it shall be treated as illegal trust unless and until it can be separately carried on with legal object.

Exemption [Sec. 11]

As per sec. 11(1)(a), income derived from property held under trust wholly for charitable or religious purpose(s), shall be exempted from tax, to the extent to which such income is applied to such purposes in India.

Taxpoint:

- Any amount credited or paid to any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sec. 10(23C)(iv) or (v) or (vi) or (via) or other registered trust or institution, being

Contribution with a specific direction that they shall form part of the corpus	It shall not be treated as application of income for charitable or religious purposes
Contribution without such direction	It shall be treated as application for charitable or religious purposes only to the extent of 85% of such amount credited or paid

- In order to claim exemption, a trust must apply its income for charitable purpose(s). Income which is not applied for the purpose for which charitable trust is created, shall not be eligible for exemption.
  - Any sum payable by any trust or institution shall be considered as application of income in the previous year in which such sum is **actually paid** by it (irrespective of the previous year in which the liability to pay such sum was incurred by the trust or institution according to the method of accounting regularly employed by it)
  - Further, where during any previous year, any sum has been claimed to have been applied by the trust or institution, such sum shall not be allowed as application in any subsequent previous year.
- Anonymous donation referred u/s 115BBC is not exempt.
- Where a trust or an institution has been granted registration and the said registration is in force for any previous year, then, no exemption u/s 10 [other than sec.10(1), 10(23C) and 10(46)] is available to such trust or institution

Anonymous donation [Sec. 115BBC]

Where the total income of an assessee being –

- Any University or other educational institution referred u/s 10(23C)(iiiad) or (vi)
- Any hospital or other institution referred u/s 10(23C)(iiiae) or (via)
- Any fund or institution referred u/s 10(23C)(iv) or (v)
- Any trust or institution referred u/s 11.
  - includes any income by way of anonymous donation[#] in excess of specified limit[##], such donation shall be taxed @ 30% (+SC+EC+SHEC)

[#] Anonymous donation means any voluntary contribution, where a person receiving such contribution does not maintain a record of the identity indicating the name and address of the person making such contribution and other prescribed particulars.

[##] **Specified limit:** Anonymous donation received being higher of the following:

- 5% of the total donations received by the assessee; or
- ₹ 1,00,000

Exceptions

The above provision shall not apply to any anonymous donation received by –

- Any trust or institution created wholly for religious purposes
- Any trust or institution created wholly for religious and charitable purposes other than any anonymous donation made with a specific direction that such donation is for any University or other education institution or hospital or other medical institution run by such trust or institution.
- Anonymous donation received upto specified limit.

Free Accumulation of Income

However, trust is allowed to accumulate 15% of its income and such accumulation shall be treated as application of income. For such 15% accumulation of income, trust need not to apply any one. Such accumulation of income is freely allowed.

Taxpoint:

- In order to claim 100% exemption, trust must apply 85% of its income for charitable purpose(s)for which it is created.
- For this purpose, income means accounting income and not income as per the Income Tax Act.

Example: If a trust has earned income of ₹ 3,00,000 for the year 2023-24, and applied its income for charitable purpose(s) during the year 2023-24, ₹ 1,80,000. The taxable income shall be –

Income of the trust	₹ 3,00,000
Less: 15% free accumulation	₹ 45,000
Balance	₹ 2,55,000
Less: Amount applied for the prescribed purposes	₹ 1,80,000
Taxable income	**₹ 75,000**

Notes regarding computation of income / Income of trusts or institutions

a. **Voluntary contribution:** As per sec. 12(1), any voluntary contributions (not being contributions made with a specific direction that they shall form part of the corpus of the trust or institution) received by a trust created wholly for charitable or religious purpose(s), shall be deemed to be income of the trust.

Taxpoint:

- Contributions made with a specific direction that they shall form part of the corpus of the trust shall not be treated as income of the trust subject to the condition that such voluntary contributions are invested or deposited in one or more of the forms or modes specified in sec. 11(5) maintained specifically for such corpus.
- Application for charitable or religious purposes from such corpus shall not be treated as application of income for charitable or religious purposes. However, the amount not so treated as application shall be treated as application for charitable or religious purposes in the previous year in which the amount is invested or deposited back, into one or more of the forms or modes specified in sec. 11(5) maintained specifically for such corpus, from the income of that year and to the extent of such investment or deposit.

b. **Value of services:** As per sec. 12(2), the value of any service, being medical or educational service, provided by the charitable or religious trust running a hospital or medical institution or an educational institution, shall

be deemed to be income of the trust during the previous year in which such services are provided and shall be chargeable to income-tax.

c. **Business Income of the Trust [Sec.11(4) & (4A)]:** On fulfillment of following two conditions, income of any such undertaking shall not be included in the total income of the trust -

1. The trust or institution can carry out business activities provided such activities are incidental to the object of the trust.
2. Trust needs to maintain separate books of account in respect of such business.
3. The purpose of the trust or institute must be relief to the poor, education or medical relief.

Taxpoint

- Property held under trust includes a business undertaking so held.
- The Assessing Officer has power to determine the income of such undertaking in accordance with the provisions of this Act.
- In case, income so determined is in excess of the income as shown in the accounts of the undertaking, such excess shall be deemed to be applied for the purposes other than charitable or religious purposes.

Notes regarding application of income

- Application of amount may be of revenue or capital nature.
- Application for charitable or religious purposes, from corpus or any loan or borrowing, shall not be treated as application of income for charitable or religious purposes.

  However, if trust or institution invest or deposits back the amount into corpus or repays the loan within 5 years of application from the corpus or loan, then such investment or depositing back into corpus or repayment of loan will be allowed as application.

  Further, following conditions should be fulfilled at the time of initial utilisation of corpus or loan:
  - It should not be in the form of corpus donation to other trust
  - Carry forward and set off of excess application is not allowed
  - It is allowed in the year in which it was actually paid
  - It has not been made for the benefit of any person referred to in sec. 13(1)
  - It should be in India except with the approval of the Board.
  - TDS, if any, has been deducted
  - It should not disallowed u/s 40A(3)
- Loan granted to poor person for education or medical treatment shall be treated as application of income. However, when such loan is repaid, it shall be treated as income of the trust.
- The calculation of income required to be applied or accumulated during the previous year shall be made without any set off or deduction or allowance of any excess application of any of the year preceding the previous year.
- Where any income is required to be applied or accumulated or set apart for application, then, for such purposes the income shall be determined without any deduction or allowance by way of depreciation or otherwise in respect of any asset, acquisition of which has been claimed as an application of income in the same or any other previous year

Illustration 26.

Compute taxable income of a charitable trust for the A.Y 2024-25 under the following cases:

Particulars	Case 1	Case 2	Case 3
Income other than voluntary contribution	4,00,000	5,00,000	15,00,000
Voluntary contribution	1,00,000	80,000	2,00,000
Voluntary contribution in the corpus of the trust	2,00,000	1,50,000	5,00,000
Income applied for the purpose for which trust is created	4,50,000	4,93,000	2,00,000

Solution:

Computation of taxable income of the charitable trust for the A.Y 2024-25

Particulars	Amount		
	Case 1	Case 2	Case 3
Income other than voluntary contribution	4,00,000	5,00,000	15,00,000
Add: Voluntary contribution	1,00,000	80,000	2,00,000
Total income of the trust	5,00,000	5,80,000	17,00,000
Less: 15% Free accumulation	(75,000)	(87,000)	(2,55,000)
Balance	4,25,000	4,93,000	14,45,000
Less: Income exempted to the extent applied for the purpose	4,25,000	4,93,000	2,00,000
Total Income	**Nil**	**Nil**	**12,45,000**
Note: Contribution in corpus of the trust shall not be treated as income of the trust.			

Deferment of application of income [Explanation to Sec. 11(1)]

When due to certain reasons application of income is below 85% of its income, trust has the option to apply for deferment of application of income.

Time limit for application of deferment of income: such option to be exercised at least 2 months prior to the expiry of the due date for furnishing the return of income specified u/s 139(1), in prescribed form and manner.

Reasons, Deferment Period and effect of non application of income within the deferred period:

Reasons	Deferred period	Effect when income is not applied within the deferred period
The whole or any part of income has not been received during that year.	The previous year in which such income is actually received and the previous year subsequent to such year.	It shall be treated as income of the year following the previous year in which such income is actually received. **Note:** The part of income, which is not spent, shall be taxable.
Any other reason	Subsequent to the previous year in which such income is derived.	It shall be treated as income of the year following the previous year in which such income is derived

Illustration 27.

Bangur Charitable Trust has earned income of ₹ 70 lacs during the previous year 2023-24. It has applied the income of ₹ 15 lacs, during the previous year 2023-24 and also applied for deferment of application of income of -

Case 1) ₹ 32 lacs

Case 2) ₹ 45 lacs

- as such income has not yet been received by the trust.

During the previous year 2025-26 such income is received and applied as under -

Previous Year	Amount applied for charitable purposes	
	Case 1	Case 2
2025-26	₹ 12 lacs	₹ 15 lacs
2026-27	₹ 11 lacs	₹ 10 lacs
2027-28	₹ 9 lacs	₹ 20 lacs

Compute taxable income of the A.Y. 2024-25 and 2027-28

Solution:

Computation of income of Bangur Charitable Trust for the A.Y.2024-25

Particulars	Amount	
	Case 1	Case 2
Income earned	70 lacs	70 lacs
Less: Free accumulation of income @ 15%	10.5 lacs	10.5lacs
Balance	59.5 lacs	59.5 lacs
Less: Application of income during the previous year	15 lacs	15 lacs
	44.5 lacs	44.5 lacs
Less: Amount for which deferment is allowed [Max. of taxable income before deferment]	32 lacs	44.5 lacs
Taxable income	**12.5 lacs**	**Nil**

Computation of income of Bangur Charitable Trust for the A.Y.2027-28

Particulars	Amount	
	Case I	Case II
Amount deferred in the P.Y. 2023-24 and are to be applied till P.Y. 2026-27 i.e. one year after the year in which such income is received	32	44.5
Less: Amount applied before 31/3/2027	23	25
Taxable income	**9**	**19.5**

Conditional Accumulation [Sec. 11(2)]

Where a trust could not apply its 85% of income for charitable or religious purpose(s), then it may accumulate or set aside its income (in full or in part) for a maximum period of 5 years to be applied for specific purposes. In such case subject to the following conditions income so accumulated shall not be included in total income of the trust:

Conditions

- **Statement to the Assessing Officer:** Such person furnishes a statement in the prescribed form (Form 10) and in the prescribed manner to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is to be accumulated or set apart, which shall in no case exceed 5 years.
  - In computing the period of 5 years, the period during which the income could not be applied for the purpose for which it is so accumulated or set apart, due to an order or injunction of any court, shall be excluded.
- **Time-limit**: The statement shall be furnished 2 months prior to the due date of furnishing return as specified u/s 139(1).
- **Return of income**: The return of income for the previous year is required to be furnished by such person on or before the due date specified u/s 139(1) for furnishing the return of income for the said previous year.
- **Investment of accumulated income:** The money so accumulated or set apart is invested or deposited in the forms or modes specified in the following mode being stated in sec.11(5):

(a) Investment in Government Savings Certificates and any other securities or certificates issued by the Central Government under the Small Savings Schemes of that Government.

(b) Deposit in any account with the Post Office Savings Bank;

(c) Deposit in any account with a scheduled bank or a co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank);

(d) Investment in units of the Unit Trust of India;

(e) Investment in the Central Government or a State Government securities;

(f) Investment in debentures issued by any company or corporation, both the principal whereof and the interest whereon are fully and unconditionally guaranteed by the Central Government or by a State Government;

(g) Investment or deposit in any public sector company;

(h) Deposits with or investment in any bonds issued by a financial corporation which is engaged in providing long-term finance for industrial development in India and which is eligible for deduction u/s 36(1)(viii);

(i) Deposits with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes and which is eligible for deduction u/s 36(1)(viii);

(j) Deposits with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for urban infrastructure in India;

(k) Investment in an immovable property. Immovable property does not include any machinery or plant (other than machinery or plant installed in a building for the convenient occupation of the building) even though attached to or permanently fastened to earth;

(l) Deposits with the Industrial Development Bank of India;

(m) Invest in any other form or mode of investment or deposit as may be prescribed e.g. Investment by way of acquiring equity shares of a depository, Units of Mutual Fund, etc.

Application to Assessing Officer for applying the income for the purpose other than the purpose for which it was accumulated [Sec. 11(3A)]

In case where due to circumstances beyond the control of the trust, accumulated income cannot be applied for the purpose for which it was accumulated or set apart, the trust can apply to Assessing Officer to apply such income for other charitable or religious purpose in India in conformity with the objects of the trust. Assessing Officer may, on receipt of such application, allow use of such accumulated income for the purpose(s) as specified in the application.

Withdrawal of benefit of accumulation of income [Sec. 11(3)]

Cases	Tax treatment
When income so set aside is applied for the purpose other than specified purpose	Such income shall be deemed to be the taxable income of the previous year in which it is so applied.
When income so set aside, ceases to be accumulated	Such income shall be deemed to be the taxable income of the previous year in which it so ceases to be accumulated
When income so set aside, ceases to remain so invested or deposited in mode mentioned in Sec. 11(5)	Such income shall be deemed to be the taxable income of the previous year in which it so ceases to be so invested.
When such income is not utilized for the purpose for which it is so accumulated or set apart during the period allowable for accumulation	Such income shall be deemed to be the income of such person of the previous year in which such period expires
When income so set aside is credited or paid to – ➢ any registered trust/institution; or ➢ to any fund, institution, trust, any university, other educational institution, any hospital or other medical institution referred to in Sec.10(23C) (iv), (v), (vi) or (via)	Such income shall be deemed to be the taxable income of the previous year in which it is so credited or paid.

Taxpoint: In case the trust or institution, which has accumulated its income, is dissolved, the Assessing Officer may allow application of such income in payment to another registered trust or institution u/s 10(23C)(iv), (v), (vi), (via) in the year in which such trust or institution was dissolved.

Tax Treatment of Capital Gains on transfer of Capital Assets

Capital gain arises on transfer of 'property held under trust for charitable purpose' shall be eligible for exemption if the consideration or part thereof is applied in acquisition of new property. Such amount applied in acquiring the new capital assets shall be held as part of the corpus of the trust. Exemption shall be as per the following table:

Property transferred	Amount to be applied	Exemption
Capital asset being property held under trust for charitable purpose.	The net sale consideration.	Entire Capital gain
	Only a part of the net sale consideration	[(Amount so utilised) – (the cost of acquisition and cost of improvement of the transferred asset)]
Capital asset, being property held under trust in part only for such purposes	The net sale consideration	The proportionate amount of the capital gain.
	Only a part of the net sale consideration	Proportionate amount of - [(Amount so utilised) – (the cost of the transferred asset)]
Notes: Proportionate amount is calculated having regard to the proportion, which the amount of income applicable to charitable purpose bears to the whole of income from such property.		

Registration of Trust [Sec.12A & 12AB]

The person in receipt of the income has made an application in the prescribed form and manner to the Principal Commissioner or Commissioner, for registration of the trust or institution u/s 12AB:

S.No.	Case	Time limit
i	Where the trust or institution is registered u/s 12AB and the period of the said registration is due to expire	At least 6 months prior to expiry of the said period
ii	Where the trust or institution has been provisionally registered	At least 6 months prior to expiry of period of the provisional registration or within 6 months of commencement of its activities, whichever is earlier
iii	Where registration of the trust or institution has become inoperative due to sec. 11(7)	At least 6 months prior to the commencement of the assessment year from which the said registration is sought to be made operative
iv	Where the trust or institution has adopted or undertaken modifications of the objects which do not conform to the conditions of registration	Within a period of 30 days from the date of the said adoption or modification
v	In any other case	
	- Where activities of the trust or institution have not commenced	At least 1 month prior to the commencement of the previous year relevant to the assessment year from which the said registration is sought.
	- Where activities of the trust or institution have commenced and no income or part thereof of the said trust or institution has been excluded from the total income on account of applicability of 10(23C)(iv) or (v) or (vi) or (via), or sec. 11 or sec. 12, for any previous year ending on or before the date of such application	At any time after the commencement of such activities

Procedure for Registration [Sec.12AB]

On receipt of an application u/s 12A, the Principal Commissioner or Commissioner shall:

Cases covered in S. No. i to iv of the above table	a. call for such documents or information from the trust or institution or make such inquiries as he thinks necessary in order to satisfy himself about: A. the genuineness of activities of the trust or institution; and B. the compliance of such requirements of any other law for the time being in force by the trust or institution as are material for the purpose of achieving its objects; b. after satisfying himself about the objects of the trust or institution and the genuineness of its activities and compliance of the requirements: A. pass an order, within 6 months from the end of the month in which the application was received, in writing registering the trust or institution for a period of 5 years; or B. if he is not so satisfied, pass an order in writing rejecting such application and also cancelling its registration after affording a reasonable opportunity of being heard; and send a copy of such order to the trust or institution.

Cases covered in S. No. v of the above table	Pass an order, within 1 month from the end of the month in which the application was received, in writing provisionally registering the trust or institution for a period of 3 years from the assessment year from which the registration is sought, and send a copy of such order to the trust or institution.

Taxpoint: A refusal-order shall not be passed unless the applicant has been given a reasonable opportunity of being heard.

Cancellation of Registration

Where registration or provisional registration of a trust or an institution has been granted and subsequently,:

a. the Principal Commissioner or Commissioner has noticed occurrence of one or more specified violations during any previous year; or

- "specified violation" means:

a. where any income derived from property held under trust, wholly or in part for charitable or religious purposes, has been applied, other than for the objects of the trust or institution; or

b. the trust or institution has income from profits and gains of business which is not incidental to the attainment of its objectives or separate books of account are not maintained by such trust or institution in respect of the business which is incidental to the attainment of its objectives; or

c. the trust or institution has applied any part of its income from the property held under a trust for private religious purposes, which does not enure for the benefit of the public; or

d. the trust or institution established for charitable purpose created or established after the commencement of this Act, has applied any part of its income for the benefit of any particular religious community or caste; or

e. any activity being carried out by the trust or institution—

   i. is not genuine; or

   ii. is not being carried out in accordance with all or any of the conditions subject to which it was registered; or

f. the trust or institution has not complied with the requirement of any other applicable law and the order, direction or decree, by whatever name called, holding that such non-compliance has occurred, has either not been disputed or has attained finality.

g. the application for registration or approval is not complete or it contains false or incorrect information.

b. the Principal Commissioner or Commissioner has received a reference from the Assessing Officer under the second proviso to sec. 143(3) for any previous year; or

c. such case has been selected in accordance with the risk management strategy, formulated by the Board from time to time, for any previous year,

the Principal Commissioner or Commissioner shall—

i. call for such documents or information from the trust or institution, or make such inquiry as he thinks necessary in order to satisfy himself about the occurrence or otherwise of any specified violation;

ii. pass an order in writing, cancelling the registration of such trust or institution, after affording a reasonable opportunity of being heard, for such previous year and all subsequent previous years, if he is satisfied that one or more specified violations have taken place;

iii. pass an order in writing, refusing to cancel the registration of such trust or institution, if he is not satisfied about the occurrence of one or more specified violations;

iv. forward a copy of the order to the Assessing Officer and such trust or institution.

Time limit for passing such order: The order shall be passed before the expiry of a period of 6 months, calculated from the end of the quarter in which the first notice is issued by the Principal Commissioner or Commissioner calling for any document or information, or for making any inquiry.

Forfeiture of Exemption [Sec.13]

Nothing contained in section 11 [or section 12] shall operate in respect of —

- **Income for private purposes**: Any part of the income from the property held under a trust for private religious purposes, which does not ensure for the benefit of the public.
- **Income for the benefit of particular religious community**: in the case of a trust for charitable purposes or a charitable institution created or established after the commencement of this Act, any income thereof if the trust or institution is created or established for the benefit of any particular religious community or caste.
- **Funds are invested** in securities/deposits which is **not** specified u/s 11(5), then income to the extent of such investment shall be taxable. It is to be noted that holding shares in a public sector company would not disqualify the trust from claiming exemption.
- **Income applied for the benefit of Interested person**: In the case of a trust for charitable or religious purposes, any income thereof:
  - if such trust or institution has been created or established after the commencement of this Act and under the terms of the trust, any part of such income ensures, directly or indirectly for the benefit of interested person[#]
  - if any part of such income or any property of the trust or the institution (whenever created or established) is during the previous year used or applied, directly or indirectly for the benefit of any interested person[#].
  - Such part of the income is not exempted.

Note: The above provision shall not apply to a trust or institution created or established before the commencement of this Act, to any use or application, whether directly or indirectly, of any part of such income or any property of the trust or institution for the benefit of any Interested person, if such use or application is by way of compliance with a mandatory term of the trust or a mandatory rule governing the institution

[#] Income applied for the benefit of interested persons

Interested person: Following are the interested persons -

- **Author:** The author of the trust or the founder of the institution.
- **Contributory:** Any person whose total contribution up to the end of the relevant previous year to the trust/ institution exceeds ₹ 50,000.
- **Trustee:** Any trustee of the trust or manager (by whatever name called) of the institution.
- **Relatives of Author / Contributory / Trustee:** Any relative of any such author, founder, person, member, trustee or manager as aforesaid.

Note: Where an HUF is the author, founder or any member of such HUF.

- **Other:** Any concern in which any of the above-referred person has a substantial interest.

Income applied for the benefit of interested persons: Income or the property of the trust or any part of such income or property shall be deemed to have been used or applied for the benefit of a person –

(a) If any part of the income or property of the trust or institution is lent to any interested person for any period during the previous year without either adequate security or adequate interest or both;

(b) If any land, building or other property of the trust or institution is made available for the use of any interested person, for any period during the previous year without charging adequate rent or other compensation;

(c) If any amount is paid by way of salary, allowance or otherwise during the previous year to any interested person and the amount so paid is in excess of what may be reasonably paid for such services;

(d) If the services of the trust or institution are made available to any interested person during the previous year without adequate remuneration or other compensation;

(e) If any share, security or other property is purchased by or on behalf of the trust or institution from any interested person during the previous year for consideration which is more than adequate;

(f) If any share, security or other property is sold by or on behalf of the trust or institution to any interested person during the previous year for consideration which is less than adequate;

(g) If any income or property of the trust or institution is diverted during the previous year in favour of any interested person.

Computation of income in case of certain violation [Sec. 13(10) / (11)

Where

i. The trust is carrying on any activity in the nature of trade, commerce or business (for which exemption is not available u/s 11 or 12); or

ii. The trust is not maintaining books of account; or

iii. The trust has not obtained the audit report; or

iv. The trust has not filed its return of income within the time allowed u/s 139(4A)

- its income chargeable to tax shall be computed after allowing deduction for the expenditure (other than capital expenditure) incurred in India, for the objects of the trust or institution, subject to fulfilment of the following conditions:

a. such expenditure is not from the corpus standing to the credit of the trust or institution as on the end of the financial year immediately preceding the previous year relevant to the assessment year for which income is being computed;

b. such expenditure is not from any loan or borrowing;

c. claim of depreciation is not in respect of an asset, acquisition of which has been claimed as application of income, in the same or any other previous year; and

d. such expenditure is not in the form of any contribution or donation to any person.

Taxpoint:

- The provisions of sec. 40(a)(ia) and sec. 40A(3) / (3A), shall apply as they apply in computing the income chargeable under the head "Profits and gains of business or profession".
- For the purposes of computing income chargeable to tax, no deduction in respect of any expenditure or allowance or set-off of any loss shall be allowed to the assessee under any other provision of this Act.

Tax on specified income of certain institutions [Sec. 115BBI]

Where the total income of an assessee, being a person in receipt of income on behalf of any fund or institution or trust or university or other educational institution or any hospital or other medical institution referred to in sec. 10(23C)(iv) / (v) / (vi) / (via) or any trust or institution referred to in sec. 11, includes any income by way of any specified income, the income-tax payable shall be the aggregate of:

Nature of Income	Rate of tax
Specified income	30%
Other income	Regular rate i.e. slab rate

Taxpoint:

- No deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee under any provision of this Act in computing the specified income.
- "Specified income" means:
  a. income accumulated or set apart in excess of 15% of the income where such accumulation is not allowed under any specific provision of this Act; or
  b. deemed income referred to in Explanation 4 to the third proviso to sec. 10(23C) or sec. 11(1B) / (3) [i.e., default relating to accumulation of income]; or
  c. any income, which is not exempt u/s 10(23C) on account of violation of the provisions of clause (b) of the third proviso of clause (23C) of section 10, or not to be excluded from the total income u/s 13(1)(d) [i.e., investment of fund in non-specified modes]; or
  d. any income which is deemed to be income under the twenty-first proviso to sec. 10(23C) or which is not excluded from the total income u/s 13(1)(c) [i.e., misutilisation of funds for the benefit of specified persons]; or
  e. any income which is not excluded from the total income u/s 11(1)(c) [i.e., income applied outside India].

Tax on accreted income [Sec. 115TD] i.e. Exit Plan for the Charitable Trust

- Where in any previous year, a specified person has:
  a. converted into any form which is not eligible for grant of registration u/s 12AA or 12AB, or approval u/s 10(23C)(iv) or (v) or (vi) or (via);
  b. merged with any entity other than an entity which is a trust or institution having objects similar to it and registered u/s 12AA or 12AB or approved u/s 10(23C)(iv) or (v) or (vi) or (via); or

c. failed to transfer upon dissolution all its assets to any other specified person within a period of 12 months from the end of the month in which the dissolution takes place,

then, the accreted income of the specified person as on the specified date shall be charged to tax at the maximum marginal rate (MMR) [herein referred to as tax on accreted income]

Taxpoint

- Such tax is in addition to the income-tax chargeable in respect of the total income of such specified person.
- Specified date means the date of conversion or the date of merger or the date of dissolution, as the case may be.
- Specified person means:

  a. any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in sec. 10(23C)(iv) or (v) or (vi) or (via); or

  b. a trust or institution registered u/s 12AA or section 12AB;

- The accreted income means the amount by which the aggregate fair market value of the total assets of the specified person, as on the specified date, exceeds the total liability of such specified person, computed in accordance with the prescribed method of valuation.
  - Accreted income = Aggregate fair market value of the total assets - Total liability
  - However, so much of the accreted income as is attributable to the following asset and liability, if any, related to such asset, shall be ignored:

    i. any asset which is established to have been directly acquired by the specified person out of its income of the nature referred to in sec. 10(1);

    ii. any asset acquired by the specified person during the period beginning from the date of its creation or establishment and ending on the date from which the registration u/s 12AA or section 12AB or approval u/s 10(23C) became effective, if the specified person has not been allowed any benefit of sec. 11 and 12 or sec. 10(23C(iv) or (v) or (vi) or (via) during the said period

  - Where due to specified reasons, the exemption have been allowed to the specified person in respect of any previous year(s) prior to the date from which the registration or approval is effective, then, the registration or approval shall be deemed to have become effective from the first day of the earliest previous year.
  - While computing the accreted income in a case of dissolution, assets and liabilities, if any, related to such asset, which has been transferred to any other specified person within the specified period, shall be ignored.
- A specified person shall be deemed to have been converted into any form not eligible for registration u/s 12AA or 12AB or approval u/s 10(23C)(iv) or (v) or (vi) or (via) in a previous year, if:

  i. The registration or approval granted to it has been cancelled; or

  ii. It has adopted or undertaken modification of its objects which do not conform to the conditions of registration and it:

    a. has not applied for fresh registration or approval in the said previous year; or

    b. has applied for fresh registration or approval but the said application has been rejected.

iii. it fails to make an application in accordance with the provisions of sec. 10(23C) or 12A, within the period specified in respective provision, which expires in the said previous year

Taxpoint

- Date of conversion means:
  a. the date of the order cancelling the registration or approval; or
  b. the date of adoption or modification of any object.

- Notwithstanding that no income-tax is payable by a specified person on its total income computed in accordance with the provisions of this Act, the tax on the accreted income shall be payable by such specified person.

- The principal officer or the trustee of the specified person, as the case may be, and the specified person shall also be liable to pay the tax on accreted income to the credit of the Central Government within 14 days from:

Case	14 days from
When registration or approval is cancelled	a. the period for filing appeal u/s 253 against the order cancelling the registration expires and no appeal has been filed by the specified person; or b. the order in any appeal, confirming the cancellation of the registration, is received by the specified person.
Where it has adopted or undertaken modification of its objects which do not conform to the conditions of registration and	
➢ It has not applied for fresh registration or approval in the said previous year	The end of the relevant previous year
➢ It has applied for fresh registration or approval but the said application has been rejected	a. the period for filing appeal u/s 253 against the order cancelling the registration expires and no appeal has been filed by the specified person; or b. the order in any appeal, confirming the cancellation of the registration, is received by the specified person.
When it merged	Date of merger
When it is dissolved	The date on which the said period of 12 months expires

- The tax on the accreted income by the specified person shall be treated as the final payment of tax in respect of the said income and no further credit therefor shall be claimed by the specified person or by any other person in respect of the amount of tax so paid

- No deduction under any other provision of this Act shall be allowed to the specified person or any other person in respect of accreted income.

Interest payable for non-payment of tax by specified person [Sec. 115TE]

Where the principal officer or the trustee of the specified person and the specified person fails to pay the whole or any part of the tax on the accreted income, within the time allowed, he or it shall be liable to pay simple interest @ 1% for every month (or part thereof) on such tax for the period beginning on the date immediately after the last date on which such tax was payable and ending with the date on which the tax is actually paid.

When specified person is deemed to be assessee in default [Sec. 115TF]

- If any principal officer or the trustee of the specified person and the specified person does not pay tax on accreted income, then, he or it shall be deemed to be an assessee in default and all provisions for the collection and recovery shall apply.
- However, in a case where the tax on accreted income is payable due to dissolution, the person to whom any asset forming part of the computation of accreted income has been transferred, shall be deemed to be an assessee in default in respect of such tax and interest thereon and all provisions for the collection and recovery shall apply.
- The liability of such person shall be limited to the extent to which the asset received by him is capable of meeting the liability.

Mutual Association

1.4

- No one can trade with himself or make income out of himself
- A mutual association arises where persons forming a group associate together with a common object and contribute monies for achieving that object and divide the surplus amongst themselves. The cardinal requirement in the case of mutual association is that all the contributors to the fund must be entitled to participate in the surplus and *vice versa*.
- The participation in the surplus need not be immediate but it may assume the shape of a reduction in the future contribution or a division of surplus on dissolution. Further, it is not necessary that the surplus should be returned to every member in pro-rata basis.
- It does not make any difference whether the persons joining together form an association or incorporate a company.
- Where there is mutuality, the fact that some members alone take advantage of the mutual enterprise would not affect the character of mutual association.
- A mutual association may carry on non-mutual activity, but exemption is available only to the surplus arising out of mutual activity.
- However, the Act provides for assessment of income (from mutual activity) of mutual concern in the following cases:
  - Where the mutual concern is a mutual insurance society and the income is derived from the carrying on of any business of insurance [Sec. 44 read with sec. 2(24)(vii)]
  - Where the mutual concern is a trade, professional or similar association and the income is derived from specific service performed for its member [Sec. 28(iii) read with sec. 44A]
- Specific service to its member means some tangible benefits which would not available to them unless they pay the specific fees charged for such special benefits [CIT -vs.- Calcutta Stock Exchange Association Ltd. (SC)] Hence, entrance fees is not for specific service, it is not taxable u/s 28(iii).
  - To some extent, co-operative bank [Deduction u/s 80P]

However, it is to be noted that income derived from non-mutual activity is taxable.

Trade and professional association [Sec. 44A]

A *trade association* is an association of tradesmen, businessmen or manufacturers for the protection and advancement of their common interest. It is different from *trading association* [*CIT vs Royal Western India Turf Club Ltd. (SC)*]

Where income from a particular source is not chargeable to tax, a loss from such source cannot be set off against income chargeable to tax. Sec. 44A provides an exception to this general rule which is as follow:

- Where the amount received during a previous year by any trade, professional or similar association [other than an association or institution referred in sec. 10(23A)] from its members, whether by way of subscription or otherwise (not being remuneration received for rendering any specific services to such members) falls short of the expenditure incurred by such association during that previous year (not being expenditure deductible in computing the income under any other provision of this Act and not being in the nature of capital expenditure) solely for the purposes of protection or advancement of the common interests of its members, the amount so fallen short (hereinafter referred to as deficiency) shall be allowed as a deduction in computing the income of the association assessable for the relevant assessment year under the head "Profits and gains of business or profession" and if there is no income assessable under that head or the deficiency allowable exceeds such income, the whole or the balance of the deficiency, as the case may be, shall be allowed as a deduction in computing the income of the association assessable for the relevant assessment year under any other head.
  - Sec. 44A is exception of the rule that loss of un-assessable business cannot be adjusted with assessed income.
- In computing the income of the association for the relevant assessment year effect shall first be given to any other provision of this Act under which any allowance or loss in respect of any earlier assessment year is carried forward and set off against the income for the relevant assessment year.
- The amount of deficiency to be allowed as a deduction under this section shall in no case exceed ½ of the total income of the association as computed before making any allowance under this section.
- This section applies only to that trade, professional or similar association the income of which or any part thereof is not distributed to its members except as grants to any association or institution affiliated to it.

Illustration 28.

A is an association governed by the provisions of sec. 44A of the Income-tax Act. The subscription receipts for the year ended 31st March, 2024 were ₹ 60,000. The expenditure in the normal course of its activities was ₹ 85,000. Its other income taxable under the Act works out to ₹ 75,000. On these facts, you are consulted as to:

a. How A's taxable income will be determined for assessment year 2024-25.

b. In case the association did not have the other taxable income, will there be any difference in the computation of its income?

Solution:

Computation of total income

Particulars	Amount (₹)
Other Income	75,000
Less: Deficiency (Note 1)	25,000
Total Income	**50,000**

Note 1: Calculation of deficiency

Particulars	Amount (₹)
Subscription received	60,000
Less: Expenditure	85,000
Deficiency	**25,000**
Maximum deficiency can be set off against other income is lower of the following: a. Actual Deficiency i.e. ₹ 25,000 b. 50% of other income i.e., ₹ 37,500 being 50% of ₹ 75,000	

In case, association do not have any other taxable income, then the total income shall be nil and the deficiency of ₹ 25,000 shall not be carried forward.

Income of professional institutions [Sec. 10(23A)]

Any income (other than income chargeable under the head "Income from house property" or any income received for rendering any specific services or income by way of interest or dividends derived from its investments) of professional association shall be exempt provided -

a. Such association or institution is established in India having as its object the control, supervision, regulation or encouragement of the profession of law, medicine, accountancy, engineering or architecture or other specified profession;

b. Such association or institution applies its income, or accumulates it for application, solely to the objects for which it is established; and

c. The association or institution is approved by the Central Government.

Clubs

Social clubs are not trade association hence sec. 28(iii) is not applicable on it. It would be governed by general principle of mutuality. Excess over expenditure received by club from the facilities extended to members as part of advantages attached to such membership shall not be chargeable to tax on the principle of mutuality. [*CIT -vs.- Bankipur Club Ltd. (SC)*] However, it is to be noted that income derived from non-mutual activity is taxable.

Insurance Business

The profits and gains of any business of insurance, including any such business carried on by a mutual insurance company or by a co-operative society, shall be computed in accordance with the rules contained in the First Schedule of the Income Tax Act, 1961 [Sec. 44]

A. Life Insurance Business

- In the case of a person who carries on or at any time in the previous year carried on life insurance business, the profits and gains of such person from that business shall be computed separately from his profits and gains from any other business.
- The profits and gains of life insurance business shall be taken to be the annual average of the surplus arrived at by adjusting the surplus or deficit disclosed by the acturial valuation made in accordance with the Insurance Act, 1938.

- Tax on profits and gains of life insurance business [Sec. 115B]

  Where the total income of an assessee includes any profits and gains from life insurance business, the income-tax payable shall be the aggregate of:

  i. the amount of income-tax calculated on the amount of profits and gains of the life insurance business included in the total income @ 12.5%; and

  ii. the amount of income-tax with which the assessee would have been chargeable had the total income of the assessee been reduced by the amount of profits and gains of the life insurance business.

- The provision of sec. 115JB (i.e., MAT provisions) shall not apply to any income accruing or arising to a company from life insurance business.

B. Other insurance business

The profits and gains of any business of insurance other than life insurance shall be taken to be the balance of the profits disclosed by the annual accounts, copies of which are required under the Insurance Act, 1938, to be furnished to the Controller of Insurance, subject to the following adjustments:

- Any expenditure or allowance disallowed u/s 30 to 43B

  Taxpoint: Any sum payable by the assessee u/s 43B, which is added back, shall be allowed as deduction in computing the income in the previous year in which such sum is actually paid]

- Any gain or loss on realisation of investments shall be added or deducted, as the case may be, if such gain or loss is not credited or debited to the profit and loss account;

- Any provision for diminution in the value of investment debited to the profit and loss account, shall be added back

- Amount carried over to a reserve for unexpired risks shall be allowed as a deduction. As per rule 6E, any business of insurance other than life insurance, the amount carried over to a reserve for unexpired risks (including any amount carried over to any additional reserve) shall not exceed:

Nature of insurance	Ceiling
Fire insurance or engineering insurance and which provides insurance for terrorism risks	100% of the net premium income of such business of the previous year
Fire insurance or miscellaneous insurance other than above	50% of the net premium income of such business of the previous year
Marine insurance	100% of the net premium income of such business of the previous year.

  - Net premium income means the amount of premium received as reduced by the amount of reinsurance premium paid during the relevant previous year.
  - Marine insurance includes the Export Credit Insurance.

C. Non-resident Person carrying of insurance business

The profits and gains of the branches in India of a person not resident in India and carrying on any business of insurance shall be calculated on the basis of reliable data available in respect of such activity. However, in the absence of reliable data, profit may be deemed to be that proportion of the world income of such person, which corresponds to the proportion, which his premium income derived from India bears to his total premium income.

Assessment of Private Trust

Where beneficiaries share is known

Income includes business income, then taxable @ Maximum Marginal Rate of tax (MMR) [Sec. 161(1A)]

Exception

If following conditions are satisfied then taxable @ applicable to the total income of each beneficiary

a) The trust is declared by will;

b) Such trust is exclusively for the benefit of any relative dependent on him for support and maintenance; and

c) Such trust is the only trust declared by him

Income does not include business income or include business income but fall in exception, then beneficiary's share is separately taxable in the hands of trustee or beneficiary *(u/s 166)* @ applicable to the total income of each beneficiary [Sec. 161(1)]

Oral Trust

Taxable @ MMR [Sec. 164A]

Oral trust means a trust which is not declared by a duly executed instrument in writing [including any wakf deed] and which is not deemed to be a trust declared by a duly executed instrument in writing

However, following oral trust is not treated as oral trust:

A trust which is not declared by a duly executed instrument in writing [including wakf deed] shall be deemed to be a trust declared by a duly executed instrument in writing if a statement in writing, signed by trustees, setting out the purpose or purposes of the trust, particulars as to the trustees, the beneficiaries and the trust property, is forwarded to the AO:

(i) where the trust has been declared before 1-6-1981, within 3 months from 1-6-81;

(ii) in any other case, within 3 months from the date of such declaration.

i.e., share is unknown then @ MMR & share is known then @ applicable to beneficiaries.

Where beneficiaries share is unknown

Income does not include business income and fall in following cases, then @ AOP (i.e., individual rate)

a) None of the beneficiaries has income exceeding the max. amount not chargeable to tax in the case of an AOP nor is a beneficiary under any other trust; or

b) Income is receivable under a trust declared by any person by will and such trust is the only trust so declared by him; or

c) Income is receivable under a trust created before 1-3-1970 by a non-testame-ntary instrument & the AO is satisfied that the trust was created *bona fide* exclusively for the benefit of the relatives of settlor, or where settlor is a HUF, exclusively for the benefit of members of family, in circumstances where such relatives or members were mainly dependant on settlor for support and maintenance; or

d) the trustee receives income for provident fund, superannuation fund, etc. created *bona fide* by a person carrying on a business (or profession) exclusively for the benefit of persons employed in such business.

Assessee falling under these cases (*see left*) and having business income and satisfying following condition then taxable @ AOP

a) The trust is declared by will;

b) Such trust is exclusively for the benefit of any relative dependent on him for support and maintenance; and

c) Such trust is the only trust declared by him

In any other case having business income or not @MMR [Sec. 164(1)]

Solved Case :

Mamta, widow of Shri Kulkarni, supplies the following details for the P.Y. 2023-24:

a. She has two house properties. 2nd is self occupied and 1st is let-out for ₹ 10,000 p.m. Municipal tax paid for 2nd house ₹ 5,000 and that for 1st house ₹ 3,000. Interest on loan for 1st house is ₹ 22,000.

b. She is working with A Ltd. on following terms:

Basic Salary	₹ 5,000 p.m.
Bonus	₹ 40,000
D.A.	₹ 2,000 p.m.
HRA	₹ 3,000 p.m. (she resides in Kolkata)

Car of 1.4 ltr is provided for office as well as personal purpose.

c. She received interest on her fixed deposit ₹ 5,000. Interest on Saving Bank Account ₹ 6,000. Interest on deposits in a public Ltd. company ₹ 5,000.

d. She made a mediclaim policy of her dependent mother aged 62 years and paid a premium of ₹ 5,000.

e. She donated to Rajiv Gandhi Memorial Fund ₹ 10,000

f. Her handicapped brother is fully dependent on her.

g. She paid LIC premium ₹ 8,000 and made repayment of housing loan taken for acquisition of second house ₹43,000 (including ₹ 22,000 interest).

h. During the previous year, she sold 200 debenture of X Ltd. on behalf of her minor son for ₹ 1,00,000. She acquired such debenture on 1-4-2004 for ₹ 50,000 and gifted the same to her minor child on 1-4-2013.

i. She paid tuition fees for her –

- Elder son (Mumbai University) ₹ 10,000.
- Younger son (Melbourne University, Australia) ₹ 25,000

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be value of taxable perquisites?
2. What will be her taxable salary?
3. What will be her taxable income under the head income from house property?
4. What will be taxable capital gain?
5. What will be her taxable income under the head income from other sources?
6. State the amount of deduction under chapter VIA.

Solution:

Computation of total income of Mamta for A.Y.2024-25

Particulars	Details	Amount	Amount
Salaries			
Basic		60,000	
Bonus		50,000	
Allowances			
Dearness Allowance	24,000		
House Rent Allowance (as she resides in her own house)	36,000	60,000	
Perquisite u/s 17(2)			
Car facility [₹ 1,800 × 12]		21,600	
		1,91,600	
Less: Standard Deduction u/s 16(ia)		50,000	1,41,600
Income from house property			
HP 1: Let out [Sec. 23(1)]			
Gross Annual Value (being rent received)	1,20,000		
Less: Municipal Tax	3,000		
Net Annual Value	1,17,000		
Less: Deduction u/s			
24(a) Standard Deduction	35,100		
24(b) Interest on loan	22,000	59,900	
HP 2: Self occupied [Sec. 23(2)(a)]			
Net Annual Value	Nil		
Less: Deduction u/s 24(b) Interest on loan	22,000	(–) 22,000	37,900
Capital gains			
Long term capital gain of minor son [Clubbed u/s 64(1A)]			
Sale consideration		1,00,000	
Less: Cost of acquisition (Indexation benefit is not available on debenture)		50,000	
		50,000	
Less: Exemption u/s 10(32)		1,500	48,500
Income from other sources			
Interest on Fixed Deposit		5,000	
Interest on Saving Bank Account		6,000	
Interest on deposits in a public limited company		5,000	16,000
Gross Total Income			**2,44,000**

Particulars	Details	Amount	Amount
Less: Deduction u/s			
80C#		39,000	
80D (Mediclaim insurance premium paid)		5,000	
80DD (Assessee has handicapped dependent relative)		75,000	
80G (50% of donation to Rajiv Gandhi Memorial Fund)		5,000	
80TTA (Interest on Saving Bank Account)		6,000	1,30,000
Total Income			**1,14,000**
Tax on above			**Nil**

 # Deduction u/s 80C

Particulars	Amount
Insurance premium	8,000
Tuition fees (Burdwan University)	10,000
Housing loan repayment (Maximum)	21,000
Total	**39,000**

Exercise

Multiple Choice Questions

1. As per section 115JB, every taxpayer being a company is liable to pay MAT, if the Income tax payable on the total income, computed as per the provisions of the Income-tax Act in respect of any year is less than _____
   a. 15.50%
   b. 18.00%
   c. **15.00%**
   d. 20.00%
2. MAT shall not apply to any income accruing or arising to a company from
   a. Life insurance business
   b. Banking business
   c. Business of transmission of electricity
   d. All of the above
3. Book profit for the purposes of section 115JB means net profit as shown in the Statement of the Profit and Loss prepared in accordance with _____of the Companies Act as increased and decreased by certain items prescribed in this regard.
   a. Schedule V
   b. Schedule IV
   c. Schedule III
   d. Schedule II
4. Every company to whom the provisions of MAT apply is required to obtain a report from a chartered accountant in Form No. _____ on or before the due date of filing the return of income
   a. 29
   b. 29A
   c. 29B
   d. 29C
5. While computing book profit u/s 115JB, one of the following is required to be reduced from the net profit
   a. Unabsorbed Depreciation as per books of account
   b. Brought forward business loss as per books of account
   c. Brought forward loss or unabsorbed depreciation, whichever is less as per books of account
   d. Income-tax paid or payable if not already debited to the Statement of Profit and Loss

[Answer: 1-C, 2- A, 3-C, 4-C, 5-C]

Short Essay Type Questions:

1. How to compute book profit u/s 115JB?
2. State the provisions relating to registration of trust.
3. State the provisions relating to carbon credit.

Comprehensive Numerical Problems:

1. From the following particulars of Shri Khote for the year ending 31st March, 2024, find out his taxable income from business for the assessment year 2024-25:

Particulars	Amount (₹)	Particulars	Amount (₹)
To Opening Stock	1,20,000	By Sales	2,14,20,000
To Purchases	2,10,00,000	By Profit on sale of import licence	5,000
To Salaries	25,000	By Gift received	24,000
To Legal Expenses	10,000	By Closing Stock	2,00,000
To Bad Debts	5,000		
To Rent	50,000		
To Interest on loan	2,500		
To Depreciation	15,000		
To Income tax paid	2,000		
To Outstanding Customs Duty	25,000		
To Advertisement	2,000		
To Legal expenses	12,000		
To Contribution towards URPF	5,000		
To General expenses	17,500		
To Traveling expenses	1,00,000		
To Net Profit	2,58,000		
	2,16,49,000		2,16,49,000

In computing the income, the following facts are to be taken into consideration:

1. Interest on loan is paid to brother of Shri Khote for loan taken for payment of advance income tax.
2. During the previous year 2019-20, assessee had claimed ₹ 45,000 as bad debt out of which only ₹35,000 was allowed. During the previous year, he recovers ₹ 25,000.
3. Contribution towards unrecognised provident fund was paid within time.
4. Legal expenses include ₹ 2,000 paid for preparation of income tax return.
5. Stock is undervalued by 10%.
6. Gift received was given by a supplier for achieving target sale.
7. Outstanding customs duty has been paid on 31-12-2024.
8. During the previous year, he comes to know that his former employee had embezzled cash of ₹ 5,000 on 31-3-2023, which was not accounted for.
9. Traveling expenses include ₹ 50,000 being cost of trip to Singapore by an employee for 10 days. However, only 8 days of trip is useful to business and 2 days has been allowed as holiday to employee.
10. Rent includes expenditure on extension of shed on rented building ₹ 26,000. However, such extension was completed on 1-5-2024 with total cost of ₹ 50,000.
11. General expenses includes –

- Salary of ₹ 1,200 paid to domestic servant.
- Compensation of ₹ 2,000 paid for retrenchment of an employee.

Compute his business income for the A.Y. 2024-25

[Ans: ₹ 3,38,589]

Unsolved Case:

I. Barun Co. Ltd. is engaged in the business of manufacture of chemicals since June, 2006. The Statement of Profit and Loss for the year ended 31.03.2024 shows a Net Profit of ₹ 35,60,000 and aggregate turnover which never exceeded ₹ 25 crores. The following additional information is provided:

a) Depreciation debited in the books ₹ 19,40,000 (it includes depreciation on revalued plant and machinery of ₹ 3,00,000). Amount of depreciation deductible under Income-tax Rules ₹ 13,15,000.

b) Interest payable to financial institutions ₹ 5,20,000 debited in the books but ₹ 3,90,000 was actually paid during the previous year and up to the date of filing the return of income under section 139(1).

c) Provision for doubtful debts ₹ 8 lakhs being 5% on debtors debited to Statement of Profit and Loss.

d) Expenditure towards issue of bonus shares ₹ 2 lakhs and alteration of memorandum of association for increasing the authorized capital ₹ 1 lakh. Both have been debited in the books as expenditure.

e) Purchase of agricultural produce being raw material for manufacture by making cash payment on 15.08.2023 ₹ 60,000 and on 26.01.2024 ₹ 40,000. Also, cash payments of ₹ 50,000 made for purchases of the previous year 2022-2023 on 03.05.2023.

f) Contract payments made during the year ₹ 5,10,000 to ABC Ltd., Chennai. Tax was not deducted at source in respect of the payments of ₹ 1,50,000.

g) Provision for taxation ₹ 2 lakhs and proposed dividend ₹ 80,000 debited to Statement of Profit and Loss.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. Please state the amount of addition / disallowance to be made in relation to expenditure incurred towards issue of bonus shares and expenditure incurred towards increase in authorized capital while computing taxable income

   a. ₹ 1,00,000

   b. ₹ 3,00,000

   c. Nil

   d. None of the above

2. Please state the amount of addition required to be made as per sec. 40A(3) while computing taxable income

   a. ₹ 50,000

   b. ₹ 1,50,000

   c. ₹ 1,20,000

   d. None of the above

3. What will be total income of the assessee (without considering the provision of sec. 115JB)?
   a. ₹ 55,90,000
   b. ₹ 56,05,000
   c. ₹ 56,95,000
   d. None of the above
4. Please state the amount of addition / disallowance to be made in relation to expenditure incurred towards issue of bonus shares and expenditure incurred towards increase in authorized capital while computing book profit u/s 115JB
   a. ₹ 1,00,000
   b. ₹ 3,00,000
   c. Nil
   d. None of the above
5. What will be book profit for the purpose of sec. 115JB?
   a. ₹ 48,50,000
   b. ₹ 49,40,000
   c. ₹ 40,50,000
   d. None of the above
6. What will be its tax liability?
   a. ₹ 14,53,400
   b. ₹ 17,16,000
   c. ₹ 7,70,640
   d. None of the above

2. AC Flour Mills Ltd., a domestic company engaged in manufacture of wheat flour, furnishes the following information pertaining to the year ended 31-3-2024:

(i) Net profit as per the Statement of Profit and Loss is ₹ 77 lakhs after considering the following items listed in (ii) to (viii) below.

(ii) The company is a member of VF & Co., an AOP in which the members' shares are determinate and their shares in profit/loss are clearly known. The entire income of the AOP is from business activities. During the year, the company has derived share income of ₹ 9 lakhs from the AOP. The company has spent a sum of ₹ 90,000 towards earning such income.

(iii) The company has provided for income-tax (including interest u/s 234B and 234C of ₹ 62,000) for ₹ 3 lakhs and ₹ 5 lakhs towards share in loss of foreign subsidiary.

(iv) Amount debited to the Statement of Profit and Loss towards interest to a public financial institution is ₹ 12 lakhs. Of this, ₹ 4 lakhs was paid on 12-12-2023 only.

(v) The company committed breach of building norms while extending the factory building. The City Corporation initiated proceedings against the company and the company settled the issue by paying compounding fee of ₹ 1 lakh. This amount forms part of general expenses, which has been debited to the Statement Profit and Loss.

(vi) In the administrative expenses, the company has debited a sum of ₹ 70,000 towards fee for delayed filing of statement of TDS under section 234E of the Income-tax Act, 1961.

(vii) The company has credited ₹ 10 lakhs to revaluation surplus on fair valuation of assets.

(viii) During the current year, the depreciation charged as per books of account of the company is the same as allowable under the Income-tax Act, 1961 [before considering the provisions of section 32(2)]. The company proposes to adopt this practice consistently in the future years.

The turnover of the company never exceeds ₹ 100 crore.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. State the amount of addition required to be made while computing total income on account of fee paid u/s 234E
   a. Nil
   b. ₹ 70,000
   c. ₹ 21,000
   d. None of the above
2. What will be total income of the assessee without considering provision of sec. 115JB
   a. ₹ 85,90,000
   b. ₹ 86,11,000
   c. ₹ 87,11,000
   d. None of the above
3. State the net impact of income from AOP (and expenditure relating thereto) while computing book profit u/s 115JB
   a. (₹ 8,10,000)
   b. ₹ 8,10,000
   c. Nil
   d. None of the above
4. What will be book profit u/s 115JB of the company?
   a. ₹ 76,90,000
   b. ₹ 85,00,000
   c. ₹ 67,90,000
   d. None of the above
5. What will be tax liability of the company?
   a. ₹ 22,33,000
   b. ₹ 25,43,200
   c. ₹ 14,27,500
   d. None of the above

3. S Textiles (P) Ltd., Surat earned a profit of ₹ 20 lakhs after debit/credit of the following items to its statement of profit and loss for the year ended 31.03.2024:

Particulars		(₹)
Items debited to statement of profit and loss:		
(i)	Provision for the loss of subsidiary	2,00,000
(ii)	Provision for Doubtful Debts	1,50,000
(iii)	Provision for Income-tax	3,00,000
(iv)	Provision for Gratuity (based on actuarial valuation ` 5 lakhs)	7,00,000
(v)	Depreciation (including ` 1,60,000 on account of revaluation of fixed assets)	5,60,000
(vi)	Interest to financial institution (unpaid till filing of return)	2,50,000
(vii)	Penalty for infraction of law	60,000
Items credited to statement of profit and loss:		
(i)	Royalty in respect of patent (chargeable to tax under section 115BBF)	6,00,000
(ii)	Share income as partner in a firm	1,20,000
(iii)	Agricultural income	75,000
(iv)	Long term capital gains on sale of vacant land	4,00,000

Other information:

(i) Depreciation as per Income-tax Rules is ₹ 2,80,000.

(ii) Income tax liability on income computed as per regular provisions for the A.Y. 2024-25 is ₹ 1,22,070 excluding tax on royalty chargeable to tax u/s 115BBF.

You are required to compute

a. Book Profits under section 115JB of the Income-tax Act, 1961 for Assessment Year 2024-25;

b. Tax on Book Profits u/s 115JB of the Income-tax Act, 1961 for Assessment Year 2024-25 (including applicable surcharge and cess); and

c. tax credit eligible for carry forward by the company (including applicable surcharge and cess)

1. What will be book profit u/s 115JB of the company?

   a. ₹ 22,15,000

   b. ₹ 26,76,000

   c. ₹ 20,18,000

   d. None of the above

2. What will be tax liability of the company?

   a. ₹ 4,77,940

   b. ₹ 4,07,940

   c. ₹ 3,45,540

   d. None of the above

3. Is any tax credit eligible for carry forward by the company (including applicable surcharge and cess)?
   a. ₹ 4,07,940
   b. ₹ 1,60,070
   c. ₹ 2,23,470
   d. None of the above

4. Father Ltd., an Indian company, earned a profit of ₹ 54 lakhs after debit/ credit of the following items to its Statement of Profit and Loss for the year ended on 31.3.2024:

A. Items debited to Statement of Profit and Loss

Sl No.	Particulars	(₹)
1.	Provision for the loss of subsidiary	83,000
2.	Provision for doubtful debts	92,000
3.	Provision for income-tax	1,45,000
4.	Provision for gratuity based on actuarial valuation	4,17,000
5.	Depreciation	3,07,000
6.	Interest to financial institution (unpaid before filing of return)	72,000
7.	Penalty for infraction of law	14,000

B. The following are credited in P/L Account Statement:

Sl No.	Particulars	(₹)
1.	Profit from unit established in special economic zone	15,20,000
2.	Share in income of an AOP as a member	1,95,000
3.	Long term capital gains	3,20,000

Other Information*:*

i. Depreciation includes ₹ 81,000 on account of revaluation of fixed assets.
ii. Depreciation as per Income-tax Rules, 1962 is ₹ 4,12,000
iii. Balance of Statement of Profit and Loss shown in Balance Sheet at the asset side as at 31.3.2023 was ₹ 32 lakhs which includes unabsorbed depreciation of ₹ 18 Lakhs.
iv. The AOP, of which the company is a member, has paid tax at maximum marginal rate.
v. Provision for income-tax includes ₹ 65,000 of interest payable on income-tax.

Based on the above information you are required to answer the following questions.

1. What will be book profit u/s 115JB of the company?
   a. ₹ 42,06,000
   b. ₹ 38,06,000
   c. ₹ 26,86,000
   d. None of the above
2. What will be tax liability of the company?
   a. ₹ 6,86,870
   b. ₹ 6,56,140

c. ₹ 8,25,150

d. None of the above

3. What would be tax amount u/s 115JB (after rounded off), if Father Ltd. is a unit located in an IFSC and derives its income solely in convertible foreign exchange?

a. ₹ 4,47,940

b. ₹ 3,93,680

c. ₹ 3,23,470

d. None of the above

5. Profit and Loss account of X Ltd. for the year ending on 31st March 2024 shows a net profit of ₹ 75,00,000 after debiting / crediting the following items:

a) Depreciation ₹ 24,00,000 including ₹ 4,00,000 on revaluation

b) Interest to financial institution not paid before the due date of filing return of income ₹ 6,00,000

c) Provision for doubtful debts ₹ 1,00,000

d) Provision for unascertained liabilities ₹ 2,00,000

e) Transferred to General Reserve ₹ 5,00,000

f) Net agricultural income ₹ 16,00,000

g) Amount withdrawn from reserve created during 2017-18 ₹ 3,00,000 (book profit was increased by the amount transferred to such reserve in the assessment year 2018-19)

Other information: Brought forward loss and unabsorbed depreciation as per books are ₹ 12,00,000 and ₹ 10,00,000 respectively.

Based on the above information you are required to answer the following questions.

1. What will be book profit u/s 115JB of the company?

a. ₹ 58,00,000

b. ₹ 68,06,000

c. ₹ 57,86,000

d. None of the above

2. What will be tax liability of the company?

a. ₹ 7,96,980

b. ₹ 8,74,870

c. ₹ 9,04,800

d. None of the above

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Tax Management, Return and Assessment Procedure

2

This Module includes:

2.1 Return of Income

2.2 Assessment Procedure including Dispute Resolution Process

2.3 Interest and Fees

2.4 Survey, Search and Seizure

2.5 Collection, Recovery and Refund of Tax

Tax Management, Return and Assessment Procedure

SLOB Mapped against the Module:

To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure.

Module Learning Objectives:

After studying this module, the students will be able to -

- Appreciate when return filing become mandatory
- Identify the various due dates for filing return
- Appreciate the procedure of assessment
- Understand the provisions relating to interest

Introduction

2

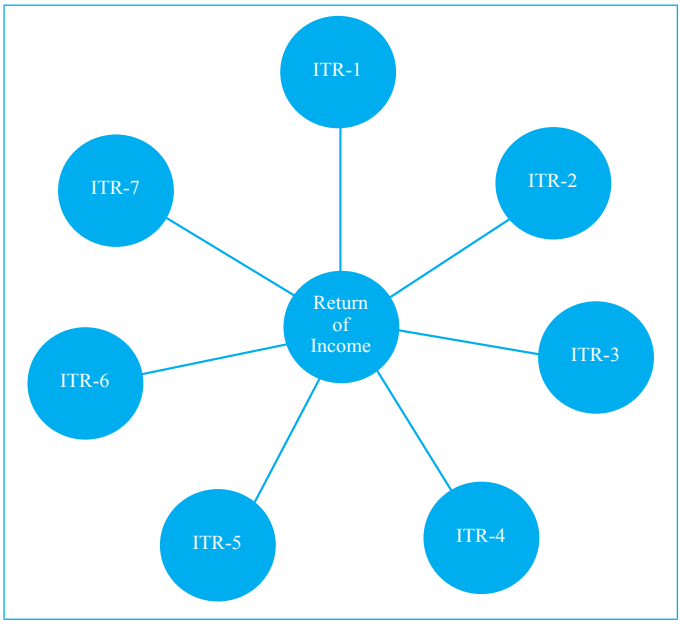
Tax management involves the compliance of law regularly and timely as well as the arrangement of the affairs of the business in such a manner that it reduces the tax liability. Functions under tax management includes maintenance of accounts, filing of return, deduction and deposit of TDS on timely basis, payment of tax on time. Poor tax management can lead to imposition of interest, penalty, prosecution. Losses may not be carried forward and set off if return of loss is not filed by due date. Tax management emphasizes on compliance of legal formalities for minimization of taxes while tax planning emphasis on minimization of tax burden.

Tax Management relates to Past, Present, and Future.

Past – Assessment Proceedings, Appeals, Revisions etc.
Present – Filing of Return, payment of advance tax etc.
Future – To take corrective action

Return of Income

2.1



Every person:

a. being a company or a firm; or

b. being a person other than a company or a firm, if his total income or the total income of any other person in respect of which he is assessable under this Act [income before giving effect to sec. 54, 54B, 54D, 54EC, 54F, 54G, 54GA, 54GB and chapter VIA (i.e., deduction u/s 80C to 80U)] during the previous year exceeded the maximum amount which is not chargeable to income-tax, shall, on or before the due date, furnish a return of his income or the income of such other person during the previous year, in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed – [Sec. 139(1)]

Compulsory filing of return

A **Compulsory filing of return**

Any person, being resident other than not ordinarily resident, shall furnish, a return, within due date, in respect of his income or loss for the previous year irrespective of the fact that his total income does not exceed basic exemption limit or does not have any taxable income, if he:

(i) holds, as a beneficial owner or otherwise, any asset (including any financial interest in any entity) located outside India or has signing authority in any account located outside India; or

(ii) is a beneficiary of any asset (including any financial interest in any entity) located outside India.

Exception: An individual, being a beneficiary of any asset (including any financial interest in any entity) located outside India where, income, if any, arising from such asset is includible in the income of the person referred above in accordance with the provisions of this Act.

➢ "Beneficial owner" in respect of an asset means an individual who has provided, directly or indirectly, consideration for the asset for the immediate or future benefit, direct or indirect, of himself or any other person.

- "Beneficiary" in respect of an asset means an individual who derives benefit from the asset during the pervious year and the consideration for such asset has been provided by any person other than such beneficiary.

"**Mandatory furnishing of return in case of high value transactions [7th Proviso to Sec. 139(1)]**

A person (other than firm and company), who is not required to furnish a return as per aforesaid provision, and who during the previous year:

a) has deposited an aggregate amount exceeding ₹ 1 crore in one or more current accounts maintained with a banking company or a co-operative bank; or

b) has incurred expenditure of an aggregate amounts exceeding ₹ 2 lakh for himself or any other person for travel to a foreign country; or

c) has incurred expenditure of an aggregate amount exceeding ₹ 1 lakh towards consumption of electricity; or

d) fulfils such other conditions as may be prescribed,

The following are prescribed [Rule 12AB]:

- If his total sales, turnover or gross receipts, as the case may be, in the business exceeds ₹60 lakhs during the previous year; or
- If his total gross receipts in profession exceeds ₹ 10 lakh during the previous year; or
- If the aggregate of TDS and TCS during the previous year, in the case of the person, is ₹ 25,000 or more (in case of senior citizen ₹ 50,000); or
- The deposit in one or more savings bank account of the person, in aggregate, is ₹ 50 lakh or more during the previous year

shall furnish a return of his income on or before the due date in such form and verified in such manner and setting forth such other particulars, as may be prescribed.

2.1.1 Forms – Return of income

Rule 12 provides the following Form for filing a return of income for different assessee:

ITR - 1 (Sahaj) — For Individuals having Income from Salaries, one house property (does not have any brought forward loss), other sources [Interest (does not have any loss under the head) etc. but except winnings from lottery or income from race horses] and having total income upto ₹ 50 lakh

However, the form is not to be used by an individual who:

a. has any brought forward / carry forward loss under the head 'Income from House Property';

b. has assets (including financial interest in any entity) located outside India;

c. has signing authority in any account located outside India;

d. has income from any source outside India;

e. has income to be apportioned in accordance with provisions of section 5A

f. has claimed deduction u/s 57, other than deduction from family pension;

g. is a director in any company;

h. has held any unlisted equity share at any time during the previous year;

i. is assessable for the whole or any part of the income on which tax has been deducted at source in the hands of a person other than the assessee;

j. has claimed any relief of tax u/s 90 or 90A or 91;

k. has agricultural income, exceeding ₹ 5,000;

l. has total income, exceeding ₹ 50 lakh;

m. has income of the nature referred to in section 115BBE;

n. is a person in whose case tax has been deducted u/s 194N; or

o. is a person in whose case payment or deduction of tax has been deferred u/s 191(2) or 192(1C)

p. has to furnish return under 7th proviso to sec. 139(1)

q. has income under the head "Capital Gains" and/or "Profits and Gains of Business or Profession"; or

r. has loss under the head "Income from Other Sources".

ITR - 2 For Individuals and HUFs not carrying out business or profession under any proprietorship

ITR - 3 For individuals and HUFs having income from a proprietary business or profession

ITR - 4 (Sugam) In the case of a person being an individual (ordinarily resident) or a HUF (ordinarily resident) or a resident firm (other than LLP), deriving income under the head "Profits or gains of business or profession" and such income is computed in accordance sec. 44AD, 44ADA and 44AE

Taxpoint: The form is applicable to an assessee computing his business or profession income u/s 44AD, 44ADA and 44E.

The form is not applicable to a person who:

a. has assets (including financial interest in any entity) located outside India;

b. has signing authority in any account located outside India;

c. has income from any source outside India;

d. has income to be apportioned in accordance with provisions of sec. 5A;

e. is a director in any company;

f. has held any unlisted equity share at any time during the previous year;

g. has total income, exceeding ₹ 50 lakh;

h. owns more than one house property, the income of which is chargeable under the head "Income from house property";

i. has any brought forward loss or loss to be carried forward under any head of income;

j. is assessable for the whole or any part of the income on which tax has been deducted at source in the hands of a person other than the assessee;

k. has claimed any relief u/s 90 or 90A or deduction of tax u/s 91;

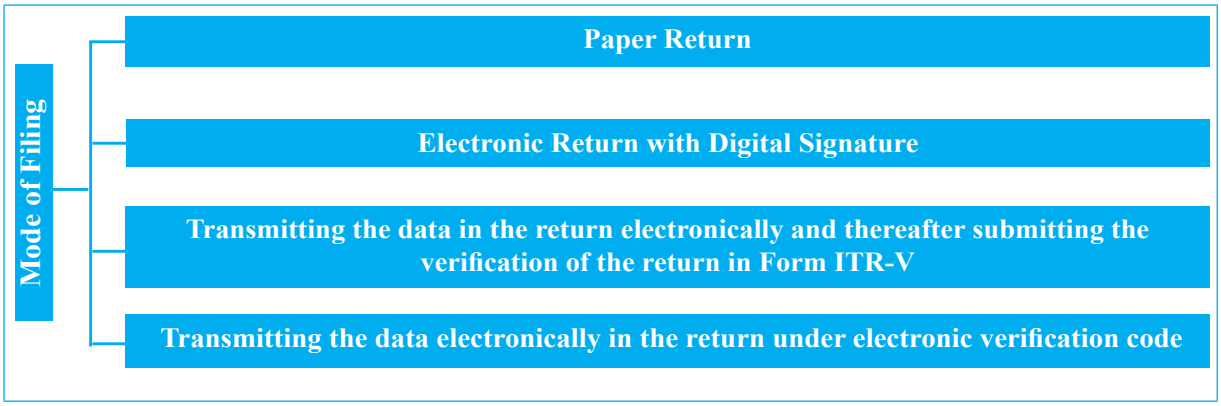
l. has agricultural income, exceeding ₹ 5,000;

m. has income of the nature referred to in sec. 115BBE;

n. has income of the nature specified in sec. 17(2)(vi) on which tax is payable or deductible, as the case may be, u/s 191(2) or 192(1C).

ITR - 5 For a person other than (i) Individual; (ii) HUF; (iii) Company; & (iv) Person filing Form ITR-7
ITR - 6 For Companies other than companies claiming exemption u/s 11
ITR - 7 For persons including companies required to furnish return u/s 139(4A) or 139(4B) or 139(4C) or 139(4D) or 139(4F)
ITR - V Income Tax Return Verification Form [Where the data of the aforesaid Return of Income has been transmitted electronically without digital signature]

2.1.2 Mode of furnishing Income-tax Return



The table enumerates mode of filing of return of income:

Person	Condition	Mode
Company	-	Electronically with digital sign
Political Party	-	
Firm or LLP or Individual or HUF	Audit u/s 44AB required	
Individual	Where total income assessable during the previous year of a person, being an individual of the age of 80 years or more at any time during the previous year, and who furnishes the return in Form number SAHAJ (ITR-1) or Form number SUGAM (ITR-4)	Any of the given mode
Any other person		Any mode other than paper mode

Taxpoint

- A resident Individual (other than not-ordinarily resident) or a resident HUF (other than not-ordinarily resident) must file the return of income electronically (with or without digital sign) if he/it has:
  (a) assets (including financial interest in any entity) located outside India; or
  (b) signing authority in any account located outside India.
- Further, any person who has claimed any relief u/s 90 or 90A or 91, is required to file return electronically.

- In respect of any electronic transmission of return data, the return should be verified through e-verification or submission of ITR-V. Such verification should be done within 30 days from the date of transmitting/uploading the data of return of income electronically.
- Further, where ITR data is electronically transmitted and e-verified/ITR-V submitted within 30 days of transmission of data - in such cases the date of transmitting the data electronically shall be considered as the date of furnishing the return of income. However, where ITR data is electronically transmitted but e-verified or ITR-V submitted beyond the time-limit of 30 days of transmission of data - in such cases the date of e-verification/ITR-V submission shall be treated as the date of furnishing the return of income and all consequences of late filing of return under the Act shall follow.

26AS Statement

The following details (on yearly basis) have been provided in 26AS statement:

- Tax paid through Tax Deducted at Source (TDS) or TCS on behalf of the assessee
- Details of TDS for 15G / 15H
- TDS/TCS defaults
- Details of Tax Deducted at Source u/s 194IA/ 194IB / 194M/ 194S (For Seller/Landlord of Property/Contractors or Professionals/ Seller of Virtual Digital Asset)
- Details of Tax Deducted at Source u/s 194IA / 194IB / 194M / 194S (For Buyer/Tenant of Property /Person making payment to contractors or Professionals / Buyer of Virtual Digital Asset)
- Details of Transactions/Demand Payments under Proviso to sec.194S(1) as per Form 26QE (For Buyer / Seller of Virtual Digital Assets)
- Refund issued by the CPC-TDS

Annual Tax Statement available on TRACES portal will display only TDS/TCS related data. Other details would be available in the AIS (Annual Information Statement) at e-filing portal

Functionalities available at e-Filing Portal [www.incometax.gov.in]

Few of the functionalities available at e-filing portal are as follow:

- View Form 26AS / AIS
- View (with download facility) e-Filed Return / Form
- Download pre-filled json
- e-Verify Return
- Generate EVC
- Add / Disengage CA
- Add / Register as Representative
- Filing of Returns
- Filing of return in response of notice u/s 139(9)
- Aadhar linking
- e-Proceedings
- Filing of appeal
- Registration or updation of Digital Sign
- Refund reissue request

- Validation of Bank Account or Demat Account
- Profile updation

2.1.3 Time limit for filing return of income [Explanation 2 to Sec. 139(1)]

A return should be filed on or before the following due date (of respective assessment year):

Assessee	Due date
⊙ Where the assessee (including the partners of the firm) is required to furnish a report in Form 3CEB u/s 92E pertaining to international transaction(s)	30th November
⊙ Where the assessee is a partner[1] in a firm and the said firm is required to furnish report in Form 3CEB u/s 92E pertaining to international transaction(s)	30th November
⊙ Where the assessee is a company not having international transaction(s)	31st October
⊙ Any other assessee	
– Where accounts of the assessee are required to be audited under any law	31st October
– Where the assessee is a partner[1] in a firm and the accounts of the firm are required to be audited under any law	31st October
– In any other case	31st July

2.1.4 Fee for default in furnishing return of income [Sec. 234F]

Where a person required to furnish a return of income u/s 139, fails to do so within the due date, he shall pay fee of:

Case	Fee
Total income does not exceed ₹ 5 lakh	₹ 1,000
Total income exceeds ₹ 5 laks	₹ 5,000

2.1.5 When a return of loss should be filed [Sec. 139(3)]

An assessee, other than few, is not compulsorily required to furnish return of loss. However, the following losses cannot be carried forward if the return of loss is not submitted within the time allowed u/s 139(1) -

a. Business loss (speculative or otherwise);

b. Capital loss;

c. Loss from the activity of owning and maintaining race horses

d. Loss from business specified u/s 35AD

Notes:

a. Loss declared in belated return cannot be carried forward. However, set-off of losses of current year is not prohibited while computing the total income, even if the return of loss is filed after the due date.

b. Delay in filing the return of loss may be condoned in certain cases

c. Unabsorbed depreciation u/s 32 and loss under the head "Income from house property" can be carried forward

[1] Also spouse of such partner if the provisions of section 5A applies to such spouse

even if the loss return is filed after the due date u/s 139(1).

d. Although the loss of the current year cannot be carried forward unless the return of loss is submitted before the due date but the loss of earlier years can be carried forward if the return of loss of that year was submitted within the due date.

2.1.6 Belated Return [Sec. 139(4)]

If an assessee fails to file return within the time limit allowed u/s 139(1) or within the time allowed under a notice issued u/s 142(1), he can file a belated return.

Time limit: Assessee may file such return -

- before 31st December of the relevant assessment year; or
- before the completion of assessment (u/s 144),

  - whichever is earlier.

  However, if an assessee files a belated return,

  - he would be liable to fee u/s 234F
  - he would be liable to interest u/s 234A
  - certain profit based deductions under chapter VIA are not available
  - certain losses of the previous year [as provided in sec.193(3)] are not allowed to be carried forward

2.1.7 Return of income of Charitable Trust [Sec. 139(4A)]

Every person who is in receipt of –

- income from property held under the trust or other legal obligation wholly or partly for charitable or religious purpose; or
- income by way of voluntary contribution on behalf of such trust or institution,

and if such income before allowing exemption u/s 11 or 12 exceeds the maximum amount which is not chargeable to tax, must file a return before the due date as per sec.139(1).

Penalty: Where an assessee fails to file return of income under this section, within the time limit, it shall be liable to pay a penalty of ₹ 100 per day during which such failure continues [Sec. 272A(2)].

2.1.8 Return of income of Political Party [Sec. 139(4B)]

The chief executive officer (whether such chief executive officer is known as Secretary or by any other designation) of any political party is required to furnish a return in respect of income of such political party, if the amount of gross total income before allowing exemption u/s 13A exceeds the maximum amount not chargeable to tax.

2.1.9 Return of income of scientific research association, etc. [Sec. 139(4C)]

Every -

- Research Association referred to in sec. 10(21);
- News agency referred to in sec. 10(22B);
- Association or institution referred to in sec. 10(23A) or sec. 10(23B);

- Specified Employee Welfare Fund referred to in sec. 10(23AAA);
- Any university or other educational institution referred to in sec. 10(23C)(iiiad) or (iiiab);
- Any hospital or other medical institution referred to in sec. 10(23C)(iiiae) or (iiiac);
- Fund or institution referred to in sec. 10(23C)(iv);
- Trust or institution referred to in sec. 10(23C)(v);
- Any university or other educational institution referred to in sec. 10(23C)(vi);
- Any hospital or other medical institution referred to in sec. 10(23C)(via);
- Mutual Fund referred to in sec. 10(23D);
- Securitisation trust referred to in sec. 10(23DA);
- Investor Protection Fund referred to in sec. 10(23EC) or sec. 10(23ED);
- Core Settlement Guarantee Fund referred to in sec. 10(23EE);
- Venture Capital Company or Venture Capital Fund referred to in sec. 10(23FB);
- Trade union or an association of such union referred to in sec. 10(24);
- Body or authority or Board or Trust or Commission referred to in sec. 10(46) or 10(29A);
- Infrastructure debt fund referred to in sec. 10(47),

must file a return, if the total income without giving effect to the provisions of sec. 10, exceeds the maximum amount which is not chargeable to income-tax.

Penalty: Where an assessee fails to file return of income under this section, within the time limit, it shall be liable to pay a penalty of ₹ 100 per day during which such failure continues [Sec. 272A(2)].

2.1.10 Return of income by a University/ College etc. [Sec. 139(4D)]

Every University, college or other institutions referred to in sec. 35(1)(ii) or (iii) is required to furnish a return in respect of income or loss irrespective of size of income or loss.

2.1.11 Return of income of a Business Trust [Sec. 139(4E)]

Every business trust, which is not required to furnish return of income or loss under any other provisions of this section, shall furnish the return of its income in respect of its income or loss in every previous year and all the provisions of this Act shall, so far as may be, apply if it were a return required to be furnished u/s 139(1).

2.1.12 Return of income of Investment Fund [Sec. 139(4F)]

Every investment fund referred to in sec. 115UB, which is not required to furnish return of income or loss under any other provisions of this section, shall furnish the return of income in respect of its income or loss in every previous year and all the provisions of this Act shall, so far as may be, apply as if it were a return required to be furnished u/s 139(1)

2.1.13 Revised Return [Sec. 139(5)]

If an assessee discovers any omission or wrong statement (bonafide in nature) in the return filed, he can revise his return u/s 139(5).

Time limit: Assessee may file the revised return -

- before 31st December of the relevant assessment year; or
- before completion of regular assessment,

  - whichever is earlier.

Notes:

a) **Replacement of original return:** Once a revised return is filed, it replaces the earlier return. This signifies that the revised return should be complete in itself and not merely an accessory to the original return.

b) **Revision of revised return:** A revised return can again be revised i.e. a second revised return can be filed u/s 139(5) for correcting any omission or wrong statement made in the first revised return within specified time.

c) **Revision of belated return:** A belated return u/s 139(4) can be revised.

d) **Revision of loss return:** A loss return can be revised

e) Return filed pursuant to notice u/s 142(1) cannot be revised.

2.1.14 Defective Return [Sec. 139(9)]

When a return is termed defective - A return of income is said to be defective where all the following conditions are not fulfilled:

- The return is furnished without paying self-assessment tax along with interest, if any.
- The annexure, statements and columns in the return of income have been duly filled in.
- The return is accompanied by the following documents -

  a. a statement showing the computation of tax liability;

  b. the audit report u/s 44AB (where the report has been submitted prior to the furnishing of return, a copy of audit report together with proof of furnishing the report);

  c. the proof of tax deducted or collected at source, advance tax paid and tax paid on self-assessment;

  d. where regular books of account are maintained by the assessee:

     i. copies of Manufacturing A/c, Trading A/c, Profit and Loss A/c or Income and Expenditure A/c or any other similar account and Balance Sheet;

     ii. in the case of –

     - A proprietary business or profession - the personal account of the proprietor;
     - A firm, AOP or BOI - personal account of the partners or members; or
     - A partner or member of the firm, AOP or BOI - his personal account in the firm, association of persons or body of individuals;

     where regular books of account are not maintained by the assessee –

  e. where regular books of account are not maintained by the assessee:

     i. a statement indicating the amount of turnover or gross receipts, gross profit, expenses and net profit of the business or profession and the basis on which such amount have been computed; and

ii. the amount of sundry debtors, sundry creditors, stock and cash balance as at the end of the previous year.

f. where the accounts of the assessee have been audited, copies of the audited Profit and Loss A/c, Balance Sheet and a copy of the Auditor's report;

g. Cost audit report u/s 233B of the Companies Act, 1956 (if any).

Effect: Where the Assessing Officer considers that the return of income furnished by the taxpayer is defective, he may intimate the defect to the taxpayer and give him an opportunity to rectify the defect(s).

Time limit for rectification: The assessee must rectify the error within a period of 15 days from the date of intimation (served on the assessee) or within such extended time as allowed by the Assessing Officer. Where the taxpayer rectifies the defect after the expiry of the period of 15 days or such extended period but before the assessment is completed, the Assessing Officer can condone such delay.

Consequence when defect is not rectified: If defect is not rectified within the time limit, the Assessing Officer will treat the return as an invalid return and provisions of the Act will apply as if the taxpayer had failed to furnish the return at all.

Note: Currently, the assessee is required to furnish paper-less return. i.e., no documents, proof or report (other than some specified report required to be furnished electronically) is required to be attached with return of income. In this regard, return of income shall not be considered as defective return. However, the assessee should retain these documents, proof or report with himself. If called for by the income-tax authority during any proceeding, it shall be incumbent upon the assessee to furnish/produce the same.

2.1.15 Verification of Return [Sec. 140]

The return of income is required to be verified:

Assessee	Case	Verified by
Individual	In general	Individual himself
	Where the individual concerned is absent from India	Individual himself or by the duly authorized person of such individual
	Where the individual is mentally incapacitated	Guardian of such individual or any other person competent to act on his behalf
	Where by any other reason it is not possible for the individual to verify the return.	Any person duly authorised by him
	Note: When return is verified by any authorised person in that case the return should be accompanied with power of attorney.	
HUF	In general	Karta
	Where the 'karta' is absent from India or is mentally incapacitated	Any adult member of the family.
Firm	In general	Managing partner
	If due to any reason it is not possible for managing partner to verify or where there is no managing partner	Any adult partner

Assessee	Case	Verified by
Limited liability partnership	In general	Designated partner
	If due to any unavoidable reason such designated partner is not able to verify the return, or where there is no designated partner as such	Any partner or any other prescribed person
Local authority	Principal Officer	
Political party	Chief Executive Officer	
Company	In general	Managing Director (MD)
	If due to any reason it is not possible for MD to verify or where there is no MD	Any director or any other prescribed person
	Where an application for corporate insolvency resolution process has been admitted by the Adjudicating Authority under Insolvency and Bankruptcy Code, 2016	Insolvency professional appointed by such Adjudicating Authority
	Non-resident company	A person holding a valid power of attorney. Copy of such power of attorney must be attached with the return.
	Company in process of winding up	Liquidator of the company
	Where the management of the company has been taken over by the Central or State Government.	Principal officer
Any other association	Any member or principal officer	
Any other person	Such person or any other person competent to act on its behalf.	

2.1.16 Quoting of Aadhaar number [Sec. 139AA]

Every person who is eligible to obtain Aadhaar number shall quote Aadhaar number:

a. in the application form for allotment of permanent account number;

b. in the return of income:

Note:

- Where the person does not possess the Aadhaar Number, the Enrolment ID of Aadhaar application form issued to him at the time of enrolment shall be quoted.
- Every person who has been allotted PAN before 01-07-2017 and who is eligible to obtain Aadhaar number, shall intimate his Aadhaar number to such authority on or before specified date (31-03-2022). In case of failure to intimate the Aadhaar number, the PAN allotted to the person shall be made inoperative after the notified date in such manner as may be prescribed.
- The provisions of this section shall not apply to notified persons or State

- **Fee for default relating to intimation of Aadhaar number [Sec. 234H]**: Where a person fails to intimate his aadhaar number on or before prescribed date, he shall be liable to pay such fee, as may be prescribed, not exceeding ₹ 1,000, at the time of making intimation after the said date.

2.1.17 Updated Return [Sec. 139(8A)]

Who can file updated return: Any person, whether or not he has furnished a return u/s 139(1) or (4) or (5), for an assessment year, may furnish an updated return of his income or the income of any other person in respect of which he is assessable under this Act, for the previous year relevant to such assessment year, in the prescribed form, verified in such manner and setting forth such particulars as may be prescribed.

Taxpoint

- An updated return cannot be filed, if the updated return:
  a. is a return of a loss; or
  b. has the effect of decreasing the total tax liability determined on the basis of return already furnished u/s 139(1) or (4) or (5) [in nutshell, a person cannot reduce his tax liability by filing updated return]; or
  c. results in refund or increases the refund due on the basis of return furnished u/s 139(1) or (4) or (5), of such person for the relevant assessment year.
- A person shall not be eligible to furnish an updated return, where:
  a. a search has been initiated u/s 132 or books of account or other documents or any assets are requisitioned u/s 132A in the case of such person; or
  b. a survey has been conducted u/s 133A [other than sec. 133A(2A)], in the case such person; or
  c. a notice has been issued to the effect that any money, bullion, jewellery or valuable article or thing, seized or requisitioned u/s 132 or 132A in the case of any other person belongs to such person; or
  d. a notice has been issued to the effect that any books of account or documents, seized or requisitioned u/s 132 or 132A in the case of any other person, pertain or pertains to, or any other information contained therein, relate to, such person,

  for the assessment year relevant to the previous year in which such search is initiated or survey is conducted or requisition is made and any assessment year preceding such assessment year.
- No updated return shall be furnished by any person for the relevant assessment year, where:
  a. an updated return has already been furnished by him for the relevant assessment year; or
  b. any proceeding for assessment or reassessment or recomputation or revision of income is pending or has been completed for the relevant assessment year in his case; or
  c. the Assessing Officer has information in respect of such person for the relevant assessment year in his possession under the Smugglers and Foreign Exchange Manipulators (Forfeiture of Property) Act, 1976 or the Prohibition of Benami Property Transactions Act, 1988 or the Prevention of Money-laundering Act, 2002 or the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 and the same has been communicated to him, prior to the date of furnishing of return under this sub-section; or
  d. information for the relevant assessment year has been received under an agreement referred to in sec. 90 or 90A in respect of such person and the same has been communicated to him, prior to the date of furnishing of return under this sub-section; or

e. any prosecution proceedings under the Chapter XXII have been initiated for the relevant assessment year in respect of such person, prior to the date of furnishing of return; or

f. he is such person or belongs to such class of persons, as may be notified by the Board in this regard.

- If any person has sustained a loss in any previous year and has furnished a return of loss in the prescribed from within the time allowed u/s 139(1) and verified in the prescribed manner and containing such other particulars as may be prescribed, he shall be allowed to furnish an updated return where such updated return is a return of income.
- If the loss or any part thereof carried forward or unabsorbed depreciation carried forward or tax credit carried forward u/s 115JAA or u/s 115JD is to be reduced for any subsequent previous year as a result of furnishing of updated return for a previous year, an updated return shall be furnished for each such subsequent previous year.

Time limit for filing updated return: At any time within 24 months from the end of the relevant assessment year.

Taxpoint: The updated return is accompanied by the proof of payment of tax as required u/s 140B

2.1.18 Tax on updated return [Sec. 140B]

i. **Where assessee has not furnished return earlier**

Where no return of income u/s 139(1) or (4) has been furnished by an assessee and tax is payable, on the basis of updated return to be furnished by such assessee, after taking into account:

i. the amount of tax, if any, already paid as advance tax;

ii. TDS or TCS;

iii. any relief u/s 89;

iv. any relief u/s 90 or 91 on account of tax paid in a country outside India;

v. any relief u/s 90A on account of tax paid in any specified territory outside India; and

vi. any tax credit claimed to be set off in accordance with the provisions of sec. 115JAA or 115JD,

the assessee shall be liable to pay such tax together with interest and fee payable for any delay in furnishing the return or any default or delay in payment of advance tax, along with the payment of additional income-tax, before furnishing the return and the return shall be accompanied by proof of payment of such tax, additional income-tax, interest and fee.

ii. **Where assessee has furnished return earlier**

Where, return of income u/s 139(1) or (4) or (5) (referred to as earlier return) has been furnished by an assessee and tax is payable on the basis of updated return to be furnished by such assessee

a) after taking into account*:*

i. the amount of relief or tax referred to in sec. 140A(1), the credit for which has been taken in the earlier return;

ii. TDS or TCS on any income which is taken into account in computing total income and which has not been included in the earlier return;

iii. any relief claimed u/s 90 or 91 on account of tax paid in a country outside India on such income which

has not been included in the earlier return;

iv. any relief claimed u/s 90A on account of tax paid in any specified territory outside India on such income which has not been included in the earlier return;

v. any tax credit claimed, to be set off in accordance with the provisions of sec. 115JAA or 115JD, which has not been claimed in the earlier return; and

b) as increased by the amount of refund, if any, issued in respect of such earlier return,

the assessee shall be liable to pay such tax together with interest for any default or delay in payment of advance tax along with the payment of **additional income-tax** as reduced by the amount of interest paid in the earlier return, before furnishing the return and the return shall be accompanied by proof of payment of such tax, additional income-tax, interest and fee.

Computation of Additional Income Tax

The additional income-tax payable at the time of furnishing the updated return shall be:

if such return is furnished after expiry of the time available u/s 139(4) or (5) **and** before completion of the period of 12 months from the end of the relevant assessment year	25% of aggregate of tax (+ surcharge + cess) and interest payable on tax calculated above
if such return is furnished after the expiry of 12 months from the end of the relevant assessment year but before completion of the period of 24 months from the end of the relevant assessment year	50% of aggregate of tax (+ surcharge + cess) and interest payable on tax calculated above

Assessment Procedure including Dispute Resolution Process

2.2

Assessment means to assess the income of the assessee i.e. to decide the income and tax liability of the assessee on the basis of the return filed, information gathered, or to the best of the judgment of the income tax department. It begins with self-assessment i.e. assessment by the assessee himself.

2.2.1 Self-Assessment [Sec. 140A]

In self-assessment, assessee itself is responsible to determine its taxable income, tax liability and to pay tax accordingly. Provision of sec. 140A is as follows -

a) Where any tax is payable (after deducting relief, rebate, advance payment of tax or tax deducted or collected at source or MAT or AMT credit, if any, or any tax or interest payable u/s 191(2)) on the basis of return furnished the assessee is required to pay such tax before filing the return.

   Taxpoint: A return furnished without paying self-assessment tax & interest, if any, shall be treated as defective return.

b) If any interest is payable for delayed filing of return (u/s 234A) or default in payment of advance tax (u/s 234B) or for deferment of advance tax (u/s 234C) or fee (u/s 234F) is payable for filing return after due date, then such interest or fee should be paid along with self-assessment tax.

   Note: While calculating above interest for the purpose of self-assessment, tax on the total income declared in the return shall be considered.

c) Where the amount paid by the assessee falls short of the aggregate of tax, interest and fee, the amount so paid shall first be adjusted towards fee and thereafter towards interest payable and the balance, if any, shall be adjusted towards tax payable.

d) After assessment, any amount paid under this section shall be deemed to have been paid towards such assessment.

e) If an assessee fails to pay whole or any part of such tax or interest or both in accordance with the provisions of sec. 140A, he shall be deemed to be an assessee in default.

2.2.2 Intimation or Assessment by Income tax department

After submission of the return or on non-submission of return by the assessee, assessment is made by the Income-tax department. The Assessing Officer can assess the income of the assessee in any of the following manners:

1. Intimation u/s 143(1);
2. Scrutiny Assessment u/s 143(3);

3. Best Judgment Assessment u/s 144;
4. Income Escaping Assessment u/s 147

For making assessment, the Assessing Officer can make an inquiry. Provision relating to inquiry before assessment are as under:

2.2.3 Inquiry before assessment

1. Issue of notice to the assessee [Sec. 142(1)]

   - to submit a return [Sec. 142(1)(i)]

   - to produce accounts, documents etc. [Sec. 142(1)(ii) & (iii)]
2. Making inquiry [Sec. 142(2)]
3. Giving direction to get books of account audited [Sec. 142(2A) to (2D)]
4. Opportunity of being heard [Sec. 142(3)]
5. Estimate by Valuation Officer in certain cases [Sec. 142A]

Issue of notice to the assessee [Sec. 142(1)]

For the purpose of making the assessment, the Assessing Officer (or prescribed income tax authority) may serve a notice on any person -

- who has submitted a return u/s 139; or
- in whose case the time allowed u/s 139(1) for furnishing the return has expired.

Such notice may relate to any of the following matter -

1. **Notice to submit a return [Sec. 142(1)(i)]:** If the assessee has not submitted a return of income within specified time, the Assessing Officer may require him to submit a return in the prescribed form on or before the date specified in the notice.

   Taxpoint: In case assessee has not furnished the return of income, it is not mandatory for the Assessing Officer to issue notice u/s 142(1)(i) if he wishes to make best judgment assessment.

2. **Notice to produce accounts, documents etc. [Sec. 142(1)(ii)]:** The Assessing Officer may ask the assessee to produce such documents or accounts as he may require.

   Exception: Assessing Officer shall not require the production of any accounts pertaining to a period more than 3 years prior to the previous year.

3. **Notice to furnish information [Sec. 142(1)(iii)]:** Assessing Officer may require the assessee to furnish in writing information in such form and on such points or matters as he may require (including a statement of all assets and liabilities of the assessee, whether included in the accounts or not). However, prior approval of the Joint Commissioner shall be obtained before requiring the assessee to furnish a statement of all assets and liabilities not included in the accounts.

   Taxpoint: Notice u/s 142(1)(i) can be served only if return has not been submitted whereas notice u/s 142(1)(ii) & (iii) can be served whether return has been furnished or not.

Making inquiry [Sec. 142(2)]

For the purpose of obtaining full information in respect of the income (or loss) of any person, the Assessing Officer may make such inquiry, as he considers necessary.

Taxpoint: U/s 142(1) Assessing Officer collects information from the assessee, however u/s 142(2) Assessing Officer has the power to collect information from any source.

Giving direction to get books of account audited / valuation of inventory [Sec. 142(2A) to (2D)]

The Assessing Officer (after giving reasonable opportunity to the assessee) having regard to the -

- nature and complexity of the accounts, volume of the accounts, doubts about the correctness of the accounts, multiplicity of transactions in the accounts or specialised nature of business activity of the assessee; and
- interest of revenue.

may direct the assessee if he is of the opinion that it is necessary to do so

- to get his accounts audited by an accountant; or
- to get the inventory valued by a cost accountant

Notes

a. Direction can be issued to get audit or get inventory valued or both

b. Such direction can be issued even if the accounts of the assessee have already been audited u/s 44AB or any other law for the time being in force

c. Such direction can be issued only with the prior approval of the Principle Chief Commissioner / Principle Commissioner / Chief Commissioner / Commissioner.

d. The Principle Chief Commissioner / Principle Commissioner / Chief Commissioner / Commissioner nominates such accountant / cost accountant.

e. Such order can be issued at any stage of the proceedings before the Assessing Officer. However, no such order shall be issued after the completion of assessment/reassessment.

Time Limit for report: The report shall be furnished by the assessee within the period specified by the Assessing Officer. The Assessing Officer has power to extend such period on an application made by the assessee or *suomotu*. However, the aggregate period (fixed originally and extended) shall not exceed 180 days from the date on which such direction is received by the assessee.

Form of report: The nominated accountant or cost accountant shall submit the report in Form 6B to the assessee. Thereafter such report is to be submitted by the assessee to the Assessing Officer within such period as allowed by the Assessing Officer.

Fees: The remuneration or fees and incidental expenditure shall be determined by the Principle Chief Commissioner/ Principle Commissioner / Chief Commissioner / Commissioner (which shall be final) and paid by the Central Government.

Consequences of failure: In case assessee fails to follow the direction, it -

- will be liable to Best Judgment Assessment u/s 144; and
- attracts penalty and prosecution.

Note: Penalty etc. are attracted only if there is a default by the assessee. If nominated accountant refuses to audit the accounts, the assessee cannot be held responsible.

Opportunity of being heard [Sec. 142(3)]

The assessee must be given an opportunity of being heard in respect of any material gathered on the basis of any inquiry u/s 142(2) or any audit / valuation u/s 142(2A) and is proposed to be utilised for the purpose of the assessment.

Note: Sec. 142(3) shall not be applicable in case of assessment u/s 144.

Estimation by Valuation Officer in certain cases [Sec. 142A]

- The Assessing Officer may, for the purposes of assessment or reassessment, make a reference to a Valuation Officer to estimate the value, including fair market value, of any asset, property or investment and submit a copy of report to him.
  - "Valuation Officer" has the same meaning as in clause (r) of section 2 of the Wealth-tax Act, 1957
- The Assessing Officer may make a reference to the Valuation Officer whether or not he is satisfied about the correctness or completeness of the accounts of the assessee.
- The Valuation Officer, on a reference made, shall, for the purpose of estimating the value of the asset, property or investment, have all the powers that he has under section 38A of the Wealth-tax Act, 1957.
- The Valuation Officer shall, estimate the value of the asset, property or investment after taking into account such evidence as the assessee may produce and any other evidence in his possession gathered, after giving an opportunity of being heard to the assessee.
- The Valuation Officer may estimate the value of the asset, property or investment to the best of his judgment, if the assessee does not co-operate or comply with his directions.
- The Valuation Officer shall send a copy of the report of the estimate made to the Assessing Officer and the assessee, within a period of 6 months from the end of the month in which a reference is made.
- The Assessing Officer may, on receipt of the report from the Valuation Officer, and after giving the assessee an opportunity of being heard, take into account such report in making the assessment or reassessment.

2.2.4 Faceless inquiry or Valuation [Sec. 142B]

- The Central Government may notify a scheme for the purposes of issuing notice u/s 142(1) or making inquiry before assessment u/s 142(2), or directing the assessee to get his accounts audited u/s 142(2A) or estimating the value of any asset, property or investment by a Valuation Officer u/s 142A, so as to impart greater efficiency, transparency and accountability by:
  a. eliminating the interface between the income-tax authority or Valuation Officer and the assessee or any person to the extent technologically feasible;
  b. optimising utilisation of the resources through economies of scale and functional specialisation;
  c. introducing a team-based issuance of notice or making of enquiries or issuance of directions or valuation with dynamic jurisdiction.

2.2.5 Intimation / Assessment by Assessing Officer

The Assessing Officer makes the following order:

Intimation [Sec. 143(1)]

On the basis of return filed; or

Regular assessment

- On the basis of further evidence gathered by him [Scrutiny Assessment u/s 143(3)]
- On the basis of best of his judgement [Best Judgement Assessment u/s 144]

2.2.6 Intimation [Sec. 143(1)]

Where a return has been made u/s 139 or in response to a notice u/s 142(1), such return shall be processed in the following manner, namely:—

a. the total income or loss shall be computed after making the following adjustment:

   i. any arithmetical error in the return;

   ii. an incorrect claim, if such incorrect claim is apparent from any information in the return;

   iii. disallowance of loss claimed, if return of the previous year for which set off of loss is claimed was furnished after the due date;

   iv. disallowance of expenditure or increase in income indicated in the audit report but not taken into account in computing the total income in the return;

   v. disallowance of deduction claimed u/s 10AA or under any of the provisions of Chapter VI-A under the heading "C.—Deductions in respect of certain incomes", if the return is furnished after the due date;

   Such adjustments shall not be made unless an intimation is given to the assessee of such adjustments either in writing or in electronic mode. The response received from the assessee, if any, shall be considered before making any adjustment, and in a case where no response is received within 30 days of the issue of such intimation, such adjustments shall be made.

b. the tax, interest and fee, if any, shall be computed on the total income computed above;

c. the sum payable by (or the amount of refund due to), the assessee shall be determined after adjustment of the tax, interest and fee, if any, by any TDS, TCS, advance tax paid, any relief, tax paid on self-assessment and any amount paid otherwise by way of tax, interest or fee;

d. an intimation shall be prepared or generated and sent to the assessee specifying the sum determined to be payable by, or the amount of refund due to, the assessee; and

e. the amount of refund due to the assessee in pursuance of the determination shall be granted to the assessee.

f. An intimation shall also be sent to the assessee in a case where the loss declared in the return by the assessee is adjusted but no tax or interest or fee is payable by, or no refund is due to, him.

Time limit for intimation: No intimation shall be **sent** after the expiry of 12 months from the end of the financial year in which the return is made. The period of limitation will run from the date of filing of latest revised return.

Notes

- An incorrect claim apparent from any information in the return shall mean a claim, on the basis of an entry, in the return,—

  a) of an item, which is inconsistent with another entry of the same or some other item in such return;

  b) in respect of which the information required to be furnished under this Act to substantiate such entry has not been so furnished; or

c) in respect of a deduction, where such deduction exceeds specified statutory limit which may have been expressed as monetary amount or percentage or ratio or fraction;

- The acknowledgment of the return shall be deemed to be intimation where either no sum is payable by the assessee or no refund is due to him.
- In case, where refund becomes due to the assessee u/s 143(1) and the Assessing Officer is of the opinion, having regard to the fact that a notice has been issued u/s 143(2) in respect of such return, that the grant of the refund is likely to adversely affect the revenue, he may, for reasons to be recorded in writing and with the previous approval of the Principal Commissioner or Commissioner, as the case may be, withhold the refund up to the date on which the assessment is made [Sec. 241A]

2.2.7 Scrutiny Assessment u/s 143(3)

Where the Assessing Officer or the prescribed income-tax authority (here-in-after collectively referred to as 'Assessing Officer') considers it necessary to ensure that the assessee has not -

- understated his income; or
- declared excessive loss; or
- under paid the tax,

he can make a scrutiny in this regard and gather such information and evidence as he deems fit. And on the basis of such information and evidence so collected, he shall pass an assessment order. Such order shall be treated as regular assessment order.

Conditions for scrutiny assessment

- A return has been furnished u/s 139 or in response to a notice u/s 142(1); and
- Assessing Officer considers it necessary or expedient to ensure that the assessee has not understated his income, declared excessive loss or under-paid the tax.

Procedure

Notice for scrutiny [Sec. 143(2)]

Assessing Officer shall serve on the assessee a notice requiring the assessee, on a date specified in the notice, to produce, or cause to be produced, any evidence on which assessee may rely, in support of the return.

Time limit of notice

No notice shall be served on the assessee after the expiry of 3 months from the end of the financial year in which the return is furnished.

Order

After collecting such information and hearing such evidence as the assessee produces in response to the notice u/s 143(2) and after taking into account all relevant materials, which the Assessing Officer has gathered;

The Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee and determine the sum payable by him or refund of any amount due to him on the basis of such assessment.

Time limit for completion of scrutiny assessment

Assessment u/s 143(3) should be completed within 12 months from the end of the relevant assessment year.

However, where an updated return u/s 139(8A) is furnished, an order of assessment u/s 143 may be made at any time before the expiry of 12 months from the end of the financial year in which such return was furnished.

Special procedure in case of research association etc. [First Proviso to Sec. 143(3)]

Applicable to

- Research association referred in sec. 10(21);
- News agency referred in sec. 10(22B);
- Association or institution referred in sec. 10(23A);
- institution referred in sec. 10(23B);

  - which is required to furnish the return of income u/s 139(4C)

Assessment Order

Order for assessment of such assessee shall be made after giving effect to the provisions of sec. 10. However, in the following case assessment of such assessee shall be made without giving effect to the provisions of sec. 10—

a. The Assessing Officer has intimated the Central Government or the prescribed authority about contravention made by above assessee of respective provision of sec. 10 on the basis of which exemption has been granted; and

b. Approval granted to such assessee has been withdrawn or rescinded by such authority.

Special procedure in case of trust, etc. [Second Proviso to Sec. 143(3)]

Applicable to

- Fund or institution referred to in sec. 10(23C)(iv); or
- Trust or institution referred to in sec. 10(23C)(v); or
- Any university or other educational institution referred to in sec. 10(23C)(vi); or
- Any hospital or other medical institution referred to in sec. 10(23C)(via); or
- Any trust or institution referred to in sec. 11

Assessment Order

Where the Assessing Officer is satisfied that aforesaid assessee has committed any specified violation as defined in Explanation 2 to the fifteenth proviso to sec. 10(23C) or the Explanation to sec. 12AB(4), as the case may be, he shall:

a. send a reference to the Principal Commissioner or Commissioner to withdraw the approval or registration, as the case may be; and

b. no order making an assessment of the total income or loss of such assessee shall be made by him without giving effect to the order passed by the Principal Commissioner or Commissioner on this matter.

Special procedure in case of university, etc. [Third Proviso to Sec. 143(3)]

Applicable to: University, college or other institution referred to in sec. 35(1)(ii) and (iii)

Assessment Order

Where the Assessing Officer is satisfied that the activities of such assessee are not being carried out in accordance with all or any of the conditions subject to which such university, college or other institution was approved, he may, after giving a reasonable opportunity of showing cause against the proposed withdrawal to the concerned university, college or other institution, recommend to the Central Government to withdraw the approval and that Government may by order, withdraw the approval and forward a copy of the order to the concerned university, college or other institution and the Assessing Officer

2.2.8 Best Judgment Assessment [Sec. 144]

Under this section, assessment shall be made by the Assessing Officer to the best of his judgment after considering all relevant materials which he has gathered.

Assessing Officer cannot reduce the tax liability of the assessee by assessment under this section.

Taxpoint: A refund cannot be granted u/s 144.

Situation in which it is applicable: In the following situations assessment shall be made under this section -

a. If the person fails to file the return u/s 139(1), 139(4) or 139(5) or an updated return u/s 139(8A); or

b. If the person fails to comply with the terms of notice u/s 142(1); or

c. If the person fails to comply with the directions u/s 142(2A) requiring him to get his accounts audited; or

d. If the person fails to comply with the terms of notice u/s 143(2), requiring his presence or production of evidence and documents.

Note: In any of the given situation, the Assessing Officer is *under an obligation* to make an assessment under this section. In other words, Best judgment assessment is not the discretionary power of the Assessing Officer but mandatory in nature.

Opportunity of being heard

The assessment u/s 144 can only be made after giving the assessee a reasonable opportunity of being heard. Such opportunity shall be given by serving a "Show cause notice" calling upon the assessee to show cause(s), on a date and time specified in the notice, why the assessment should not be completed to the best of judgment of the Assessing Officer.

Exception: Such opportunity need not be given, where notice u/s 142(1) has already been issued.

Time limit for completion of assessment [Sec. 153(1)]

12 months from the end of relevant assessment year. However, where an updated return u/s 139(8A) is furnished, an order of assessment u/s 144 may be made at any time before the expiry of 12 months from the end of the financial year in which such return was furnished.

Other points

Non-maintenance of proper accounts: As per sec. 145(3), if the Assessing Officer is not satisfied with the correctness or the completeness of the accounts of the assessee or if no regular method of accountancy or accounting standards [as notified by the Central Government u/s 145(2)] is followed by the assessee, the Assessing Officer may make an assessment in the manner provided u/s 144.

2.2.9 Power of Joint Commissioner to issue directions in certain cases [Sec. 144A]

Joint Commissioner may (on his own motion or on a reference being made to him by the Assessing Officer or on the application of an assessee) -

a) Call for and examine the record of any proceeding in which an assessment is pending; and

b) Having regard to the nature of the case or the amount involved or for any other reason,

- issue such directions as he thinks fit for the guidance of the Assessing Officer to enable him to complete the assessment and such directions shall be binding on the Assessing Officer.

Note: Directions, which are prejudicial to the assessee, shall not be issued without giving the assessee an opportunity of being heard. However, the direction of investigation shall not be deemed to be a direction prejudicial to the assessee.

2.2.10 Faceless Assessment [Sec. 144B]

The assessment, reassessment or recomputation u/s 143(3) or 144 or 147, as the case may be, with respect to the cases [in respect of such territorial area, or persons or class of persons, or incomes or class of incomes, or cases or class of cases, as may be specified by the Board], shall be made in a faceless manner as per the following procedure, namely:—

i. the National Faceless Assessment Centre (here-in-after referred to as NaFAC) shall assign the case selected for the purposes of faceless assessment under this section to a specific assessment unit through an automated allocation system;

ii. the NaFAC shall intimate the assessee that assessment in his case shall be completed in accordance with the procedure laid down under this section.

iii. a notice shall be served on the assessee, through the National Faceless Assessment Centre, u/s 143(2) or u/s 142(1) and the assessee may file his response to such notice within the date specified therein, to the NaFAC which shall forward the same to the assessment unit;

iv. where a case is assigned to the assessment unit, it may make a request through the NaFAC for:

   a. obtaining such further information, documents or evidence from the assessee or any other person, as it may specify;

   b. conducting of enquiry or verification by verification unit;

   c. seeking technical assistance in respect of determination of arm's length price, valuation of property, withdrawal of registration, approval, exemption or any other technical matter by referring to the technical unit;

v. where a request [for (a) supra] has been initiated by the assessment unit, the NaFAC shall serve appropriate notice or requisition on the assessee or any other person for obtaining the information, documents or evidence requisitioned by the assessment unit and the assessee or any other person, as the case may be, shall file his response to such notice within the time specified therein or such time as may be extended on the basis of an application in this regard, to the NaFAC which shall forward the reply to the assessment unit;

vi. where a request,—

   a. for conducting of enquiry or verification by the verification unit has been made by the assessment unit [for (b) supra], the request shall be assigned by the NaFAC to a verification unit through an automated allocation system; or

b. for reference to the technical unit has been made by the assessment unit [for (c) supra], the request shall be assigned by the NaFAC to a technical unit through an automated allocation system;

vii. the NaFAC shall send the report received from the verification unit or the technical unit, as the case may be, based on the request to the concerned assessment unit;

viii. where the assessee fails to comply with the notice served [as per (v) above or notice issued u/s 142(1)] or the terms of notice issued u/s 143(2), the NaFAC shall intimate such failure to the assessment unit;

ix. the assessment unit shall serve upon such assessee, as referred to in (viii) above, a notice, through the National Faceless Assessment Centre, u/s 144, giving him an opportunity to show-cause on a date and time as specified in such notice as to why the assessment in his case should not be completed to the best of its judgment;

x. the assessee shall, within the time specified in the aforesaid notice or such time as may be extended on the basis of an application in this regard, file his response to the NaFAC which shall forward the same to the assessment unit;

xi. where the assessee fails to file response to the notice served [clause (ix)] within the time specified therein or within the extended time, if any, the NaFAC shall intimate such failure to the assessment unit;

xii. the assessment unit shall, after taking into account all the relevant material available on the record, prepare, in writing,:

a. an income or loss determination proposal, where no variation prejudicial to assessee is proposed and send a copy of such income or loss determination proposal to the National Faceless Assessment Centre; or

b. in any other case, a show cause notice stating the variations prejudicial to the interest of assessee proposed to be made to the income of the assessee and calling upon him to submit as to why the proposed variation should not be made and serve such show cause notice, on the assessee, through the National Faceless Assessment Centre;

xiii. the assessee shall file his reply to the show cause notice served under clause (xii)(b) on a date and time as specified therein or such time as may be extended on the basis of an application made in this regard, to the National Faceless Assessment Centre, which shall forward the reply to the assessment unit;

xiv. where the assessee fails to file response to the notice served under clause (xii)(b) within the time specified therein or within the extended time, if any, the NaFAC shall intimate such failure to the assessment unit;

xv. the assessment unit shall, after considering the response received [clause (xiii)] or after receipt of intimation [clause (xiv)], as the case may be, and taking into account all relevant material available on record, prepare an income or loss determination proposal and send the same to the National Faceless Assessment Centre;

xvi. upon receipt of the income or loss determination proposal, as referred to in clause (xii)(a) or clause (xv), as the case may be, the NaFAC may, on the basis of guidelines issued by the Board,—

a. convey to the assessment unit to prepare draft order in accordance with the income or loss determination proposal, which shall thereafter prepare a draft order; or

b. assign the income or loss determination proposal to a review unit through an automated allocation system, for conducting review of such proposal;

xvii. the review unit shall conduct review of the income or loss determination proposal assigned to it by the National Faceless Assessment Centre, under clause (xvi)(b), whereupon it shall prepare a review report and send the same to the National Faceless Assessment Centre;

xviii. the NaFAC shall, upon receiving the aforesaid review report, forward the same to the assessment unit which had proposed the income or loss determination proposal;

xix. the assessment unit shall, after considering such review report, accept or reject some or all of the modifications proposed therein and after recording reasons in case of rejection of such modifications, prepare a draft order;

xx. the assessment unit shall send such draft order prepared under clause (xvi)(a) or (xix) to the National Faceless Assessment Centre;

xxi. in case of an eligible assessee, where there is a proposal to make any variation which is prejudicial to the interest of such assessee, as mentioned in sec. 144C(1), the NaFAC shall serve the aforesaid draft order on the assessee;

xxii. in any other case, the NaFAC shall convey to the assessment unit to pass the final assessment order in accordance with such draft order, which shall thereafter pass the final assessment order and initiate penalty proceedings, if any, and send it to the National Faceless Assessment Centre;

xxiii. upon receiving the final assessment order, the NaFAC shall serve a copy of such order and notice for initiating penalty proceedings, if any, on the assessee, along with the demand notice, specifying the sum payable by, or refund of any amount due to, the assessee on the basis of such assessment;

xxiv. where a draft order is served on the assessee as referred to in clause (xxi), such assessee shall,

a. file his acceptance of the variations proposed in such draft order to the National Faceless Assessment Centre; or

b. file his objections, if any, to such variations, with—

I. the Dispute Resolution Panel, and

II. the National Faceless Assessment Centre,

- within the period specified in sec. 144C(2);

xxv. the NaFAC shall,—

a. upon receipt of acceptance from the eligible assessee; or

b. if no objections are received from the eligible assessee, within the period specified in sec. 144C(2),

- intimate the assessment unit to complete the assessment on the basis of the draft order;

xxvi. the assessment unit shall, upon receipt of intimation [clause (xxv)], pass the assessment order, in accordance with the relevant draft order, within the time allowed u/s 144C(4) and initiate penalty proceedings, if any, and send the order to the National Faceless Assessment Centre;

xxvii. where the eligible assessee files objections with the Dispute Resolution Panel, [clause (xxiv)(b)], the NaFAC shall send such intimation along with a copy of objections filed to the assessment unit;

xxviii. the NaFAC shall, in such case [clause (xxvii)], upon receipt of the directions issued by the Dispute Resolution Panel u/s 144C(5), forward such directions to the assessment unit;

xxix. the assessment unit shall, in conformity with the directions issued by the Dispute Resolution Panel u/s 144C(5), complete the assessment within the time allowed in sec. 144C(13) and initiate penalty proceedings, if any, and send a copy of the assessment order to the National Faceless Assessment Centre;

xxx. the NaFAC shall, upon receipt of the assessment order referred to in clause (xxvi) or clause (xxix), as the case may be, serve a copy of such order and notice for initiating penalty proceedings, if any, on the assessee,

along with the demand notice, specifying the sum payable by, or the amount of refund due to, the assessee on the basis of such assessment;

xxxi. the NaFAC shall, after completion of assessment, transfer all the electronic records of the case to the Assessing Officer having jurisdiction over the said case for such action as may be required under the provisions of this Act;

xxxii. if at any stage of the proceedings before it, the assessment unit having regard to the nature and complexity of the accounts, volume of the accounts, doubts about the correctness of accounts, multiplicity of transactions in the accounts or specialised nature of business activity of the assessee, and the interests of the revenue, is of the opinion that it is necessary to do so, it may, upon recording its reasons in writing, refer the case to the NaFAC stating that the provisions of sec. 142(2A) may be invoked and such case shall be dealt with in accordance with the provisions of sec. 144B(7).

Taxpoint

- The Board may, for the purposes of faceless assessment, set up the following Centres and units and specify their functions and jurisdiction, namely:

  i. a NaFAC to facilitate the conduct of faceless assessment proceedings in a centralised manner;

  ii. such assessment units, as it may deem necessary to conduct the faceless assessment, to perform the function of making assessment, which includes identification of points or issues material for the determination of any liability (including refund) under this Act, seeking information or clarification on points or issues so identified, analysis of the material furnished by the assessee or any other person, and such other functions as may be required for the purposes of making faceless assessment, and the term "assessment unit", wherever used in this section, shall refer to an Assessing Officer having powers so assigned by the Board;

  iii. such verification units, as it may deem necessary to facilitate the conduct of faceless assessment, to perform the function of verification, which includes enquiry, cross verification, examination of books of account, examination of witnesses and recording of statements, and such other functions as may be required for the purposes of verification and the term "verification unit", wherever used in this section, shall refer to an Assessing Officer having powers so assigned by the Board:

     - Further, the function of verification unit under this section may also be performed by a verification unit located in any other faceless centre set up under the provisions of this Act or under any scheme notified under the provisions of this Act; and the request for verification may also be assigned through the NaFAC to such verification unit;

  iv. such technical units, as it may deem necessary to facilitate the conduct of faceless assessment, to perform the function of providing technical assistance which includes any assistance or advice on legal, accounting, forensic, information technology, valuation, transfer pricing, data analytics, management or any other technical matter under this Act or an agreement entered into u/s 90 or 90A, which may be required in a particular case or a class of cases, under this section and the term "technical unit", wherever used in this section, shall refer to an Assessing Officer having powers so assigned by the Board;

  v. such review units, as it may deem necessary to facilitate the conduct of faceless assessment, to perform the function of review of the income determination proposal assigned under clause (xvi)(b) [supra], which includes checking whether the relevant and material evidence has been brought on record, relevant points of fact and law have been duly incorporated, the issues requiring addition or disallowance have been incorporated and such other functions as may be required for the purposes of review and the term "review unit", wherever used in this section, shall refer to an Assessing Officer having powers so assigned by the Board.

- The assessment unit, verification unit, technical unit and the review unit shall have the following authorities, namely:

  i. Additional Commissioner or Additional Director or Joint Commissioner or Joint Director, as the case may be;

  ii. Deputy Commissioner or Deputy Director or Assistant Commissioner or Assistant Director, or Income-tax Officer, as the case may be;

  iii. such other income-tax authority, ministerial staff, executive or consultant, as may be considered necessary by the Board.

- All communications,

  i. among the assessment unit, review unit, verification unit or technical unit or with the assessee or any other person with respect to the information or documents or evidence or any other details, as may be necessary for the purposes of making a faceless assessment shall be through the National Faceless Assessment Centre;

  ii. between the NaFAC and the assessee, or his authorised representative, or any other person shall be exchanged exclusively by electronic mode; and

  iii. between the NaFAC and various units shall be exchanged exclusively by electronic mode:

  The said provisions shall not apply to the enquiry or verification conducted by the verification unit in the circumstances as may be specified by the Board in this behalf.

- For the purposes of faceless assessment—

  i. an electronic record shall be authenticated by—

    a. the NaFAC by way of an electronic communication;

    b. the assessment unit or verification unit or technical unit or review unit, as the case may be, by affixing digital signature;

    c. assessee or any other person, by affixing his digital signature or under electronic verification code, or by logging into his registered account in the designated portal;

  ii. every notice or order or any other electronic communication shall be delivered to the addressee, being the assessee, by way of—

    a. placing an authenticated copy thereof in the registered account of the assessee; or

    b. sending an authenticated copy thereof to the registered email address of the assessee or his authorised representative; or

    c. uploading an authenticated copy on the Mobile App of the assessee,

    - and followed by a real time alert;

  iii. every notice or order or any other electronic communication shall be delivered to the addressee, being any other person, by sending an authenticated copy thereof to the registered email address of such person, followed by a real time alert;

  iv. the assessee shall file his response to any notice or order or any other electronic communication, through his registered account, and once an acknowledgement is sent by the NaFAC containing the hash result generated upon successful submission of response, the response shall be deemed to be authenticated;

v. the time and place of dispatch and receipt of electronic record shall be determined in accordance with the provisions of sec. 13 of the Information Technology Act, 2000;

vi. a person shall not be required to appear either personally or through authorised representative in connection with any proceedings before any unit set up under this section;

vii. in a case where a variation is proposed in the income or loss determination proposal or the draft order, and an opportunity is provided to the assessee by serving a notice calling upon him to show cause as to why the assessment should not be completed as per such income or loss determination proposal, the assessee or his authorised representative, as the case may be, may request for personal hearing so as to make his oral submissions or present his case before the income-tax authority of the relevant unit;

viii. where the request for personal hearing has been received, the income-tax authority of relevant unit shall allow such hearing, through National Faceless Assessment Centre, which shall be conducted exclusively through video conferencing or video telephony, including use of any telecommunication application software which supports video conferencing or video telephony, to the extent technologically feasible, in accordance with the procedure laid down by the Board;

ix. any examination or recording of the statement of the assessee or any other person (other than the statement recorded in the course of survey u/s 133A) shall be conducted by an income-tax authority in the relevant unit, exclusively through video conferencing or video telephony, including use of any telecommunication application software which supports video conferencing or video telephony, to the extent technologically feasible, in accordance with the procedure laid down by the Board [this provision is subject to the proviso to sec. 144B(5)],

x. the Board shall establish suitable facilities for video conferencing or video telephony including telecommunication application software which supports video conferencing or video telephony at such locations as may be necessary, so as to ensure that the assessee, or his authorised representative, or any other person is not denied the benefit of faceless assessment merely on the consideration that such assessee or his authorised representative, or any other person does not have access to video conferencing or video telephony at his end;

xi. the Principal Chief Commissioner or the Principal Director General, as the case may be, in-charge of the NaFAC shall, with the prior approval of the Board, lay down the standards, procedures and processes for effective functioning of the NaFAC and the units set up, in an automated and mechanised environment.

(a) The Principal Chief Commissioner or the Principal Director General, as the case may be, in-charge of the NaFAC shall, in accordance with the procedure laid down by the Board in this regard, if he considers appropriate that the provisions of sec. 142(2A) may be invoked in the case,:

i. forward the reference received from an assessment unit under clause (xxxii) of to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner having jurisdiction over such case, and inform the assessment unit accordingly;

ii. transfer the case to the Assessing Officer having jurisdiction over such case;

(b) where aforesaid reference has been received by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, he shall direct the Assessing Officer, having jurisdiction over the case, to invoke the provisions of sec. 142(2A);

(c) where a reference has not been forwarded to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, having jurisdiction over the case, the assessment unit shall proceed to complete the assessment in accordance with the procedure laid down in this section – Sec. 144B(7)

- The Principal Chief Commissioner or the Principal Director General, as the case may be, in-charge of NaFAC may, at any stage of the assessment, if considered necessary, transfer the case to the Assessing Officer having jurisdiction over such case, with the prior approval of the Board.

Definitions

- "automated allocation system" means an algorithm for randomised allocation of cases, by using suitable technological tools, including artificial intelligence and machine learning, with a view to optimise the use of resources;
- "automated examination tool" means an algorithm for standardised examination of draft orders, by using suitable technological tools, including artificial intelligence and machine learning, with a view to reduce the scope of discretion;
- "computer resource of assessee" shall include assessee's registered account in designated portal of the Income-tax Department, the Mobile App linked to the registered mobile number of the assessee, or the registered e-mail address of the assessee with his e-mail service provider;
- "designated portal" means the web portal designated as such by the Principal Chief Commissioner or Principal Director General, in charge of the National Faceless Assessment Centre;
- "faceless assessment" means the assessment proceedings conducted electronically in 'e-Proceeding' facility through assessee's registered account in designated portal;
- "eligible assessee" shall have the same meaning as assigned to in sec. 114C(15)(b);
- "e-mail" or "electronic mail" and "electronic mail message" means a message or information created or transmitted or received on a computer, computer system, computer resource or communication device including attachments in text, image, audio, video and any other electronic record, which may be transmitted with the message;
- "electronic verification code" means a code generated for the purpose of electronic verification as per the data structure and standards specified by the Principal Director General or Director General, as the case may be, in-charge of information technology;
- "Mobile app" shall mean the application software of the Income-tax Department developed for mobile devices which is downloaded and installed on the registered mobile number of the assessee;
- "real time alert" means any communication sent to the assessee, by way of Short Messaging Service on his registered mobile number, or by way of update on his Mobile App, or by way of an e-mail at his registered e-mail address, so as to alert him regarding delivery of an electronic communication;
- "registered account" of the assessee means the electronic filing account registered by the assessee in designated portal;
- "registered e-mail address" means the e-mail address at which an electronic communication may be delivered or transmitted to the addressee, including—

  a. the e-mail address available in the electronic filing account of the addressee registered in designated portal; or

     i. the e-mail address available in the last income-tax return furnished by the addressee; or

     ii. the e-mail address available in the Permanent Account Number database relating to the addressee; or

     iii. in the case of addressee being an individual who possesses the Aadhaar number, the e-mail address of addressee available in the database of Unique Identification Authority of India; or

iv. in the case of addressee being a company, the e-mail address of the company as available on the official website of Ministry of Corporate Affairs; or

v. any e-mail address made available by the addressee to the income-tax authority or any person authorised by such authority.

- "registered mobile number" of the assessee means the mobile number of the assessee, or his authorised representative, appearing in the user profile of the electronic filing account registered by the assessee in designated portal;
- "video conferencing or video telephony" means the technological solutions for the reception and transmission of audio-video signals by users at different locations, for communication between people in real-time.

2.2.11 Reference to Dispute Resolution Panel [Sec. 144C]

The dispute resolution mechanism presently in place is time consuming and finality in high demand cases is attained only after a long drawn litigation till Supreme Court. Flow of foreign investment is extremely sensitive to prolonged uncertainity in tax related matter. Therefore, the Income-tax Act is amended to provide for an alternate dispute resolution mechanism which will facilitate expeditious resolution of disputes in a fast track basis. The provision relating to alternate dispute resolution mechanism are as under:

1. The Assessing Officer shall, in the first instance, forward a draft of the proposed order of assessment (hereafter in this section referred to as the draft order) to the eligible assessee[#] if he proposes to make any variation which is prejudicial to the interest of such assessee.

   [#] Eligible assessee means:

   (i) Any person in whose case the variation referred to arises as a consequence of the order of the Transfer Pricing Officer passed u/s 92CA(3); and

   (ii) Any non resident person not being a company or a foreign company

2. On receipt of the draft order, the eligible assessee shall, within 30 days of the receipt by him of the draft order:

   (a) File his acceptance of the variations to the Assessing Officer; or

   (b) File his objections, if any, to such variation with,—

      (i) The Dispute Resolution Panel; and

      (ii) The Assessing Officer.

   [$] Dispute Resolution Panel means a collegium comprising of 3 Commissioners of Income-tax constituted by the Board for this purpose.

3. The Assessing Officer shall complete the assessment on the basis of the draft order, if:

   (a) The assessee intimates to the Assessing Officer the acceptance of the variation; or

   (b) No objections are received within 30 days as specified above.

   Time limit for passing of order: The Assessing Officer shall pass such order within 1 month from the end of the month in which,—

   (i) The acceptance is received; or

   (ii) The period of filing of objections (i.e. 30 days) expires.

The time limit is irrespective of time limit given u/s 153 for passing an assessment order.

4. The Dispute Resolution Panel shall, in a case where any objections are received, issue such directions, as it thinks fit, for the guidance of the Assessing Officer to enable him to complete the assessment.
5. The Dispute Resolution Panel shall issue the directions, for guidance of the Assessing Officer, after considering the following:
   a. Draft order;
   b. Objections filed by the assessee;
   c. Evidence furnished by the assessee;
   d. Report, if any, of the Assessing Officer, Valuation Officer or Transfer Pricing Officer or any other authority;
   e. Records relating to the draft order;
   f. Evidence collected by it; and
   g. Result of any enquiry made by it.
6. The Dispute Resolution Panel may, before issuing any directions:
   a. Make such further enquiry, as it thinks fit; or
   b. Cause any further enquiry to be made by any income tax authority and report the result of the same to it.
7. The Panel may confirm, reduce or enhance the variations proposed in the draft order so, however, that it shall not set aside any proposed variation or issue any direction for further enquiry and passing of the assessment order.
8. If the members of the Panel differ in opinion on any point, the point shall be decided according to the opinion of the majority of the members.
9. Every direction issued by the Dispute Resolution Panel shall be binding on the Assessing Officer.
10. No direction shall be issued unless an opportunity of being heard is given to the assessee and the Assessing Officer on such directions which are prejudicial to the interest of the assessee or the interest of the revenue, respectively.
11. No direction shall be issued after 9 months (irrespective of any limitation given u/s 153) from the end of the month in which the draft order is forwarded to the eligible assessee.
12. Upon receipt of the directions, the Assessing Officer shall, in conformity with the directions, complete, the assessment without providing any further opportunity of being heard to the assessee, within 1 month from the end of the month in which the direction is received.
13. The provisions of this section shall not apply to any assessment or reassessment order passed by the Assessing Officer with the prior approval of the Principal Commissioner or Commissioner as provided in sec. 144BA
14. The Board may make rules for the efficient functioning of the Dispute Resolution Panel and expeditious disposal of the objections filed by the eligible assessee.
15. The Central Government may make a scheme for the purposes of issuance of directions by the dispute resolution panel, so as to impart greater efficiency, transparency and accountability by—
   a. eliminating the interface between the dispute resolution panel and the eligible assessee or any other person to the extent technologically feasible;

b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a mechanism with dynamic jurisdiction for issuance of directions by dispute resolution panel.

2.2.12 Reference to Pr. Commissioner or Commissioner in certain cases [Sec. 144BA][1]

1. If, the Assessing Officer, at any stage of the assessment or reassessment proceedings before him having regard to the material and evidence available, considers that it is necessary to declare an arrangement as an impermissible avoidance arrangement and to determine the consequence of such an arrangement within GAAR[1], then, he may make a reference to the Principal Commissioner or Commissioner in this regard.
2. The Principal Commissioner or Commissioner shall, on receipt of a reference, if he is of the opinion that the provisions of GAAR are required to be invoked, issue a notice to the assessee, setting out the reasons and basis of such opinion, for submitting objections, if any, and providing an opportunity of being heard to the assessee within such period, not exceeding 60 days, as may be specified in the notice.
3. If the assessee does not furnish any objection to the notice within the time specified in the notice, the Principal Commissioner or Commissioner shall issue such directions as he deems fit in respect of declaration of the arrangement to be an impermissible avoidance arrangement.
4. In case the assessee objects to the proposed action, and the Principal Commissioner or Commissioner after hearing the assessee in the matter is not satisfied by the explanation of the assessee, then, he shall make a reference in the matter to the Approving Panel for the purpose of declaration of the arrangement as an impermissible avoidance arrangement.
5. If the Principal Commissioner or Commissioner is satisfied, after having heard the assessee that the provisions of GAAR are not to be invoked, he shall by an order in writing, communicate the same to the Assessing Officer with a copy to the assessee.
6. The Approving Panel, on receipt of a reference from the Principal Commissioner or Commissioner [as per 4 supra], shall issue such directions, as it deems fit, in respect of the declaration of the arrangement as an impermissible avoidance arrangement in accordance with the provisions of GAAR including specifying of the previous year or years to which such declaration of an arrangement as an impermissible avoidance arrangement shall apply.
7. Such direction shall not be issued unless an opportunity of being heard is given to the assessee and the Assessing Officer on such directions which are prejudicial to the interest of the assessee or the interests of the revenue, as the case may be.
8. The Approving Panel may, before issuing any direction:
   i. if it is of the opinion that any further inquiry in the matter is necessary, direct the Principal Commissioner or Commissioner to make such inquiry or cause the inquiry to be made by any other income-tax authority and furnish a report containing the result of such inquiry to it; or
   ii. call for and examine such records relating to the matter as it deems fit; or
   iii. require the assessee to furnish such documents and evidence as it may direct.

[2] Due to the introduction of the faceless assessment scheme, the provision is applicable subject to certain exceptions, modifications, and adaptations given under Notification No. 62/2019 (as amended).

[3] General Anti-Avoidance Rule (GAAR)

9. If the members of the Approving Panel differ in opinion on any point, such point shall be decided according to the opinion of the majority of the members.

10. The Assessing Officer, on receipt of directions of the Principal Commissioner or Commissioner or of the Approving Panel, shall proceed to complete the proceedings in accordance with such directions and the provisions of GAAR.

11. If any direction specifies that declaration of the arrangement as impermissible avoidance arrangement is applicable for any previous year other than the previous year to which the proceedings pertains, then, the Assessing Officer while completing any assessment or reassessment proceedings of the assessment year relevant to such other previous year shall do so in accordance with such directions and the provisions of GAAR and it shall not be necessary for him to seek fresh direction on the issue for the relevant assessment year.

12. No order of assessment or reassessment shall be passed by the Assessing Officer without the prior approval of the Principal Commissioner or Commissioner, if any tax consequences have been determined in the order under the provisions of GAAR.

13. The Approving Panel shall issue directions within a period of 6 months from the end of the month in which the reference was received.

    Taxpoint: In computing the period, the following shall be excluded:

    i. the period commencing from the date on which the first direction is issued by the Approving Panel to the Principal Commissioner or Commissioner for getting the inquiries conducted through the authority competent under an agreement referred to in sec. 90 or 90A and ending with the date on which the information so requested is last received by the Approving Panel or 1 year, whichever is less;

    ii. the period during which the proceeding of the Approving Panel is stayed by an order or injunction of any court

    However, where immediately after the exclusion of the aforesaid time or period, the period available to the Approving Panel for issue of directions is less than 60 days, such remaining period shall be extended to 60 days and the aforesaid period of 6 months shall be deemed to have been extended accordingly.

14. The directions issued by the Approving Panel shall be binding on—

    i. the assessee; and

    ii. the Pr. Commissioner or Commissioner and the income-tax authorities subordinate to him,

    and no appeal under the Act shall lie against such directions.

15. The Central Government shall, for the purposes of this section, constitute one or more Approving Panels as may be necessary and each panel shall consist of three members including a Chairperson.

16. The Chairperson of the Approving Panel shall be a person who is or has been a judge of a High Court, and—

    i. one member shall be a member of Indian Revenue Service not below the rank of Principal Chief Commissioner or Chief Commissioner of Income-tax; and

    ii. one member shall be an academic or scholar having special knowledge of matters, such as direct taxes, business accounts and international trade practices.

17. The term of the Approving Panel shall ordinarily be for one year and may be extended from time to time up to a period of 3 years.

18. The Chairperson and members of the Approving Panel shall meet, as and when required, to consider the references made to the panel and shall be paid such remuneration as may be prescribed.
19. In addition to the powers conferred on the Approving Panel under this section, it shall have the powers which are vested in the Authority for Advance Rulings u/s 245U.
20. The Board shall provide to the Approving Panel such officials as may be necessary for the efficient exercise of powers and discharge of functions of the Approving Panel under the Act.
21. The Board may make rules for the purposes of the constitution and efficient functioning of the Approving Panel and expeditious disposal of the references.

2.2.13 Income Escaping Assessment [Sec. 147]

If any income chargeable to tax, in the case of an assessee, has escaped assessment for any assessment year, the Assessing Officer may, subject to the provisions of sec. 148 to 153, assess or reassess such income or recompute the loss or the depreciation allowance or any other allowance or deduction for such assessment year.

For the purpose of assessment or reassessment or recomputation, the Assessing Officer may assess or reassess the income in respect of any issue, which has escaped assessment, and such issue comes to his notice subsequently in the course of the proceedings under this section, irrespective of the fact that the provisions of sec. 148A have not been complied with.

Issue of notice where income has escaped assessment [Sec. 148]

- **Notice for filing return:** Before making the assessment, reassessment or recomputation u/s 147, and subject to the provisions of sec. 148A, the Assessing Officer shall serve on the assessee a notice, along with a copy of the order passed, if required, u/s 148A(d), requiring him to furnish within 3 months from the end of the month in which such notice is issued, or such further period as may be allowed by the Assessing Officer on the basis of an application made in this regard by the assessee, a return of his income or the income of any other person in respect of which he is assessable under this Act during the previous year corresponding to the relevant assessment year. For filing of such return, provision relating to sec. 139 shall be applicable.

  Taxpoint: Any return of income, required to be furnished by an assessee under this section and furnished beyond the period allowed shall not be deemed to be a return u/s 139.

- **Prior Information and approval:** No notice shall be issued unless there is information with the Assessing Officer which suggests that the income chargeable to tax has escaped assessment in the case of the assessee for the relevant assessment year and the Assessing Officer has obtained prior approval of the specified authority to issue such notice.
  - However, no such approval shall be required where the Assessing Officer, with the prior approval of the specified authority, has passed an order u/s 148A(d) to the effect that it is a fit case to issue a notice under this section.
  - The information with the Assessing Officer which suggests that the income chargeable to tax has escaped assessment means:
    i. Any information in the case of the assessee for the relevant assessment year in accordance with the risk management strategy formulated by the Board from time to time;
    ii. Any audit objection to the effect that the assessment in the case of the assessee for the relevant assessment year has not been made in accordance with the provisions of this Act; or

iii. Any information received under an agreement referred to in sec. 90 or 90A; or

iv. Any information made available to the Assessing Officer under the scheme notified u/s 135A; or

v. Any information which requires action in consequence of the order of a Tribunal or a Court.

- Where,

i. a search is initiated u/s 132 or books of account, other documents or any assets are requisitioned u/s 132A, on or after 01-04-2021, in the case of the assessee; or

ii. a survey is conducted u/s 133A, other than u/s 133A(2A), on or after 01-04-2021, in the case of the assessee; or

iii. the Assessing Officer is satisfied, with the prior approval of the Principal Commissioner or Commissioner, that any money, bullion, jewellery or other valuable article or thing, seized or requisitioned u/s 132 or 132A in case of any other person on or after 01-04-2021, belongs to the assessee; or

iv. the Assessing Officer is satisfied, with the prior approval of Principal Commissioner or Commissioner, that any books of account or documents, seized or requisitioned u/s 132 or 132A in case of any other person on or after 01-04-2021, pertains or pertain to, or any information contained therein, relate to, the assessee,

the Assessing Officer shall be deemed to have information which suggests that the income chargeable to tax has escaped assessment in the case of the assessee where the search is initiated or books of account, other documents or any assets are requisitioned or survey is conducted in the case of the assessee or money, bullion, jewellery or other valuable article or thing or books of account or documents are seized or requisitioned in case of any other person.

Taxpoint: In aforesaid cases, order of assessment or reassessment or recomputation under this Act shall be passed by an Assessing Officer below the rank of Joint Commissioner, with the prior approval of the Additional Commissioner or Additional Director or Joint Commissioner or Joint Director – Sec. 148B.

- Specified authority means the specified authority referred to in sec. 151.

Conducting inquiry, providing opportunity before issue of notice u/s 148 [Sec. 148A]

The Assessing Officer shall, before issuing any notice u/s 148:

a. conduct any enquiry, if required, with the prior approval of specified authority (as referred to in sec. 151), with respect to the information which suggests that the income chargeable to tax has escaped assessment;

b. provide an opportunity of being heard to the assessee, by serving upon him a notice to show cause within such time, as may be specified in the notice, being not less than 7 days and but not exceeding 30 days from the date on which such notice is issued, or such time, as may be extended by him on the basis of an application in this behalf, as to why a notice u/s 148 should not be issued on the basis of information which suggests that income chargeable to tax has escaped assessment in his case for the relevant assessment year and results of enquiry conducted, if any, as per (a);

c. consider the reply of assessee furnished, if any, in response to the show-cause notice referred to in (b);

d. decide, on the basis of material available on record including reply of the assessee, whether or not it is a fit case to issue a notice u/s 148, by passing an order, with the prior approval of specified authority, within 1 month from the end of the month in which the reply is received by him, or where no such reply is furnished, within 1 month from the end of the month in which time or extended time allowed to furnish a reply expires:

Exception

The provisions of this section shall not apply in a case where:

a. a search is initiated u/s 132 or books of account, other documents or any assets are requisitioned u/s 132A in the case of the assessee on or after 01-04-2021; or

b. the Assessing Officer is satisfied, with the prior approval of the Principal Commissioner or Commissioner that any money, bullion, jewellery or other valuable article or thing, seized in a search u/s 132 or requisitioned u/s 132A, in the case of any other person on or after 01-04-2021, belongs to the assessee; or

c. the Assessing Officer is satisfied, with the prior approval of the Principal Commissioner or Commissioner that any books of account or documents, seized in a search u/s 132 or requisitioned u/s 132A, in case of any other person on or after 01-04-2021, pertains or pertain to, or any information contained therein, relate to, the assessee; or

d. The Assessing Officer has received any information under the scheme notified u/s 135A pertaining to income chargeable to tax escaping assessment for any assessment year in the case of the assessee.

Time limit for notice [Sec. 149]

No notice u/s 148 shall be issued for the relevant assessment year:

General Case	Within 3 years from the end of the relevant assessment year, unless the case falls below
Special Case	Within 10 years from the end of the relevant assessment year if the Assessing Officer has in his possession books of account or other documents or evidence which reveal that the income chargeable to tax, represented in the form of: i. an asset; ii. expenditure in respect of a transaction or in relation to an event or occasion; or iii. an entry or entries in the books of account, which has escaped assessment amounts to or is likely to amount to ₹ 50 lakh or more.

Taxpoint:

- For the purposes of computing the period of limitation, the time or extended time allowed to the assessee, as per show-cause notice issued u/s 148A or the period during which the proceeding u/s 148A is stayed by an order or injunction of any court, shall be excluded.
- Where immediately after the exclusion of the said period, the period of limitation available to the Assessing Officer for passing an order u/s 148A does not exceed 7 days, such remaining period shall be extended to seven days and the period of limitation shall be deemed to be extended accordingly.
- "Asset" shall include immovable property, being land or building or both, shares and securities, loans and advances, deposits in bank account.
- No notice shall be issued without getting approval u/s 151
- Where the income chargeable to tax represented in the form of an asset or expenditure in relation to an event or occasion of aforesaid value [i.e., ₹ 50 lakh or more], has escaped the assessment and the investment in such asset or expenditure in relation to such event or occasion has been made or incurred, in more than one previous years relevant to the assessment years within the period [i.e., 10 years], a notice u/s 148 shall be issued for every such assessment year for assessment, reassessment or recomputation, as the case may be.

- In case of search (not survey) referred to in clauses (i), (iii) and (iv) of Explanation 2 to sec. 148, where:
  - a search is initiated u/s 132; or
  - a search u/s 132 for which the last of authorisations is executed; or
  - requisition is made u/s 132A,

  after the 15th day of March of any financial year and the period for issue of notice u/s 148 expires on the 31st day of March of such financial year, a period of 15 days shall be excluded for the purpose of computing the period of limitation and the notice issued u/s 148 in such case shall be deemed to have been issued on the 31st day of March of such financial year.
- Where the information as referred to in Explanation 1 to sec. 148 emanates from a statement recorded or documents impounded u/s 131 or 133A, as the case may be, on or before the 31st day of March of a financial year, in consequence of,—
  - a search u/s 132 which is initiated; or
  - a search u/s 132 for which the last of authorisations is executed; or
  - a requisition made u/s 132A,

  after the 15th day of March of such financial year, a period of 15 days shall be excluded for the purpose of computing the period of limitation and the notice issued u/s 148A(b) in such case shall be deemed to have been issued on the 31st day of March of such financial year.
- As per sec. 150(1), the notice may be issued at any time for the purpose of making assessment or reassessment in consequence of or to give effect to any findings or directions contained in an order passed by -
  - any authority in any proceedings under this Act by way of appeal, reference or revision; or
  - a court in any proceeding under any other law.

  Exception: The provisions shall not apply in any case where any such assessment (reassessment or recomputation) relates to an assessment year in respect of which an assessment (reassessment or recomputation) could not have been made at the time the order which was the subject-matter of the appeal, reference or revision, as the case may be, was made by reason of aforesaid time-limitation.

Sanction for issue of notice [Sec. 151]

Specified authority for the purposes of sec. 148 and 148A shall be:

Case	Specified Authority
Where 3 years have not elapsed from the end of the relevant assessment year	Principal Commissioner or Principal Director or Commissioner or Director
Where more than 3 years have elapsed from the end of the relevant assessment year	Principal Chief Commissioner or Principal Director General or Chief Commissioner or Director General

Taxpoint: The period of 3 years for aforesaid purposes shall be computed after taking into account the period of limitation as excluded or extended by sec. 149

Faceless assessment of income escaping assessment [Sec. 151A]

The Central Government may make a scheme for the purposes of assessment, reassessment or re-computation u/s 147 or issuance of notice u/s 148 or 148A or sanction for issue of such notice u/s 151, so as to impart greater efficiency, transparency and accountability by—

a. eliminating the interface between the income-tax authority and the assessee or any other person to the extent technologically feasible;

b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a team-based assessment, reassessment, re-computation or issuance or sanction of notice with dynamic jurisdiction.

Rate of taxation [Sec. 152(1)]

If an assessment/reassessment is made u/s 147, then tax shall be chargeable at the rates at which it would have been charged had the income not escaped assessment.

When can a reassessment proceeding be dropped [Sec. 152(2)]

Where an assessment is reopened u/s 147 and the assessee -

a) has not opposed any part of the original assessment order for that year either u/s 246 to 248 or u/s 264; and

b) shows that he had been assessed on an amount or to a sum not lower than what he would be rightly liable for even if the income alleged to have escaped assessment had been taken into account, or the assessment or computation had been properly made.

- then the proceedings u/s 147 shall be dropped.

Time limit for completion of assessment u/s 147

No order of assessment, reassessment shall be made u/s 147 after the expiry of 12 months from the **end of the financial year** in which notice u/s 148 was **served**.

However, where an assessment or reassessment is pending on the date of initiation of search u/s 132 or making of requisition u/s 132A, the period available for completion of assessment or reassessment, as the case may be, under the said sections shall,—

a. in a case where such search is initiated u/s 132 or such requisition is made u/s 132A

b. in the case of an assessee, to whom any money, bullion, jewellery or other valuable article or thing seized or requisitioned belongs to

c. in the case of an assessee, to whom any books of account or documents seized or requisitioned pertains or pertain to, or any information contained therein, relates to,

- be extended by 12 months.

2.2.14 Period excluded from time limit for completion of assessment [Expl. 1 to sec. 153]

In computing the time limitation for completion of assessment, following period shall be excluded —

1. Time taken in reopening the whole or any part of the proceeding or in giving an opportunity to the assessee to be re-heard under the proviso to sec. 129; or

2. Period during which the assessment proceeding is stayed by an order or injunction of a court; or

3. Period commencing from the date on which the Assessing Officer intimates under proviso to sec. 143(3) to the Central Government or the prescribed authority, the contravention of the provisions of sec. 10(21) or (22B) or (23A) or (23B) or (23C)(iv) or (23C)(v) or (23C)(vi) or (23C)(via), and ending with the date on which the copy of the order withdrawing the approval or rescinding the notification, as the case may be, under those clauses is received by the Assessing Officer;

4. Period commencing from the date on which the Assessing Officer directs the assessee to get his accounts audited or inventory valuation u/s 142(2A) and ending with the last date on which the assessee is required to

furnish a report of such audit or report (where such direction is challenged before a court, ending with the date on which the order setting aside such direction is received by the Commissioner); or

5. Period commencing from the date on which the Assessing Officer makes a reference to the Valuation Officer u/s 142A and ending with the date on which the report of the Valuation Officer is received by the Assessing Officer; or
6. In a case, where an application made before the Settlement Commission u/s 245C is rejected, the period commencing from the date on which such application is made and ending with the date on which the rejection order is received by the Principal Commissioner or Commissioner; or
7. Period commencing from the date on which an application is made before the Board for Advance Rulings u/s 245Q and ending with the date on which the order rejecting the application is received by the Principal Commissioner or Commissioner; or
8. Period commencing from the date on which an application is made before the Board for Advance Rulings u/s 245Q and ending with the date on which the order of the advance ruling pronounced by the authority is received by the Principal Commissioner or Commissioner; or
9. Period (maximum period of 1 year) commencing from the date on which a reference (or first reference, if many references are made) for exchange of information is made by an authority competent under an agreement referred to in sec. 90 / 90A and ending with the date on which the information so requested is last received by the Principal Commissioner or Commissioner; or
10. Period commencing from the date on which a reference for declaration of an arrangement to be impermissible avoidance arrangement is received by the Principal Commissioner or Commissioner u/s 144BA(1) and ending on the date on which a direction u/s 144BA(3) or (6) or an order u/s 144BA(5) is received by the Assessing Officer
11. Period (not exceeding 180 days) commencing from the date on which a search is initiated u/s 132 or a requisition is made u/s 132A and ending on the date on which the books of account or other documents, or any money, bullion, jewellery or other valuable article or thing seized u/s 132 or requisitioned u/s 132A, as the case may be, are handed over to the Assessing Officer having jurisdiction over the assessee,—
    a. in whose case such search is initiated u/s 132 or such requisition is made u/s 132A; or
    b. to whom any money, bullion, jewellery or other valuable article or thing seized or requisitioned belongs to; or
    c. to whom any books of account or documents seized or requisitioned pertains or pertain to, or any information contained therein, relates to
12. Period commencing from the date on which the Assessing Officer makes a reference to the Principal Commissioner or Commissioner under the second proviso to sec. 143(3) and ending with the date on which the copy of the order under clause (ii) or clause (iii) of the fifteenth proviso to sec. 10(23C) or sec. 12AB(4)(ii) or (iii), as the case may be, is received by the Assessing Officer.

    Note: However, where immediately after the exclusion of the aforesaid time or period, the period available to the Assessing Officer for making an assessment, is less than 60 days, such remaining period shall be extended to 60 days.

Taxpoint

- Where a reference u/s 92CA is made to the transfer pricing officer during the course of the proceeding for the assessment or reassessment, the period available for completion of assessment or reassessment, as the case may be, shall be extended by 12 months.

- Where the Transfer Pricing Officer gives effect to an order or direction u/s 263 by an order u/s 92CA and forwards such order to the Assessing Officer, the Assessing Officer shall proceed to modify the order of assessment or reassessment or recomputation, in conformity with such order of the Transfer Pricing Officer, within 2 months from the end of the month in which such order of the Transfer Pricing Officer is received by him.
- Where the period available to the Transfer Pricing Officer is extended to 60 days [as per proviso to sec. 92CA(3A)] and the period of limitation available to the Assessing Officer for making an order of assessment (reassessment or recomputation) is less than 60 days, such remaining period shall also be extended to 60 days.
- Where the assessee exercises the option to withdraw the application u/s 245M, the period of limitation available to the Assessing Officer for making an order of assessment, reassessment or recomputation, is, after the exclusion of the period u/s 245M(5), less than 1 year, limitation period shall be deemed to have been extended to 1 year.

Summary of time limit for various purposes [Sec. 153]

Particulars	Section	Time limit
Intimation of summary assessment	143(1)	Must be send within 12 months from the end of financial year in which return of income is filed.
Issuance of notice for scrutiny assessment	143(2)	Must be served within 3 months from the end of the financial year in which return of income is filed.
Completion of Scrutiny assessment u/s 143(3)	153(1)	Assessment must be completed within 12 months. However, where an updated return u/s 139(8A) is furnished, an order of assessment u/s 143 or 144 may be made at any time before the expiry of 12 months from the end of the financial year in which such return was furnished.
Completion of Best judgment assessment u/s 144		
Issuance of notice for Income escaping assessment u/s 147	149	Notice must be issued within 3 years (maximum: 10 years) from the end of the relevant assessment year.
Completion of Income escaping assessment u/s 147	153(2)	Assessment must be completed within 12 months from the end of the financial year in which notice for such assessment u/s 148 was served.

Fresh Assessment [Sec. 153(3)]

An order of fresh assessment [or fresh order u/s 92CA] in pursuance of an order u/s 254, 263 or 264 may be made for setting aside or canceling an assessment or an order u/s 92CA.

Time limit for making fresh assessment -

In case of the order passed	Time limit
U/s 254	Within 12 months from the end of the financial year in which such order is received by the Principal Chief Commissioner or Principal Commissioner or Chief Commissioner or Commissioner.
U/s 263 or 264	Within 12 months from the end of the financial year in which such order is passed by the Principal Chief Commissioner or Principal Commissioner or Chief Commissioner or Commissioner.

Note: Where an order is cancelled, then fresh assessment shall be made under the same section [like 143(3) or 144] in which the original assessment was passed.

2.2.15 Demand Notice [Sec.156]

On completion of assessment, a demand notice is *served* for additional demand raised in the assessment.

Time limit for payment of tax: The assessee should make the payment of amount demanded within 30 days of service of notice [Sec. 220(1)] Where the Assessing Officer has any reason to believe that it will be detrimental to revenue if the full period of 30 days is allowed, then he may with the previous approval of the Joint Commissioner direct that the sum specified in the notice of demand shall be paid within such time as may be specified by him in the notice.

Interest on delay in payment: If the payment is not made within 30 days (or time allowed in the notice), interest shall be payable @ 1% for every month (or part thereof) of the delay [Sec. 220(2)]

An assessee in default shall be liable to a penalty of an amount not exceeding the amount of tax in arrears. [Sec. 221(1)]

Note: Where any sum is determined to be payable by the assessee or by the deductor or collector u/s 143(1) or 200A(1) or 206CB(1), the intimation under those sections shall be deemed to be a notice of demand for the purposes of this section.

Modification and revision of notice in certain cases [Sec. 156A]

- Where any tax, interest, penalty, fine or any other sum in respect of which a notice of demand has been issued u/s 156, is reduced as a result of an order of the Adjudicating Authority of the Insolvency and Bankruptcy Code, 2016, the Assessing Officer shall modify the demand payable in conformity with such order and shall thereafter serve on the assessee a notice of demand specifying the sum payable, if any, and such notice of demand shall be deemed to be a notice u/s 156.
- Where the aforesaid order is modified by the National Company Law Appellate Tribunal or the Supreme Court, as the case may be, the modified notice of demand, issued by the Assessing Officer shall be revised accordingly.

Interest and Fees

2.3

Interest payable by the assessee

1. For failure to deduct and pay tax at source [Sec. 201(1A)]
2. For failure to collect and pay tax at source [Sec. 206C(7)]
3. For default in furnishing return of income [Sec. 234A]
4. For default in paying advance tax [Sec. 234B]
5. For deferment of advance tax [Sec. 234C]
6. For excess refund granted to the assessee [Sec. 234D]
7. For failure to pay tax according to demand notice [Sec. 220(2)]

Interest receivable by the assessee

Interest receivable by the assessee on refund [Sec.244A]

Important notes regarding calculation of interest

Following points are to be noted regarding calculation of interest, whether such interest is receivable from or payable to the Central Government (Rule 119A):

1. **Rounding off the amount on which interest is to be calculated**

   Amount on which such interest is calculated will be rounded off to the multiple of 100 by ignoring any fraction of 100. E.g., amount on which interest is to be calculated is ₹ 240 or ₹ 290, then it is to be rounded off to ₹ 200 by ignoring fraction of ₹ 40 or ₹ 90.

2. **Rounding off the period for which interest is to be calculated**

   - When interest is calculated on monthly basis, any fraction of the month shall be taken as full month. E.g., Interest is to be calculated from 1st August to 5th December, then interest shall be calculated for 5 months.
   - When interest is calculated on annual basis, any fraction of the month shall be ignored.

2.3.1 Interest for failure to deduct and pay tax at source [Sec. 201(1A)]

Condition: Where a person, responsible for deducting tax at source, fails to -

(a) deduct tax at source; or

(b) deposit such tax after deducting the same.

Amount on which interest is to be charged: On the amount of such tax.

Rate of Interest:

Period	Rate of Interest
From the date on which such tax was **deductible** to the date on which such tax is **deducted**	Simple interest @ 1% per month or part thereof
From the date on which such tax was **deducted** to the date on which such tax is **actually paid**	Simple interest @ 1.50% per month or part thereof

Period: From the date on which such tax was deductible to the date on which such tax is actually paid.

Note: In case any person fails to deduct such tax on the sum paid or payable but is not deemed to be an assessee in default (as per first proviso to sec. 201(1)), the interest shall be payable from the date on which such tax was deductible to the date of furnishing of return of income by such payee.

2.3.2 Interest for failure to collect and pay tax at source [Sec. 206C(7)]

Condition: Where a person, responsible for collecting tax at source, fails to -

(a) collect tax at source; or

(b) deposit such tax after collecting the same.

Amount on which interest is to be charged: On the amount of such tax

Rate of Interest: Simple interest @ 1% per month or part thereof

Period: From the date on which such tax was collectible to the date on which such tax is actually paid.

Note: Any person (other than seller of bullion or jewellery), responsible for collecting tax, fails to collect such tax on the amount received or receivable from a buyer or licensee or lessee but is not deemed to be an assessee in default (as per First proviso of sec. 206C(6A)], the interest shall be payable from the date on which such tax was collectible to the date of furnishing of return of income by such buyer or licensee or lessee.

2.3.3 Interest for default in furnishing return of income [Sec. 234A]

Condition: Where a person, who is required to furnish return of income -

(a) fails to furnish a return; or

(b) furnishes it after the due date specified u/s 139(1).

Amount on which interest is to be charged: On the amount of tax determined u/s 143(1) or on regular assessment as reduced by advance tax paid and tax deducted or collected at source, if any.

In other words, interest is to be calculated on the following amount:

Particulars	Amount	Amount
Tax determined u/s 143(1) or on Regular assessment*		***
Less: Advance Tax paid	***	
Relief u/s 89 or 90 or 90A or 91	***	
Credit allowed u/s 115JAA / 115JD (MAT or AMT Credit)	***	
Tax deducted/collected at source	***	***
Amount for interest calculation		***

* Regular Assessment means assessment u/s 143(3)/144/147 (first time)/153A(first time).

Rate of Interest: Simple interest @ 1% per month or part thereof

Period: For every month or part of a month commencing from the day immediately following the due date for furnishing return for the relevant assessment year and ending on -

- Where the return is furnished after due date : Date of furnishing return
- Where the return is not furnished at all : Date of completion of assessment u/s 144

Notes:

1. For the purpose of self-assessment u/s 140A, interest shall be calculated on tax liability as declared in the return by the assessee.
2. As interest liability u/s 234A is different, in case of assessment by assessee himself (i.e. self- assessment) and assessment made by income tax authority (i.e. assessment u/s 143(1) or regular assessment), therefore, interest paid u/s 234A at the time of self-assessment shall be reduced from final interest liability u/s 234A.
3. The liability u/s 234A, 234B & 234C is automatic and the question of granting opportunity of being heard does not arise
4. Demand notice for interest u/s 234A, 234B & 234C shall not be issued unless assessment order contains such levy.
5. No interest u/s 234A is chargeable on the amount of self-assessment tax paid by the assessee before the due date of filing of return of income [Circular No 2/2015 dated 10/2/ 2015]
6. **Updated Return u/s 139(8A)**: Where an assessee has not filed any return u/s 139(1) or 139(4) and he is filing an updated return u/s 139(8A), then, interest u/s 234A is payable on tax computed on the total income as declared in the updated return for the period commencing from the date immediately following the due date of filing original return and ending with the date on which the updated return is furnished.
7. "Tax on total income as determined u/s 143(1)" shall not include the additional income-tax, if any, payable u/s 140B or 143.
8. "Tax on the total income determined under regular assessment shall not include the additional income-tax payable u/s 140B.
9. **Reassessment**: Where -

   a) a return of income is required to be furnished due to notice u/s 148 or 153A (second and subsequent time); &

b) assessee fails to furnish such return within time allowed under that section or fails to furnish return of income at all,

- then, assessee shall be liable to pay simple interest @ 1% for every month or part thereof.

Amount on which interest is to be charged: On the amount by which tax on total income as per sec.147, exceeds the tax on the total income determined on the basis of earlier assessment

Period: Commencing on the day immediately following the expiry of the time allowed under that notice and ending on –

- Where the return is furnished after the expiry of time allowed : Date of furnishing return
- Where the return is not furnished at all : Date of completion of reassessment u/s 147 or 153A

7. Adjustment in interest: Where tax payable is reduced or increased by an order u/s 154, 155, 245D, 250, 254, 260, 262, 263 & 264, the amount of interest shall be reduced or increased accordingly.

Illustration 1:

Calculate interest u/s 234A in the following cases –

Name of the assessee	A	A Ltd.	B
Due date of furnishing return	31st July	31st October	31st July
Date of filing return	4th December	28th December	Not filed
Date of completion of assessment	1st March	15th April	15th February
Income as per return	₹ 8,80,000	₹ 5,00,000	--
Assessed Income	₹ 9,10,000	₹ 5,50,000	₹ 12,00,000
Advance tax paid	₹ 10,000	₹ 25,000	₹ 10,000
Tax deducted at source	₹ 10,000	₹ 15,000	₹ 3,600
Tax paid along with return	₹ 6,000	₹ 1,50,000	--

Also state interest payable u/s 234A for the purpose of sec.140A. Ignore interest under any other section.

Solution:

Computation of interest u/s 234A

Particulars	Code	A	A Ltd.	B
Period of default	A#	5 months (Aug. to Dec.)	2 months (Nov. to Dec.)	7 months (Aug. to Feb.)
Assessed Income	B	9,10,000	5,50,000	12,00,000
Tax rate	C	Slab-rate	30%	Slab rate
Tax liability before surcharge	D=B*C	46,500	1,65,000	90,000
Rate of Surcharge	E	Nil	Nil	Nil
Surcharge	F=D*E	Nil	Nil	Nil
Tax and surcharge payable	G=D+F	46,500	1,65,000	90,000
Health & Education cess	H=G*4%	1,860	6,600	3,600

Particulars	Code	A	A Ltd.	B
Tax liability on assessed income	I=G+H	48,360	1,71,600	93,600
Less: Advance tax paid & tax deducted at source	J	20,000	40,000	13,600
Shortfall	K=I-J	28,360	1,31,600	80,000
Rounded off	L	28,300	1,31,600	80,000
Interest (1% * A * L)		**1,415**	**2,632**	**5,600**
Note: Tax paid along with return shall not be reduced while computing interest u/s 234A				

Computation of interest u/s 234A for the purpose of sec.140A

Name of the assessee	Code	A	A Ltd.
Period of default	A#	5 months (Aug. to Dec.)	2 months (Nov. to Dec.)
Returned Income	B	8,80,000	5,00,000
Tax rate	C	Slab-rate	30%
Tax liability before surcharge	D = B * C	43,000	1,50,000
Rate of Surcharge	E	Nil	Nil
Surcharge	F = D * E	Nil	Nil
Tax & surcharge on above	G=D+F	43,000	1,50,000
Health & Education cess	H=G*4%	1,720	6,000
Tax liability on assessed income	I=G+H	44,720	1,56,000
Less: Advance tax paid & tax deducted at source	J	24,720	40,000
Shortfall	K=I-J	24,700	1,16,000
Rounded off	L	9,600	1,16,000
Interest (1% * A * L)		**1,235**	**2,320**

It is to be noted that when interest is calculated on monthly basis, any fraction of the month shall be taken as full month.

Note: In case of B, return has not been filed, hence interest payable u/s 234A at the time of self-assessment cannot be computed.

2.3.4 Interest for default in paying advance tax [Sec. 234B]

Condition: Where a person, who is required to pay advance tax, fails to pay -

(a) advance tax at all; or

(b) 90% of assessed tax as advance tax.

Amount on which interest is to be charged –

Particulars	Interest
Where no tax is paid u/s 140A	Assessed tax – Advance tax paid
Where tax is paid u/s 140A	
Period upto the date on which tax as per self-assessment is paid	Assessed tax – Advance tax paid

Particulars	Interest
Period after the date on which the tax as per self assessment is paid	Assessed Tax – Advance tax paid - Tax paid on Self Assessment*
# Assessed tax means tax determined u/s 143(1) or Regular assessment as reduced by - Tax deducted or collected at source; - Relief allowed u/s 89 or 90 or 90A or 91; - Credit allowed u/s 115JAA or 115JD (MAT or AMT Credit)	
* Where amount paid under self-assessment falls short of tax and interest calculated as per self-assessment, then amount paid shall be first adjusted towards interest and balance, if any, shall be adjusted towards tax payable.	

Rate of interest: Simple interest @ 1% per month or part thereof

Period: For every month or part of a month commencing from 1st day of April of the relevant assessment year and ending on the date of determination of tax u/s 143(1) or on regular assessment.

Notes

1. For the purpose of self-assessment u/s 140A, interest shall be calculated on tax as per income shown in the return.
2. As interest liability u/s 234B is different in case of assessment by assessee himself (i.e. self- assessment) and assessment made by income tax authority (i.e. assessment u/s 143(1), regular assessment), therefore interest paid u/s 234B at the time of self-assessment shall be reduced from final interest liability u/s 234B.
3. **Updated Return u/s 139(8A)**: Where an assessee has filed any return u/s 139(1) or 139(4) and he is filing an updated return u/s 139(8A), then, assessed tax means the tax on the total income as declared in the updated return as reduced by advance tax, the credit for which has been claimed in the earlier return, if any and TDS/ TCS, tax credit, DTAA relief, etc. Further, assessed tax shall be increased by the amount of refund, if any, issued to the assessee in respect of such earlier return.
4. "Tax on total income as determined u/s 143(1)" shall not include the additional income-tax, if any, payable u/s 140B or 143.
5. "Tax on the total income determined under regular assessment shall not include the additional income-tax payable u/s 140B.
6. **Reassessment**: Where as a result of an order of reassessment or recomputation u/s 147 or 153A, the amount on which interest is payable is increased, the assessee shall be liable to pay simple interest @ 1% for every month or part thereof.

   Amount on which interest is to be charged: Such interest shall be payable on the amount by which tax on total income exceeds the tax on total income determined on the basis of earlier assessment.

   Period -

   Commencing on : 1st day of the relevant assessment year

   Ending on : Date of the reassessment or recomputation u/s 147 or 153A.

7. **Adjustment in interest**: Where tax payable is reduced or increased by an order u/s 154, 155, 245D, 250, 254, 260, 262, 263 & 264, the amount of interest shall be reduced or increased accordingly.

Illustration 2:

A firm furnished its return of income on 30th June, 2024 showing income of ₹ 1,00,000. The return shows other particulars as follows -

Advance tax ₹ 20,000

TDS ₹ 1,000

The AO passed the assessment order enhancing income by ₹ 5,000 on 29-3-2025. Compute interest u/s 234B.

Solution:

Computation of interest u/s 234B

Particulars	Amount
Assessed Income	1,05,000
Tax liability before surcharge [₹ 1,05,000 x 30%]	31,500
Add: Health & Education cess @ 4%	1,260
Tax and cess payable	32,760
Less: Tax deducted at source	1,000
Assessed tax	31,760
90% of above	28,584
Advance tax paid	20,000
Since advance tax paid by the firm is less than 90% of assessed tax, sec. 234B is applicable	
Shortfall (Assessed tax less Advance tax paid)	11,760
Rounded off	11,700
Period of default [From April 2024 to March 2025]	12 months
Interest u/s 234B (1% x ₹ 11,700 x 12)	1,404

Illustration 3:

How shall your answer differ if the assessee pays ₹ 10,200 as self-assessment tax along with return. Ignore interest u/s 234C.

Solution:

Computation of interest u/s 234B

Particulars	As per	
	Assessed income	Returned income
Income	1,05,000	1,00,000
Tax on above (including cess)	32,760	31,200
Less: TDS and Advance tax	21,000	21,000
Shortfall for the period April' 2024 to June' 2024	11,760	10,200
Rounded off (a)	11,700	10,200
Period of default (b) [From April' 2024 to June' 2024]	3 months	3 months

Particulars	As per	
	Assessed income	Returned income
Interest u/s 234B (1% x a x b)	351	306
Shortfall for the period July' 2024 to March' 2025 (₹ 11,760 – ₹ 9,894 as paid u/s 140A) [Note]	1,866	
Rounded off (c)	1,800	
Period of default (d) [From July' 2024 to March' 2025]	9 months	
Interest u/s 234B (1% x c x d)	162	

Note:

Since, shortfall till June 2024 is ₹ 11,760 and thereafter assessee has paid ₹ 9,894 [i.e. ₹ 10,200 (amount paid u/s 140A) – ₹ 306 (interest u/s 234B for the purpose of sec.140A)], hence interest shall be calculated on the following-

For the period April' 24 to June' 24 - On ₹ 11,760

For the period July' 24 to March' 25 - On ₹ 1,866

Statement showing interest payable u/s 234B

Particulars	Amount
For the period April to June	351
For the period July to March	162
	513
Less: Interest paid on self-assessment	306
Interest payable	207

2.3.5 For deferment of Advance Tax [Sec. 234C]

Condition: Payment of advance tax is to be made as per the schedule (mentioned in the chapter *"Advance Tax"*). In case assessee fails to pay the amount or pays lesser amount as required by the schedule, then assessee will have to pay interest u/s 234C for such deferment.

Amount on which interest is payable:

Specified % of tax* on the total income declared in the return filed by the assessee	***
Less: Tax deducted/collected at source	***
Less: Amount of advance tax paid on or before the due date of payment as per the advance tax payment schedule.	***
Less: Relief allowed u/s 89 or 90 or 90A or 91	***
Less: Credit allowed u/s 115JAA or 115JD (MAT or AMT Credit)	***
Amount on which interest shall be calculated	***

* Specified % of tax for calculation of interest under this section

Assessee	Due date of installment (of previous year)	Minimum amount payable
An eligible assessee in respect of an eligible business referred to in sec. 44AD or 44ADA	On or before March 15	100% of advance tax liability
Other Assessee	On or before June 15	Upto 15% of advance tax liability
	On or before September 15	Upto 45% of advance tax liability
	On or before December 15	Upto 75% of advance tax liability
	On or before March 15	Upto 100% of advance tax liability

Notes

1. Where an assessee has paid 12% or more of tax as advance tax on or before June 15, then no interest u/s 234C is payable.
2. Where an assessee has paid 36% or more of tax as advance tax on or before September 15, then no interest u/s 234C is payable.

Rate of interest: Simple interest @ 1% per month or part thereof

Period: 3 months (1 month for last instalment)

Other Points

- **Updated Return u/s 139(8A)**: Where an assessee has filed any return u/s 139(1) or 139(4) and he is filing an updated return u/s 139(8A), then, interest u/s 234C shall be computed after considering the total income furnished in the updated return as the returned income.
- No interest will be levied in respect of any shortfall in the payment of advance tax due on the returned income, if -

  a) The shortfall is on account of under-estimation or failure to estimate the amount of:

     i. capital gains; or

     ii. income of the nature referred to in section 2(24)(ix) [i.e. lottery, cross-word, etc.];

     iii. income under the head "Profits and gains of business or profession" in cases where the income accrues or arises under the said head for the first time;

     iv. dividend; or

  b) The assessee has paid the whole of the amount of tax payable in respect of such income as part of the remaining installment(s) of advance tax which were due or where no installment is due, by March 31 of the previous year.

Illustration 4:

A firm made the following payments of advance tax during the financial year 2023-24:

	₹ in lakh
September 15, 2023	7.00
December 15, 2023	7.75
March 15, 2024	10.75
	25.50

The return of income is filed on 31-7-2024 showing -

Business income ₹ 80 lakh

Long term capital gain taxable @ 20% (as on 1-12-2023) ₹ 10 lakh

Compute interest payable u/s 234C.

Solution:

Computation of tax liability for A.Y. 2024-25 ₹ in lakh

Particulars	Business income	Long term capital gain
Income	80.00	10.00
Tax rate	30%	20%
Tax liability before cess	24.00	2.00
Add: Health & Education cess	0.96	0.08
Tax liability including cess	24.96	2.08

Computation of interest payable u/s 234C

Particulars	Installment of Advance tax			
	15/6/2023	15/9/2023	15/12/2023	15/3/2024
Rate of Advance tax	15%	45%	75%	100%
Amount payable				
(₹ 24,96,000 x 15%)	3,74,400			
(₹ 24,96,000 x 45%)		11,23,200		
[(₹ 24,96,000 + ₹ 2,08,000) x 75%]			20,28,000	
[(₹ 24,96,000 + ₹ 2,08,000) x 100%]				27,04,000
Less: Amount paid till date	Nil	7,00,000	14,75,000	25,50,000
Shortfall	3,74,400	4,23,200	5,53,000	1,54,000
Rounded off (a)	3,74,400	4,23,200	5,53,000	1,54,000
Period of default (b)	3 months	3 months	3 months	1 month
Interest (1% x a x b)	₹ 11,232	₹ 12,696	₹ 16,590	₹ 1,540
Total interest payable u/s 234C	**₹ 42,058**			

Illustration 5:

A Ltd. made the following payments of advance tax during the financial year 2023-24:

	₹ in lakh		₹ in lakh
June 15, 2023	3.70	September 15, 2023	3.50
December 15, 2023	10.25	March 18, 2024	8.80

The return of income is filed on 31-7-2024 showing -

Business income	₹ 80 lakh
Long term capital gain taxable @ 20% (as on 1-12-2023)	₹ 10 lakh

Compute interest payable u/s 234C.

Solution:

Computation of tax liability for A.Y. 2024-25 (₹ in lakh)

Particulars	Business income	Long term capital gain
Income	80.00	10.00
Tax rate	30%	20%
Tax liability before surcharge	24.00	2.00
Add: Surcharge	Nil	Nil
Tax liability after surcharge	24.00	2.00
Add: Education cess	0.96	0.08
Tax liability after surcharge and cess	**24.96**	**2.08**

Computation of interest payable u/s 234C

Particulars	Installment of Advance tax			
	15/6/2023	15/9/2023	15/12/2023	15/3/2023
Rate of Advance tax	15%	45%	75%	100%
Amount payable				
(₹ 24,96,000 x 15%)	3,74,400			
(₹ 24,96,000 x 45%)		11,23,200		
[(₹ 24,96,000 + ₹ 2,08,000) x 75%]			20,28,000	
[(₹ 24,96,000 + ₹ 2,08,000) x 100%]				27,04,000
Less: Amount paid till date	3,70,000	7,20,000	17,45,000	17,45,0003
Shortfall	Nil1	4,03,200	2,83,000	9,59,000
Rounded off (a)	Nil	4,03,200	2,83,000	9,59,000
Period of default (b)	--	3 months	3 months	1 month
Interest (1% x a x b)	--	₹ 12,096	₹ 8,490	₹ 9,590
Total interest payable u/s 234C	**₹ 30,176**			

1. Since assessee has paid at least 12% of tax (i.e. ₹ 2,99,520) on or before 15th June, 2023, hence no interest u/s

234C shall be levied.

2. Since assessee fails to pay 36% of tax (i.e. ₹ 8,98,560) on or before 15th September, 2023, hence interest u/s 234C shall be levied. It is to be noted that interest shall be payable considering 45% of tax.

3. As payment has not been made within due date, hence advance tax paid on 18-03-2024 has not been considered.

2.3.6 Interest for excess refund granted to the assessee [Sec. 234D]

Condition: Where any refund is granted to the assessee u/s 143(1) and –

a) no refund is due on regular assessment; or

b) the amount refunded exceeds the amount refundable on regular assessment;

Rate of interest: Simple interest @ ½% for every month or part of the month

Amount on which interest is to be charged: On the whole or excess amount refunded

Period: From the date of grant of refund to the date of such regular assessment

Adjustment in interest: Where amount of refund is reduced or increased by an order u/s 154, 155, 245D, 250, 254, 260, 262, 263 & 264, the amount of interest shall be reduced or increased accordingly.

2.3.7 Fee for defaults in furnishing statements [Sec. 234E]

Condition: Where a person fails to deliver a quarterly TDS / TCS return within the prescribed time.

Amount of Fee: ₹ 200 for every day during which the failure continues subject to maximum of amount of TDS/ TCS

Note:

- The fee shall be paid before delivering a statement.
- The fee is in addition to other consequences of non-delivering such return

2.3.8 Fee for default in furnishing return of income [Sec. 234F]

Where a person required to furnish a return of income u/s 139(1), fails to do so within the due date, he shall pay fee of:

Case	Fee
Total income does not exceed ₹ 5 lakh	₹ 1,000
Total income exceeds ₹ 5 lakh	₹ 5,000

2.3.9 Fee for default relating to statement or certificate [Sec. 234G]

Where:

a. the research association, university, college or other institution or company referred to in 35(1)(ii) or (iii) or (iia) fails to deliver a statement within the time prescribed u/s 35(1A); or

b. the institution or fund fails to deliver a statement within the time prescribed u/s 80G(5)(viii) or fails to furnish a certificate u/s 80G(5)(ix)

it shall be liable to pay fee @ ₹ 200 for every day during which the failure continues.

Maximum Fee: The amount of fee shall not exceed the amount in respect of which the failure referred to therein has occurred.

Taxpoint: Such fee shall be paid before delivering the statement or before furnishing such certificate.

2.3.10 Interest for failure to pay tax according to demand notice [Sec. 220(2)]

Any amount specified as payable in a notice of demand u/s 156 should be paid within 30 days (or lesser period as specified by the Assessing Officer with prior approval of Joint Commissioner) of the service of the notice.

Condition: Any person fails to pay such amount within such time

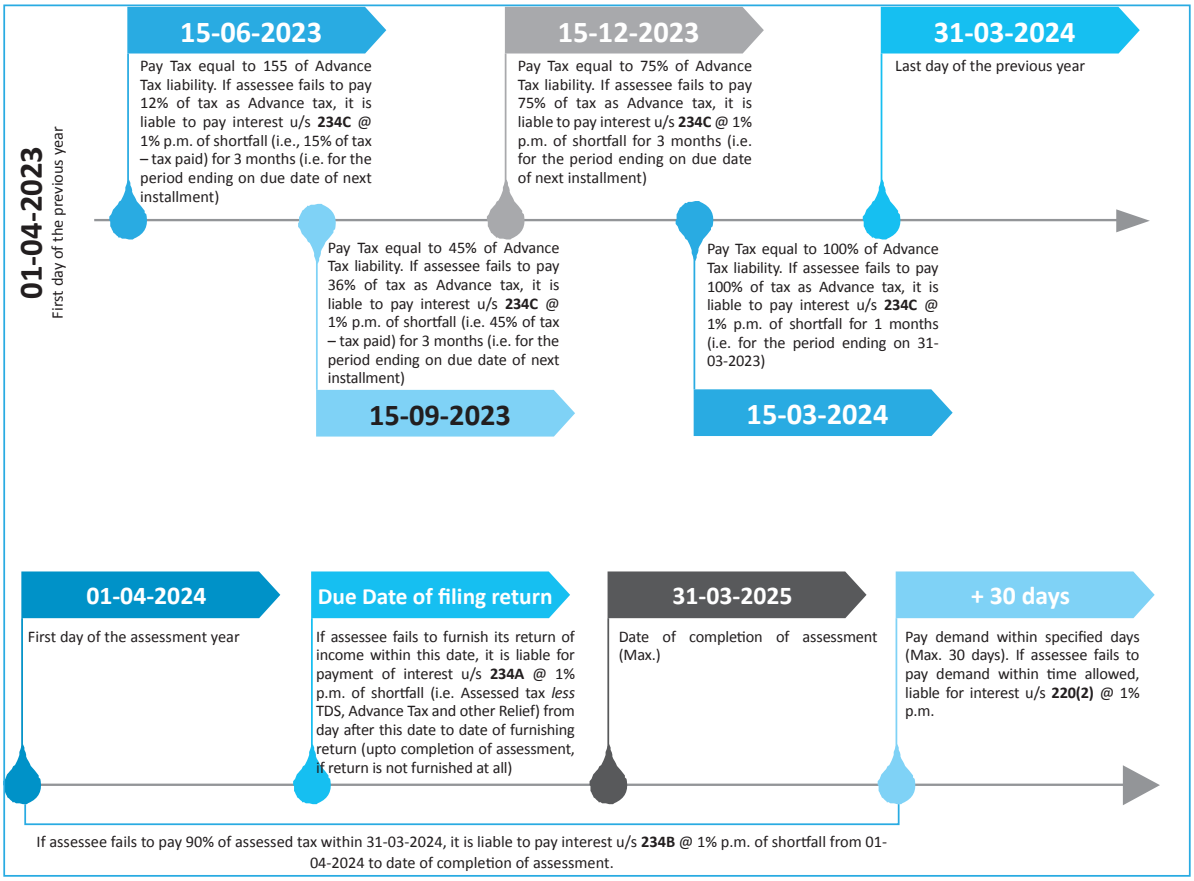
Rate of interest: Simple interest @ 1% for every month or part thereof.

Amount on which interest is to be charged: On the amount specified in the notice of demand.

Period: Interest shall be charged for a period commencing from the day immediately after the expiry of 30 days (or specified period[1]) and ending on the day on which such amount is paid.

Note

1. Where the Assessing Office has any reason to believe that it will be detrimental to revenue if the full period of 30 days is allowed, then he may with the previous approval of the Joint Commissioner direct that the sum specified in the notice of demand shall be paid within such time as may be specified by him in the notice. In such case interest shall be calculated for a period commencing from the period specified in the notice.
2. Where interest is charged u/s 201(1A) on the amount of tax specified in the intimation issued u/s 200A(1) for any period, then, no interest shall be charged under this section on the same amount for the same period. Similarly, where interest is charged u/s 206C(*7*) on the amount of tax specified in the intimation issued u/s 206CB(*1*) for any period, then, no interest shall be charged under this section on the same amount for the same period.
3. Adjustment in interest: Where amount of refund is reduced or increased by an order u/s 154, 155, 250, 254, 260, 262, 264 & 245D, the amount of interest shall be reduced or increased accordingly.
4. Where any notice of demand has been served upon an assessee and any appeal or other proceeding, as the case may be, is filed or initiated in respect of the amount specified in the said notice of demand, then, such demand shall be deemed to be valid till the disposal of the appeal by the last appellate authority or disposal of the proceedings, as the case may be.



Summary of Interest payable

Dates	Interest liability of an assessee
01-04-2023	First day of the Previous Year
15-06-2023	Pay Tax equal to 15% of Advance Tax liability. If assessee fails to pay 12% of tax as Advance tax, it is liable to pay interest u/s 234C @ 1% p.m. of shortfall (i.e., 15% of tax – tax paid) for 3 months (i.e. for the period ending on due date of next installment)
15-09-2023	Pay Tax equal to 45% of Advance Tax liability. If assessee fails to pay 36% of tax as Advance tax, it is liable to pay interest u/s 234C @ 1% p.m. of shortfall (i.e., 45% of tax – tax paid) for 3 months (i.e. for the period ending on due date of next installment)
15-12-2023	Pay Tax equal to 75% of Advance Tax liability. If assessee fails to pay 75% of tax as Advance tax, it is liable to pay interest u/s 234C @ 1% p.m. of shortfall for 3 months (i.e. for the period ending on due date of next installment)
15-03-2024	Pay Tax equal to 100% of Advance Tax liability. If assessee fails to pay 100% of tax as Advance tax, it is liable to pay interest u/s 234C @ 1% p.m. of shortfall for 1 months (i.e. for the period ending on 31-03-2023)
31-03-2024	Last day of the Previous Year

01-04-2024	First day of Asst. Year	If assessee fails to pay 90% of assessed tax within 31-03-2024, it is liable to pay interest u/s **234B** @ 1% p.m. of shortfall from 01-04-2024 to date of completion of assessment.
31-07-2024 / 31-10-2024 / 30-11-2024	Due Date of furnishing return2. If assessee fails to furnish its return of income within this date, it is liable for payment of interest u/s 234A @ 1% p.m. of shortfall (i.e. Assessed tax less TDS, Advance Tax and other Relief) from day after this date to date of furnishing return (upto completion of assessment, if return is not furnished at all)	
31-03-2025	Date of completion of assessment (Max.)	
	Pay demand within specified days (Max. 30 days)	
	If assessee fails to pay demand within time allowed, liable for interest u/s 220(2) @ 1% p.m.	

2.3.11 Waiver or reduction of interest u/s 234A, 234B & 234C

1. The Chief Commissioners and the Directors-General (Investigation) is empowered to reduce or waive penal interest u/s 234A, 234B and 234C in the following circumstances* -

   a) Where, in the course of search and seizure operation, books of account have been taken over by the Department and were not available to the taxpayers to prepare his return of income.

   b) Where, in the course of search and seizure operation, cash had been seized, which was not permitted to be adjusted against arrears of tax or payment of advance tax installments falling due after the date of the search.

   c) Any income other than capital gains which was received or accrued after the date of first or subsequent installment of advance tax, which was neither anticipated nor contemplated by the taxpayer and on which advance tax was paid by the taxpayer after the receipt of such income.

   d) Where, as a result of any retrospective amendment of law or the decisions of the Supreme Court after the end of the relevant previous year, certain receipts, which were earlier treated as exempted income, now become taxable.

   e) Where return of income is filed voluntarily without detection by the Income tax Department and due to circumstances beyond control of the taxpayer such return of income was not filed within the stipulated time-limit or advance tax was not paid at the relevant time.

   * The above circumstances are indicative only.

2. The Chief Commissioner of Income Tax/Director–General are empowered to waive or reduce interest u/s 234A, 234B and 234C on income which accrues or arises for any previous year due to the operation of any order of a Court, statutory authority or of the Government (other than an order of assessment, appeal reference or revision passed under the provisions of the Income tax Act) passed after the close of the said previous year [Order F. No. 212/495/92-ITA-II dt. 2-5-1994]

Notes

a) Board can grant relief u/s 234A, 234B or 234C

b) Waiver of interest can be considered only if the return of income is filed voluntarily without detection by the Assessing Officer.

[4] In some cases, 30th November

2.3.12 Interest payable to the assessee

Interest on refund [Sec. 244A]

An assessee who is entitled to get refund shall also be entitled to interest on such refund. Provision relating to interest is enumerated below -

Rate of interest: Simple interest @ ½% per month or part thereof

Period for calculation of interest

Case	Period
1. Refund is out of TDS or TCS or Advance tax (Note 1)	
– Where return of income is furnished within due date	From first day of relevant assessment year to the date on which such refund is granted.
– Where return is after due date	From the date of furnishing return to the date on which such refund is granted.
2. Refund is out of self-assessment tax (Note 1)	From the date of furnishing return or payment of tax, whichever is later to the date on which such refund is granted.
3. Refund due to any other reason	From date of payment of such tax to the date on which such refund is granted.
4. Refund due to excess payment of TDS by deductor	From the date on which claim for refund is made (however, where refund arise on account of giving effect to an order u/s 250 or 254 or 260 or 262, from date of payment of tax) to the date on which refund is granted.

Notes

1. **Interest on refund due to TDS or TCS:** In case (1) and (2), no interest on refund shall be allowed if the amount of refund is less than 10% of the tax determined u/s 143(1) or on regular assessment.
2. **Interest on Refund arising out of giving effect to an order:** In a case where a refund arises as a result of giving effect to an order u/s 250 or 254 or 260 or 262 or 263 or 264, wholly or partly, otherwise than by making a fresh assessment or reassessment, the assessee shall be entitled to receive, in addition to the interest payable (as aforesaid), an additional interest on such amount of refund calculated at the rate of 3% p.a., for the period beginning from the date following the date of expiry of the time allowed u/s 153(5) [i.e., 3 months from the end of the month in which appellate order is received by the CIT) to the date on which the refund is granted.

   However, where proceedings for assessment or reassessment are pending in respect of an assessee, in computing the period for determining the additional interest payable to such assessee, the period beginning from the date on which such refund is withheld by the Assessing Officer u/s 245(2) and ending with the date on which such assessment or reassessment is made, shall be excluded.
3. **Taxability of refund and interest on refund:** It is to be noted that refund of tax itself is not taxable. However, interest received on delayed refund is taxable under the head "Income from other sources".
4. **Adjustment in interest:** Where tax payable is reduced or enhanced by an order u/s 143(3), 144, 147, 154, 155, 250, 254, 260, 262, 263, 264 & 245D(4), the amount of interest shall be reduced or enhanced accordingly.
5. **Delay in refund due to reason attributable to the assessee:** Where the refund is delayed for the reason attributable to the assessee (or deductor), the period of delay so attributable to him shall be excluded from the period for which interest is payable. Further, where any question arises as to the period to be excluded, it shall be decided by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner whose decision shall be final.
6. **Interest on refund arising on application made by the assessee u/s 155(20)**: Where refund arises as a result of an order passed by the Assessing Officer in consequence of an application made by the assessee u/s 155(20), such interest shall be calculated at the rate of 0.5% for every month or part of a month comprised in the period from the date of such application to the date on which the refund is granted.

Survey, Search and Seizure

2.4

2.4.1 Power regarding discovery, production of evidence, etc. [Sec. 131]

Power of income tax authority while trying a suit

The income-tax authority [being Assessing Officer, Deputy Commissioner (Appeals), Joint Commissioner, Commissioner (Appeal), Joint Commissioner (Appeals), Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner and the Dispute Resolution Panel] have the same powers as are vested in a court under the Code of Civil Procedure, 1908, when trying a suit in respect of the following matters —

a) Discovery and inspection;

b) Enforcing the attendance of any person, including any officer of a banking company and examining him on oath;

c) Compelling the production of books of account and other documents; and

d) Issuing commissions

Power before initiating search and seizure u/s 132 [Sec. 131(1A)]

The income-tax authority [being Principal Director-General or Director-General or Principal Director or Director or Joint-Director or Assistant Director or Deputy Director or any authorized officer referred u/s 132(1)] before taking any action u/s 132, can exercise above power if he has ***reason to suspect*** that any income has been concealed (or is likely to be concealed), by any person (or class of persons), within his jurisdiction and for the purposes of making any enquiry or investigation relating thereto, it shall be competent for him to exercise above powers.

Taxpoint:

- Above action can be taken even though no proceedings with respect to such person is pending before any income-tax authority.
- In case inquiry (even no proceedings are pending) or investigation is related to an agreement referred to in sec. 90 or 90A, such power can be excersied by any notified income-tax authority (not below the rank of Assistant Commissioner) [Sec. 131(2)]

Power to impound or retain books [Sec. 131(3)]

Any income tax authority [referred in sec. 131(1) or (1A) or (2)] may impound and retain in its custody any books of account or other documents produced before it in any proceedings under this Act. However, an Assessing Officer or an Assistant Director or Deputy Director shall not -

a) Impound any books of account or other documents without recording his reasons for doing so; or

b) Retain in his custody any such books or documents for a period exceeding *15 days (exclusive of holidays*) without obtaining (prior) approval of the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General or Principal Commissioner or Commissioner or Principal Director or Director.

2.4.2 Search and seizure [Sec. 132]

Who can authorize (i.e., issue search warrants) proceedings u/s 132

Sec.132 empowers the Principal Director General or Director General or Principal Director or Director or the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner to authorize proceedings under this section.

Taxpoint: Proceeding means any proceeding in respect of any year, which may be pending on the date on which a search is authorised under this section or which may have been completed on or before such date and includes also all proceedings which may be commenced after such date in respect of any year.

Circumstances when search can be conducted

Any authority (mentioned above) can direct proceedings u/s 132 against the following person where he has reason to believe (in consequence of information in his possession, which is something more than mere rumor or gossip) that:

Person	Circumstances
Any person to whom a summons u/s 131(1) or a notice u/s 142(1) was issued to produce any books of account or other documents	Such person has omitted or failed to do so
Any person to whom a summons or notice as aforesaid has been or might be issued	Such person will fail to do so
Any person is in possession of any money, bullion, jewellery or other valuable article or thing	Such money, bullion, jewellery or other valuable article or thing represents either wholly or partly undisclosed income or undisclosed property

Taxpoint: The reason to believe, as recorded by the income-tax authority, shall not be disclosed to any person or any authority or the Appellate Tribunal.

Who can conduct search

Income tax authority, having power to initiate search u/s 132, can authorise its subordinate(s) (not below the rank of Income tax officer) to conduct search. Following subordinates can be authorised -

Authorized Officer who can conduct search	Authorized from
Additional Director or Additional Commissioner or Joint Director, Joint Commissioner, Assistant Director, Deputy Director, Assistant Commissioner, Deputy Commissioner or Income tax officer	Principal Director General or Director General or Principal Director or Director or Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner

Authorized Officer who can conduct search	Authorized from
Assistant Director, Deputy Director, Assistant Commissioner, Deputy Commissioner or Income tax officer	Additional Director or Additional Commissioner or Joint Director or Joint Commissioner (on the basis of authorization from above authority and being empowered by the Board)

Power of authorized officer

While conducting search, authorized officer has following powers -

a. Enter and search any building, etc.: Enter and search any building, place, vessel, vehicle or aircraft where he has reason to suspect that such books of account, other documents, money, bullion, jewellery or other valuable article or thing are kept.

b. Break open the lock of any door, etc.: Break open the lock of any door, box, locker, safe, almirah or other receptacle, where the keys thereof are not available.

c. Search person: Search any person who -

- has got out of; or
- is about to get into; or
- is in,

the building, place, vessel, vehicle or aircraft if the authorised officer has reason to suspect that such person has secreted about his person any books of account, other documents, money, bullion, jewellery or other valuable article or thing.

d. Require any person to facilitate the authorised officer: Require any person who is found to be in possession or control of any books of account or other documents maintained in the form of electronic record, to afford the authorised officer the necessary facility to inspect such books of account or other documents.

e. Seizure: Seize any such books of account, other documents, money, bullion, jewellery or other valuable article or thing found as a result of such search.

f. Place marks of identification: Place marks of identification on any books of account or other documents or make extracts or copies therefrom.

g. Make inventory: Make a note or an inventory of any such money, bullion, jewellery or other valuable article or thing.

h. Examine on oath: Examine on oath any person who is found to be in possession or control of any books of account, documents, money, bullion, jewellery or other valuable article or thing. Any statement made by such person during such examination may thereafter be used as evidence in any proceeding.

i The examination of any person may be not merely in respect of any books of account, other documents or assets found as a result of the search, but also in respect of all matters relevant for the purposes of any investigation connected with any proceeding under Act

Taxpoint

- **No seizure of stock in trade**

  Bullion, jewellery or other valuable article or thing, being stock-in-trade of the business, shall not be seized but the authorized officer shall make a note or inventory of such stock-in-trade.

- **Extention of jurisdictional area**
  - Where any building, place, vessel, vehicle or aircraft is within the area of jurisdiction of any Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, but such authority has no jurisdiction over such person; and
  - Such authority has reason to believe that any delay in getting the authorisation from the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner having jurisdiction over such person may be prejudicial to the interests of the revenue,

  - then it shall be competent for him to exercise the above powers.

  Handing over of seized assets to the Assessing Officer having jurisdiction: Any asset or document so seized shall be handed over to the Assessing Officer having jurisdiction over such person within a period of 60 days from the date on which the last of the authorizations for search was executed. Thereafter, such Assessing Officer exercises all other powers.

- **Extension of Authorisation [Sec. 132(1A)]**
  - Where a search for any books of account, other document, money, bullion, jewellery or other valuable article or thing is authorized; and
  - Other Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner in consequence of information in his possession, has reason to suspect that such document or asset is kept in any other building, place, vessel, vehicle or air craft not mentioned in the authorization,

  - then such other Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner can authorize the officer to search such other building, place, vessel, vehicle or air craft.

  Taxpoint: The reason to suspect, as recorded by the income-tax authority, shall not be disclosed to any person or any authority or the Appellate Tribunal.

- **Deemed or constructive Seizure [Second Proviso to Sec. 132(1)]**

  Conditions

  Where it is not possible or practicable to take physical possession of any valuable article or thing and remove it to a safe place due to reason of its -
  - volume, weight or other physical characteristics; or
  - being of a dangerous nature.

  Procedure

  The authorised officer may serve an order on -
  - the owner; or
  - the person who is in immediate possession or control of any valuable article or things,

  - that he shall not remove, part with or otherwise deal with such article or thing without the prior permission of such authorised officer.

  Effect

  Such action of the authorised officer shall be deemed to be seizure of such article or thing.

Notes

a) No such order can be passed for any article or thing, being stock-in-trade.

b) Though such order can also be passed for reasons other than those mentioned above, but in that case, the order shall not be deemed to be seizure of such article or things and it shall not be in force for a period exceeding 60 days from the date of the order [Sec. 132(3) & (8A)]

- **Provisional Attachment**
  - Where

    a. during the course of the search or seizure; or

    b. within a period of 60 days from the date on which the last of the authorisations for search was executed,

    the authorised officer may attach provisionally any property belonging to the assessee and for the said purpose, the provisions of the Second Schedule shall, mutatis mutandis, apply.
  - Such attachment shall be subject to following conditions:

    a) The authorised officer is satisfied that for the purpose of protecting the interest of revenue, it is necessary to do so.

    b) The reasons for such provisional attachment should be recorded in writing

    c) Previous approval (in writing) of the Principal Director General or Director General or the Principal Director or Director has taken.
  - Every provisional attachment shall cease to have effect after the expiry of 6 months from the date of such order.
  - The authorised officer may, during the course of the search or seizure or within a period of 60 days from the date on which the last of the authorisations for search was executed, make a reference to,—

    i. a Valuation Officer referred to in sec. 142A; or

    ii. any other person or entity or any valuer registered by or under any law for the time being in force, as may be approved by the Principal Chief Commissioner or the Chief Commissioner or the Principal Director General or the Director General, in accordance with the prescribed procedure

    - who shall estimate the fair market value of the property in the prescribed manner and submit a report of the estimate to the authorised officer or the Assessing Officer, as the case may be, within a period of 60 days from the date of receipt of such reference

Authorisation and assessment in case of search or requisition [Sec. 292CC]

- It shall not be necessary to issue an authorisation u/s 132 or make a requisition u/s 132A separately in the name of each person.
- Where an authorisation u/s 132 has been issued or requisition u/s 132A has been made mentioning therein the name of more than one person, the mention of such names of more than one person on such authorisation or requisition shall not be deemed to construe that it was issued in the name of an association of persons or body of individuals consisting of such persons.
- Though authorisation u/s 132 or requisition u/s 132A has been made mentioning therein the name of more than one person, the assessment or reassessment shall be made separately in the name of each of the persons mentioned in such authorisation or requisition.

Time limit for retention [Sec. 132(8)]

The books of account or other documents seized or deemed seized shall not be retained by the authorised officer for a period exceeding 30 days from the date of the order of assessment u/s 143 or 144 or 147..

Exception

It can be retained for more than 30 days on fulfillment of the following conditions -

1. The reasons for retaining the same are recorded in writing; and
2. The (prior) approval of the Principal Chief Commissioner or Chief Commissioner, Principal Commissioner or Commissioner, Principal Director General or Director General or Principal Director or Director for such retention is obtained.

Taxpoint

a) **Maximum retention**

The aforesaid authorities shall not authorise the retention of the books of account and other documents for a period exceeding 30 days after all the proceedings in respect of the years for which the books of account or other documents are relevant, are completed.

b) **Power of the Board to pass an order [Sec. 132(10)]**

- Where a person is legally entitled to the books of account or other documents seized;
- Such person objects for any reason to the approval given by the authorities; and
- Such person makes an application to the Board stating therein the reasons for such objection and requesting for the return of the books of account or other documents.

- then the Board may, after giving the applicant an opportunity of being heard, pass such orders as it thinks fit.

Presumption in case of search [Sec. 132(4A)]

Where any books of account, other documents, money, bullion, jewellery or other valuable article or thing are, or is found in the possession or control of any person in the course of search, it may be presumed that -

- Such books of account, other documents, money, bullion, jewellery or other valuable article or thing belongs to such person;
- The contents of such books of account and other documents are true;
- The signature and every other part of such books of account and other documents which purport to be in the handwriting of any particular person, are in that person's handwriting; and
- In the case of a document stamped, executed or attested, it was duly stamped and executed or attested by the person by whom it purports to have been so executed or attested.

Other Provisions

1. Assistance from other [Sec. 132(2)]: The authorised officer may requisition the services of,—
   i. any police officer or of any officer of the Central Government, or of both; or
   ii. any person or entity as may be approved by the Principal Chief Commissioner or the Chief Commissioner or the Principal Director General or the Director General, in accordance with the prescribed procedure
   - to assist him for all or any of the purposes of search and it shall be the duty of every such officer or person or entity to comply with such requisition

2. Right to make copies or take extract [Sec. 132(9)]: The person from whose custody books of account or other documents are seized may make copies thereof or take extracts therefrom. Such right can be exercised in the presence of the authorized officer or any other person empowered by him in this behalf, at such place and time as the authorized officer may appoint in this behalf.

3. Last of authorisation for search: The last of authorisation for search shall be deemed to have been executed:

   a. in the case of search, on the conclusion of search as recorded in the last panchnama drawn in relation to any person in whose case the warrant of authorisation has been issued; or

   b. in the case of requisition u/s 132A, on the actual receipt of the books of account or other documents or assets by the authorised officer

4. Power of Board to make rules [Sec 132(14)]: The Board may make rules in relation to any search or seizure providing the procedure to be followed by the authorised officer -

   i) for obtaining ingress (i.e. right to enter) into any building, place, vessel, vehicle or aircraft to be searched where free ingress thereto is not available;

   ii) for ensuring safe custody of any books of account or other documents or assets seized.

5. The provisions of the Code of Criminal Procedure, 1973 relating to searches and seizure shall apply, so far as may be, to search and seizure [Sec. 132(13)].

2.4.3 Powers to requisition books of account, assets, etc. [Sec. 132A]

Circumstances when power u/s 132A can be invoked

Where income-tax authority (being Principal Director General or Director General or Principal Director or Director or the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner) in consequence of information in his possession, has reason to believe that -

a) Any person to whom a summon u/s 131(1) or a notice u/s 142(1) was issued to produce any books of account or other documents -

   1. Has omitted or failed to produce such books of account or other documents; and

   2. The said books of account or other documents have been taken into custody by any officer or authority under any other law for the time being in force (hereinafter referred as other authority)

b) Any books of account or other documents will be useful for, or relevant to, any proceeding under this Act and any person to whom a summon or notice has been issued will not produce such books of account or other documents on its returning by other authority

c) Any assets taken into custody by any officer or authority under any other law for the time being in force is undisclosed (wholly or partly).

Who can requisition books

Requisitioning Officer who can require books, etc.	Authorized from
Additional Director, Additional Commissioner, Joint Director, Joint Commissioner, Assistant Director, Deputy Director, Assistant Commissioner, Deputy Commissioner or Income tax officer	Principal Director General or Director General or Principal Director or Director or the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner

Power of Requisitioning Officer

The requisitioning officer can make a requisition for delivery of books of account, etc., to such other authority. Such other authority shall deliver the books of account, other documents or assets to the requisitioning officer when such officer or authority is of the opinion that it is no longer necessary to retain the same in his or its custody. For instance, any books of account seized by an officer under Customs Act can be requisitioned by income-tax authority to deliver such books of account.

On the requisition, other authority delivers books of account, etc. to the requisitioning officer. Such books of account, documents, etc. shall be deemed as seized u/s 132(1).

Taxpoint

- The reason to believe, as recorded by the income-tax authority, shall not be disclosed to any person or any authority or the Appellate Tribunal.
- A bank draft when presented for clearing by the customer to the bank cannot be said to have been taken into custody by the bank to attract the applicability of section 132A. Resultantly, the warrant of authorisation requisitioning the same by the competent authority is totally without jurisdiction [*Samta Construction Co.* -vs.- *Pawan Kumar Sharma*]

2.4.4 Application of seized or requisitioned assets [Sec. 132B]

The seized assets may be adjusted with:

a) The amount of any existing liability under -

   i) The Income-tax Act, 1961;

   ii) The Wealth-tax Act, 1957 (now abolished);

   - The existing liability does not include advance tax payable.

b) The amount of liability determined on completion of the assessment u/s 153A;

c) The amount of liability determined on completion of the assessment of the year relevant to the previous year in which search is initiated or requisition is made;

   (including any penalty levied or interest payable in connection with such assessment); and

d) The amount in respect of which such person is in default or is deemed to be in default or the amount of liability arising on an application made before the Settlement Commission.

2.4.5 Release of asset [First Proviso to sec. 132B]

Condition for release of asset

Where the following conditions are satisfied, the amount of any existing liability may be recovered out of such asset and the remaining portion of the asset may be released to the person from whose custody the assets were seized -

1. The person concerned makes an application to the Assessing Officer within 30 days from the end of the month in which the asset was seized for release of asset;
2. The nature and source of acquisition of such asset is explained to the satisfaction of the Assessing Officer; and

3. The Assessing Officer obtains the prior approval of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner.

Time limit for release of asset

Asset or any portion thereof shall be released within a period of 120 days from the date on which the last of the authorisations for search u/s 132 or for requisition u/s 132A, as the case may be, was executed.

No seized asset shall be retained by the Department during pendency of appeal filed by Revenue [Naresh Kumar Kohali -vs.- CIT (P&H)]

Order of assets to be applied for discharging liability

The above liability shall be discharged by applying the seized asset in the following order –

a) Money;

b) Asset other than money (as laid down in the Third Schedule).

It is to be noted that the assessee shall be discharged of the liability to the extent of the money and asset so applied. However, Assessing Officer shall not be precluded from the recovery of above liabilities by any other mode.

Discharge of excess money

After discharging all liabilities if any assets or proceeds thereof left, then it shall be returned to the persons from whose custody such assets were seized.

Interest payable to the assessee

Where the aggregate amount of money (either seized or realized through sale of assets) seized exceeds the aggregate of the amount required to meet the liabilities, Government shall pay simple interest at the rate of ½% p.m. The interest shall be payable from the date immediately following the expiry of the period of 120 days (from the date on which the last of the authorisations for search u/s 132 or requisition u/s 132A was executed) to the date of completion of the assessment u/s 153A.

2.4.6 Power to call for information [Sec. 133]

The income-tax authority [being Assessing Officer, Deputy Commissioner (Appeals), Joint Commissioner, Commissioner (Appeals) or Joint Commissioner (Appeals)] may -

1. Require any firm to furnish him with a return of the names and addresses of the partners of the firm and their respective shares;
2. Require any Hindu undivided family to furnish him with a return of the names and addresses of the manager and the members of the family;
3. Require any person whom he has reason to believe to be a trustee, guardian or agent, to furnish him with a return of the names of the persons for or of whom he is a trustee, guardian or agent, and of their addresses;
4. Require any assessee to furnish a statement of the names and addresses of all persons to whom he has paid in any previous year rent, interest, commission, royalty or brokerage, or any annuity (not being any annuity taxable under the head "Salaries") amounting to more than Rs.1000, together with particulars of all such payments made;
5. Require any dealer, broker or agent or any person concerned in the management of a stock or commodity exchange to furnish a statement of the names and addresses of all persons -

a) to whom he or the exchange has paid any sum in connection with the transfer of assets; or

b) on whose behalf or from whom he or the exchange has received any such sum,

- together with particulars of all such payments and receipts;

6. Require any person, including a banking company or any officer thereof, to furnish information in relation to such points or matters, or to furnish statements of accounts and affairs,

- which will be useful for, or relevant to, any enquiry or proceeding under this Act.

Taxpoint

- Where no proceeding is pending, the power u/s 133 shall not be exercised by any income-tax authority below the rank of Principal Director or Director or Principal Commissioner or Commissioner, other than the Joint Director or Deputy Director or Assistant Director, without the prior approval of the Principal Director or Director or the Principal Commissioner or Commissioner.
- It is to be noted that power referred in point (6) above may also be exercised by the Principal Director General or Director-General, the Principal Chief Commissioner or Chief Commissioner, the Principal Director or Director or the Principal Commissioner or Commissioner or the Joint Director or Deputy Director or Assistant Director.

2.4.7 Power of Survey [Sec. 133A]

Who can survey

The income-tax authority being a Principal Commissioner or Commissioner, a Principal Director or Director, a Joint Commissioner or Joint Director, an Assistant Director or a Deputy Director or an Assessing Officer, or a Tax Recovery Officer or Inspector (in some circumstances) who is subordinate to the Principal Director General or the Director General or the Principal Chief Commissioner or the Chief Commissioner, as may be specified by the Board.

However, no action under this section shall be taken by an income-tax authority without the approval of the Principal Director General or the Director General or the Principal Chief Commissioner or the Chief Commissioner

Jurisdiction of Income-Tax Authority for conducting survey

An income-tax authority may conduct survey at -

- Any place within the limits of the area assigned to him; or
- Any place occupied by any person in respect of whom he exercises jurisdiction; or
- Any place in respect of which he is authorised for the purposes of this section by such income-tax authority, who is assigned the area within which such place is situated or who exercises jurisdiction in respect of any person occupying such place,

- where a business or profession or an activity for charitable purpose is carried on.

Power of Income Tax Authority

While conducting survey, income tax authority may exercise following power –

1. Enter in such place of business;
2. Require any proprietor, trustee, employee or any other person who may at that time and place be attending or helping in, the carrying on of such business or profession or such activity for charitable purpose -

a) To afford him the necessary facility to inspect such books of account or other documents as he may require and which may be available at such place;

➢ Inspector is also considered as income-tax authority for this purpose.

b) To afford him the necessary facility to check or verify the cash, stock or other valuable article or thing which may be found therein; and

c) To furnish such information as he may require as to any matter which may be useful for, or relevant to, any proceeding under this Act.

3. Place marks of identification on the books of account or other documents inspected by him and make extracts or copies therefrom;

➢ Inspector is also considered as income-tax authority for this purpose.

4. Impound and retain in his custody any books of account or other documents inspected by him;

Survey	Search & Seizure
Survey can take place only at a business premises or place of the profession. However, if books are kept at residential premises, then residential premises is covered	Search can take place at any building or place within the jurisdiction of the officer.
Survey take place only during working hours and on business days. However, once started, it can continue even after working hours	Search can take place on any day. It can start after sunrise, but continue until the procedures are completed
In survey, following can be done by the officer: • Inspection of books or documents; • Verification of cash or inventory • Impound and retain of books or other documents	In search, following can be done by the officer: • Entire place is searched to unearth hidden assets • Locks can be break • Undisclosed asset can be seized and carried away
Personal search of a person cannot be done. However, statement shall be recorded.	Every person in the premises, going out or coming in, can be personally searched and their statement can be recorded.
In case of survey help of police officer cannot be taken	The search team search team is generally accompanied by police officer

5. Make an inventory of any cash, stock or other valuable article or thing checked or verified by him;

6. Record the statement of any person, which may be useful for, or relevant to, any proceeding under this Act.

Proceeding means any proceeding under this Act in respect of any year which may be pending on the date on which the powers under this section are exercised or which may have been completed on or before such date and includes also all proceedings under this Act which may be commenced after such date in respect of any year.

Taxpoint

(i) **Deemed place of business or profession or activity for charitable purpose is carried on:** Where the person carrying on the business or profession or activity for charitable purpose states that any of his books of account or other documents or any part of his cash or stock or other valuable article or thing relating to his business or profession or activity for charitable purpose are kept, then survey shall also be conducted at that place.

(ii) In case where survey is for the purpose of verifying that tax has been deducted or collected at source as per relevant provisions of the Act, in that case the income-tax authority cannot take exercise power mentioned in point 4 and 5 (above).

Restriction on Income-tax Authority

An income-tax authority shall not -

a) Impound any books of account or other documents without recording his reasons for doing so; or

b) Retain in his custody any books of account or other documents for a period exceeding 15 days (exclusive of holidays) without obtaining the approval of the Principal Chief Commissioner or the Chief Commissioner or the Principal Director General or the Director General or the Principal Commissioner or the Commissioner or the Principal Director or the Director thereof, as the case may be;

c) Remove or cause to be removed any cash, stock or other valuable article or thing.

d) The place of business or profession cannot be sealed under survey – [*Shyam Jewellers -vs.- CIT (All)*]

Time for survey

An income-tax authority may **enter** into –

Place where business or profession is carried on	During the business hours
In case of deemed place of business or profession	Only after sunrise and before sunset

Survey of certain expenditure [Sec. 133A(5)]

a) The income tax authority (including Inspector), having regard to the nature and scale of expenditure incurred by an assessee, in connection with any function, ceremony or event, is of the opinion that it is necessary or expedient to do so, he may, at any time after such function, ceremony or event, require -

   - Assessee, who incurred such expenditure; or
   - Any person, who is likely to possess information in respect of such expenditure,

   - to furnish such information as he may require as to any matter which may be useful for, or relevant to, any proceeding under this Act.

b) He may record the statements of the assessee or any other person in this regard and such recorded statement may thereafter be used as evidence in any proceeding under this Act.

Effect of non co-operation or non-compliance

If a person does not co-operate or comply during survey, the income-tax authority shall have all the powers u/s 131(1) for enforcing compliance with the requirement made.

2.4.8 Power to collect certain information [Sec. 133B] (Door to door survey)

The income-tax authority (being Joint Commissioner, Assistant Director, Deputy Director, Assessing Officer, authorised Inspector) may, for the purpose of collecting any information, which may be useful for, or relevant to the purposes of this Act:

a) Enter into —

   - Any building or place within the limits of the area assigned to such authority; or
   - Any building or place occupied by any person in respect of whom he exercises jurisdiction,

   - where a business or profession is carried on.

b) Require any proprietor, employee or any other person who may at that time and place be attending or helping in such business or profession to furnish such information as may be prescribed

Time for Entrance

An Income-tax authority may enter into such place only during the hours at which such place is open for the conduct of business or profession.

Restriction on Income-tax Authority

An income-tax authority shall not remove any books of account or other documents, cash, stock or other valuable article or thing.

2.4.9 Power to call for information by prescribed income-tax authority [Sec. 133C]

- The prescribed income-tax authority (being Principal Director General or Director General or Principal Director or Director) may, for the purposes of verification of information in its possession relating to any person, issue a notice to such person requiring him, on or before a date to be specified therein, to furnish information or documents verified in the manner specified therein, which may be useful for, or relevant to, any inquiry or proceeding under this Act.
- Where any information or document has been received in response to a notice, the income-tax authority may process and utilise such information and document in accordance with the scheme notified u/s 135A.

2.4.10 Power to inspect registers of companies [Sec. 134]

The Income tax authority [being Assessing Officer, Deputy Commissioner (Appeals), Joint Commissioner, Commissioner (Appeals), Joint Commissioner (Appeals) or any other authorized person] may inspect and take copies of any register of the members, debenture-holders or mortgagees of any company or of any entry in such register.

2.4.11 Power of certain authorities [Sec. 135]

The Income tax authorities (being Principal Director General or Director General or Principal Director or Director, the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner and the Joint Commissioner) shall be competent to make any enquiry under this Act, and for this purpose shall have all the powers that an Assessing Officer has under this Act in relation to the making of enquiries.

2.4.12 Faceless collection of information [Sec. 135A]

The Central Government may make a scheme for the purposes of calling for information u/s 133, collecting certain information u/s 133B, or calling for information by prescribed income-tax authority u/s 133C, or exercise of power to inspect register of companies u/s 134, or exercise of power of Assessing Officer u/s 135 so as to impart greater efficiency, transparency and accountability by:

a. eliminating the interface between the income-tax authority and the assessee or any other person to the extent technologically feasible;

b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a team-based exercise of powers, including to call for, or collect, or process, or utilise, the information, with dynamic jurisdiction.

2.4.13 Proceedings before income-tax authorities to be judicial proceedings [Sec.136]

Any proceeding under this Act before an income-tax authority shall be deemed to be a judicial proceeding within the meaning of sec. 193, 196 and 228 of the Indian Penal Code, 1860 and every income-tax authority shall be deemed to be a Civil Court for the purposes of sec. 195, but not for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973.

2.4.14 Disclosure of information in respect of assessee [Sec. 138]

To the authority of other law

The Board or any authorized income-tax authority may furnish necessary information received or obtained by them to the officer, authority or body under any law (hereinafter referred as other authority) for enabling other authority to perform his duty. Such other authority shall be the officer, authority or body under any law -

a) relating to the imposition of any tax, duty or cess, or to dealings in foreign exchange as defined in sec. 2(n) of the Foreign Exchange Management Act, 1999; or

b) as the Central Government may, if in its opinion it is necessary so to do in the public interest, specify by notification in the Official Gazette.

To any other person

Where a person makes an application to the authority (being Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner) for any information relating to any assessee received or obtained by any income-tax authority in the performance of his functions under this Act, then the such authority may (if he is satisfied that it is in the public interest so to do) furnish such information. His decision in this behalf shall be final and shall not be called in question in any court.

Restriction on disclosure of information

The Central Government may (having regard to the practices and usages customary or any other relevant factors) direct that no information or document shall be furnished or produced by a public servant in respect of such matters relating to such class of assessees or except to such authorities as may be specified in the order.

Collection, Recovery and Refund of Tax 2.5

Collection and Recovery

2.5.1 Demand Notice [Sec. 156] & Provisions relating thereto [Sec. 220]

On completion of assessment (or intimation generated after processing of TDS statement), a demand notice [in Form 7] is *served* for additional demand raised in the assessment.

Time limit for payment of tax: The assessee should make the payment of amount demanded within 30 days of service of notice [Sec. 220(1)] Where the Assessing Officer has any reason to believe that it will be detrimental to revenue if the full period of 30 days is allowed, then he may with the previous approval of the Joint Commissioner direct that the sum specified in the notice of demand shall be paid within such time as may be specified by him in the notice.

Extension of time limit: On an application made by the assessee before the expiry of due date, the Assessing Officer may extend the time for payment or allow payment by installments, subject to such conditions as he may think fit to impose in the circumstances of the case.

Interest on delay in payment: If the payment is not made within 30 days (or time allowed in the notice), interest shall be payable @ 1% for every month (or part thereof) of the delay [Sec. 220(2)]

Taxpoint: Where interest is charged u/s 201(1A) on the amount of tax specified in the intimation issued u/s 200A(1) for any period, then, no interest shall be charged under this section on the same amount for the same period. Similarly, where interest is charged u/s 206C(7) on the amount of tax specified in the intimation issued u/s 206CB(1) for any period, then, no interest shall be charged under this section on the same amount for the same period.

Waiver or reduction of interest [Sec.220(2A)]: The Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may reduce or waive the amount of interest paid or payable by an assessee u/s 220(2), if he satisfied that:

a) payment of such amount has caused or would cause genuine hardship to the assessee;

b) default in the payment of the amount on which interest has been paid or was payable under the said sub-section was due to circumstances beyond the control of the assessee; and

c) the assessee has co-operated in any inquiry relating to the assessment or any proceeding for the recovery of any amount due from him.

The order accepting or rejecting the application of the assessee, either in full or in part, shall be passed within a period of 12 months from the end of the month in which the application is received. No order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard.

Assessee in default [Sec.220(4)]: If the amount is not paid within the time (or extended time) at the place and to the person mentioned in the said notice the assessee shall be deemed to be in default. Further, if, in a case where payment by installments is allowed, the assessee commits default in paying any one of the installments within the time, the assessee shall be deemed to be in default as to the whole of the amount then outstanding, and the other installment or installments shall be deemed to have been due on the same date as the installment actually in default.

Exception: In the following circumstances, the assessee may not be considered as an assessee in default:

a) Where an assessee has presented an appeal u/s 246A, the Assessing Officer may, in his discretion and subject to such conditions as he may think fit to impose in the circumstances of the case, treat the assessee as not being in default in respect of the amount in dispute in the appeal, even though the time for payment has expired, as long as such appeal remains undisposed of.

b) Where an assessee has been assessed in respect of income arising outside India in a country, the laws of which prohibit or restrict the remittance of money to India, the Assessing Officer shall not treat the assessee as in default in respect of that part of the tax which is due in respect of that amount of his income which, by reason of such prohibition or restriction, cannot be brought into India, and shall continue to treat the assessee as not in default in respect of such part of the tax until the prohibition or restriction is removed.

For this purpose, income shall be deemed to have been brought into India if it has been utilised or could have been utilised for the purposes of any expenditure actually incurred by the assessee outside India or if the income, whether capitalised or not, has been brought into India in any form.

2.5.2 Penalty payable when tax in default [Sec. 221]

When an assessee is in default or is deemed to be in default in making a payment of tax, he shall, in addition to the amount of the arrears and the amount of interest payable u/s 220(2), be liable, by way of penalty, to pay such amount as the Assessing Officer may direct, and in the case of a continuing default, such further amount or amounts as the Assessing Officer may, from time to time, direct, so, however, that the total amount of penalty does not exceed the amount of tax in arrears.

Notes:

a) The assessee shall be given a reasonable opportunity of being heard.

b) Where the assessee proves to the satisfaction of the Assessing Officer that the default was for good and sufficient reasons, no penalty shall be levied under this section.

c) An assessee shall not cease to be liable to any penalty merely by reason of the fact that before the levy of such penalty he has paid the tax.

d) Where as a result of any final order the amount of tax, with respect to the default in the payment of which the penalty was levied, has been wholly reduced, the penalty levied shall be cancelled and the amount of penalty paid shall be refunded.

2.5.3 Certificate to Tax Recovery Officer [Sec. 222]

- When an assessee is in default or is deemed to be in default in making a payment of tax, the Tax Recovery Officer may draw up under his signature a statement in the prescribed form (Form 57) specifying the amount of arrears due from the assessee (such statement being hereafter referred to as "certificate") and shall proceed to recover from such assessee the amount specified in the certificate by one or more of the modes mentioned below (in accordance with the rules laid down in the Second Schedule)

a. attachment and sale of the assessee's movable property;

b. attachment and sale of the assessee's immovable property;

c. arrest of the assessee and his detention in prison;

d. appointing a receiver for the management of the assessee's movable and immovable properties.

- The assessee's movable or immovable property shall include any property which has been transferred, directly or indirectly after 31-5-1973, by the assessee to his spouse or minor child or son's wife or son's minor child, otherwise than for adequate consideration, **and** which is held by, or stands in the name of, any of the persons aforesaid.

  If the movable or immovable property was transferred to his minor child or his son's minor child, it shall, even after the date of attainment of majority by such minor child or son's minor child, as the case may be, continue to be included in the assessee's movable or immovable property for recovering any arrears due from the assessee.

- No step in execution of a certificate shall be taken until the period of 15 days has elapsed since the date of the service of the notice. However, if the Tax Recovery Officer is satisfied that the defaulter is likely to conceal, remove or dispose of his property, he may at any time direct, for reasons to be recorded in writing, an attachment of such property.

  Further, if the defaulter whose property has been so attached furnishes security to the satisfaction of the Tax Recovery Officer, such attachment shall be cancelled from the date on which such security is accepted by the Tax Recovery Officer.

- Arrear amount includes:

  (a) interest upon the amount of tax or penalty or other sum to which the certificate relates as is payable in accordance with sec. 220(2); and

  (b) all charges incurred in respect of:

    (i) the service of notice and of warrants and other processes; &

    (ii) all other proceedings taken for realising the arrears

- The proceeds shall be disposed of in the following manner:

  (a) they shall first be adjusted towards the amount due under the certificate in execution of which the assets were realised and the costs incurred in the course of such execution;

  (b) if there remains a balance, the same shall be utilised for satisfaction of any other amount recoverable from the assessee under this Act which may be due on the date on which the assets were realised; &

  (c) the balance, if any, remaining after above adjustments shall be paid to the defaulter.

- The order of Tax Recovery Officer relating to the execution or discharge etc. shall be final.

  However, a suit may be brought in a civil court upon the ground of fraud.

- If at any time after the certificate is drawn up by the Tax Recovery Officer the defaulter dies, the proceedings (except arrest and detention) may be continued against the legal representative of the defaulter.

- An appeal from any original order passed by the Tax Recovery Officer shall lie to the Chief Commissioner or Commissioner. Such appeal must be presented within 30 days from the date of the order appealed against. Pending the decision of any appeal, execution of the certificate may be stayed if the appellate authority so directs, but not otherwise.

2.5.4 Tax Recovery Officer by whom recovery is to be effected [Sec. 223]

- The Tax Recovery Officer competent to take action u/s 222 shall be:

  (a) the Tax Recovery Officer within whose jurisdiction the assessee carries on his business or profession or within whose jurisdiction the principal place of his business or profession is situate; or

  (b) the Tax Recovery Officer within whose jurisdiction the assessee resides or any movable or immovable property of the assessee is situate,

  the jurisdiction for this purpose being the jurisdiction assigned to the Tax Recovery Officer under the orders or directions issued by the Board, or by the Chief Commissioner or Commissioner who is authorised in this behalf by the Board in pursuance of sec. 120.

- Where an assessee has property within the jurisdiction of more than one Tax Recovery Officer and the Tax Recovery Officer by whom the certificate is drawn up:

  (a) is not able to recover the entire amount by sale of the property, movable or immovable within his jurisdiction; or

  (b) is of the opinion that, for the purpose of expediting or securing the recovery of the whole or any part of the amount, it is necessary so to do,

  he may send the certificate or, where only a part of the amount is to be recovered, a copy of the certificate certified in the prescribed manner and specifying the amount to be recovered to a Tax Recovery Officer within whose jurisdiction the assessee resides or has property and, thereupon, that Tax Recovery Officer shall also proceed to recover the amount as if the certificate or copy thereof had been drawn up by him.

2.5.5 Validity of certificate and cancellation or amendment thereof [See. 224]

It shall not be open to the assessee to dispute the correctness of any certificate drawn up by the Tax Recovery Officer on any ground whatsoever, but it shall be lawful for the Tax Recovery Officer to cancel the certificate if, for any reason, he thinks it necessary so to do, or to correct any clerical or arithmetical mistake therein.

2.5.6 Stay of proceedings [Sec. 225]

- It shall be lawful for the Tax Recovery Officer to grant time for the payment of any tax and when he does so, he shall stay the proceedings for the recovery of such tax until the expiry of the time so granted.
- Where the order giving rise to a demand of tax for which a certificate has been drawn up is modified in appeal or other proceeding under this Act, and, as a consequence thereof, the demand is reduced but the order is the subject-matter of further proceeding under this Act, the Tax Recovery Officer shall stay the recovery of such part of the amount specified in the certificate as pertains to the said reduction for the period for which the appeal or other proceeding remains pending.
- When the order which was the subject-matter of such appeal or other proceeding has become final and conclusive, TRO shall amend the certificate or cancel it.

2.5.7 Other modes of recovery [Sec. 226]

- Whether or not certificate has been drawn up u/s 222, the Assessing Officer may recover the tax by any one or more of the modes provided in this section.

- **Attachment of salary:** If any assessee is in receipt of any income chargeable under the head "Salaries", the Assessing Officer or Tax Recovery Officer may require any person paying the same (i.e., the employer) to deduct from any payment subsequent to the date of such requisition, any arrears of tax due from such assessee. The employer shall comply with any such requisition and shall pay the sum so deducted to the credit of the Central Government or as the Board directs:

- **Garnishee order:** The Assessing Officer or Tax Recovery Officer may by notice in writing require, any person from whom money is due or any person holds or may subsequently hold money for or on account of the assessee, to pay to the Assessing Officer or Tax Recovery Officer so much of the money (subject to maximum of amount payable to assessee) as is sufficient to pay the amount due by the assessee.

  If the person to whom a notice is sent fails to make payment in pursuance thereof to the Assessing Officer or Tax Recovery Officer, he shall be deemed to be an assessee in default in respect of the amount specified in the notice and further proceedings may be taken against him for the realisation of the amount as if it were an arrear of tax due from him, in the manner provided in sec. 222 to 225.

  Any person discharging any liability to the assessee after receipt of a notice shall be personally liable to the Assessing Officer or Tax Recovery Officer to the extent of his own liability to the assessee so discharged or to the extent of the assessee's liability for any sum due under this Act, whichever is less.

  A copy of the notice shall be forwarded to the assessee at his last address known to the Assessing Officer or Tax Recovery Officer.

  Where a person to whom a notice is sent objects to it by a statement on oath that the sum demanded or any part thereof is not due to the assessee or that he does not hold any money for or on account of the assessee, then, nothing shall be deemed to require such person to pay any such sum or part thereof. But if it is discovered that such statement was false in any material particular, such person shall be personally liable to the Assessing Officer or Tax Recovery Officer to the extent of his own liability to the assessee on the date of the notice, or to the extent of the assessee's liability for any sum due under this Act, whichever is less.

- The Assessing Officer or Tax Recovery Officer may apply to the court in whose custody there is money belonging to the assessee for payment to him of the entire amount of such money, or, if it is more than the tax due, an amount sufficient to discharge the tax.

- The Assessing Officer or Tax Recovery Officer may, if authorised by the Chief Commissioner or Commissioner by general or special order, recover any arrears of tax due from an assessee by distraint and sale of his movable property in the manner laid down in the Third Schedule.

2.0.8 Recovery through State Government [See. 227]

The recovery of tax in any area has been entrusted to a State Government, the State Government may recovers any arrears of tax in the same manner as the municipal tax or local rate is recovered.

2.5.9 Recovery of tax in pursuance of agreements with foreign countries [Sec. 228A]

- Where an agreement is entered into by the Central Government with the Government of any country outside India for recovery of income-tax under this Act and the corresponding law in force in that country and the Government of that country or any authority under that Government which is specified in this behalf in such agreement sends to the Board a certificate for the recovery of any tax due under such corresponding law from a resident or a person having any property in India, the Board may forward such certificate to any Tax

Recovery Officer having jurisdiction over the resident or within whose jurisdiction such property is situated and thereupon such Tax Recovery Officer shall:

(a) proceed to recover the amount specified in the certificate in the manner in which he would proceed to recover the amount specified in a certificate drawn up by him u/s 222; and

(b) remit any sum so recovered by him to the Board after deducting his expenses in connection with the recovery proceedings.

- Where an assessee is in default or is deemed to be in default in making a payment of tax, the Tax Recovery Officer may, if the assessee is a resident of a country (being a country with which the Central Government has entered into an agreement for the recovery of income-tax under this Act and the corresponding law in force in that country) or has any property in that country, forward to the Board a certificate drawn up by him u/s 222 and the Board may take such action thereon as it may deem appropriate having regard to the terms of the agreement with such country.

2.5.10 Recovery of penalties, fine, interest and other sums [Sec. 229]

Any sum imposed by way of interest, fine, penalty, or any other sum payable under the provisions of this Act, shall be recoverable in the manner provided for the recovery of arrears of tax.

2.5.11 Tax clearance certificate [Sec. 230]

Person not domiciled in India

- No person,—

(a) who is not domiciled in India;

(b) who has come to India in connection with business, profession or employment; and

(c) who has income derived from any source in India,

shall leave the territory of India by land, sea or air unless he furnishes to the prescribed authority:

(i) an undertaking in the prescribed form [Form 30A] from his employer; or

(ii) through whom such person is in receipt of the income,

to the effect that tax payable by such person who is not domiciled in India shall be paid by the employer or the payer, and the prescribed authority shall, on receipt of the undertaking, immediately give to such person a no objection certificate [Form 30B], for leaving India.

- The aforesaid provision is not applicable to a person who is not domiciled in India but visits India as a foreign tourist or for any other purpose not connected with business, profession or employment.

Person domiciled in India

- Every person, who is domiciled in India at the time of his departure from India, shall furnish, in the prescribed form [Form 30C] to the income-tax authority or such other prescribed authority.

(a) the permanent account number allotted to him u/s 139A

  - However, where permanent account number has not been allotted to him, or his total income is not

chargeable to income-tax or he is not required to obtain a permanent account number under this Act, such person shall furnish a certificate in the prescribed form.

(b) the purpose of his visit outside India;

(c) the estimated period of his stay outside India:

- No person:

  (i) who is domiciled in India at the time of his departure; and

  (ii) in respect of whom circumstances exist which, in the opinion of an income-tax authority render it necessary for such person to obtain a certificate under this section,

  shall leave the territory of India by land, sea or air unless he obtains a certificate from the income-tax authority stating that he has no liabilities under direct tax, or that satisfactory arrangements have been made for the payment of all or any of such taxes which are or may become payable by that person.

  - No such order shall be made unless such income tax authority records the reasons therefor and obtains the prior approval of the Principal Chief Commissioner or Chief Commissioner of Income-tax.

Liability of the carrier

- If the owner or charterer of any ship or aircraft carrying persons from any place in the territory of India to any place outside India allows any of the aforesaid person to travel by such ship or aircraft without first satisfying himself that such person is in possession of a certificate as required, he shall be personally liable to pay the whole or any part of the amount of tax, if any, payable by such person as the Assessing Officer may, determine.
- In respect of any sum payable by the owner or charterer of any ship or aircraft, the owner or charterer, as the case may be, shall be deemed to be an assessee in default for such sum, and such sum shall be recoverable from him as if it were an arrear of tax.

  - Owner and charterer include any representative, agent or employee empowered by the owner or charterer to allow persons to travel by the ship or aircraft.

2.5.12 Faceless collection and recovery of tax [Sec. 231]

- The Central Government may make a scheme for the purposes of issuance of certificate for deduction of income-tax at any lower rates or no deduction of income-tax u/s 197, or deeming a person to be an assessee in default u/s 201(1) or u/s 206C(6A), issuance of certificate for lower collection of tax u/s 206C(9) or passing of order or amended order u/s 210(3) or 210(4), or reduction or waiver of the amount of interest paid or payable by an assessee u/s 220(2A), or extending the time for payment or allowing payment by instalment u/s 220(3), or treating the assessee as not being in default u/s 220(6) or 220(7), or levy of penalty u/s 221, or drawing of certificate by the Tax Recovery Officer u/s 222, or jurisdiction of Tax Recovery Officer u/s 223, or stay of proceedings in pursuance of certificate and amendment or cancellation thereof by the Tax Recovery Officer u/s 225, or other modes of recovery u/s 226 or issuance of tax clearance certificate u/s 230 so as to impart greater efficiency, transparency and accountability by:

  a. eliminating the interface between the income-tax authority and the assessee or any other person to the extent technologically feasible;

  b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a team-based issuance of certificate for deduction or collection of income-tax at lower rate, or for no deduction, or for deeming a person to be an assessee in default, or for passing of an order or amended order, or extending the time for payment, or allowing payment by instalment, or reduction or waiver of interest, or for treating the assessee as not being in default, or for levy of penalty or for drawing of certificate or stay of proceedings in pursuance of certificate and amendment or cancellation thereof, by, or jurisdiction of, Tax Recovery Officer or other modes of recovery or issuance of tax clearance certificate, with dynamic jurisdiction.

2.5.13 Recovery by suit or under other law not affected [Sec. 232]

The several modes of recovery specified in this Chapter shall not affect in any way:

(a) any other law for the time being in force relating to the recovery of debts due to Government; or

(b) the right of the Government to institute a suit for the recovery of the arrears due from the assessee;

and it shall be lawful for the Assessing Officer or the Government, as the case may be, to have recourse to any such law or suit, notwithstanding that the tax due is being recovered from the assessee by any mode specified in this Chapter.

2.5.14 Provisional attachment to protect revenue in certain cases [Sec. 281B]

- Where, during the pendency of any proceeding for the assessment or reassessment or for imposition of penalty u/s 271AAD where the aggregate amounts of penalty likely to be imposed under the said section exceeds ₹ 2 crore, the Assessing Officer is of the opinion that for the purpose of protecting the interests of the revenue it is necessary so to do, he may, with the previous approval of the Chief Commissioner, Commissioner, Director General or Director, by order in writing, attach provisionally any property belonging to the assessee in the manner provided in the Second Schedule.
- Every such provisional attachment shall cease to have effect after the expiry of a period of 6 months from the date of such order.

  However, Principal Chief Commissioner or Chief Commissioner, Principal Commissioner or Commissioner, Principal Director General or Director General or Principal Director or Director may, for reasons to be recorded in writing, extend the aforesaid period by such further period or periods as he thinks fit, so, however, that the total period of extension shall not in any case exceed 2 years or 60 days after the date of order of assessment or reassessment, whichever is later.
- Where the assessee furnishes a guarantee from a scheduled bank for an amount not less than the fair market value of the property provisionally attached, the Assessing Officer shall, by an order in writing, revoke such attachment. However, where the Assessing Officer is satisfied that a guarantee from a scheduled bank for an amount lower than the fair market value of the property is sufficient to protect the interests of the revenue, he may accept such guarantee and revoke the attachment.
- The Assessing Officer may, for the purposes of determining the value of the property provisionally attached, make a reference to the Valuation Officer referred to in sec. 142A, who shall estimate the fair market value of the property in the manner provided under that section and submit a report of the estimate to the Assessing Officer within a period of 30 days from the date of receipt of such reference.
- An order revoking the provisional attachment shall be made:
  - within 45 days from the date of receipt of the guarantee, where a reference to the Valuation Officer has been made; or
  - within 15 days from the date of receipt of guarantee in any other case.

- Where a notice of demand specifying a sum payable is served upon the assessee and the assessee fails to pay that sum within the time specified in the notice of demand, the Assessing Officer may invoke the guarantee furnished, wholly or in part, to recover the amount.
- The Assessing Officer shall, in the interests of the revenue, invoke the bank guarantee, if the assessee fails to renew the guarantee, or fails to furnish a new guarantee from a scheduled bank for an equal amount, 15 days before the expiry of the guarantee.
- The amount realised by invoking the guarantee shall be adjusted against the existing demand which is payable by the assessee and the balance amount, if any, shall be deposited in the Personal Deposit Account of the Principal Commissioner or Commissioner in the branch of the Reserve Bank of India or the State Bank of India or of its subsidiaries or any bank as may be appointed by the Reserve Bank of India as its agent at the place where the office of the Principal Commissioner or Commissioner is situate.
- Where the Assessing Officer is satisfied that the guarantee is not required anymore to protect the interests of the revenue, he shall release that guarantee forthwith.

2.5.15 Certain transfers to be void [Sec. 281]

- Where, during the pendency of any proceeding under this Act or after the completion thereof, but before the service of notice by TRO, any assessee creates a charge on or parts with the possession (by way of sale, mortgage, gift, exchange or any other mode of transfer whatsoever) of, any of his assets in favour of any other person, such charge or transfer shall be void as against any claim in respect of any tax or any other sum payable by the assessee as a result of the completion of the said proceeding or otherwise.
- Assets means land, building, machinery, plant, shares, securities and fixed deposits in banks, to the extent to which any of the assets aforesaid does not form part of the stock-in-trade of the business of the assessee.
- However, such charge or transfer shall not be void if it is made:

  (i) for adequate consideration and without notice of the pendency of such proceeding or without notice of such tax or other sum payable by the assessee; or

  (ii) with the previous permission of the Assessing Officer.
- This section applies to cases where the amount of tax or other sum payable or likely to be payable exceeds ₹ 5,000 and the assets charged or transferred exceed ₹ 10,000 in value.

2.5.16 Service of notice generally [Sec. 282]

The service of a notice or summon or requisition or order or any other communication under this Act (hereafter in this section referred to as "communication") may be made by delivering or transmitting a copy thereof, to the person therein named:

a) by post or by such courier services as may be approved by the Board; or

b) in such manner as provided under the Code of Civil Procedure, 1908 for the purposes of service of summons; or

c) by e-mail; or

d) by any other means of transmission of documents as provided by rules made by the Board in this behalf.

2.5.17 Authentication of notices and other documents [Sec. 282A]

- Where the Act requires a notice or other document to be issued by any income-tax authority, such notice or other document shall be signed and issued in paper form or communicated in electronic form by that authority in accordance with such procedure as may be prescribed.
- Every notice or other document to be issued, served or given for the purposes of this Act by any income-tax authority, shall be deemed to be authenticated if the name and office of a designated income-tax authority is printed, stamped or otherwise written thereon.

2.5.18 Return of income, etc., not to be invalid on certain grounds [Sec. 292B]

No return of income, assessment, notice, summons or other proceeding, furnished or made or issued or taken or purported to have been furnished or made or issued or taken in pursuance of any of the provisions of this Act shall be invalid merely by reason of any mistake, defect or omission in such return of income, assessment, notice, summons or other proceeding if such return of income, assessment, notice, summons or other proceeding is in substance and effect in conformity with or according to the intent and purpose of this Act.

2.5.19 Notice deemed to be valid in certain circumstances [Sec. 292BB]

Where an assessee has appeared in any proceeding or co-operated in any inquiry relating to an assessment or reassessment, it shall be deemed that any notice, which is required to be served upon him, has been duly served upon him in time in accordance with the provisions of this Act and such assessee shall be precluded from taking any objection in any proceeding or inquiry under this Act that the notice was—

(a) not served upon him; or

(b) not served upon him in time; or

(c) served upon him in an improper manner.

However, aforesaid provision is not applicable, where the assessee has raised such objection before the completion of such assessment or reassessment.

REFUND

2.5.20 Meaning of Refund [Sec. 237]

Where the tax paid by the assessee[#] is in excess of his tax liability, then such assessee shall be entitled to receive back such excess amount, called refund.

As per sec.237, if any person satisfies the Assessing Officer that the amount of tax paid by him (or on his behalf) for any assessment year, exceeds the amount with which he is chargeable under this Act, then he shall be entitled to a refund of such excess amount.

[#] Tax paid by the assessee includes the following -

1. Advance tax;
2. Tax deducted at source (TDS);
3. Tax collected at source (TCS);
4. Self assessment tax; and
5. Tax paid on demand

2.5.21 Who can claim refund

Following person can claim refund -

1. A person who has paid tax more than the amount for which he is chargeable under this Act [Sec. 237];
2. Where the income of one person is included in the total income of other person, such other person is entitled to claim refund on tax paid on such income [Sec. 238(1)]
3. Where due to death, incapacity, insolvency, liquidation or any other cause, a person is unable to claim or receive any refund due to him, his legal representative, trustee, guardian or receiver, as the case may be, can claim and receive such refund for the benefit of such person or his estate [Sec. 238(2)]

2.5.22 Form and Time limit for claiming refund [Sec. 239]

Every claim for refund shall be made by furnishing return in accordance with the provisions of sec. 139.

2.5.23 Refund on Appeal, etc. [Sec. 240]

Where any refund becomes due as a result of any order passed in appeal or other proceedings, the Assessing Officer shall refund the amount to the assessee *suomoto* i.e. without any claim being made by the assessee in this behalf. Such refund shall become due on –

Case	When refund becomes due
Where an assessment is set aside or cancelled and an order of fresh assessment is directed to be made	The refund shall become due on completion of such fresh assessment and amount of refund shall be decided as per the fresh assessment.
Where the assessment is annulled	The refund shall become due when such assessment is annulled. The refund shall be only of the amount of the tax paid in excess of tax as per return.

2.5.24 Correctness of assessment not to be questioned [Sec. 242]

In a claim of refund, it shall not be open to the assessee to question the correctness of any assessment or other matter decided which has become final and conclusive or ask for a review of the same, and the assessee shall not be entitled to any relief on such claim except refund of tax wrongly paid or paid in excess.

2.5.25 Set-off of refund against tax remaining payable [Sec. 245]

Where refund becomes due or is found to be due to any person, the Assessing Officer or Commissioner or Principal Commissioner or Chief Commissioner or Principal Chief Commissioner, as the case may be, may, in lieu of payment of the refund, set off the amount to be refunded or any part of that amount, against the sum, if any, remaining payable by the person to whom the refund is due. However, such action can be taken after giving an intimation in writing to such person.

Withholding in Anticipation of tax liability: Where a part of the refund is set off or where no such amount is set off, and refund becomes due to a person, and the Assessing Officer, having regard to the fact that proceedings for assessment or reassessment are pending in the case of such person, is of the opinion that the grant of refund is likely to adversely affect the revenue, he may, for reasons to be recorded in writing and with the previous approval of the Principal Commissioner or the Commissioner, as the case may be, withhold the refund up to the date on which such assessment or reassessment is made

2.5.26 Refund for denying liability to deduct tax in certain cases [Sec. 239A]

- Tax deducted by a person u/s 195 may be refunded to the deductor, if the following conditions are satisfied:
  a. There is an agreement (or other arrangement), in writing, under which tax deductible on any income, other than interest, u/s 195 is to be borne by the payer of the income
  b. Such person has paid tax to the credit of the Central Government
  c. After payment, he is claiming that no tax was required to be deducted on such income.
  d. Such claim can be made within a period of 30 days from the date of payment of such tax by filing an application before the Assessing Officer in the prescribed form.
- The Assessing Officer shall, by an order in writing, allow or reject the application after giving an opportunity of being heard and making such inquiry as he considers necessary.
- Such order shall be passed within 6 months from the end of the month in which application is received
- If the applicant is not satisfied with the order, he may file an appeal before the Commissioner (Appeals) u/s 246A.

2.5.27 Interest on Refund [Sec. 244A]

Refer Interest.

Exercise

Multiple Choice Questions

1. What is the due date of filing the return of income in case of a company who is required to furnish a report in Form No. 3CEB under section 92E?
   A. September 30 of the assessment year
   B. November 30 of the assessment the year
   C. July 31 of the assessment year
   D. June 30 of relevant assessment the year

2. One of the following, can be carried forward even return of income is filed after due date:
   A. Unabsorbed Depreciation
   B. Business Loss
   C. Short term capital loss
   D. Long term capital loss

3. Return filed under following sections can be revised u/s 139(5)
   A. 139(1)
   B. 139(4)
   C. 139(5)
   D. All of the above

4. Assessment under following section is termed as scrutiny assessment
   A. 143(3)
   B. 144
   C. Both of the above
   D. None of the above

5. When an assessee has paid advance tax more than the tax due on the returned income and the return is filed before the 'due date' specified in section 139(1), the refund amount is eligible for interest @ —

   A. 1% per month

   B. ½% per month

   C. ¾% per month

   D. 1.50% per month

[Answer : 1 – B, 2 – A, 3 – D, 4 – A, 5 - B]

Short Essay Type Questions

1. State the provisions relating to filing of belated return.
2. State the power of the income-tax authority u/s 131.
3. What do you mean by deemed seizure?
4. State the procedure of scrutiny assessment.

Comprehensive Numerical Problems

1. The following particulars are furnished by Ms. Devi for the financial year 2023-24:

   - Tax on total income (paid on 10.08.2024) ₹ 1,50,000.
   - Date of filing the return 10.08.2024
   - Due date for filing the return 31.07.2024

   Compute the total interest payable under sections 234A, 234B & 234C.

[Ans. ₹ 15,075]

Reference

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Grievance Redressal 3

This Module includes:

3.1 Appeal

3.2 Rectification

3.3 Revision

3.4 Settlement Commission

3.5 Advance Ruling

Grievance Redressal

SLOB Mapped against the Module:

To acquire knowledge on various provisions and processes available as per taxation laws that offers for redressal of taxpayers' grievances.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify the order appealable before different forum
- Appreciate the time limit for filing grievance
- Appreciate the procedure before various grievance redressal authorities
- Analyse and apply his skill to determine whether an order is appealable or not.

Introduction

3

One Law Dictionary defines 'appeal' as the act of asking a higher authority to change a decision of a lower authority. Right to appeal under income tax law is a creation of statute and not an inherent right. Appeal can be filed only against orders listed in the Income Tax Act and not any order.

Initially, following course of action are available in the Income-tax Act:

Assessee	Department
Rectificatin u/s 154	Rectificatin u/s 154
Appeals	Revision u/s 263
Revision u/s 264	Reassessment u/s 147

Appeal

3.1

Appellate Authorities in Income-tax Act

Appeal	Appellate authority	Against which order	Appellant
1st	Joint Commissioner (Appeals) or Commissioner (Appeals)	Against specified order of the Assessing Officer	Assessee only
2nd	Income Tax Appellate Tribunal (ITAT)	Against the order of Commissioner (Appeals)	Assessee or the Commissioner (or Principal Commissioner) of Income tax.
3rd	High Court	Against the order of ITAT (the case must involve substantial question of law)	
Final	Supreme Court	Against the order of High Court	

3.1.1 Appeals before Joint Commissioner (Appeals) [JCIT (A)] [Sec. 246]

As per the existing scheme for appeals, the first appellate authority for an assessee aggrieved by any order issued under the Act is the Commissioner (Appeals). Such Commissioner (Appeals) has the powers to confirm, reduce, enhance or annul/ cancel an order of assessment or an order of penalty, after providing an opportunity of being heard to the assessee and the AO. The order passed by the Commissioner (Appeals) are appealable before the Appellate Tribunal.

However, as the first authority for appeal, Commissioner (Appeals) were overburdened due to the huge number of appeals and the pendency being carried forward every year. In order to clear this bottleneck, a new authority for appeals is created at Joint Commissioner/ Additional Commissioner level to handle certain class of cases involving small amount of disputed demand. Such authority has all powers, responsibilities and accountability similar to that of Commissioner (Appeals) with respect to the procedure for disposal of appeals

Any assessee aggrieved by any of the following orders of an Assessing Officer (below the rank of Joint Commissioner) may appeal to the Joint Commissioner (Appeals) against:

a. an intimation u/s 143(1), where the assessee objects to the making of adjustments; or

b. Any order of assessment u/s 143(3) or sec. 144, where the assessee objects to the amount of income assessed, or to the amount of tax determined, or to the amount of loss computed, or to the status (Status means the category under which the assessee is assessed as “individual”, “Hindu undivided family” and so on) under which he is assessed;

c. an order of assessment, reassessment or recomputation u/s 147;

d. an intimation u/s 200A(1);

e. an order u/s 201;

f. an intimation u/s 206C(6A);

g. an order u/s 206CB(1);

h. an order imposing a penalty under Chapter XXI; and

i. an order u/s 154 or sec. 155 amending any of the orders mentioned above

Exception

No appeal shall be filed before the Joint Commissioner (Appeals) if any of the aforesaid order is passed by or with the prior approval of, an income-tax authority above the rank of Deputy Commissioner.

Taxpoint

- Transfer of appeals: Where any appeal filed against any of the aforesaid order is pending before the Commissioner (Appeals), the Board or authorised income-tax authority may transfer such appeal and any matter arising out of or connected with such appeal and which is so pending, to the Joint Commissioner (Appeals) who may proceed with such appeal or matter, from the stage at which it was before, it was so transferred.
  - The Board or authorised income-tax authority may transfer any appeal which is pending before a Joint Commissioner (Appeals) and any matter arising out of or connected with such appeal and which is so pending, to the Commissioner (Appeals) who may proceed with such appeal or matter, from the stage at which it was before, it was so transferred.
  - After such transfer of an appeal, the appellant shall be given an opportunity of being reheard.
- The provision shall not apply to any case or any class of cases as specified by the Board.
- Scheme for disposal of the appeal: For the purposes of disposal of appeal by the Joint Commissioner (Appeals), the Central Government may make a scheme so as to dispose of appeals in an expedient manner with transparency and accountability, by eliminating the interface between the Joint Commissioner (Appeals) and the appellant, in the course of appellate proceedings to the extent technologically feasible and direct that any of the provisions of this Act relating to jurisdiction and procedure for disposal of appeals by the Joint Commissioner (Appeals), shall not apply or shall apply with such exceptions, modifications and adaptations as may be specified in the notification.

3.1.2 Appeals to Commissioner of Income Tax (Appeals) [CIT (A)] [Sec. 246A to 250]

Aggrieved tax payer can file appeal before the Commissioner (Appeals) having, jurisdiction over the tax payer. Designation of the Commissioner (Appeals), with whom appeal is to be filed is also mentioned in the notice of demand issued by the Assessing Officer u/s 156.

Provision regarding appeal to the Commissioner (Appeal) are enumerated below:

Appealable Orders	**U/s 246A** ➢ Order passed by a Joint Commissioner u/s 115VP(3)(ii); ➢ Order against the assessee, where the assessee denies his liability to be assessed under this Act; ➢ Intimation u/s 143(1) or 143(1B) or 200A(1) or 206CB(1) or Order of assessment u/s 143(3) [Scrutiny assessment] [except an order passed in pursuance of directions of the Dispute Resolution Panel or an order referred to in sec. 144BA(12)] or u/s 144 [Best judgment assessment] in respect of income assessed or tax determined or loss computed or residential status;

	➢ Order of assessment, reassessment or recomputation u/s 147 [(except an order passed in pursuance of directions of the Dispute Resolution Panel or an order referred to in sec. 144BA(12)], 150 & 153A [except an order passed in pursuance of directions of the Dispute Resolution Panel or an order referred to in sec. 144BA(12)]; ➢ Order u/s 154 (Rectification of Mistake) or u/s 155 (other amendments) having the effect of enhancing the assessment or reducing a refund or an order refusing to allow the claim made by the assessee [except where it is in respect of an order referred to in sec. 144BA(12)] ➢ Order u/s 92CD(3) ➢ Order u/s 163 treating assessee as an agent of a non-resident; ➢ Order u/s 170 relating to assessment on succession; ➢ Order u/s 171 refusing to recognize partition of an HUF; ➢ Order u/s 201 or 206C(6A) for default of provisions of TDS/TCS; ➢ Order u/s 237 relating to refunds or sec. 239A; ➢ Order relating to Penalty; ➢ Order imposing penalty under chapter XXI; ➢ An order of penalty imposed under chapter XXI or an order of imposing or enhancing penalty u/s 275(1A) ➢ Any order made by an Assessing Officer other than a Joint Commissioner, as the Board may direct.	
	Notes: a) Even when reassessment proceedings have been initiated u/s 147, an appeal can still be filed against the original assessment order passed u/s 143(3) b) Assessee has the right to appeal against an order of the Assessing Officer which is passed while giving effect to the decision of the appellate authority.	
Time limit for filing appeal	Appeal should be filed within 30 days from -	
	Where the appeal is u/s 248	The date of payment of the tax
	Where the appeal relates to any assessment or penalty	The date of service of notice of demand relating to the assessment or penalty
	In any other case	The date on which intimation or the order, sought to be appealed against, is served.
	Period to be excluded [Sec.268] While calculating the above time limit, following period shall be excluded - a) The day on which order complained of was served; and b) Time required for obtaining a copy of the order, where a copy of the order was not furnished with notice of demand. c) Where an application has been made u/s 270AA (seeking immunity from penalty and prosecution), the period beginning from the date on which the application is made, to the date on which the order rejecting the application is served on the assessee	

Delay in filing appeal	The Joint Commissioner (appeals) or Commissioner (Appeals) may admit belated application on sufficient cause being shown. **Note:** It is statutory obligation of the appellate authority (where an application for condonation is filed) to consider whether sufficient cause was shown by the appellant
Form of appeal	Form 35 (Mode of filing depends i.e., electronically or in paper form, on mode of filing return of income of the assessee)
Documents to be submitted	➢ Memorandum of appeal ➢ Order against which appeal is made ➢ Statement of facts ➢ Grounds of appeal ➢ Notice of demand (in Original) ➢ Challan New Form 35 does not prescribe any documents but earlier Form 35 prescribed aforesaid documents should accompany with the form.
Verification of Form	Form & grounds of appeal must be verified by the person authorised to verify the return of income u/s 140
Payment of tax before filing of appeal	**If a return has been filed –** Tax as per the return should be paid. **If no return has been filed –** The assessee should pay an amount equal to the advance tax which was payable by him. However, JCIT(A) or CIT(A) may, for any good and sufficient reason (recorded in writing), accept the appeal without payment of such advance tax. **Power of Assessing Officer:** As per sec. 220(6), where an assessee has presented an appeal u/s 246A, Assessing Officer may treat the assessee as not being in default in respect of the amount in dispute in the appeal. It may be applied - ➢ at the discretion of the Assessing Officer; ➢ subject to such conditions as Assessing Officer may think fit to impose; ➢ even though the time for payment has expired; ➢ as long as such appeal remains undisposed of. In the event of Assessing Officer rejecting assessee's application u/s 220(6), the assessee can prefer an application to the jurisdictional Commissioner for staying the demand of tax in dispute till the hearing and final disposal of the assessee's appeal by the JCIT (A) or Commissioner (Appeals) If the JCIT (A) or Commissioner (A) fails to discharge his duty, the assessee may file a Writ Petition. However, when an appeal is pending before the Income Tax Appellate Tribunal, the assessee can file a Stay Petition before the Income Tax Appellate Tribunal to stay the recovery proceedings. **Taxpoint:** The first appellate authority has power to grant stay, which is incidental and ancilliary to its appellate jurisdiction.

Fee	Where assessed income as computed by the Assessing Officer is -	
	➢ Up to ₹ 1,00,000	– ₹ 250
	➢ Exceeds ₹ 1,00,000 but does not exceed ₹ 2,00,000	– ₹ 500
	➢ Exceeds ₹ 2,00,000	– ₹ 1,000
	Where the subject matter of appeal is not covered in above cases	– ₹ 250
Procedure	1. **Fixation of Day & Place:** The JCIT (Appeals) or Commissioner (Appeals) shall fix a day and place for the hearing of the appeal, and shall give notice of the same to the appellant and to the Assessing Officer against whose order the appeal is preferred. 2. **Hearing:** The appellant (either in person or by an authorised representative) and the Assessing Officer (either in person or by an authorised representative) shall have the right to be heard at the hearing of the appeal. **Taxpoint:** Where the assessee does not insist on a personal hearing the appeal may be decided on the basis of written submission made by him. [Letter No. 277/7/84 of November, 1985] 3. **Adjournment:** The JCIT (Appeals) or Commissioner (Appeals) shall have the power to adjourn the hearing of the appeal from time to time. 4. **Inquiry:** The JCIT (Appeals) or Commissioner (Appeals) may, before disposing of any appeal, make such further inquiry as he thinks fit, or may direct the Assessing Officer to make further inquiry and report the result of the same to the JCIT (Appeals) or Commissioner (Appeals). 5. **Order:** JCIT (Appeals) or Commissioner (Appeals) must dispose of the appeal by passing an order which shall - ➢ be in writing; ➢ mention the points for determination; ➢ mention the decision thereon; and ➢ mention the reason for the decision.	
	6. **Communication of Order:** The JCIT (Appeals) or Commissioner (Appeals) shall communicate the order passed by him to the assessee and to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner. **Note:** If during pendency of an appeal, provision of any law has changed with retrospective effect, then such changed law shall be applicable on such appeal too. Law amended retrospectively would be a good law for applicability during the pendency of the appeal	
New grounds during hearing	The JCIT (Appeals) or Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the 'grounds of appeal', if he is satisfied that the omission of that ground from the Form of appeal was not wilful or unreasonable.	
Time limit for disposal of appeal	Within one year (if possible) from the end of financial year in which appeal is filed before him or transferred to him.	

<table>
<tr><td>Production of additional evidence</td><td colspan="2">Appellate authority has the power to accept additional evidence (after recording reason for its admission in writing) and may make further enquiry at his discretion before disposing of the appeal

In the following circumstances additional evidence shall be admitted by the JCIT (A) or Commissioner (Appeals):

a) Where the Assessing Officer has refused to admit evidence which ought to have been admitted; or

b) Where appellant was prevented by sufficient cause from producing before the Assessing Officer any evidence, which is related to any ground of appeal; or

c) Where the appellant was prevented by sufficient cause from producing the evidence, which he was called upon to produce by the Assessing Officer; or

d) Where the Assessing Officer has made an order (appealed against) without giving sufficient opportunity to the appellant to produce evidence relevant to any ground of appeal.

Taxpoint: Before taking into account the additional evidence filed, JCIT (A) or Commissioner (Appeals) is to provide reasonable opportunity to the Assessing Officer for examining the additional evidence or the witness as well as to produce evidences to rebut additional evidences filed by the tax payer.</td></tr>
<tr><td rowspan="4">Powers of Joint Commissioner (Appeals) or Commissioner (Appeals) u/s 251</td><td>1. Against an order of assessment</td><td>To confirm, reduce, enhance or annul the assessment</td></tr>
<tr><td>2. Against an order imposing a penalty</td><td>To confirm or cancel such order or vary it so as either to enhance or to reduce the penalty;</td></tr>
<tr><td>3. Relating to any other case</td><td>To pass such orders as he thinks fit.</td></tr>
<tr><td colspan="2">Notes:

1. The Joint Commissioner (Appeals) or Commissioner (Appeals) may consider and decide any matter arising out of the proceedings in which the order appealed against was passed, notwithstanding that such matter was not raised before the Joint Commissioner (Appeals) or Commissioner (Appeals) by the appellant.

2. The Joint Commissioner (Appeals) or Commissioner (Appeals) does not have any power to set a site the assessment for fresh assessment by the Assessing Officer

3. The Joint Commissioner (Appeals) or Commissioner (Appeals) shall not enhance an assessment or a penalty or reduce the amount of refund unless the appellant has had a reasonable opportunity of showing cause against such enhancement or reduction.

4. An assessment order, which is void ab initio cannot become a valid order simply by virtue of the fact that it has been confirmed by an appellate authority.</td></tr>
<tr><td>Withdrawal of appeal</td><td colspan="2">Appeal once filed cannot be withdrawn.</td></tr>
</table>

Faceless	The Central Government may make a scheme for the purposes of disposal of appeal by Commissioner (Appeals), so as to impart greater efficiency, transparency and accountability by: a. eliminating the interface between the Commissioner (Appeals) and the appellant in the course of appellate proceedings to the extent technologically feasible; b. optimising utilisation of the resources through economies of scale and functional specialisation; c. introducing an appellate system with dynamic jurisdiction in which appeal shall be disposed of by one or more Commissioner (Appeals). Faceless Appeal Scheme 2021 has been notified.

3.1.3 Appeals to Income Tax Appellate Tribunal (ITAT) [Sec. 252 to 255]

Appeal against an order of Commissioner (Appeals) lies with the Income Tax Appellate Tribunal (ITAT). Both taxpayer and the Assessing Officer can file an appeal before the Appellate Tribunal. Several Benches of the Appellate Tribunal are constituted all over India by the Central Government and it functions under the Ministry of Law. It consists of as many judicial and accountant members as the Central Government thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.

Qualification of members

Member	Qualification
Judicial	➢ He has held a post of Judicial Officer in the territory of India for at least 10 years; or ➢ He has been served as a member of the Indian Legal Service in Grade II post or any higher post for at least 3 years; or ➢ He has been an advocate for at least 10 years.
Accountant	➢ He has practiced as a Chartered Accountant for at least 10 years; or ➢ He has practiced as a registered accountant for at least 10 years; or ➢ He has practiced partly as a registered accountant and partly as a Chartered Accountant for at least 10 years; or ➢ He has been a member of the Indian Income-tax Service, Group A, and has held the post of the Additional Commissioner of Income-tax or any equivalent or higher post for at least 3 years.

President of the ITAT

- The Central Government shall appoint:
  a. a person who is a sitting or retired Judge of a High Court and who has completed not less than 7 years of service as a Judge in a High Court; or
  b. one of the Vice-Presidents of the Appellate Tribunal,
  - to be the President thereof.
- The Central Government may appoint one or more members of the Appellate Tribunal to be the Vice-President(s) thereof.
- The Vice-President shall exercise such of the powers and perform such of the functions of the President as may be delegated to him by the President by a general or special order in writing.

Appealable Orders and Procedure of Appeal

Appealable Orders	**A. Appeal by assessee** 1. An order passed by a Commissioner (Appeals) u/s 154, 250, 270A, 271, 271A, 271AAB, 271AAC, 271AAD, 271J or 272A; or 2. An order passed by a Joint Commissioner (Appeals) u/s 154, 250, 270A, 271, 271A, 271AAC, 271AAD or 271J; or 3. an order passed by, — a Principal Commissioner or Commissioner u/s 12AA or 12AB or 80G(5)(vi) or 263 or 270A or 271 or 272A or an order passed by him u/s 154 amending any such order; or — a Principal Chief Commissioner or Chief Commissioner or a Principal Director General or Director General or a Principal Director or Director u/s 263 or 272A or an order passed by him u/s 154 amending any such order 4. An order passed by an Assessing Officer u/s 143(3) or 147 or 153A or 153C in pursuance of the directions of the Dispute Resolution Panel or with the the approval of the Commissioner (or Principal Commissioner) as referred to in sec. 144BA(12) or an order passed u/s 154 or 155 in respect of such order. 5. An order passed by an Assessing Officer u/s 115VZC(1) 6. An order passed by the prescribed authority u/s 10(23C)(iv) or (v) or (vi) or (via)
	B. Appeal by the Principal Commissioner or Commissioner The Principal Commissioner or Commissioner may direct the Assessing Officer to appeal against the order passed by the Joint Commissioner (Appeals) or Commissioner (Appeals) u/s 154 or 250 [The Board has directed that the appeal shall not be filed by the department where the tax effect does not exceed ₹ 50,00,000, subject to certain exceptions]
Time limit for filing appeal	Within 60 days. The period shall start from the date on which order sought to be appealed is communicated to the assessee or Commissioner.
Delay in filing appeal	Tribunal may admit belated application on sufficient cause being shown.
Withdrawal of appeal	An assessee cannot withdraw an appeal filed to Tribunal
Form	Form 36
Documents to be submitted	1. Memorandum of Appeal (in triplicate) 2. Two copies of the order appealed against (including one certified copy) 3. Two copies of the order of Assessing Officer 4. Two copies of the grounds of appeal before first appellate authority 5. Two copies of the statement of facts filed before first appellate authority 6. In case, appeal against order levying penalty, relevant order (two copies)

Fee payable by assessee	Where assessed income as computed by the Assessing Officer is -	
	➢ Upto ₹ 1,00,000	₹ 500
	➢ Exceeds ₹ 1,00,000 but does not exceed ₹ 2,00,000	₹ 1,500
	➢ Exceeds ₹ 2,00,000	1% of Assessed income [Max. ₹ 10,000]
	Stay petition	₹ 500
	Any other case	₹ 500
Fee payable by CIT	No fees shall be payable in case of appeal by Commissioner	
Verification of Form	Form 36 and grounds of appeal should be verified by the person authorized to verify the return of income u/s 140 [Rule 47]	
Cross objection	Assessing Officer or the assessee, as the case may be, on receipt of notice that an appeal has been filed by the other party, may file a memorandum of cross objection with the Tribunal	
Time limit for filing of cross-objections	Within 30 days of receipt of notice that appeal has been filed by the other party. However, Tribunal may admit belated memorandum of cross objection on sufficient cause being shown.	
Form for filing of cross-objections	Form 36A	
Fee for cross objection	Nil	
Order of tribunal	The Appellate Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders as it thinks fit. Tribunal must record its reasons for its decisions. Order should set out all facts and contentions. **Communication of order:** Tribunal shall send a copy of the order passed by it to the assessee and to the Principal Commissioner or Commissioner. **Notes:** a) Decision of Tribunal on matter involving question of fact is final. However, one can file a writ petition. b) A decision of the tribunal, when passed in appeal, is final not only for the assessee but also for the tribunal itself. c) The assessee cannot seek to reopen and reargue the whole matter. i.e. order of Tribunal cannot be reviewed by Tribunal. d) On a question of fact determined by ITAT, a writ petition can be filed to the High Court challenging the fact finding process adopted by the ITAT. If the High Court is satisfied that the fact finding process was not correct, then it will quash the order passed by the ITAT and direct the ITAT to do the fact finding in the proper manner and/or as per the direction of the High Court. If the writ petition is dismissed by the High Court then the assessee can file a Special Leave Petition to the Apex Court challenging the fact finding process of the ITAT. If the Apex Court is satisfied that the fact finding process was incorrect then the Apex Court quash the order passed by the ITAT and direct the ITAT to do the fact finding in the proper manner and/or as per the direction of the Apex Court.	

Rectification of mistake (Miscellaneous Application)	➢ The Tribunal may, at any time within 6 months from the end of the month in which the order was passed, with a view to rectify any mistake apparent from the record, amend any order passed by it. ➢ Mistake may be brought to the notice of the Tribunal by the assessee or the Assessing Officer. ➢ Where assessee applies for any rectification, it shall be accompanied by a fee of ₹ 50. ➢ An amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee, shall not be made unless the Appellate Tribunal has given notice to the assessee of its intention to do so and has allowed the assessee a reasonable opportunity of being heard. ➢ It is to be noted that income tax authority [including CIT(A)] can rectify order u/s 154, however in that case: a. Assessee is not required to pay any fee; and b. Time limit is 4 years from the end of the financial year in which the order sought to be rectified was passed.
Additional grounds which may be taken in appeal	Tribunal has discretionary power to refuse additional ground to be raised. Tribunal may permit the assessee to urge grounds of appeal not mentioned in the memorandum of appeal.
Additional evidence	The parties to the appeal are not entitled to produce additional evidence of any kind, either oral or documentary before the Tribunal. However, if the Tribunal requires production of any document, examination of any witness or filing of any affidavit to enable it to pass orders, it may allow such document to be produced, witness to be examined, affidavit to be filed and such evidence to be adduced.
Time limit for passing order	Appellate Tribunal, where it is possible, may hear and decide such appeal within a period of 4 years from the end of the financial year in which such appeal is filed. However, the Tribunal, after considering the merits, may pass an order of stay in any proceedings for a period not exceeding 180 days (provided the assessee deposits not less than 20% of the amount of tax, interest, fee, penalty, or any other sum payable or furnishes security of equal amount in respect thereof) from the date of such order and the Tribunal shall dispose of the appeal within the said period of stay specified in that order. However, no extension of stay shall be granted by the Appellate Tribunal, where such appeal is not so disposed of within the said period of stay as specified in the order of stay, unless the assessee makes an application and has complied with the condition and the Appellate Tribunal is satisfied that the delay in disposing of the appeal is not attributable to the assessee, so however, that the aggregate of the period of stay originally allowed and the period of stay so extended shall not exceed 365 days and the Appellate Tribunal shall dispose of the appeal within the period or periods of stay so extended or allowed. Further if such appeal is not so disposed of within the period allowed (original and extended), the order of stay shall stand vacated after the expiry of such period (i.e., 365 days), even if the delay in disposing of the appeal is not attributable to the assessee[1].

[1] Wherever appeal could not be decided by the tribunal due to pressure of pendency of cases and delay in disposal of appeal was not attributable to the assessee in any manner, interim protection of stay could continue beyond 365 days in deserving cases [PCIT -vs.- Comverse Network Systems India (P) Ltd. (2019) 262 Taxman 99 (SC)]

Cost of appeal	Cost of appeal shall be borne by the person as decided by the Tribunal.
Procedure	➢ The powers and functions of the Appellate Tribunal may be exercised and discharged by Benches constituted by the President of the Appellate Tribunal from among the members thereof. ➢ A Bench shall consist of one judicial member and one accountant member. However, in some case, single member bench may be constituted. ➢ The President or any other member of the Appellate Tribunal authorised in this behalf by the Central Government may, sitting **singly**, dispose of any case which has been allotted to the Bench of which he is a member and which pertains to an assessee whose total income as computed by the Assessing Officer in the case does not exceed ₹ 50 lakh. ➢ The President may, for the disposal of any particular case, constitute a Special Bench consisting of 3 or more members, one of whom shall necessarily be a judicial member and one an accountant member. ➢ If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority. But if the members are equally divided, then the case shall be referred by the President of the Appellate Tribunal for hearing on such point by one or more of the other members of the Appellate Tribunal, and such point shall be decided according to the opinion of the majority of the members of the Appellate Tribunal who have heard the case, including those who first heard it.
Faceless	The Central Government may make a scheme, for the purposes of appeal to the Appellate Tribunal, so as to impart greater efficiency, transparency and accountability by: a. optimising utilisation of the resources through economies of scale and functional specialisation; b. introducing a team-based mechanism for appeal to the Appellate Tribunal, with dynamic jurisdiction.

3.1.4 Appeal to High Court [Sec. 260A]

Who can file appeal	Assessee or the Principal Chief Commissioner / Chief Commissioner / Principal Commissioner / Commissioner, being aggrieved by the order of ITAT. **Taxpoint:** Only order passed by the ITAT (which involves substantial question of law) can be appealed in the High court. [The Board has directed that the appeal shall be filed by the department only if tax effect exceeds ₹ 1,00,00,000, subject to certain exceptions]
Appealable order	Any order of the Tribunal, if the High Court is satisfied that the case involves a substantial question of law.
Substantial question of law	➢ The word "substantial" means having substance, essential, real, of sound worth, important or considerable; ➢ The substantial question of law, need not necessarily be a substantial question of law of general importance (i.e. it should be a question of law between the parties); ➢ To be "substantial", a question of law must be debatable, not previously settled by law of the land or a binding precedent, and must have a material bearing on the decision of the case.

Time limit for filing appeal	120 days from the date on which order of the Tribunal is received by the assessee or Principal Chief Commissioner / Chief Commissioner / Principal Commissioner / Commissioner The High Court may admit an appeal after the expiry of said period, if it is satisfied that there was sufficient cause for not filing the same within that period.
Court Fee	The Court fee shall be as specified in relevant law relating to Court fees for filing an appeal to High Court
Manner of appeal	The appeal shall be in form of a memorandum of appeal, precisely stating the substantial question of law involved in the appeal.
Formulation of question of law	➢ Where the High Court is satisfied that a substantial question of law is involved, it shall formulate the question. ➢ The appeal is to be heard only on the questions formulated. However, the respondents shall, at the hearing of appeal, be allowed to argue that the case does not involve such question.
Hearing of appeal	➢ The appeal is to be heard by a bench of not less than 2 judges of the High Court. Decision will be in accordance with opinion of the majority of judges. ➢ Where judges are equally divided in their opinions, the case on the point on which they differ shall be heard by one or more other judges of the High Court.
Hearing of other substantial question of law	The Court has the power to hear the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.
Decision	The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the ground on which such decision is founded and may award such cost as it deems fit. The High Court may determine any issue which - a) has not been determined by the Tribunal; or b) has been wrongly determined by the Tribunal, by reason of a decision on such question of law .
Stay of recovery proceedings	High Court has power to stay proceedings for recovery of demand arising out of the assessment order, pending disposal of appeal.

3.1.5 Appeal to the Supreme Court [Sec. 261]

Who can file appeal	Assessee or the Principal Chief Commissioner / Chief Commissioner / Principal Commissioner / Commissioner aggrieved from the judgment of High Court. [The Board has directed that the appeal shall be filed by the department only if tax effect exceeds ₹ 2,00,00,000, subject to certain exceptions]
Order against which appeal is possible	Any order passed in the High Court, provided that High Court ➢ is satisfied that the case involves a substantial question of law; and ➢ certifies the case is fit for appeal to the Supreme Court.

If High Court refuses to certify the case	The aggrieved party may make an application to the Supreme Court under Article 136 of the Constitution of India.
Cost of appeal	The costs of the appeal shall be borne by the person as decided by the Supreme Court
Effect of judgment	Where the judgment of the High Court is varied or reversed by the Supreme Court, Tribunal should pass necessary order to dispose the case in conformity with such judgment.

3.1.6 Special provision for avoiding repetitive appeals [Sec. 158A]

- Where an assessee claims (a declaration in the Form 8 and verified in the prescribed manner) that:
  - any question of law arising in his case for an assessment year which is pending before the Assessing Officer or any appellate authority (such case being hereafter in this section referred to as the relevant case) is identical
  - with a question of law arising in his case for another assessment year which is pending before the High Court or the Supreme Court (such case being hereafter in this section referred to as the other case),
  - and if the Assessing Officer or the appellate authority, as the case may be, agrees to apply in the relevant case the final decision on the question of law in the other case,
  - he shall not raise such question of law in the relevant case in appeal before any appellate authority or the High Court or the Supreme Court.
- The Assessing Officer or the appellate authority, as the case may be, may, by order in writing:
  i. admit the claim of the assessee if he or it is satisfied that the question of law arising in the relevant case is identical with the question of law in the other case; or
  ii. reject the claim if he or it is not so satisfied.
- Such order shall be final and shall not be called in question in any proceeding by way of appeal or revision under this Act.
- Where a claim is admitted:
  a. the Assessing Officer or the appellate authority may make an order disposing of the relevant case without awaiting the final decision on the question of law in the other case; and
  b. the assessee shall not be entitled to raise, in relation to the relevant case, such question of law in appeal.
- When the decision on the question of law in the other case becomes final, it shall be applied to the relevant case and the Assessing Officer or the appellate authority, shall, if necessary, amend the order conformably to such decision.

3.1.7 Procedure where an identical question of law is pending before High Courts or Supreme Court [Sec. 158AB]

- Where the collegium is of the opinion that:
  a. any question of law arising in the case of an assessee for any assessment year (such case being herein referred to as the relevant case) is identical with a question of law arising,—

i. in his case for any other assessment year; or

ii. in the case of any other assessee for any assessment year; and

b. such question is pending before the jurisdictional High Court u/s 260A or the Supreme Court in an appeal u/s 261 or in a special leave petition under article 136 of the Constitution, against the order of the Appellate Tribunal or the jurisdictional High Court, as the case may be, which is in favour of such assessee (such case being herein referred to as the other case),

the collegium may, decide and inform the Principal Commissioner or Commissioner not to file any appeal, at this stage, to the Appellate Tribunal or to the jurisdictional High Court in the relevant case against the order of the Joint Commissioner (Appeals) or Commissioner (Appeals) or the Appellate Tribunal, as the case may be.

Taxpoint: Collegium means a collegium comprising of two or more Chief Commissioners or Principal Commissioners or Commissioners, as may be specified by the Board in this behalf.

- The Principal Commissioner or the Commissioner shall, on receipt of a communication from the collegium, direct the Assessing Officer to make an application to the Appellate Tribunal or the jurisdictional High Court, as the case may be, within a period of 120 days from the date of receipt of the order of the Joint Commissioner (Appeals) or Commissioner (Appeals) or of the Appellate Tribunal, as the case may be, stating that an appeal on the question of law arising in the relevant case may be filed when the decision on such question of law becomes final in the other case.
- The Principal Commissioner or Commissioner shall direct the Assessing Officer to make an application only if an acceptance is received from the assessee to the effect that the question of law in the other case is identical to that arising in the relevant case; and in case no such acceptance is received, the Principal Commissioner or Commissioner shall, proceed with appeals
- Where the order of the Joint Commissioner (Appeals) or Commissioner (Appeals) or the order of the Appellate Tribunal, as the case may be, is not in conformity with the final decision on the question of law in the other case, as and when such order is received, the Principal Commissioner or Commissioner may direct the Assessing Officer to appeal to the Appellate Tribunal or the jurisdictional High Court, as the case may be, against such order.
- Every appeal shall be filed within a period of 60 days to the Appellate Tribunal or 120 days to the High Court as the case may be, from the date on which the order of the jurisdictional High Court or the Supreme Court in the other case is communicated to the Principal Commissioner or the Commissioner (having jurisdiction over the relevant case), in accordance with the procedure specified by the Board in this behalf.

Rectification

3.2

Rectification of Mistake [Sec.154]

An income-tax authority, is empowered (suo moto or on application by assessee) to -

a. rectify any mistake apparent in an order passed by him; or

b. amend any intimation issued u/s 143(1) or deemed intimation

c. amend any intimation issued u/s 200A(1) or 206CB(1).

Taxpoint: Such order of rectification must be passed in writing.

Time limit for Rectification [Sec. 154(7)]

Within 4 years from the end of the financial year in which the order sought to be amended was passed.

However, in respect of an application made by the assessee or deductor or collector, the authority shall, within a period of 6 months from the end of the month in which the application is received by it, pass an order -

a. making the amendment; or

b. refusing to allow the claim.

Opportunity of being heard [Sec. 154(3)]: If such rectification order is prejudicial to the assessee or deductor or collector, an opportunity of being heard must be given to the assessee, before passing such order.

Taxpoint

- Where any such amendment has the effect of reducing the assessment or otherwise reducing the liability of the assessee or the deductor or collector, the Assessing Officer shall make any refund which may be due to such assessee or the deductor or collector.
- Where any such amendment has the effect of enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee or the deductor or collector, the Assessing Officer shall serve on the assessee or the deductor or collector, as the case may be a notice of demand in the prescribed form specifying the sum payable, and such notice of demand shall be deemed to be issued u/s 156.
- Mistake apparent from record may be a mistake of fact or mistake of law.

Faceless rectification, amendments and issuance of notice or intimation [Sec. 157A]

The Central Government may make a scheme, for the purposes of rectification of any mistake apparent from record u/s 154 or other amendments u/s 155 or issue of notice of demand u/s 156, or intimation of loss u/s 157, so as to impart greater efficiency, transparency and accountability by—

a. eliminating the interface between the income-tax authority and the assessee or any other person to the extent technologically feasible;

b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a team-based rectification of mistakes, amendment of orders, issuance of notice of demand or intimation of loss, with dynamic jurisdiction.

Revision

3.3

3.3.1 Revision of order prejudicial to the revenue [Sec. 263]

Orders which may be revised	Any order passed by the Assessing Officer or the Transfer Pricing Officer, which is - a) Erroneous; b) Prejudicial to the interests of the revenue; and c) Passed by an authority subordinate to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner. **Notes** a) Orders passed by the Assessing Officer or the Transfer Pricing Officer includes - i. An order of assessment made by the Assistant Commissioner on the basis of the directions issued by the Joint Commissioner u/s 144A; ii. An order made by the Joint Commissioner as an Assessing Officer or the Transfer Pricing Officer. iii. An order u/s 92CA by the Transfer Pricing Officer. b) Even an intimation u/s 143(1) can be revised **Taxpoint** - Order made by the Assessing Officer after making proper enquiries and considering relevant details and decisions of Supreme Court cannot be said to be erroneous and prejudicial to the interest of the revenue, hence such order cannot be revised. - An order passed by the Assessing Officer or the Transfer Pricing Officer shall be deemed to be erroneous in so far as it is prejudicial to the interests of the revenue, if, in the opinion of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner: a) the order is passed without making inquiries or verification which should have been made; b) the order is passed allowing any relief without inquiring into the claim; c) the order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or d) the order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person

Treatment of an order, which is subject matter of the appeal	Revision u/s 263 of an order, which is subject matter of appeal, cannot be made. **Notes** ➢ The Principal Commissioner or Commissioner can revise such order (which has been a subject matter of appeal) which had not been considered and decided in such appeal. E.g., From the perusal of the order u/s 143(3) passed by the Assessing Officer following was observed: – Point A: Against the assessee – Point B: In favour of the assessee The assessee being aggrieved with point A in the order passed by the Assessing Officer, preferred an appeal to the Commissioner (Appeals). However, the Commissioner wants to revise the order u/s 263 for point B (subject to other conditions being fulfilled). It is possible as doctrine of partial merger of the order is applicable in case of sec. 263. However, the Commissioner cannot revise the order for point A (as the same is subject matter of an appeal) ➢ An order cannot be said to have been made subject of an appeal if the appeal has been disposed of by the appellate authority without passing an order
Procedure to be followed	1. **Examination of Records:** The Principal Commissioner or Commissioner may call for and examine the records of any proceeding under the Act. If he considers that any order passed by the Assessing Officer is prejudicial to the interest of the revenue, he can revise and rectify the assessment. Record shall include all records relating to any proceeding under this Act available at the time of examination by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner. This means that any material, which was not available at the time of assessment but available at the time of examination by the Principal Commissioner or Commissioner, shall also be considered for order u/s 263. 2. **Inquiry:** He must make or cause to be made such inquiry as he deems necessary. 3. **Opportunity of being Heard:** No revision order shall be passed u/s 263 without giving the assessee an opportunity of being heard. 4. **Order:** Finally, he may pass such revision order as the circumstances of the case justify including a. an order enhancing or modifying the assessment or cancelling the assessment and directing a fresh assessment; or b. an order modifying the order u/s 92CA; or c. an order cancelling the order u/s 92CA and directing a fresh order under the said section

Time limit for passing revision order	2 years from the end of the financial year in which the order sought to be revised was passed. In computing the above period of limitation following period shall be excluded - ➢ Time taken in giving an opportunity to the assessee of being re-heard u/s 129; & ➢ Any period during which any proceeding under this section is stayed by an order or injunction of any court. **Exception:** There is no time limit for passing a revision order to give effect to, or in consequence of, an order of the ITAT, the High Court or the Supreme Court.
Appeal against order u/s 263	A revisional order passed by the Principal Commissioner or Commissioner u/s 263 can be appealed to the Tribunal.
Sec.263 vs. sec.154: Principal Commissioner or Commissioner can exercise the power even in a case where the issue is debatable. Revisional power u/s 263 is not comparable with the power of rectification of mistake u/s 154	

3.3.2 Revision of Order not Prejudicial to Revenue [Sec. 264]

Orders which may be revised	Any order which is - ➢ erroneous; ➢ not covered u/s 263 (i.e. not prejudicial to the interest of the revenue); ➢ passed by an authority subordinate to the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner. **Taxpoint:** No order under this section can be passed which is prejudicial to the assessee. **Notes:** Order which is not appealable before the Joint Commissioner (Appeals) or Commissioner (Appeal) can also be referred to the aforesaid authorities for revision.
On whose motion is revision possible	Either on own motion of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner or on an application by the assessee for revision.
Procedure to be followed	1. **Examination of Records:** Once revision proceedings have been initiated, the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may call for and examine the record of any proceeding. 2. **Inquiry:** He must also make or cause to be made such inquiry as he deems necessary 3. **Order:** He may pass such revision order as the circumstances of the case justify. However, the order passed should not be prejudicial to the assessee.

Time limit for filing an application	Where revision has been initiated by the assessee, the application must be made within **1 year** from the date on which the order in question was communicated to the assessee or the date on which he otherwise came to know of it, whichever is earlier. However, the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner can admit a belated application if the assessee was prevented by sufficient cause from making the application within time. In computing the above period of limitation following time shall be excluded: ➢ The day on which the order complained of was served; and ➢ If the assessee had not received the copy of the order, the time required to obtain copy of such order.
Time limit for passing a revisional order	Where the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner acts on his own motion – Within 1 year from the date of original order Where the application is made by the assessee – Within 1 Year from the end of the financial year in which such application is made. In computing the above period of limitation following period shall be excluded. ➢ Time taken in giving an opportunity to the assessee of being re-heard u/s 129; & ➢ Any period during which any proceeding under this section is stayed by an order or injunction of any court. [Sec. 264(6)] ➢ However, there is no time limit for passing a revision order for giving effect to, or in consequence of, an order of the ITAT, the High Court or the Supreme Court.
Orders which cannot be revised	a) Where an order is appealable but no appeal has been made to Joint Commissioner (Appeals) or CIT (Appeals) or to the Tribunal and time within which such appeal can be made, has not expired. **Note:** Where an appeal lies to the Joint Commissioner (Appeals) or Commissioner (Appeals) or to the Appellate Tribunal and the right of appeal is waived by the assessee, the Principal Commissioner Chief Commissioner or Chief Commissioner or Principal or Commissioner may revise the order even before the expiry of time limit of appeal. b) Where the order has been made the subject of an appeal to the Joint Commissioner (Appeals) or Commissioner (Appeals) or to the Appellate Tribunal. E.g., the assessee has been aggrieved with point A and point B in the order passed by the Assessing Officer. He preferred an appeal to the Joint Commissioner (Appeals) in respect of point A and seeks to file revision petition u/s 264 in respect of point B. It is not possible, he cannot file revision petition u/s 264 due to doctrine of total (or complete) merger of the order. He has to choose either way of the course. It is to be noted that for the purpose of sec. 264, doctrine of total merger is applicable, on the other hand, for the purpose of sec. 147, 154 and 263, doctrine of partial merger is applicable. **Note:** The assessment order could not be said to have been made subject matter of appeal, where an appeal was dismissed - a) on the ground that the same was incompetent; or b) as barred by limitation; or

Fee	₹ 500 where the application for revision is made by the assessee.
Appeal against order u/s 264	A revisional order passed by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner u/s 264 cannot be appealed to the Tribunal or the High Court. However, a petition for a writ of certiorari under Article 226 is maintainable
Other points	➢ The assessee cannot claim the right of revision in respect of an earlier year on the basis of finding of the Tribunal for a subsequent year. ➢ An order by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner declining to interfere shall not be deemed to be an order prejudicial to the assessee.

3.3.3 A comparative study of revision u/s 263 & revision u/s 264

Basis	Sec. 263	Sec. 264
Which order can be revised	Order, which is prejudicial to the interest of revenue.	Order, which is prejudicial to the interest of assessee.
Proceedings at the motion of	At the own motion of the authorities.	At the own motion of the authorities or on the application of the assessee.
Scope	Revision is possible of the issues which have not been considered and decided in an appeal, i.e., doctrine of partial merger is applicable	Revision u/s 264 is not possible on any issue if an appeal has been filed, i.e., doctrine of total merger is applicable
Time limit for application	Assessee does not apply	Within 1 year from the date on which the order in question was communicated to the assessee
Time limit for passing a revisional order	2 years from the end of the financial year in which the order sought to be revised was passed.	➢ Where the authorities act on his own motion: within 1 year from the date of original order. ➢ Where the application is made by the assessee: within 1 year from the end of the financial year in which such application is made.
Fee	Not applicable	₹500 where the application for revision is made by the assessee.
Appeal against order	Appeal can be filed to the Tribunal	No appeal can be filed.
Beneficial to	Revenue	Assessee

3.3.4 Faceless revision of orders [Sec. 264A]

The Central Government may make a scheme, for the purposes of revision of orders u/s 263 or 264, so as to impart greater efficiency, transparency and accountability by:

a. eliminating the interface between the income-tax authority and the assessee or any other person to the extent technologically feasible;

b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a team-based revision of orders, with dynamic jurisdiction.

Similarly, scheme may also be made by the Central Government for the purposes of giving effect to an order u/s 250, 254, 260, 262, 263 or 264. [Sec. 264B]

Settlement Commission

3.4

- Settlement Commission shall cease to operate after 31/01/2021
- No application for settlement shall be made after aforesaid date
- In respect of pending applications, the Central Government shall constitute one or more Interim Boards for Settlement, as may be necessary, for the settlement of pending applications.
- Every Interim Board shall consist of 3 members, each being an officer of the rank of Chief Commissioner, as may be nominated by the Board.
- If the Members of the Interim Board differ in opinion on any point, the point shall be decided according to the opinion of the majority.

Dispute Resolution Committee [Sec. 245MA]

- The Central Government shall constitute Dispute Resolution Committees (one or more) for dispute resolution in the case of such persons or class of persons, as may be specified by the Board.
- The assessee have an option to opt (or not to opt) for dispute resolution in respect of dispute arising from any variation in the specified order in his case and who fulfils the specified conditions.
- Notwithstanding anything contained in sec. 144C, upon receipt of the order of the Dispute Resolution Committee, the Assessing Officer shall,—

  a. in a case where the specified order is a draft of the proposed order of assessment u/s 144C(1), pass an order of assessment, reassessment or recomputation; or

  b. in any other case, modify the order of assessment, reassessment or recomputation,

  in conformity with the directions contained in the order of the Dispute Resolution Committee within a period of 1 month from the end of the month in which such order is received.
- The Dispute Resolution Committee, subject to such conditions, as may be prescribed, shall have the powers to reduce or waive any penalty imposable under this Act or grant immunity from prosecution for any offence punishable under this Act in case of a person whose dispute is resolved under this Chapter.

Taxpoint

- "Specified conditions" in relation to a person means a person who fulfils the following conditions:

  I. where he is not a person,—

  a. in respect of whom an order of detention has been made under the provisions of the Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974.

b. in respect of whom prosecution for any offence punishable under the provisions of the Indian Penal Code, the Unlawful Activities (Prevention) Act, 1967, the Narcotic Drugs and Psychotropic Substances Act, 1985, the Prohibition of Benami Transactions Act, 1988, the Prevention of Corruption Act, 1988 or the Prevention of Money-laundering Act, 2002 has been instituted and he has been convicted of any offence punishable under any of those Acts;

c. in respect of whom prosecution has been initiated by an income-tax authority for any offence punishable under the provisions of this Act or the Indian Penal Code or for the purpose of enforcement of any civil liability under any law for the time being in force, or such person has been convicted of any such offence consequent upon the prosecution initiated by an income-tax authority;

d. who is notified u/s 3 of the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992;

II. such other conditions, as may be prescribed.

- "Specified order" means such order, including draft order, as may be specified by the Board, and,—

  i. aggregate sum of variations proposed or made in such order does not exceed ₹ 10 lakhs;

  ii. where return has been filed by the assessee for the assessment year relevant to such order, total income as per such return does not exceed ₹ 50 lakhs

Exception

Specified order does not include the order which is based on search-initiated u/s 132 or requisition u/s 132A in the case of assessee or any other person or survey u/s 133A or information received under an agreement referred to in sec. 90 or sec. 90A.

- The Central Government may make a scheme (for faceless proceedings), for the purposes of dispute resolution, so as to impart greater efficiency, transparency and accountability by—

  a. eliminating the interface between the Dispute Resolution Committee and the assessee in the course of dispute resolution proceedings to the extent technologically feasible;

  b. optimising utilisation of the resources through economies of scale and functional specialisation;

  c. introducing a dispute resolution system with dynamic jurisdiction.

  e-Dispute Resolution Scheme, 2022 notified.

Advance Ruling

3.5

3.5.1 Board For Advance Ruling (BAR)

The Central Government shall constitute Boards for Advance Rulings (one or more) for giving advance rulings. The Board for Advance Rulings shall consist of two members, each being an officer not below the rank of Chief Commissioner, as may be nominated by the Board [Sec. 245-OB]

Taxpoint:

- No proceeding before, or pronouncement of advance ruling by, the Board shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the Board for Advance Rulings [Sec. 245P]
- The Ruling or the Order of the Board will not be binding on the Department or on the applicant.

3.5.2 Advance Ruling [Sec. 245N(a)]

Advance ruling means:

(i) A determination by the Board for Advance Rulings in relation to a transaction which has been undertaken or is proposed to be undertaken by a non-resident applicant; or

(ii) A determination by the Board for Advance Rulings in relation to the tax liability of a non-resident arising out of a transaction which has been undertaken or is proposed to be undertaken by a resident applicant with such non-resident; or

(iia) A determination by the Board for Advance Rulings in relation to the tax liability of a resident applicant, arising out of a transaction which has been undertaken or is proposed to be undertaken by such applicant

In above cases, such determination shall include the determination of any question of law or of fact specified in the application.

(iii) A determination or decision by the Board for Advance Rulings in respect of an issue relating to computation of total income which is pending before any income-tax authority or the Appellate Tribunal and such determination or decision shall include the determination or decision of any question of law or of fact relating to such computation of total income specified in the application.

(iv) A determination or decision by the Board for Advance Rulings whether an arrangement, which is proposed to be undertaken by any person being a resident or a non-resident, is an impermissible avoidance arrangement as referred to in Chapter X-A or not.

3.5.3 Applicant [Sec. 245N(b)]

Applicant means any person who is:

a) a non-resident referred to in sub-clause (i) of clause (a) above; or

b) a resident referred to in sub-clause (ii) of clause (a) above; or

c) a resident who has undertaken or propose to undertake one or more transactions of value of ₹ 100 crore or more in total [Notification No. 73, dated 28-11-2014]

d) a public sector company [Notification No. 725, dated 03-08-2000]

e) a resident or a non-resident referred to in sub-clause (iv) of clause (a) above

- makes an application u/s 245Q

3.5.4 Application for Advance Ruling [Sec. 245-Q]

- An applicant desirous of obtaining an advance ruling may make an application stating the question on which the advance ruling is sought.
- The application shall be accompanied by a fee of
  a. ₹ 10,000 or
  b. such fees as may be prescribed.
  – whichever is higher
- An applicant may withdraw an application within 30 days from the date of the application.

3.5.5 Procedure on Receipt of Application [Sec. 245R]

- On receipt of an application, the Board for Advance Rulings shall cause a copy thereof to be forwarded to the Principal Commissioner or Commissioner and, if necessary, call upon him to furnish the relevant records. Where any records have been called for by the Board for Advance Rulings, such records shall, as soon as possible, be returned to the Principal Commissioner or Commissioner.
- The Board for Advance Rulings may, after examining the application and the records called for, by order, either allow or reject the application. However, where the question raised in the application -
  (i) is already pending before any income-tax authority or Appellate Tribunal [except in the case of a resident applicant falling in sec. 245N(b)(iii)] or any court;
  (ii) involves determination of fair market value of any property;
  (iii) relates to a transaction or issue which is designed prima facie for the avoidance of income-tax [except in the case of a resident applicant falling in sec. 245N(b)(iii)]
  - shall be rejected by the Board for Advance Rulings.
- The words 'already pending', should be interpreted to mean: 'already pending as on the date of the application' and not with reference to any future date [Monte Harris -vs.- CIT (AAR)]
- No application shall be rejected unless an opportunity has been given to the applicant of being heard. Further, where the application is rejected, reasons for such rejection shall be given in the order.
- A copy of every order (allowing or rejecting) shall be sent to the applicant and to the Principal Commissioner or Commissioner.
- Where an application is allowed, the Board for Advance Rulings shall, after examining such further material as may be placed before it by the applicant or obtained by the Board for Advance Rulings, pronounce its advance ruling on the question specified in the application.
- On a request received from the applicant, the Board for Advance Rulings shall, before pronouncing its advance ruling, provide an opportunity to the applicant of being heard, either in person or through a duly authorised representative.

- The Board for Advance Rulings shall pronounce its advance ruling in writing within 6 months of the receipt of application.
- A copy of the advance ruling pronounced by the Board for Advance Rulings, duly signed by the Members and certified in the prescribed manner shall be sent to the applicant and to the Principal Commissioner or Commissioner, as soon as may be, after such pronouncement.
- Faceless Proceedings: The Central Government may make a scheme[2] for the purposes of giving advance rulings by the Board for Advance Rulings, so as to impart greater efficiency, transparency and accountability by:
  a. eliminating the interface between the Board for Advance Rulings and the applicant in the course of proceedings to the extent technologically feasible;
  b. optimising utilisation of the resources through economies of scale and functional specialisation;
  c. introducing a system with dynamic jurisdiction.

3.5.6 Appellate Authority not to Proceed in certain Cases [Sec. 245RR]

No Income-tax authority or the Appellate Tribunal shall proceed to decide any issue in respect to which an application has been made by an applicant, being a resident, u/s 245Q.

3.5.7 Advance Ruling to be void in certain circumstances [Sec. 245-T]

- Where the Board for Advance Rulings finds, on a representation made by the Principal Commissioner or Commissioner or otherwise, that an advance ruling pronounced has been obtained by the applicant by fraud or misrepresentation of facts, it may, by order, declare such ruling to be void ab initio and thereupon all the provisions of this Act shall apply to the applicant as if such advance ruling had never been made.
- A copy of such order shall be sent to the applicant and the Principal Commissioner or Commissioner.

3.5.8 Powers of the Board for Advance Rulings [Sec. 245U]

The Board for Advance Rulings shall, for the purpose of exercising its powers, have all the powers of a civil court under the Code of Civil Procedure, 1908 as are referred to in section 131 of this Act.

3.5.9 Appeal [Sec. 245W]

- The applicant, if he is aggrieved by any ruling pronounced or order passed by the Board for Advance Rulings or the Assessing Officer, on the directions of the Principal Commissioner or Commissioner, may appeal to the High Court against such ruling or order of the Board for Advance Rulings within 60 days from the date of the communication of that ruling or order, in such form and manner, as may be prescribed.
- Where the High Court is satisfied, on an application made by the appellant in this behalf, that the appellant was prevented by sufficient cause from presenting the appeal within the specified period, it may grant further period of 30 days for filing such appeal.
- The Central Government may make a scheme for the purposes of filing appeal to the High Court by the Assessing Officer, so as to impart greater efficiency, transparency and accountability by:
  a. optimising utilisation of the resources through economies of scale and functional specialisation;
  b. introducing a team-based mechanism with dynamic jurisdiction.

[2] e-Advance Rulings Scheme, 2022 is notified.

Exercise

Multiple Choice Questions

1. Any mistake which is apparent from the record in any order passed by the Assessing Officer can be rectified under section _____.
   a. 154
   b. 147
   c. 143
   d. 254

2. In case of an application made by the assessee u/s 154, the income-tax authority shall rectify the order/refuse the rectification within _____ from the end of the month in which the application is received by the authority.
   a. 4 years
   b. 2 years
   c. 1 year
   d. 6 months

3. An appeal to the Commissioner of Income-tax (Appeals) shall be filed in Form No. _____.
   a. 35
   b. 36
   c. 34C
   d. 35B

4. The Joint Commissioner of Income-tax (Appeals) is the _____ appellate authority
   a. First
   b. Second
   c. Third
   d. Fourth

5. Provisions relating to advance ruling are provided in sections _____.
   a. 80C to 80U
   b. 245A to 245L
   c. 237 to 245
   d. 245N to 245V

6. Assessing Officer or the assessee, as the case may be, on receipt of notice that an appeal against the order of the Commissioner (Appeals) has been filed by the other party, may file a memorandum of cross objection with the Tribunal in Form _____ and within _____ days of receipt of notice that appeal has been filed by the other party.

   a. Form 36A; 15 days

   b. Form 36A; 45 days

   c. Form 36A; 30 days

   d. Form 36; 60 days

7. Where revision u/s 264 has been initiated by the assessee, the application must be made within _____ from the date on which the order in question was communicated to the assessee or the date on which he otherwise came to know of it, whichever is earlier.

   a. 1 year

   b. 4 years

   c. 2 years

   d. 30 days

Answer: 1 – A; 2 – D, 3 – A; 4 – A; 5 – D; 6 – C; 7 - A]

Short Essay Type Questions

1. Mention any five orders which are appealable before CIT (Appeals).
2. Write a note of revisionary power of the Commissioner u/s 263.
3. State the provisions u/s 154 relating to rectifying mistakes.
4. Who can apply for advance ruling?

Reference

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Penalties and Prosecutions 4

This Module includes:

4.1 Penalties

4.2 Penalty for Under-reporting and Misreporting of Income [Sec. 270A]

4.3 Power to Reduce or Waive Penalty, etc., in Certain Cases [Sec. 273A]

4.4 When Assessee becomes Liable for Prosecution

Penalties and Prosecutions

SLOB Mapped against the Module:

To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify and examine the cases where penalty is applicable
- Understand the provisions relating to quantify the penalty
- Appreciate the limitation period
- Appreciate the provisions relating to waiver of the penalties

Penalties

4.1

Penalty is imposed on an assessee for violating the different provisions of the Act. The provisions of penalty are tabulated below:

Section	Nature of default	Penalty	
		Minimum	Maximum
221(1)	Failure in making the payment of tax, interest or any demand within the prescribed time limit	Amount decided by the Assessing Officer	Tax or interest or both in arrears
140A(3)	Failure to pay whole or any part of income tax and/ or interest as per sec.140A(1)		
270A	Penalty for under-reporting and misreporting of income (Discussed later on in details)	50% of the tax on under-reported income	200% of the tax on misreported income
271A	Failure to comply with sec. 44AA i.e. to keep or maintain books of account, documents, etc.	₹ 25,000	
271AA(1)	Failure to keep and maintain, information and documents for international transactions or specified domestic transaction or fails to report such transaction	2% of the value of each international transaction or specified domestic transaction	
271AA(2)	Fails to furnish the information and the document as required u/s 92D(4)	₹ 5,00,000	
271AAB(1A)	Undisclosed income in case of search initiated on or after 15-12-2016	60% of the undisclosed income of the specified previous year	
	However, if the assessee: a) in the course of the search, in a statement u/s 132(4), admits the undisclosed income and specifies the manner in which such income has been derived. b) substantiates the manner in which the undisclosed income was derived; and c) on or before the specified date: A. pays the tax, together with interest in respect of the undisclosed income; and B. furnishes the return of income for the specified previous year declaring such undisclosed income therein	30% of the undisclosed income of the specified previous year	

Section	Nature of default	Penalty	
		Minimum	Maximum
271AAC	Where the income determined includes any income referred to in sec. 68, 69, 69A, 69B, 69C or 69D for any previous year	10% of tax payable u/s 115BBE No penalty shall be levied if such income has been included by the assessee in the return of income furnished u/s 139 and the tax thereon (as per sec. 115BBE) has been paid on or before the end of the relevant previous year.	
271AAD	If during any proceeding under this Act, it is found that in the books of account maintained by any person there is: a. a false entry; or b. an omission of any entry which is relevant for computation of total income of such person, to evade tax liability, Further, similar penalty may also be levied on any other person, who causes the assessee in any manner to make a false entry or omits any entry "False entry" includes use or intention to use— ➢ forged or falsified documents such as a false invoice or, in general, a false piece of documentary evidence; or ➢ invoice in respect of supply or receipt of goods or services or both issued by the person or any other person without actual supply or receipt of such goods or services or both; or ➢ invoice in respect of supply or receipt of goods or services or both to or from a person who does not exist.	A sum equal to the aggregate amount of such false or omitted entry.	
271AAE	A person, being any fund or trust or institution or hospital (or other medical institution) or any university (or other educational institution) referred to in sec. 10(23C)(iv) or (v) or (vi) or (via) or any trust or institution referred to in sec. 11 has violated the provisions of the 21st proviso to sec. 10(23C) or sec. 13(1)(c) [i.e., unreasonable benefits to the related persons like trustee or specified person]	**First time violation** 100% of the aggregate amount of income applied, directly or indirectly, for the benefit of such related person. **Second and subsequent violation** 200% of the aggregate amount of income applied, directly or indirectly, for the benefit of such related person	
271B	Failure to comply with sec. 44AB i.e. to get accounts audited or to furnish such audit report.	½% of the total sales or turnover or gross receipts	₹ 1,50,000
271BA	Failure to furnish report from an accountant as per sec.92E	₹ 1,00,000	

Section	Nature of default	Penalty	
		Minimum	Maximum
271C	Failure to deduct part or whole of tax under chapter XVII-B (i.e., TDS)	Amount of tax failed to deduct	
	Failure to pay or ensure payment of tax as per sec. 115-O(2) or proviso to sec. 194B or first proviso to sec. 194R(1) or the proviso to sec. 194S(1) or sec. 194BA(2)	Amount of tax failed to pay or ensure payment thereof	
271CA	Failure to collect tax at source	Amount of tax failed to collect	
271D	Taking or accepting any loan or deposit or specified sum in contravention of the provisions of sec.269SS	Amount of the loan or deposit or specified sum so taken/accepted However, if the assessee proves that there was reasonable cause for the failure, then penalty shall not be levied	
271DA	Receives any sum in contravention of sec. 269ST	Amount equal to such receipt	
271DB	Failure to provide facility for electronic mode of payment prescribed u/s 269SU	₹ 5,000 per day	
271E	Repayment of any loan or deposit or specified advance in contravention of the provisions of sec.269T	Amount of loan or deposit or specified advance so repaid. However, if the assessee proves that there was reasonable cause for the failure, then penalty shall not be levied	
271FA	Failure to furnish a statement of financial transaction or reportable accountas required u/s 285BA(1) within the prescribed time limit	₹ 500 for every day during which the failure continues	
Proviso to sec. 271FA	Failure to furnish the statement of financial transaction or reportable accountas within the period specified in the notice issued u/s 285BA(5)	₹ 1,000 for every day during which the failure continues, beginning from the day immediately following the day on which the time specified in such notice expires	
271FAA(1)	Person referred to in sec. 285BA(1) provides inaccurate information in the 'statement of financial transaction or reportable account'	The prescribed income-tax authority u/s 285BA(1) may direct that such person shall pay, by way of penalty, ₹ 50,000	
271FAA(2)	Where prescribed reporting financial institution u/s 285BA, who is required to furnish a statement (herein referred to as the reporting financial institution) provides inaccurate information in the statement and the inaccuracy in such statement is due to false or inaccurate information furnished by the accountholder(s) of the relevant reportable account or accounts	The prescribed income-tax authority u/s 285BA(1) shall direct that the reporting financial institution shall, in addition to the aforesaid penalty, if any, pay ₹ 5,000 for every inaccurate reportable account. However, the reporting financial institution shall be entitled to recover the sum so paid from such accountholder(s)	
271FAB	Fails to furnish information or document as required u/s 9A(5) within the prescribed time limit	₹ 5,00,000	

Section	Nature of default	Penalty	
		Minimum	Maximum
271G	Failure to furnish information or documents as required u/s 92D(3)	2% of the value of the international transaction or specified domestic transaction.	
271GA	Failure to furnish information or documents as required u/s 285A	2% of the value of the transaction, if such transaction had the effect of directly or indirectly transferring the right of management or control in relation to the Indian concern; In other case: ₹ 5,00,000	
271GB(1)	Failure by any reporting entity to furnish the report referred to in sec. 286(2) in respect of a reporting accounting year	➢ Failure does not exceed one month: ₹ 5,000 per day ➢ Failure continues beyond the period of one month: ₹ 15,000 per day ➢ Failure continues after an order of penalty has been served on the entity: ₹ 50,000 per day from the date of service of such order	
271GB(2)	Failure by any reporting entity to produce the information and documents within the period specified u/s 286(6)	➢ ₹ 5,000 per day ➢ Failure continues after an order of penalty has been served on the entity: ₹50,000 per day from the date of service of such order	
271GB(4)	Reporting entity provides inaccurate information in the report referred to in sec. 286(2)	₹ 5,00,000 Penalty shall be levied if: a) the entity has knowledge of the inaccuracy at the time of furnishing the report but fails to inform the prescribed authority; or b) the entity discovers the inaccuracy after the report is furnished and fails to inform the prescribed authority and furnish correct report within a period of 15 days of such discovery; or c) the entity furnishes inaccurate information or document in response to the notice issued u/s 286(6),	
271H[1]	Failure to furnish TDS / TCS Return or furnishing inaccurate details in these Return	₹ 10,000	₹ 1,00,000
271-I	Fails to furnish information, or furnishes inaccurate information as required u/s 195(6)	₹ 1,00,000	

[1] No penalty u/s 271H shall be levied if the person proves that after paying TDS / TCS along with the fee u/s 234E and interest, if any, to the credit of the Central Government, he had delivered the statement before the expiry of 1 year from the time prescribed for delivering such statement.

Section	Nature of default	Penalty	
		Minimum	Maximum
271J	Furnishing incorrect information in reports or certificates by an accountant or merchant banker or registered valuer	₹ 10,000 for each report Penalty is leviable by the AO or the Joint Commissioner (Appeals) or Commissioner (Appeals) who in the course of any proceedings finds that such report has incorrect information	
271K	Where a. the research association, university, college or other institution or company referred to in sec. 35(1)(ii) or (iii) or (iia) fails to deliver a statement within the time prescribed u/s 35(1A)(i), or furnish a certificate prescribed u/s 35(11A)(ii); or b. the institution or fund, if it fails to deliver a statement within the time prescribed u/s 80G(5)(viii) or furnish a certificate prescribed u/s 80G(5)(ix)	10,000	1,00,000
272A(1)(a)	Failure to answer any question (related to assessment) of an income-tax authority	₹ 10,000 for each default	
272A(1)(b)	Refuse to sign any statement made by the assessee in course of income tax proceedings		
272A(1)(c)	Failure to comply with summons u/s 131(1) to attend office or to give evidence or to produce books of account or other documents, at certain place & time		
272A(1)(d)	Fails to comply with a notice u/s 142(1) or 143(2) or fails to comply with a direction issued u/s 142(2A) [Penalty shall be levied by such authority]		
272A(2)(a)	Failure to comply with a notice issued u/s 94(6)	A sum of ₹ 500, for every day during which the failure continues: However, the amount of penalty for failures in relation to a declaration mentioned in sec. 197A, a certificate as required by sec. 203 and returns or statement u/s 200 or 206 and 206C shall not exceed the amount of tax deductible or collectible.	
272A(2)(b)	Failure to give notice of discontinuance of his business or profession as required u/s 176(3)		
272A(2)(c)	Failure to furnish in due time any of the returns, statements or particulars mentioned in section 133, 206, 206C or 285B		
272A(2)(d)	Failure to allow inspection of any register u/s 134 or of any entry in such register or to allow copies of such register or of any entry therein to be taken		
272A(2)(e)	Failure to furnish the return of income which he is required to furnish u/s 139(4A) or (4C) within time allowed and in the manner required.		
272A(2)(f)	Failure to deliver or cause to be delivered in due time a copy of the declaration mentioned in sec. 197A		

Section	Nature of default	Penalty	
		Minimum	Maximum
272A(2)(g)	Failure to furnish a certificate u/s 203 or 206C		
272A(2)(h)	Failure to deduct and pay tax u/s 226(2)		
272A(2)(i)	Failure to furnish a statement u/s 192(2C)		
272A(2)(j)	Failure to deliver a copy of declaration referred u/s 206C(1A) within due time		
272A(2)(l)	Failure to deliver or cause to be delivered the quarterly return within the time prescribed u/s 206A(1)		
272A(2)(m)	Failure to deliver a statement within the time prescribed u/s 200(*2A*) or 206C(*3A*)		
272AA	Failure to comply with the provisions of sec. 133B	Maximum up to ₹ 1,000	
272B	Failure to comply with the provisions of sec. 139A	₹ 10,000	
272BB(1A)	Failure to quote Tax deduction or collection number	₹ 10,000	
272BBB	Failure to comply with the provisions of sec. 206CA	₹ 10,000	

Notes:

1) **Specified previous year means previous year:**

   (i) which has ended before the date of search, but the date of filing the return of income u/s 139(1) for such year has not expired before the date of search and the assessee has not furnished the return of income for the previous year before the said date; or

   (ii) in which search was conducted.

2) As per sec. 274(2), in the following cases, penalty can be imposed only with the prior approval of the Joint Commissioner:

Where penalty is imposed by the Income-tax Officer	Exceeds ₹ 10,000
Where penalty is imposed by the Assistant Commissioner or Deputy Commissioner	Exceeds ₹ 20,000

Penalty for Under-reporting and Misreporting of Income [Sec. 270A]

4.2

The

- Assessing Officer; or
- Joint Commissioner (Appeals) or Commissioner (Appeals); or
- Principal Commissioner or Commissioner

may, during the course of any proceedings under this Act, direct that any person who has under-reported his income shall be liable to pay a penalty in addition to tax, if any, on the under-reported income.

Taxpoint

- Penalty proceedings must be initiated before completion of the assessment or appeal order or revision order, as the case may be.
- Penalty order is different from assessment order. Aggrieved with the penalty order passed by the Assessing Officer, the assessee is required to file separate appeal to the Commissioner (Appeals) or separate revision petition u/s 264 or separate rectification petition u/s 154. Further, appeal can be filed with the Tribunal against the penalty order passed by the Commissioner (Appeals) or Principal Commissioner or Commissioner.
- Tribunal cannot impose penalty
- Penalty shall be imposed by the respective income-tax authority on addition made by them. E.g., on addition being made by the Assessing Officer, Commissioner (Appeals) cannot levy penalty. Even the Assessing Officer fails to levy penalty on such addition, Commissioner (Appeals) cannot levy penalty on such addition made by the Assessing Officer. In *CIT -vs.- Shadiram Balmukund,* the Apex court has held that the Assessing officer can levy penalty on the additions made by him and not on the additions made by Commissioner (Appeals). Similarly, Commissioner (Appeals) can levy penalty on the additions made by him and not on the additions made by the Assessing Officer.

Quantum of penalty [Sec. 270A(7) & (8)]

- 50% of the amount of tax payable on under-reported income [Sec. 270A(7)]
- 200% of the amount of tax payable on under-reported income, where under-reported income is in consequence of any misreporting thereof by any person - [Sec. 270A(8)]

Cases of under-reporting of income [Sec. 270A(2)]

A person shall be considered to have under-reported his income, if:

a. the income assessed is greater than the income determined in the return processed u/s 143(1)(a);

b. the income assessed is greater than the maximum amount not chargeable to tax, where no return of income has been furnished or where return has been furnished for the first time u/s 148;

c. the income reassessed is greater than the income assessed or reassessed immediately before such reassessment;

d. the amount of deemed total income assessed or reassessed u/s 115JB or 115JC is greater than the deemed total income determined in the return processed u/s 143(1)(a);

e. the amount of deemed total income assessed u/s 115JB or 115JC is greater than the maximum amount not chargeable to tax, where no return of income has been filed or where return has been furnished for the first time u/s 148;

f. the amount of deemed total income reassessed u/s 115JB or 115JC is greater than the deemed total income assessed or reassessed immediately before such reassessment;

g. the income assessed or reassessed has the effect of reducing the loss or converting such loss into income.

Computation of amount of under-reported income [Sec. 270A(3)]

The amount of under-reported income shall be:

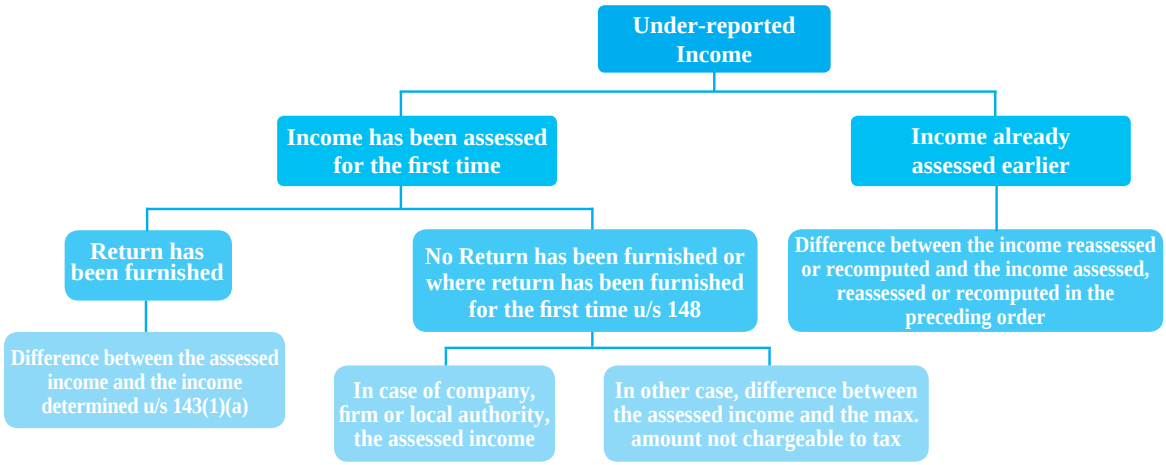
- in a case where income has been assessed for the first time:

➢ If return has been furnished	Assessed Income – Income determined u/s 143(1)(a)
➢ If return has not been furnished or where return has been furnished for the first time u/s 148	In case of company, firm or local authority: Assessed Income Other persons: Assessed Income – Basis Exemption Limit

- in a case where income has already been assessed earlier:

  Income reassessed or recomputed - Income assessed, reassessed or recomputed in a preceding order

- Preceding order means an order immediately preceding the order during the course of which the penalty has been initiated.



- in a case where under-reported income arises out of determination of deemed total income in accordance with sec. 115JB or 115JC, the amount of total under-reported income shall be determined in accordance with the following formula:

  (A — B) + (C — D)

Where,

A	=	Total income assessed as per the provisions other than the provisions contained in sec. 115JB or 115JC (herein called general provisions)
B	=	Total income that would have been chargeable had the total income assessed as per the general provisions been reduced by the amount of under-reported income;
C	=	Total income assessed u/s 115JB or 115JC
D	=	Total income that would have been chargeable had the total income assessed u/s 115JB or 115JC been reduced by the amount of under-reported income. However, where the amount of under-reported income on any issue is considered both u/s 115JB / 115JC and under general provisions, such amount shall not be reduced from total income assessed while determining the amount under item D.

- in a case where an assessment or reassessment has the effect of reducing the loss declared in the return or converting that loss into income:

The income or loss assessed or reassessed - Loss claimed

Meaning of under-reported income in a case where source is linked to earlier year [Sec. 270A(4)]

Where:

- the source of any receipt, deposit or investment in any assessment year
- is claimed to be an amount added to income or deducted while computing loss, as the case may be, in the assessment of such person
- in any year prior to the assessment year in which such receipt, deposit or investment appears (hereinafter referred to as "preceding year")
- and no penalty was levied for such preceding year,

then, the under-reported income shall include such amount as is sufficient to cover such receipt, deposit or investment.

Taxpoint

- Such amount shall be deemed to be amount of income under-reported for the preceding year in the following order:
  a. the preceding year immediately before the year in which the receipt, deposit or investment appears, being the first preceding year; and
  b. where the amount added or deducted in the first preceding year is not sufficient to cover the receipt, deposit or investment, the year immediately preceding the first preceding year and so on.
- The assessee can explain that the investment or expenditure is made out of additions made during earlier years – Anantharam Veerasinghaiah & Co. -vs.- CIT (SC)

Example

- Addition made by the Assessing Officer on estimated basis in the preceding year(s)	₹ 1,00,000
- Penalty levied on the said addition in the preceding year(s) [Due to provision of sec. 270A(6)(b) or (c)]	Nil

- In subsequent assessment year, such addition is explained as source of investment made by the assessee, citing the decision of the Apex court in the case of Anantharam Veerasinghaiah & Co.
- Despite this confession of concealment on the part of the assessee, no penalty was leviable in such cases as the time limit for initiating concealment penalty proceedings in respect of the earlier year in which addition was made would have expired. Moreover, the penalty could also not be imposed in respect of the year in which the deposit was made as there was no concealment in that year, the deposit having been explained as out of an earlier year's income.
- In this type of case, sec. 270A(4) comes into play which states that under-reported income shall include such amount.

Cases not considered as under-reported income [Sec. 270(6)]

The under-reported income shall not include the following:

a. **Proper Explanation:** The amount of income in respect of which the assessee offers an explanation and the Assessing Officer or the Commissioner (Appeals) or the Commissioner or the Principal Commissioner, as the case may be, is satisfied that the explanation is bona fide and the assessee has disclosed all the material facts to substantiate the explanation offered.

b. **Estimate by the authority:** The amount of under-reported income determined on the basis of an estimate, if the accounts are correct and complete to the satisfaction of the Assessing Officer or the Commissioner (Appeals) or the Commissioner or the Principal Commissioner, as the case may be, but the method employed is such that the income cannot properly be deduced therefrom;

c. **Estimate by the assessee:** The amount of under-reported income determined on the basis of an estimate, if the assessee has, on his own, estimated a lower amount of addition or disallowance on the same issue, has included such amount in the computation of his income and has disclosed all the facts material to the addition or disallowance.

d. **Arm's length price:** The amount of under-reported income represented by any addition made in conformity with the arm's length price determined by the Transfer Pricing Officer, where the assessee had maintained information and documents as prescribed u/s 92D, declared the international transaction under Chapter X, and, disclosed all the material facts relating to the transaction; and

e. **Undisclosed income in search operation:** The amount of undisclosed income referred u/s 271AAB

Cases of misreporting of income [Sec. 270A(9)]

The cases of misreporting of income shall be the following:

a. misrepresentation or suppression of facts;

b. failure to record investments in the books of account;

c. claim of expenditure not substantiated by any evidence;

d. recording of any false entry in the books of account;

e. failure to record any receipt in books of account having a bearing on total income; and

f. failure to report any international transaction or any transaction deemed to be an international transaction or any specified domestic transaction, to which the provisions of Chapter X apply.

Computation of tax payable on under-reported income [Sec. 270A(10)]

The tax payable in respect of the under-reported income shall be:

Where no return of income has been furnished or where return has been furnished for the first time u/s 148, and the income has been assessed for the first time	Tax calculated on the under-reported income as increased by the maximum amount not chargeable to tax as if it were the total income	
Where the total income determined u/s 143(1)(a) or assessed, reassessed or recomputed in a preceding order is a loss	Tax calculated on the under-reported income as if it were the total income	
In any other case	Tax on **(**Under-reported income + Income determined u/s 143(1(a) or income assessed, reassessed or recomputed in a preceding order**)**	***
	Less: Tax on Income determined u/s 143(1(a) or income assessed, reassessed or recomputed in a preceding order	(**)

Other Points

- No double penalty on same amount: No addition or disallowance of an amount shall form the basis for imposition of penalty, if such addition or disallowance has formed the basis of imposition of penalty in the case of the person for the same or any other assessment year – [Sec. 270A(11)].
- Written order: The penalty shall be imposed, by an order in writing, by the Assessing Officer, the Commissioner (Appeals), the Commissioner or the Principal Commissioner, as the case may be – [Sec. 270A(12)]

Illustration 1.

Computation of under-reported income assuming income has been assessed for the first time:

Assessee	Return Filed	Income u/s 143(1)(a)	Assessed Income	Under-reported Income	Tax payable on (a)	Tax payable on (b)	Tax payable on (c)	Penalty
		a	b	c = (b – a)	d	e	f = (e – d)	f × 50%
Individual	Yes	16,00,000	20,00,000	4,00,000	1,87,200	3,12,000	1,24,800	62,400
Firm	Yes	17,00,000	20,00,000	3,00,000	5,30,400	6,24,000	93,600	46,800
Firm	Yes	(8,00,000)	20,00,000	28,00,000	-	8,73,600	8,73,600	4,36,800
Individual	Yes	(19,00,000)	(3,00,000)	16,00,000	-	1,87,200*	1,87,200	62,400
Firm	No	N.A.	8,00,000	8,00,000	-	2,49,600	2,49,600	1,24,800
Individual	No	N.A.	18,00,000	15,00,000#	-	2,49,600!	2,49,600	1,24,800

* Tax on (c) ! Tax on ₹ 18,00,000/- as return was not filed

Assessed income as reduced by basic exemption

200% of (f) shall be levied as penalty if the case is misreporting of income.

Illustration 2.

Computation of under-reported income assuming income has not been assessed for the first time:

Assessee	Income assessed in the preceding order	Reassessed Income	Under-reported Income
Individual	7,00,000	12,00,000	5,00,000
Company	20,00,000	22,00,000	2,00,000

Illustration 3.

Compute penalty leviable u/s 270A in case of X Ltd from the following details:

Particulars	Total Income	Tax on Total Income	Book Profit	Tax on Book Profit
Return of income	80,00,000	24,96,000	2,00,00,000	33,38,400
Assessed income	1,20,00,000	40,06,080	2,10,00,000	35,05,320

Solution:

Computation of penalty

Particulars		Amount
Under-reported income		
Total income computed by the Assessing Officer	A	1,20,00,000
Total income as per return of income	B	80,00,000
Book profit computed by the Assessing Officer	C	2,10,00,000
Book profit as per return of income	D	2,00,00,000
Under-reported income [(A – B) + (C – D)]		**50,00,000**
Tax on under-reported income		
Tax on A	P	40,06,080
Tax on B	Q	24,96,000
Tax on C	R	35,05,320
Tax on D	S	33,38,400
Tax on Under-reported income [(P – Q) + (R – S)]	T	16,77,000
Penalty u/s 270A		
– Minimum (being 50% of T)		8,38,500
– Maximum (being 200% of T)		33,54,000

Illustration 4.

In the above example, out of addition of ₹ 10 lakh made in the book profit and ₹ 40 lakh made in the total income (under general provisions), ₹ 3,00,000 was made on the same ground. Compute penalty u/s 270A.

Solution:

Computation of penalty

Particulars		Amount
Under-reported income		
Total income computed by the Assessing Officer	A	1,20,00,000
Total income as per return of income	B	80,00,000
Book profit computed by the Assessing Officer	C	2,10,00,000
Book profit as per return of income	D	2,03,00,000
Under-reported income [(A – B) + (C – D)]		**47,00,000**
Tax on under-reported income		
Tax on A	P	40,06,080
Tax on B	Q	24,96,000
Tax on C	R	35,05,320
Tax on D	S	33,88,476
Tax on Under-reported income [(P – Q) + (R – S)]	T	16,26,924
Penalty u/s 270A		
– Minimum (being 50% of T)		8,13,462
– Maximum (being 200% of T)		32,53,848

Immunity from imposition of penalty, etc. [Sec. 270AA]

- An assessee may make an application to the Assessing Officer to grant immunity from imposition of penalty u/s 270A and initiation of proceedings u/s 276C or 276CC, if he fulfils the following conditions:
  a. the tax and interest payable as per the order of assessment or reassessment u/s 143(3) or 147, as the case may be, has been paid within the period specified in such notice of demand; and
  b. no appeal against aforesaid order has been filed.
- An application shall be made within 1 month from the end of the month in which the said order has been received and shall be made in such form (Form 68) and verified in prescribed manner.
- The Assessing Officer shall (on fulfilment of the aforesaid conditions) and after the expiry of the period of filing the appeal to the Joint Commissioner (Appeals) or Commissioner (Appeals), grant immunity from imposition of penalty u/s 270A and initiation of proceedings u/s 276C or 276CC, where the proceedings for penalty u/s 270A has **not** been initiated due to misreporting of income.
- The Assessing Officer shall, within a period of 1 month from the end of the month in which the application is received, pass an order accepting or rejecting such application after giving an opportunity of being heard to the assessee.
- The order made by the assessing officer in this regard is final.
- Where immunity is granted to the assessee, then appeal to Joint Commissioner (Appeals) or Commissioner (Appeals) or an application for revision u/s 264 shall not be admissible against the order of assessment or reassessment.

The CBDT, vide Circular No. 05/2018 dated 16-08-2018, has clarified that an application made by an assessee u/s 270AA seeking immunity, will not bar the assessee from contesting the same issue in any earlier assessment year. The circular also clarifies that the tax authority shall not take an adverse view in penalty proceedings for earlier assessment years under old penalty regime merely because the taxpayer has applied for immunity under the new penalty regime (i.e., section 270AA).

Power to Reduce or Waive Penalty, etc., in Certain Cases [Sec. 273A]

4.3

Power u/s 273A(1)

- The Principal Commissioner or Commissioner may, in his discretion, whether on his own motion or otherwise reduce or waive the amount of penalty imposed or imposable on a person u/s 270A[2] for concealment of income (not other penalty) if he is satisfied that such person:
  - (a) has, prior to the detection by the Assessing Officer, of the concealment of particulars of income or of the inaccuracy of particulars furnished in respect of such income, voluntarily and in good faith, made full and true disclosure of such particulars;
    - A person shall be deemed to have made full and true disclosure of his income or of the particulars relating thereto in any case where the excess of income assessed over the income returned is of such a nature as not to attract the provisions of sec. 270A.
  - (b) has, co-operated in any enquiry relating to the assessment of his income; and
  - (c) has either paid or made satisfactory arrangements for the payment of any tax or interest payable in consequence of an order passed under this Act in respect of the relevant assessment year.
- However, where the amount of income in respect of which the penalty is imposed or imposable for the relevant assessment year, or, where such disclosure relates to more than one assessment year, the aggregate amount of such income for those years, exceeds a sum of ₹ 5,00,000, no order reducing or waiving the penalty shall be made by the Principal Commissioner or Commissioner except with the previous approval of the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General, as the case may be.
- Where an order of waiver u/s 273A(1) has been made in favour of any person, whether such order relates to one or more assessment years, he shall not be entitled to any relief under this section in relation to any other assessment year at any time after the making of such order. That means such waiver can be done once in life of assessee.

Power u/s 273A(4)

- The Principal Commissioner or Commissioner may, on an application (not suo motu) made in this behalf by an assessee, and after recording his reasons for so doing, reduce or waive the amount of any penalty payable by the assessee under this Act, or stay or compound any proceeding for the recovery of any such amount, if he is satisfied that—
  - (i) to do otherwise would cause genuine hardship to the assessee, having regard to the circumstances of the case; and
  - (ii) the assessee has co-operated in any inquiry relating to the assessment or any proceeding for the recovery of any amount due from him.

[2] Also covered penalty imposable u/s 271(1)(c)

- Where the amount of any penalty payable under this Act or, where such application relates to more than one penalty, the aggregate amount of such penalties exceeds ₹ 1,00,000, no order reducing or waiving the amount or compounding any proceeding for its recovery shall be made by the Principal Commissioner or Commissioner except with the previous approval of the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General, as the case may be.
- The order, either accepting or rejecting the application in full or in part, shall be passed within a period of 12 months from the end of the month in which the application is received by the Principal Commissioner or the Commissioner. Further, no order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard.

Taxpoint:

- An assessee can claim relief u/s 273A(1) or 273A(4) after claiming relief u/s 273A(4). However, if assessee already claimed relief u/s 273A(1), then no relief u/s 273A(4) or 273A(1) can be granted.
- Every order made under this section shall be final and shall not be called into question by any court or any other authority.
- The "genuine hardship" referred to in the provisions of section 273A(4) should exist at the time at which the application under section 273A(4) is made by the assessee before the Commissioner and should so exist even at the time of passing of order under section 273A(4) by the Commissioner. [Circular No. 784, dated 22nd November, 1999]

Power of Principal Commissioner or Commissioner to Grant Immunity from Penalty [Sec. 273AA]

1. A person may make an application to the Principal Commissioner or Commissioner for granting immunity from penalty, if —
   (a) he has made an application for settlement u/s 245C and the proceedings for settlement have abated u/s 245HA; and
   (b) the penalty proceedings have been initiated under this Act.
2. The application to the Principal Commissioner or Commissioner shall not be made after the imposition of penalty after abatement.
3. The Principal Commissioner or Commissioner may, subject to such conditions as he may think fit to impose, grant to the person immunity from the imposition of any penalty under this Act, if he is satisfied that the person has, after the abatement, co-operated with the income-tax authority in the proceedings before him and has made a full and true disclosure of his income and the manner in which such income has been derived.
4. The order, either accepting or rejecting the application in full or in part, shall be passed within a period of 12 months from the end of the month in which the application is received by the Principal Commissioner or the Commissioner. Further, no order rejecting the application, either in full or in part, shall be passed unless the assessee has been given an opportunity of being heard.
5. The immunity granted to a person shall stand withdrawn, if such person fails to comply with any condition subject to which the immunity was granted and thereupon the provisions of this Act shall apply as if such immunity had not been granted.
6. The immunity granted to a person may, at any time, be withdrawn by the Principal Commissioner or Commissioner, if he is satisfied that such person had, in the course of any proceedings, after abatement, concealed any particulars material to the assessment from the income-tax authority or had given false evidence, and thereupon such person shall become liable to the imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

Penalty not to be Imposed in certain cases [Sec. 273B]

Penalty referred to in sec. 271A, 271AA, 271B, 271BA, 271BB, 271C, 271CA, 271D, 271E, 271FA, 271FAB, 271FB, 271G, 271GA, 271GB, 271H, 271-I, 271J, 272A(1)(c), 272A(1)(d), 272A(2), 272AA, 272B, 272BB or 272BBB, shall not be imposable on the person or the assessee, as the case may be, for any failure referred to in the said provisions if he proves that there was reasonable cause for the said failure.

Procedure [Sec. 274]

- No order imposing a penalty under this Chapter shall be made unless the assessee has been heard, or has been given a reasonable opportunity of being heard.
- No order imposing a penalty under this Chapter shall be made:

  (a) by the Income-tax Officer, where the penalty exceeds ₹ 10,000;

  (b) by the Assistant Commissioner or Deputy Commissioner, where the penalty exceeds ₹ 20,000,

  except with the prior approval of the Joint Commissioner.
- An income-tax authority on making an order under this Chapter imposing a penalty (unless he is himself the Assessing Officer) shall send a copy of such order to the Assessing Officer.
- The Central Government may make a scheme, for the purposes of imposing penalty so as to impart greater efficiency, transparency and accountability by:

  a. eliminating the interface between the income-tax authority and the assessee or any other person to the extent technologically feasible;

  b. optimising utilisation of the resources through economies of scale and functional specialisation;

  c. introducing a mechanism for imposing of penalty with dynamic jurisdiction in which penalty shall be imposed by one or more income-tax authorities.
- Similar scheme may also be made for prosecution [Sec. 279]

Bar of limitation for imposing penalties [Sec. 275]

No order imposing a penalty under this Chapter shall be passed after following time limit:

Where the relevant assessment or other order is the subject-matter of an appeal to the Joint Commissioner (Appeals) or Commissioner (Appeals) and the Joint Commissioner (Appeals) or Commissioner (Appeals) passes the order disposing of such appeal	An order imposing penalty shall be passed a. On or before the expiry of the financial year in which assessment proceedings are completed; or b. within 1 year from the end of the financial year in which the order of the Joint Commissioner (Appeals) or Commissioner (Appeals) is received by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, whichever is later
Where further appeal has been filed to ITAT	An order imposing penalty shall be passed a. On or before the expiry of the financial year in which assessment proceedings are completed; or b. On or before the expiry of 6 months from the end of the month in which the order of the ITAT is received by the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, whichever is later

Where the relevant assessment or other order is the subject-matter of revision u/s 263 or 264	Penalty order shall not be passed after the expiry of 6 months from the end of the month in which such order of revision is passed
In any other case	Penalty order shall not be passed: a. On or before the expiry of the financial year in which assessment proceedings are completed; or b. 6 months from the end of the month in which action for imposition of penalty is initiated, whichever period expires later

Taxpoint

In computing the period of limitation for the purposes of this section:

a. the time taken in giving an opportunity to the assessee to be reheard u/s 129;

b. any period during which the immunity granted u/s 245H remained in force; and

c. any period during which a proceeding for the levy of penalty is stayed by an order or injunction of any court,

- shall be excluded.

Revision of penalty order [Sec. 275(1A)]

Case:

- Where the relevant assessment or other order is the subject-matter of an appeal to the Joint Commissioner (Appeals) or Commissioner (Appeals) or to the Appellate Tribunal or to the High Court or to the Supreme Court [here-in-after referred to as 'appeal'] or revision u/s 263 or 264
- An order imposing or enhancing or reducing or cancelling penalty or dropping the proceedings for the imposition of penalty is passed before appeal order is received by the Principal Chief Commissioner or Chief Commissioner or the Principal Commissioner or Commissioner or the order of revision is passed,

then

- An order imposing or enhancing or reducing or cancelling penalty or dropping the proceedings for the imposition of penalty may be passed on the basis of assessment as revised by giving effect to such appeal and revision
- However, no order of imposing or enhancing or reducing or cancelling penalty or dropping the proceedings for the imposition of penalty shall be passed after the expiry of 6 months from the end of the month in which the appeal order is received by the Principal Chief Commissioner or Chief Commissioner or the Principal Commissioner or Commissioner or the order of revision is passed.
- Further, no penalty order is passed unless the assessee has been heard, or has been given a reasonable opportunity of being heard.

When Assessee becomes Liable for Prosecution

4.4

The Department is empowered to put on prosecution proceedings for offences committed by taxpayers. Prosecution details are tabulated below:

Section	Nature of offence	Rigorous Imprisonment and Fine	
		Minimum	Maximum
275A	Contravention of any order referred to in the second proviso to sec. 132(1) or (3)	Any period up to 2 years (and fine also)	
275B	Failure to comply with provision of sec. 132(1)(iib)		
276	Removal, concealment, transfer or delivery of property or any interest therein to prevent tax recovery.		
276A	Failure to comply with provision of sec. 178(1)/(3) by liquidator of a company.	Any period up to 2 years [No fresh prosecution under this section on or after 01-04-2023]	
276B(a)	Failure to pay to the credit of Central Government, the tax deducted at source by him under chapter XVIIB	3 months (with fine)	7 years (with fine)
276B(b)	Failure to pay or ensure payment of tax as per sec. 115-O(2) or proviso to sec. 194B or first proviso to sec. 194R(1) or the proviso to sec. 194S(1) or sec. 194BA(2)		
276BB	Failure to pay to the credit of Central Government tax collected at source u/s 206C		
276C(1)	Attempt to evade tax, penalty or interest chargeable/ imposable, or under-reports income	6 months (with fine)	7 years (with fine)
	Case I: If amount sought to be evaded exceeds ₹ 25,00,000	3 months (with fine)	2 years (with fine)
	Case II: If such amount involved does not exceed ₹ 25,00,000		
276C(2)	Attempt to evade the payment of any tax, penalty or interest.	3 months (with fine)	3 years (with fine)
276CC	Willful failure to file return of income in time u/s 139(1), or in response to notice u/s 142(1) or u/s 148 provided tax payable by such person (other than company), on the total income determined on regular assessment (as reduced by the advance tax, self-assessment tax, TDS and TCS), exceeds ₹ 10,000 or return is furnished within the assessment year or an updated return is furnished by him u/s 139(8A)		

Section	Nature of offence	Rigorous Imprisonment and Fine	
		Minimum	Maximum
	Case I: If amount of tax sought to be evaded exceeds ₹ 25,00,000	6 months (with fine)	7 years (with fine)
	Case II: If amount of tax sought to be evaded does not exceed ₹ 25,00,000	3 months (with fine)	2 years (with fine)
276D	Wilful failure to produce books of account and documents as required u/s 142(1) or wilful failure to comply with direction u/s 142(2A) to get the accounts audited	Any period up to one year (and with fine)	
277	Makes false statement in any verification or delivers a false account or statement under this Act or rules there under		
	Case I: If amount of tax sought to be evaded exceeds ₹ 25,00,000	6 months (with fine)	7 years (with fine)
	Case II: If amount of tax sought to be evaded does not exceed ₹ 25,00,000	3 months (with fine)	2 years (with fine)
277A	Where any person (hereafter referred to as the first person) wilfully and with intent to enable any other person (hereafter referred to as the second person) to evade any tax or interest or penalty chargeable and imposable under this Act, makes any entry or statement which is false and which the first person either knows to be false or does not believe to be true, in any books of account or other document being useful in any proceedings against the first person or the second person. For establishing the charge, it shall not be necessary to prove that the second person has actually evaded any tax, penalty or interest chargeable or imposable under this Act.	The first person shall be punishable with rigorous impris-onment for 3 months and with fine.	The first person shall be punishable with rigorous imprisonment for 2 years with fine.
278	Abetment or inducement in any manner to another person to make false statement or declaration relating to any income or any fringe benefits chargeable to tax. **Case I:** Where the amount of tax, penalty or interest which would have been evaded due to such false presentation, exceeds ₹ 25,00,000	6 months (with fine)	7 years (with fine)
	Case II: In any other case	3 months (with fine)	2 years (with fine)
278A	Punishment for second and subsequent offences u/s 276B, 276BB, 276C(1), 276CC, 277 or 278	6 months for every offence (with fine)	7 years for every offence (with fine)

Section	Nature of offence	Rigorous Imprisonment and Fine	
		Minimum	Maximum
278B	Where an offence under this Act has been committed by a company - ➢ The company itself; and ➢ Every person who, at the time the offence was committed, was in charge of, and was responsible to the company for the conduct of the business of the company, - shall be deemed to be guilty of the offence **Note:** Company includes firm, AOP/BOI.	Liable to be proceeded against and punished accordingly. **Note:** Where the punishment for an offence is imprisonment and fine, then such company shall be punished with fine only.	
278C	Where an offence under this Act has been committed by an HUF, the Karta thereof shall be deemed to be guilty of the offence		
280	Disclosure of any information by public servants in contravention of sec. 138(2)	Upto 6 months (with fine) (With previous sanction of the Central Government)	

Notes:

(a) No court inferior to that of a Presidency Magistrate of the first class shall try any offence under this Act [Sec. 292]

(b) Punishment shall not be imposed u/s 276A, 276B and 276BB if the assessee proves that there was reasonable cause for failure [Sec.278AA]

(c) Prosecution proceeding shall not be instituted u/s 275A, 275B, 276, 276A, 276B, 276BB, 276C, 276CC, 276D, 277, 277A and 278 without previous sanction of the Principal Commissioner or Commissioner or Joint Commissioner (Appeals) or Commissioner (Appeals) or the appropriate authority [Sec. 279]

(d) A person shall not be proceeded against for an offence u/s 276C or 277 in relation to the assessment for an assessment year in respect of which the penalty imposed or imposable on him u/s 270A has been reduced or waived u/s 273A. [Sec. 279(1A)]

Power of Commissioner to Grant Immunity from Prosecution [Sec. 273AB]

1. A person may make an application to the Principal Commissioner or Commissioner for granting immunity from prosecution, if he has made an application for settlement u/s 245C and the proceedings for settlement have abated u/s 245HA.

2. The application to the Principal Commissioner or Commissioner shall not be made after institution of the prosecution proceedings after abatement.

3. The Principal Commissioner or Commissioner may, subject to such conditions as he may think fit to impose, grant to the person immunity from prosecution for any offence under this Act, if he is satisfied that the person

has, after the abatement, co-operated with the income-tax authority in the proceedings before him and has made a full and true disclosure of his income and the manner in which such income has been derived:

4. The immunity granted to a person shall stand withdrawn, if such person fails to comply with any condition subject to which the immunity was granted and thereupon the provisions of this Act shall apply as if such immunity had not been granted.

5. The immunity granted to a person may, at any time, be withdrawn by the Principal Commissioner or Commissioner, if he is satisfied that such person had, in the course of any proceedings, after abatement, concealed any particulars material to the assessment from the income-tax authority or had given false evidence, and thereupon such person may be tried for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the proceedings.

Exercise

Multiple Choice Questions

1. Prosecution can be launched and the taxpayer can be punished if he commits wilful failure to produce before the tax authorities the accounts and documents as demanded u/s _____.
   A. 154
   B. 147
   C. 143(1)
   D. 142(1)
2. If a person fails to comply with the provisions relating to PAN (i.e. obtaining PAN, quoting PAN, etc.), then penalty can be levied under section _____
   A. 270A
   B. 272
   C. 272A
   D. 272B
3. If during any proceeding, it is found that in the books of account maintained by any person there is a false entry or an omission of any entry which is relevant for computation of total income of such person, to evade tax liability, penalty u/s 271AD or ₹ ……. is levied
   A. A sum equal to the aggregate amount of such false or omitted entry.
   B. ₹ 5,000 (subject to maximum of ₹ 1,00,000)
   C. 2% of the amount of such entry
   D. None of the above
4. If the amount of income in respect of which the penalty is imposed or imposable for the relevant year(s) exceeds ₹ _____, then no order reducing or waiving the penalty under section 273A(1) shall be made by the Principal Commissioner or Commissioner, except with the previous approval of the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General, as the case may be
   A. 1,00,000
   B. 2,00,000
   C. 5,00,000
   D. 10,00,000
5. Principal Commissioner or Commissioner of Income-tax is empowered to grant relief from penalty to taxpayers in genuine cases. Such power is granted under section 273A and section _____.
   A. 273B
   B. 273AA
   C. 273
   D. 274

[Answer: 1 – D; 2 – D,;3 – A; 4 – C; 5 - B]

Short Essay Type Questions

1. State the provisions relating to power of Commissioner to reduce or waive penalty u/s 273A
2. State the amount of penalty u/s 271GA for non filing of information required to be furnished u/s 285A
3. What do you mean by under-reporting of income?

Reference

https://www.incometaxindia.gov.in/
https://www.incometax.gov.in/
https://www.indiabudget.gov.in/

Business Restructuring 5

This Module includes:

5.1 Amalgamation

5.2 Demerger

5.3 Slump Sale

5.4 Conversion of Sole Proprietary Business to Company

5.5 Conversion of Firm into Company

5.6 Conversion of Private Limited Company / Unlisted Public Company into LLP

Business Restructuring

SLOB Mapped against the Module:

To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.

Module Learning Objectives:

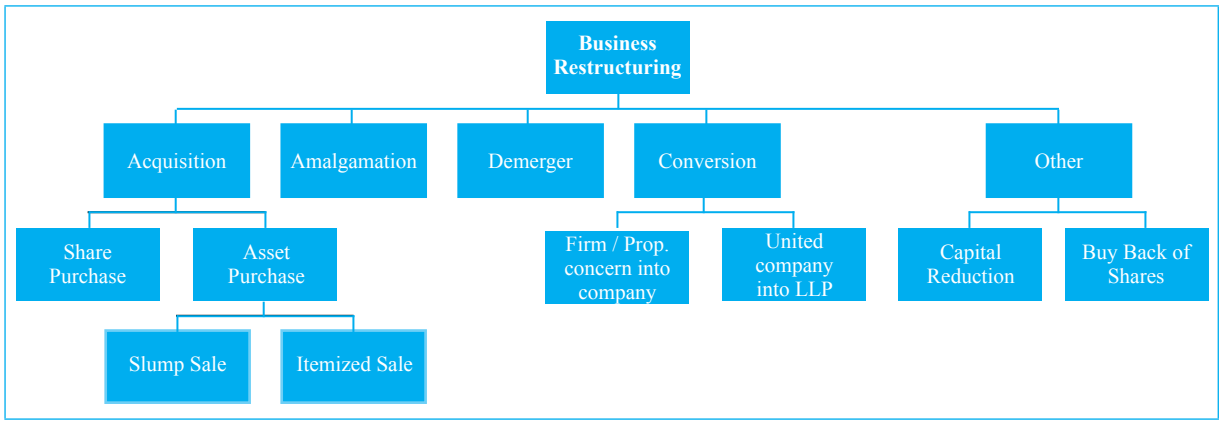
After studying this module, the students will be able to -

- Identify and examine the benefits of various mode of business restructuring
- Understand the provisions relating to tax impact of such restructuring
- Appreciate the pre and post compliance to maximize the tax benefit
- Understand the effect of such restructuring on various stakeholders

Introduction

5

Restructuring is term used for the act of reorganizing the legal, ownership, operational, or other structures of a company for the purpose of making it more profitable, or better organized for its present needs. Companies are resorting to acquisitions as a means to consolidate and grow rapidly in an ever changing business environment. As a result, there is an increase in the level of restructuring activity in various sectors. Change in ownership or operational structure transaction have tax implication. The purpose of a suitable business strategy for restructuring must increase efficiency, consolidate operations, increase market share, assist in turn around, increase market capitalization and create entry barrier for competitors. Proper tax planning in this regard shall reduce the cost of restructuring in this front. The chapter highlights the various tax aspect in hands of all concerned person.



Amalgamation

5.1

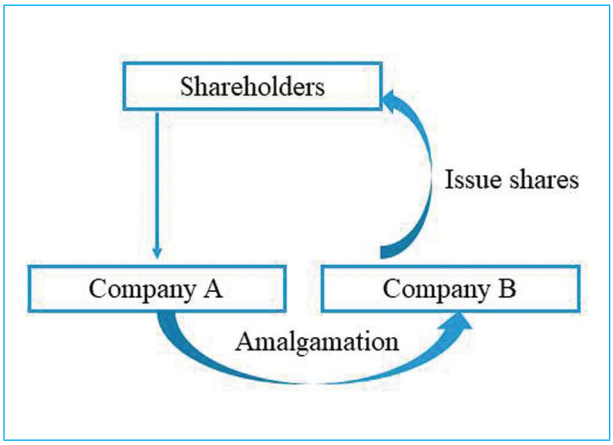
Definition [Sec. 2(1B)]

Amalgamation (in relation to companies) means:

- the merger of one or more companies with another company; or
- the merger of two or more companies to form one company;

in such a manner that—

(a) all assets and liabilities of the amalgamating company or companies immediately before the amalgamation becomes the assets and liabilities of the amalgamated company;



(b) shareholders (both equity or preference) holding not less than 75% in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders (equity or preference) of the amalgamated company.

- Number of shares allotted to the shareholders of the amalgamating company by the amalgamated company is not relevant.
- Where C Ltd. merges with Z Ltd., in a scheme of amalgamation, and immediately before the amalgamation, Z Ltd. holds 20% of the share in C Ltd., the aforesaid mentioned condition will be satisfied if shareholders holding not less than ¾th (in value) of the remaining 80% of the shares in C Ltd., i.e., 60% thereof (3/4 x 80), become shareholders of Z Ltd., by virtue of the amalgamation. Where, however, the whole of the share capital of a company is held by another company, the merger of the two companies will qualify as an amalgamation within sec. 2(1B), if the other two conditions are satisfied [Circular 5P, dated 9-10-67]

Exceptions:

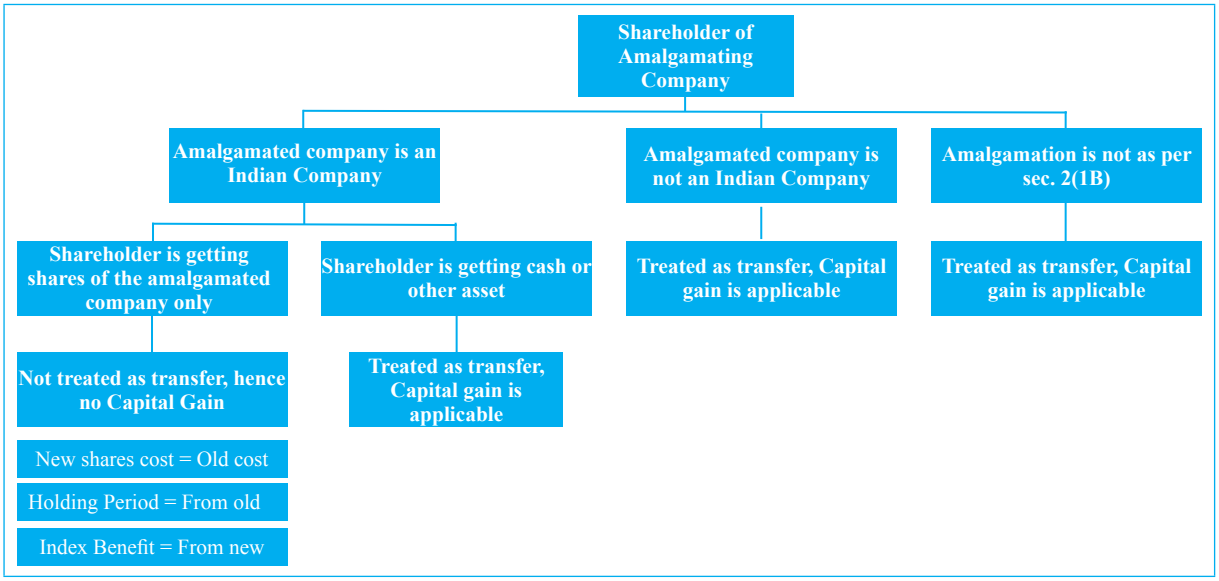
Following mergers shall not be treated as amalgamation -

- Merger as a result of acquisition of the property of one company by another company pursuant to the purchase of such property by the other company; or
- Merger as a result of distribution of such property to the other company after the winding up of the first-mentioned company.

Amalgamation & Shareholder of amalgamating company

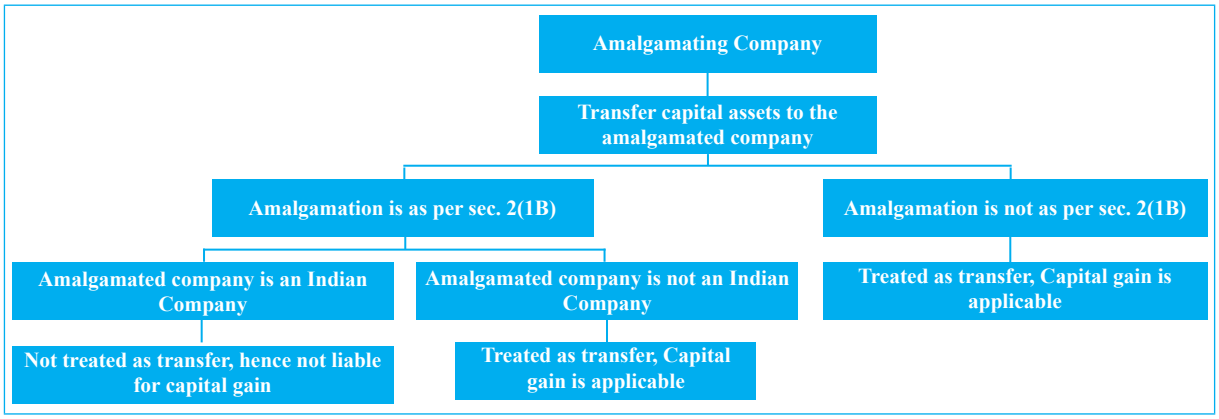
Effect of amalgamation on a shareholder are as under:

Transfer of shares of amalgamating company	As per sec. 47(vii), any transfer by a shareholder, in a scheme of amalgamation, of share(s) held by him in the amalgamating company is not treated as transfer and hence not liable to capital gain tax, if following conditions are satisfied: i. The transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company; and ii. The amalgamated company is an *Indian* company.
Cost of shares in amalgamated company	The cost of shares in amalgamating company shall be deemed to be the cost of shares in amalgamated company. [Sec. 49(2)]
Determination of nature of assets	To find whether shares in amalgamated company are long-term or short-term capital asset, the period of holding shall be calculated from the date when shares in the amalgamating company were acquired. [Sec. 2(42A)]
Indexation benefit	Indexation benefit shall be available from the year in which shares of amalgamated company were acquired by the assessee.

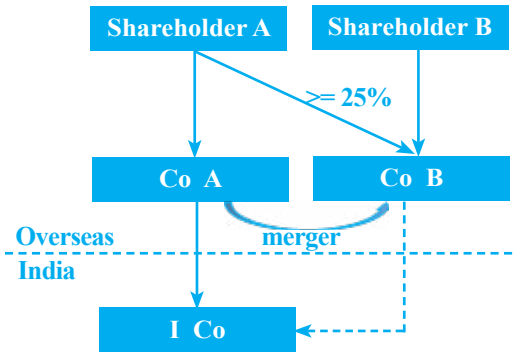


Amalgamation & amalgamating company

- As per sec. 47(vi), any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company is not treated as transfer (hence not liable to capital gain) provided the amalgamated company is an *Indian* company.
- If amalgamation does not satisfy condition of sec. 2(1B) **and** of sec. 47(vi), then exemption is not available.



- As per sec. 47(viab), any transfer, in a scheme of amalgamation, of a capital asset, being a share of a foreign company, (referred to in the Explanation 5 of sec.9(1)(i)), which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the amalgamating foreign company to the amalgamated foreign company, if:
  a. at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and
  b. such transfer does not attract tax on capital gains in the country in which the amalgamating company is incorporated.



Such transfer is exempt in foreign country

- As per sec. 47(via), any transfer, in a scheme of amalgamation, of a capital asset being a share or shares held in an Indian company, by the amalgamating foreign company to the amalgamated foreign company is not treated as transfer (hence not liable to capital gain) provided:
  a) at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and
  b) such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated.

Taxpoint

- Such transfer is in a scheme of amalgamation by the amalgamating foreign company to the amalgamated foreign company.
- Transferred asset must be a capital asset being a share or shares held in an Indian company.
- At least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company.
- Such transfer does not attract tax on capital gain in the country, in which the amalgamating company is incorporated.

Amalgamation & amalgamated company

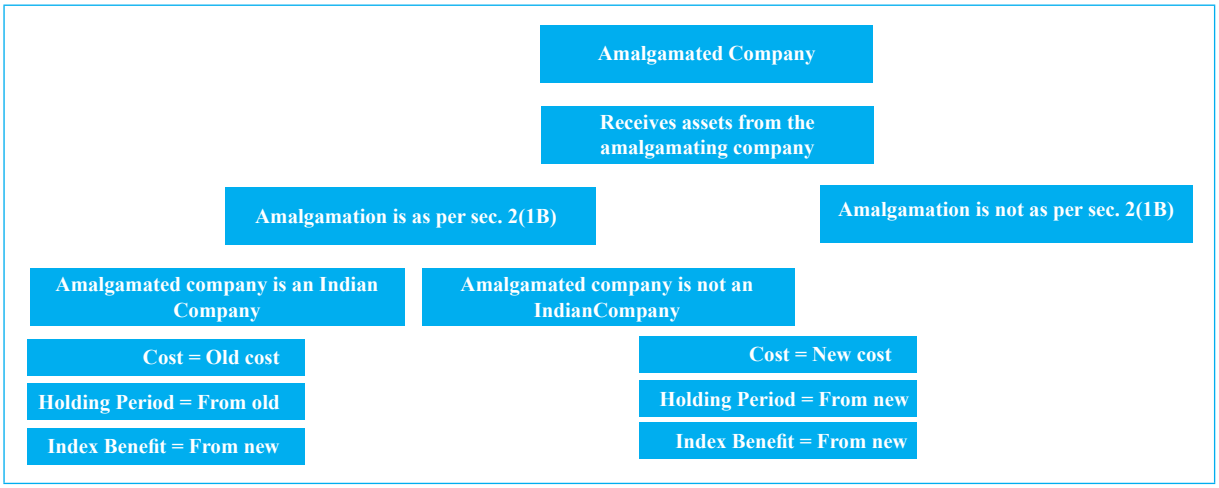
- **Value of non-depreciable capital assets for the purpose of capital gain**
  - As per sec. 49(1), where a capital asset became the property of amalgamated (Indian) company in a scheme of amalgamation, the cost of acquisition of the asset to the amalgamated company shall be deemed to be the cost for which the previous owner (i.e., amalgamating company) of the property acquired it, as increased by the cost of any improvement of the assets incurred or borne by the previous owner or the assessee, as the case may be.
  - It is to be noted that where non-depreciable asset was acquired before 1-4-2001, the cost of acquisition can be taken as cost of acquisition or fair market value of the asset as on 1-4-2001, at the option of the assessee.
  - In determining the period of holding of such asset, period of holding of previous owner shall also be considered, however, indexation benefit is available from the year of amalgamation.
- **Value of depreciable asset for the purpose of business income**
  - Where in any previous year, any block of assets is transferred by the amalgamating company to the amalgamated (Indian) company in a scheme of amalgamation, then, the actual cost of the block of assets in the case of the amalgamated company shall be the written down value of the block of assets as in the case of the amalgamating company for the immediately preceding previous year as reduced by the amount of depreciation actually allowed in relation to the said preceding previous year [Exp. 2 to sec. 43(6)]
  - Allocation of depreciation in the year of amalgamation: The aggregate deduction, in respect of depreciation allowable to the amalgamating company and the amalgamated company in the case of amalgamation shall not exceed in any previous year the deduction calculated at the prescribed rates as if the amalgamation had not taken place and such deduction shall be apportioned between the amalgamating company and the amalgamated company in the ratio of the number of days for which the assets were used by them.
- **Value of asset transferred as stock in trade**
  - Where an asset [not being an asset referred to in sec. 45(2)] which becomes the property of an amalgamated company under a scheme of amalgamation, is sold by the amalgamated company as stock-in-trade of the business carried on by it, the cost of acquisition of the said asset to the amalgamated company in computing the profits and gains from the sale of such asset shall be the cost of acquisition of the said asset to the amalgamating company, as increased by the cost, if any, of any improvement made thereto, and the expenditure, if any, incurred, wholly and exclusively in connection with such transfer by the amalgamating company [Sec. 43C(1)]

    Taxpoint: The provision is applicable where following asset of the amalgamating company is taken over by the amalgamated company as stock-in-trade at revalued price:

    a) Stock-in-trade

    b) Capital asset converted to stock-in-trade

    c) Capital asset
  - Sec. 43C is also applicable where an asset becomes the property of the assessee on the total or partial partition of HUF or under a gift or will or irrevocable trust.



⊙ Set-off and carry forward of business loss and unabsorbed depreciation [Sec. 72A]

Applicable

1. There has been an amalgamation of a company owning -
   - an industrial undertaking; or
   - a ship; or
   - a hotel,

   with another company; or

   Taxpoint: Industrial undertaking means an undertaking engaged in—
   - manufacture or processing of goods; or
   - manufacture of computer software; or
   - business of generation or distribution of electricity or any other form of power; or
   - business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services; or
   - mining; or
   - the construction of ships, aircrafts or rail systems.
2. There has been amalgamation of a banking company with a specified bank.
3. There has been amalgamation of one or more public sector company or companies with one or more public sector company or companies; or
4. There has been amalgamation of an erstwhile public sector company with one or more company or companies, if the share purchase agreement entered into under strategic disinvestment restricted immediate amalgamation of the said public sector company and the amalgamation is carried out within 5 years from the end of the previous year in which the restriction on amalgamation in the share purchase agreement ends
   - "Erstwhile public sector company" means a company which was a public sector company in earlier previous years and ceases to be a public sector company by way of strategic disinvestment by the Government;

- "Strategic disinvestment" means sale of shareholding by the Central Government or any State Government or a public sector company, in a public sector company or in a company, which results in:
  a. reduction of its shareholding to below 51%; and
  b. transfer of control to the buyer.

  However, the first condition shall apply only in a case where shareholding of the Central Government or the State Government or the public sector company was above 51% before such sale of shareholding.

  Further requirement of transfer of control may be carried out by the Central Government or the State Government or the public sector company or any two of them or all of them

Conditions to be satisfied

The accumulated loss shall not be set off or carried forward and the unabsorbed depreciation shall not be allowed in the assessment of the amalgamated company unless:

(a) The amalgamating company—
  (i) has been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for three or more years;
  (ii) has held continuously as on the date of the amalgamation at least ¾th of the book value of fixed assets held by it two years prior to the date of amalgamation.

(b) The amalgamated company—
  (i) holds continuously for a minimum period of 5 years from the date of amalgamation at least ¾th of the book value of fixed assets of the amalgamating company acquired in a scheme of amalgamation;
  (ii) continues the business of the amalgamating company for a minimum period of 5 years from the date of amalgamation;
  (iii) fulfils such other conditions* as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purpose.

* Conditions for carrying forward or set-off of accumulated loss and unabsorbed depreciation allowance in case of amalgamation [Rule 9C]

(a) The amalgamated company, owning an industrial undertaking of the amalgamating company by way of amalgamation, shall achieve the level of production of at least 50% of the installed capacity (i.e., the capacity of production existing on the date of amalgamation) of the said undertaking before the end of 4 years from the date of amalgamation and continue to maintain the said minimum level of production till the end of 5 years from the date of amalgamation.

Provided that the Central Government, on an application made by the amalgamated company, may relax the condition of achieving the level of production or the period during which the same is to be achieved or both in suitable cases having regard to the genuine efforts made by the amalgamated company to attain the prescribed level of production and the circumstances preventing such efforts from achieving the same.

(b) The amalgamated company shall furnish to the Assessing Officer a certificate in Form No. 62, duly verified by an accountant, with reference to the books of accounts and other documents showing particulars of production, along with the return of income for the assessment year relevant to the previous year during which the prescribed level of production is achieved and for subsequent assessment years relevant to the previous years falling within five years from the date of amalgamation.

Treatment

- The accumulated business (non-speculative) loss and the unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or, as the case may be, allowance for depreciation of the amalgamated company for the previous year in which the amalgamation was effected, and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.
- In a case where any of the conditions are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the amalgamated company shall be deemed to be the income of the amalgamated company chargeable to tax for the year in which such conditions are not complied with.

Deduction of expenses incurred in case of amalgamation or demerger [Sec. 35DD]

Applicable to: An Indian company

Conditions

a) Assessee has incurred certain expenditure wholly & exclusively for the purpose of amalgamation or demerger.

b) No deduction has been claimed for such expenses under any other section.

Quantum of deduction: 1/5th of expenses so incurred for a period of 5 years commencing from the year in which amalgamation or demerger takes places.

Other Provisions

Capital Expenditure on Scientific Research [Sec. 35(5)]: Provisions of sec. 35 shall apply to the amalgamated company, as it would have been applied to the amalgamating company, if the latter had not transferred such asset.

Telecom or spectrum licence: The amalgamated company or resulting company (being Indian company) as the case may be shall be entitled to claim deduction u/s 35ABB (or sec. 35ABA) for the residual period as if the amalgamating or demerged company had not transferred the licence.

Amortisation of Preliminary Expenses: In case of transfer of undertaking under the scheme of amalgamation or demerger, the amalgamated company or resulting company (being Indian company) shall be entitled to claim deduction u/s 35D for the residual period as if the amalgamation or demerger had not taken place.

Amortisation of expenditure incurred under VRS: In case of transfer of undertaking under the scheme of amalgamation or demerger, the amalgamated company or resulting company (being Indian company) as the case may be, shall be entitled to claim deduction u/s 35DDA for the residual period as if the amalgamation or demerger had not taken place.

Illustration 1.

Mr. Joseph has 1,000 equity shares of X Ltd. that he acquired on 17/08/2007 through will of his father. His father acquired such shares on 17/07/2004 through gift from his father in law (Mr. Z). Mr. Z acquired such shares on 18/08/2000 for ₹ 20 each. Fair market value of such shares as on –

1/04/2001	17/07/2004	17/08/2007
₹ 18 each	₹ 25 each	₹ 40 each

On 31/03/2013, X Ltd. amalgamated with Y Ltd. and amalgamated company issued its 3 equity shares for every two equity shares of amalgamating company. On 2/04/2023, Mr. Joseph sold 1,000 shares of Y Ltd to one of his friends for ₹ 75 each. Compute capital gain.

Solution:

1. When any shares become the property of assessee in a scheme of amalgamation, period of holding of shares in amalgamated company shall be aggregate of period of holding of shares in amalgamating company prior to amalgamation and period of holding of share in amalgamated company. Hence, in the given case, asset transferred (being shares of Y Ltd) were treated as long-term capital asset.

2. Calculation of cost of acquisition of shares of Y Ltd.

Cost of shares of X Ltd. (i.e., cost of the previous owner[#]) (1,000 share @ ₹ 20 each)	₹ 20,000
Shares received on amalgamation of Y Ltd. (3 for every 2 shares held)	1,500 shares
Cost of acquisition per share of Y Ltd. (₹ 20,000/1,500)	₹ 13.33
[#] **Previous owner:** Previous owner means the last owner who acquired the asset for a value. In the given case Mr. Joseph acquired the shares through will of his father. Hence, literally Joseph's father is previous owner. But since Joseph's father has not purchased such shares but acquired by way of gift from his father in law, hence for this purpose, Mr. Z is the previous owner. [Sec. 49(1)]	

Computation of capital gains in the hands of Mr. Joseph for the A.Y. 2024-25

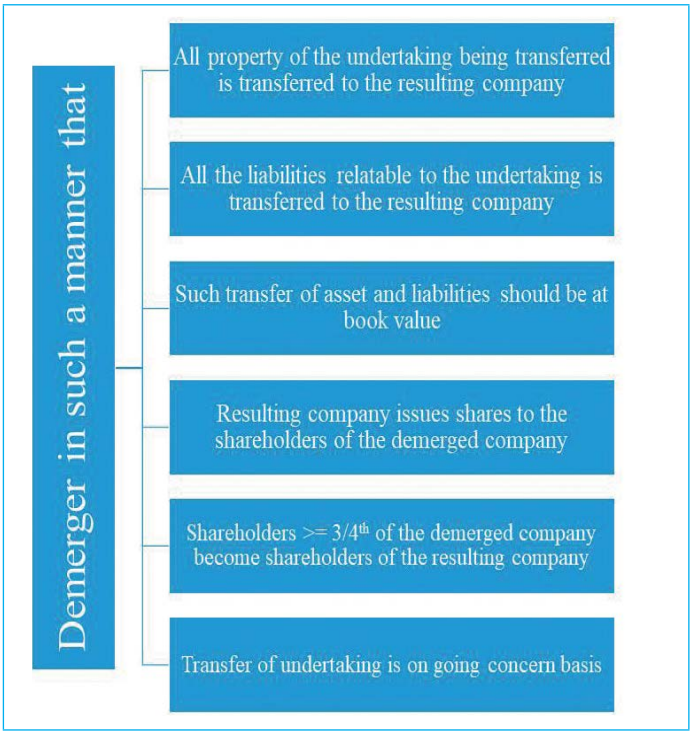
Particulars	Workings	Details	Amount
Sale consideration	1,000 * ₹ 75		75,000
Less: Expenses on transfer			Nil
Net Sale Consideration			75,000
Less: Indexed cost of acquisition	1,000 * ₹ 13.33 * 348/200	23,199	
Less: Indexed cost of improvement		Nil	23,199
Long Term Capital Gain			**51,801**

Demerger

5.2

Definition [Sec. 2(19AA)]

Demerger (in relation to companies) means the transfer, pursuant to a scheme of arrangement u/s 230 to 232 of the Companies Act, 2013, by a demerged company of its one or more undertakings to any resulting company in such a manner that:



i. **All assets and liabilities are transferred:** All assets and liabilities of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the assets and liabilities of the resulting company.

ii. **Transfer at Book value:** Assets and liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at its book-value (without considering revaluation) immediately before the demerger.

Note: Any change in the value of assets consequent to their revaluation shall be ignored.

Exception: The provisions is not applicable where the resulting company records the value of the property and the liabilities of the undertaking or undertakings at a value different from the value appearing in the books of account of the demerged company, immediately before the demerger, in compliance to the Indian Accounting Standards specified in Annexure to the Companies (Indian Accounting Standards) Rules, 2015.

iii. **Consideration in shares:** Resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis except where the resulting company itself is a shareholder of the demerged company.

iv. **Common share-holders:** Shareholders holding not less than 75% in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of

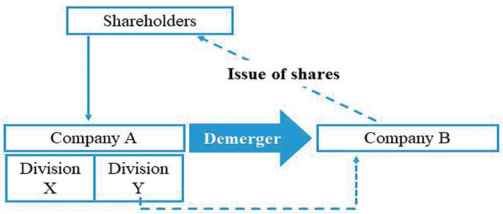
the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company.

v. **Going concern:** Transfer of the undertaking is on a going concern basis.

vi. **Other specified condition:** The demerger is in accordance with the conditions, if any, notified u/s 72A(5) by the Central Government in this behalf.

Taxpoint

- Undertaking shall include (i) any part of an undertaking, or (ii) a unit or division of an undertaking or (iii) a business activity taken as a whole, (iv) but does not include individual assets or liabilities or any combination thereof not constituting a business activity.



- The liabilities referred above, shall include:

(*a*) the liabilities which arise out of the activities or operations of the undertaking;

(*b*) the specific loans or borrowings (including debentures) raised, incurred and utilised solely for the activities or operations of the undertaking; and

(*c*) in cases of general borrowings, so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger, i.e.,

$$\text{General/multi-purpose borrowings of the demerged company} \times \frac{\text{Book value of assets (ignoring revaluation) transferred in the demerger}}{\text{Total book value of assets (ignoring revaluation) of the demerged company before demerger}}$$

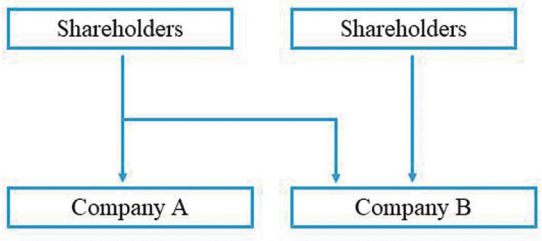
- The splitting up or the reconstruction of any authority or a body constituted or established under a Central, State or Provincial Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies, as the case may be, shall be deemed to be a demerger if such split up or reconstruction fulfils such conditions as may be notified by the Central Government.
- The reconstruction or splitting up of a company, which ceased to be a public sector company as a result of transfer of its shares by the Central Government, into separate companies, shall be deemed to be a demerger, if such reconstruction or splitting up has been made to give effect to any condition attached to the said transfer of shares and also fulfils such other conditions as may be notified by the Central Government.
- Demerged company means the company whose undertaking is transferred, pursuant to a demerger, to a resulting company [Sec. 2(19AAA)]
- Resulting company means one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and, the resulting company in consideration of such transfer of undertaking, issues shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger [Sec. 2(41A)]
- The reconstruction or splitting up of a public sector company into separate companies shall be deemed to be a demerger, if such reconstruction or splitting up has been made to transfer any asset of the demerged company to the resulting company and the resulting company—

i. is a public sector company on the appointed day indicated in such scheme, as may be approved by the Central Government or any other body authorised under the provisions of the Companies Act, 2013 or any other law for the time being in force governing such public sector companies in this behalf; and

ii. fulfils such other conditions as may be notified by the Central Government in the Official Gazette in this behalf

Demerger and Shareholder of demerged company

As per sec. 47(*vid*), any transfer or issue of shares by the resulting company, in a scheme of demerger to the shareholders of the demerged company shall not be treated as transfer if the transfer or issue is made in consideration of demerger of the undertaking.



Shareholding after demerger of company A

In case of demerger, the existing shareholder of the demerged company will now hold:

a) Shares in resulting company; and

b) Shares in demerged company.

and in case the shareholder transfers any of the above shares subsequent to the demerger, the cost of such shares shall be determined as under:

Cost of acquisition of the shares in the resulting company [Sec. 49(2C)]

The cost of acquisition of the shares in the resulting company shall be the amount which bears to the cost of acquisition of shares held by the assessee in the demerged company the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger.

Net worth shall mean the aggregate of the paid up share capital and general reserves as appearing in the books of account of the demerged company immediately before the demerger.

Cost of acquisition of the shares in demerged company [Sec. 49(2D)]

The cost of acquisition of the original shares held by the shareholder in the demerged company shall be deemed to have been reduced by the amount as so arrived at u/s 49(2C).

Taxpoint:

Cost of shares	Resulting company	Cost of acquisition of Original shares	*	Net book value of assets transferred to resulting company
		Net worth# of the company immediately before such demerger		
		# Net worth= Paid-up share capital + General reserves (as per books of account of the demerged company immediately before demerger)		
	Demerged company (after demerger)	Cost of acquisition of the original shares *Less:* Cost of shares of resulting company (as above) Cost of shares of demerged company		**** (***) ****

Determination of nature of asset	Resulting company	To find whether shares in resulting company are long-term or short term capital asset, the period of holding shall be calculated from date of acquisition of original shares in demerged company (before demerger).
	Demerged company	
Indexation benefit	Resulting company	Indexation benefit shall be available from the year in which shares in *resulting company* were acquired by the assessee.
	Demerged company	Indexation benefit shall be available from the year in which original shares in *demerged company* were acquired by the assessee.

Illustration 2.

Dona purchases 600 equity shares in XY (P) Ltd. on 1-04-2023 @ ₹ 150 each. On 31-12-2023, XY (P) Ltd. is demerged. In the scheme of demerger, division Y was transferred to Y (P) Ltd. (resulting company). On that date balance sheet of XY (P) Ltd. is as follow –

Liabilities	Division		Total	Asset	Division		Total
	X	Y			X	Y	
6,000 E. Shares			6,00,000	Land	-	2,50,000	2,50,000
General Reserve			4,00,000	Plant	1,75,000	1,00,000	2,75,000
Loan (General)			2,00,000	Investment	2,50,000	-	2,50,000
Loan (Specific)	60,000	75,000	1,35,000	Stock	1,95,000	2,30,000	4,25,000
Creditors	25,000	40,000	65,000	Debtors	55,000	45,000	1,00,000
				Cash and Bank	25,000	75,000	1,00,000
			14,00,000				**14,00,000**

Y (P) Ltd., in consideration of the demerger, issued equity share of ` 100 each (at par) to the shareholders of XY (P) Ltd. on proportionate basis. You are required to compute –

- Number of shares of Y (P) Ltd. received by Dona and cost thereof.
- Cost of acquisition of shares held by Dona in XY (P) Ltd. after demerger.
- Capital gain, if Dona sold 200 shares of XY (P) Ltd. @ ` 125 & 100 shares of Y(P) Ltd. @ ` 110 on 31-03-2024.

Solution:

Calculation of number of shares of Y (P) Ltd. received by Dona

Particulars	Amount	Amount
Net asset taken over by Y (P) Ltd		
Assets taken over		
Land		2,50,000
Plant		1,00,000
Stock		2,30,000
Debtors		45,000
Cash and bank		75,000
		7,00,000
Less: Liabilities		
Loan (Specific)	75,000	

Particulars	Amount	Amount
Creditors	40,000	
Share of General loan (₹ 2,00,000 x ₹ 7,00,000) / ₹ 14,00,000	1,00,000	2,15,000
Net asset taken over		**4,85,000**
No. of shares issued by Y (P) Ltd. (Consideration of ₹ 4,85,000 was discharged by issuing equity shares of ₹ 100 each)		4,850 shares
% of Dona's holding in XY (P) Ltd. (600 shares, out of 6,000 shares of XY (P) Ltd.)		10%
No. of shares allotted in Y (P) Ltd to Dona (10% of 4,850 shares)		485 shares

Cost of such shares is –

Cost of acquisition of shares in XY (P) Ltd. x Net book value of asset transferred to Y (P) Ltd.
Net worth of XY (P) Ltd. immediately before demerger (i.e. Paid up capital + General Reserve)

= (600 x ₹ 150) x ₹ 4,85,000

₹ 6,00,000 + ₹ 4,00,000

= ₹ 43,650

b) Cost of acquisition of shares of XY (P) Ltd. (after demerger) = Original cost of acquisition – Cost of acquisition of shares of Y (P) Ltd. (as computed above)

= ₹ 90,000 – ₹ 43,650 = ₹ 46,350

Computation of capital gain in the hands of Dona for the A.Y. 2024-25

Particulars	Details	Shares of	
		XY (P) Ltd.	Y (P) Ltd.
Sale Consideration	200 x ₹ 125	25,000	-
	100 x ₹ 110	-	11,000
Less: Expenses on transfer		Nil	Nil
Net Sale Consideration		25,000	11,000
Less: i) Cost of acquisition	[(₹ 46,350 x 200)/600]	15,450	-
	[(₹ 43,650 x 100)/485]	-	9,000
ii) Cost of improvement		Nil	Nil
Short Term Capital Gain		**9,550**	**2,000**

Demerger and Demerged company

- As per sec. 47(vib), any transfer, in a demerger, of a capital asset by the demerged company to the resulting company is not treated as transfer (hence not liable to capital gain) provided the resulting company is an Indian company.
- As per sec. 47(vic), any transfer in a demerger, of a capital asset, being a share or shares held in an Indian company, by the demerged foreign company to the resulting foreign company is not treated as transfer provided:
  a) the shareholders holding not less than ¾th in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and
  b) such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated.

The provisions of the Companies Act shall not apply in case of demergers referred to in this clause.

- As per sec. 47(vicc), any transfer in a demerger, of a capital asset, being a share of a foreign company (referred to in the Explanation 5 of sec. 9(1)(i)), which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the demerged foreign company to the resulting foreign company, if:
  a) the shareholders, holding not less than 3/4th in value of the shares of the demerged foreign company, continue to remain shareholders of the resulting foreign company; and
  b) such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated.

WDV of depreciable asset in hands of demerged company

Where in any previous year, any asset forming part of a block of assets is transferred by a demerged company to the resulting company, then, the written down value of the block of assets of the demerged company for the *immediately* preceding previous year shall be reduced by the written down value of the assets transferred to the resulting company pursuant to the demerger [Explanation 2A to Sec. 43(6)]

Demerger and Resulting Company

Actual cost of assets to the resulting company

Where, in a demerger, any capital asset is transferred by the demerged company to the resulting company and the resulting company is an *Indian* company, the actual cost of the transferred capital asset to the resulting company shall be taken to be the same as it would have been if the demerged company had continued to hold the capital asset for the purpose of its own business.

However, such actual cost shall not exceed the written down value of such capital asset in the hands of the demerged company. [Explanation 7A to sec. 43(1)]

WDV of depreciable asset in hands of resulting company

Where in a previous year, any asset forming part of a block of assets is transferred by a demerged company to the resulting company, then, the written down value of the block of assets in the case of the resulting company shall be the written down value of the transferred assets of the demerged company immediately before the demerger [Explanation 2B to Sec. 43(6)]

Allocation of depreciation in the year of demerger

The aggregate deduction, in respect of depreciation allowable to the demerged company and the resulted company in the case of demerger shall not exceed in any previous year the deduction calculated at the prescribed rates as if the demerger had not taken place and such deduction shall be apportioned between the demerged company and the resulting company in the ratio of the number of days for which the assets were used by them.

Set off and carry forward [Sec. 72A]

In the case of a demerger, the accumulated business loss (other than speculation loss) and the allowance for unabsorbed depreciation of the demerged company shall:

(a) where such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set off in the hands of the resulting company;

(b) where such loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company, be apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be.

The Central Government may, for the purposes of this Act, by notification in the Official Gazette, specify such conditions as it considers necessary to ensure that the demerger is for genuine business purposes.

Slump Sale

5.3

Definition [Sec. 2(42C)]: It means transfer, by any means, of undertaking(s) for a lump sum consideration without assigning values to the individual assets of such undertaking(s)

Undertaking shall include any part of an undertaking or a unit or division of an undertaking or a business activity taken as a whole but does not include individual assets or liabilities or any combination thereof not constituting a business activity.

Computation of capital gain

Sale consideration	Fair market value of the capital assets as on the date of transfer, calculated in the prescribed manner, shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of such capital asset Accordingly, the CBDT has prescribed that the fair market value (FMV) of capital assets would be the higher of – a. FMV 1, being the fair market value of capital assets transferred by way of slump sale (determined on the date of slump sale); and b. FMV 2, being the fair market value of the consideration (monetary and non-monetary) received or accruing as a result of transfer by way of slump sale
Cost of Acquisition or Improvement	Net worth[#] of the undertaking
Indexation Benefit	Not available
Nature of gain whether short term or long term	If undertaking is owned and held by the assessee for not more than 36 months, then capital gain shall be deemed to be short-term capital gain otherwise long-term capital gain. **Note:** Where an undertaking is owned and held by an assessee for more than 36 months immediately preceding the date of its transfer, then it shall be treated as a long-term capital asset. It makes no difference that few of the assets of the undertaking are newly acquired (i.e. for less than 36 months).

Net worth shall be the –

Aggregate value of total assets of the undertaking	****
Less: Value of liabilities of such undertaking as appearing in the books of account	****
Net worth	****

Notes

1. **Effect of revaluation:** If any change has been made in the value of assets on account of revaluation of assets etc. then such change in value shall be ignored.

2. **The aggregate value of total assets, in case of:**
   - Capital asset being goodwill of a business or profession, which has not been acquired by the assessee by purchase from a previous owner - Nil
   - Depreciable assets - WDV of block of assets
   - Capital assets in respect of which the whole of the expenditure has been allowed as a deduction under section 35AD - Nil
   - Other assets - Book value of all such assets
3. **Treatment of stock:** In case of slump sale, no profit under the head 'Profits & gains of business or profession' shall arise even if the stock of the said undertaking is transferred along with other assets.
4. **Carry-forward of losses:** In case of slump sale, benefit of unabsorbed losses and depreciation of the undertaking transferred shall be available to the transferor company and not to the transferee company.

Report of an accountant

The assessee is required to upload one month prior to the due date of filing of the return of income, a report of a chartered accountant in Form 3CEA indicating the computation of the net worth of the undertaking or division and certifying that the net worth of the undertaking or division has been correctly arrived at in accordance with the provisions of this section.

Illustration 3.

X Ltd. has several undertakings carrying on several businesses. During the year 2023-24, the company sold one of its undertaking (as it was continuously generating loss since last 5 years) for a lump sum value of ₹ 300 lacs without assigning value to individual asset and liabilities. The fair market value of the capital asset of that unit is ₹ 350 lacs. Book value of sundry assets and liabilities of the undertaking as on the date of sale is as under:

Items	Book Value
Land	₹ 50 lacs (Value for the purpose of Stamp duty ₹ 70,00,000)
Machinery	₹ 70 lacs (WDV as per IT Act ₹ 60 lacs)
Furniture	₹ 50 lacs (WDV as per IT Act ₹ 90 lacs)
Stock	₹ 30 lacs
Debtors	₹ 40 lacs
Creditors	₹ 50 lacs

Brokerage on transfer paid @ 5%. Compute capital gain.

Solution:

Since the undertaking is owned by the company for more than 3 years hence the gain on transfer shall be liable to long term. Calculation of cost of acquisition (i.e. Net worth)

Particulars	Workings	Details	Amount
Value of asset taken over			
Land	Book value of non-depreciable assets	₹ 50 lacs	
Stock	Book value of non-depreciable assets	₹ 30 lacs	

Particulars	Workings	Details	Amount
Debtors	Book value of non-depreciable assets	₹ 40 lacs	
Machinery	WDV as per I.T. Act	₹ 60 lacs	
Furniture	WDV as per I.T. Act	₹ 90 lacs	₹ 270 lacs
Less: Value of liabilities taken over			
Creditors	Book Value		₹ 50 lacs
Net worth (cost of acquisition)			**₹ 220 lacs**

Computation of capital gains in the hands of X Ltd. for the A.Y. 2024-25

Particulars	Details	Amount	Amount
Sale Consideration	Higher of actual consideration and FMV of capital assets transferred		350 lacs
Less: Expenses on transfer	5% of ₹ 300 lacs		15 lacs
Net Sale Consideration			335 lacs
Less: Cost of Acquisition	Calculated above	220 lacs	
Less: Cost of improvement		Nil	220 lacs
Long Term Capital Gain			**115 lacs**

Computation of written down value of block of assets in case of slump sale

Particulars	Amount
W.D.V of the block at the beginning of the previous year	***
Add: Purchase during the previous year	***
	Mno
Less: Sale consideration for assets sold (to the maximum of mno)	(****)
	Pqr
Less: WDV (Note) of the asset sold under slump sale	(abc)
[Value of deduction at this stage i.e. abc cannot exceed pqr]	
	XYZ
Less: Depreciation (as a % on XYZ)	(***)
WDV of the block at the end of year	****

Note: Written down value of the asset sold under slump sale

Particulars	Amount
Original cost of asset sold under slump sale	***
Less: Depreciation (actual) allowed on such asset in respect of any previous year commencing before 1987-88	(***)
Less: Depreciation (notional) that would have been allowable from the previous year 1987-88 onwards as if the asset is only asset in the relevant block.	(***)

Written down value of the asset sold under slump sale	***

Illustration 4.

M/s AP a wholesale enterprises, has sold one of its undertaking consisting of Machinery A (rate of depreciation 30%), Machinery X (rate of depreciation 15%), Building B (rate of depreciation 10%) for ₹ 15,00,000 on 1/9/2023.

- Machinery A, originally acquired for ₹ 5,00,000 on 1/8/2020
- Building B acquired on 17/7/2023 for ₹ 4,00,000.
- During the year, new machinery Z (15%) purchased for ₹ 5,00,000 on 7/7/2023.

Compute depreciation for the A.Y.2024-25:

- Machinery (rate of depreciation 30%) block [WDV as on 1/4/2023 is ₹ 9,00,000]
- Building (rate of depreciation 10%) block [WDV as on 1/4/2023 is ₹ 5,00,000].

Solution:

Computation of depreciation for Block

Particulars	Machinery (30%)	Building (10%)
W.D.V. as on 1/4/2022	9,00,000	5,00,000
Add: Purchase during the year	Nil	4,00,000
	9,00,000	9,00,000
Less: Sale under slump sale (Working)	1,71,500	4,00,000
	7,28,500	5,00,000
Depreciation	**2,18,550**	**50,000**

Working: Written down value of the asset sold under slump sale

Particulars	Machinery A	Building B
Original cost of asset sold under slump sale	5,00,000	4,00,000
Less: Depreciation (notional) that would have been allowable if the asset is only asset in the relevant block. * Depreciation ₹ 1,50,000 (for 2020-21) + ₹ 1,05,000 (for 2021-22) + ₹ 73,500 (for 2022-23)	3,28,500*	Nil
Written down value of the asset sold under slump sale	1,71,500	4,00,000

Conversion of Sole Proprietary Business to Company

5.4

Transaction not regarded as transfer for the purpose of capital gain [Sec. 47(xiv)]

Where a sole proprietary concern is succeeded by a company in the business carried on by it as a result of which the sole proprietary concern sells or otherwise transfers any capital asset to the company, the transaction is not regarded as transfer provided following conditions are satisfied:

a) All assets and liabilities of the sole proprietary concern relating to the business immediately before the succession become the assets and liabilities of the company;

b) Proprietor holds not less than 50% of the total voting power in the company and his shareholding continues to remain as such for a period of 5 years from the date of succession; and

c) The sole proprietor does not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company.

Taxpoint

- Transfer must have taken place as a result of succession of the proprietorship concern to a company.
- All assets and liabilities related to the business must have been transferred.
- The whole consideration shall be paid by allotment of shares in the company.
- Proprietor must hold at least 50% of the total voting power of the company.
- Lock in period for above share is 5 years from the date of succession.
- Exemption is available for capital gain on transfer of capital asset and not on transfer of stock in trade. Therefore, if stock is transferred at profits, it will be taxable as business income.

Conversion of Firm into Company

5.5

Transaction not regarded as transfer for the purpose of capital gain [Sec. 47(xiii)]

Any transfer of a capital asset, by a firm to a company as a result of succession of the firm by a company in the business carried on by the firm, shall not be regarded as transfer provided following conditions are satisfied:

a) All assets and liabilities of the firm relating to the business immediately before the succession become the assets and liabilities of the company.

b) All the partners of the firm immediately before the succession become the shareholders of the company in the same proportion in which their capital accounts stood in the books of the firm on the date of succession.

c) The partners of the firm do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company; and

d) The aggregate of the shareholding in the company of the partners of the firm is not less than 50% of the total voting power in the company and their shareholding continues to be as such for a period of 5 years from the date of succession.

Taxpoint

- Transfer must have taken place as a result of succession of the firm to a company.
- All assets and liabilities related to the business must have been transferred.
- All the partners become the shareholders of the company in their capital ratio (as on the date of the succession)
- The whole consideration shall be paid by allotment of shares in the company
- Partners (altogether) must hold atleast 50% of the total voting power of the company
- Lock in period for above share is 5 years from the date of succession.

Withdrawal of exemption u/s 47(xiii)/47(xiv) [Sec. 47A(3)]

On violation of conditions, exemption earlier allowed shall be withdrawn and amount of profits or gains arising from the transfer of such capital asset not charged earlier shall be deemed to be the profits and gains chargeable to tax of the successor company for the previous year in which the requirements of sec. 47(xiii)/(xiv) are violated.

Taxpoint

Withdrawal of exemption	The benefits availed shall be deemed to be the capital gain
Year of taxability	The year in which condition u/s 47(xiii) or (xiv) are violated.
Who will be liable to tax	Successor company
Benefit of indexation	Available up to the year when succession took place.

Illustration 5.

M/S ABC converted itself into a company as on 31/03/2019. As on date, balance sheet of the firm was as under:

Liabilities	Amount	Assets	Amount
A's Capital	40,000	Machinery (WDV as per IT Act)	1,00,000
B's Capital	1,10,000	Investments (acquired on 14/08/2004)	50,000
C's Capital	50,000	Stock	70,000
Creditors	1,00,000	Debtors	60,000
		Bank	20,000
	3,00,000		3,00,000

Following value was agreed upon on conversion –

Machinery	₹ 1,20,000
Investments	₹ 2,50,000
Stock	₹ 90,000
Debtors	₹ 60,000

The firm fulfilled all the conditions of sec.47(xiii) and partners account are settled by way of issuing equity shares in their capital ratio. However, on 01/04/2023, all partners transferred all of their shares. Show tax treatment.

Solution:

As per sec. 47A(3), where any of the conditions laid down in sec. 47(xiii) are not complied with, the gain exempted u/s 47(xiii) shall be charged to tax in the hands of successor company in the previous year in which the requirements of sec. 47(xiii) are violated. One of the conditions stated in sec. 47(xiii) is that the partner of the old firm cannot transfer shares of the successor company till 5 years. In the given case, all partners sold shares of the successor company within 5 years hence earlier exempted gain shall be revoked.

Computation of taxable income in the hands of successor company for the A.Y. 2024-25

Particulars	Investments	Machinery
Sale consideration	2,50,000	1,20,000
Less: Expenses on transfer	Nil	Nil
Net Sale Consideration	2,50,000	1,20,000
Less: Indexed cost of acquisition [₹ 50,000 x 280/113]	1,23,894	Nil
Less: Cost of acquisition (being WDV)	Nil	1,00,000
Long Term Capital Gain	**1,26,106**	**Nil**
Short Term Capital Gain	**Nil**	**20,000**
Note: Profit on transfer of stock by firm to company (i.e. ₹ 20,000 being ₹90,000 – ₹ 70,000) is taxable as business income of the firm for the A.Y. 2019-20.		

Value of non-depreciable capital assets for the purpose of capital gain

As per sec. 49(1), where a capital asset became the property of the company under transfer referred to in sec. 47(xiii) or 47(xiv), the cost of acquisition of the asset to the company shall be deemed to be the cost for which the previous owner (i.e., erstwhile concern or firm) of the property acquired it, as increased by the cost of any improvement of the assets incurred or borne by the previous owner or the assessee, as the case may be.

Allocation of depreciation in the year of conversion

Deduction for depreciation shall be apportioned between the proprietary concern (or firm) and the company in the ratio of the number of days for which the assets were used by them.

Illustration 6.

M/s. QQ Trading Co. a sole proprietary concern, was converted into a company w.e.f. 01-09-2023. Before the conversion, the sole proprietary concern had a block of Plant & Machinery (15%), whose WDV as on 1-4-2023 was ₹ 3,00,000. On 1st April itself, a new plant of the same block was purchased for ₹ 1,20,000. After the conversion, the company has purchased the same type of plant on 1-1-2024 for ₹ 1,60,000. Compute the depreciation that would be allocated between the concern & the company.

Solution:

Computation of depreciation on plant and machinery if there were no succession

Particulars	Plant & Machinery
W.D.V. as on 1/4/2023	3,00,000
Add: Purchase during the year	1,20,000
	4,20,000
Less: Sale during the year	Nil
	4,20,000
Depreciation @ 15% of ₹ 4,20,000	**63,000**

Allocation of depreciation between sole proprietary concern and the successor company

The depreciation of ₹ 63,000 is to be allocated in the ratio of number of days the assets were used by the sole proprietary concern and the successor company.

Calculation of allowable depreciation to sole proprietary concern

Particulars	Amount
Ex-sole proprietary:	
Plant & machinery are used by sole proprietary concern from 1/4/2023 to 31/8/2024 i.e. 153 days.	
Depreciation for 153 days (₹ 63,000 x 153/366)	26,336

Calculation of allowable depreciation to successor company

Particulars	Amount
Plant & machinery of sole proprietary concern used by the successor company from 1/9/2023 to 31/3/2024 i.e. 213 days. Depreciation for such period (₹ 63,000 x 213/366)	36,664
After conversion	
Depreciation in respect of assets purchased by the successor company on 1/1/2024 is fully allowable in the hands of successor company [50% of 15% on ₹ 1,60,000]	12,000
Total depreciation	**48,592**

Illustration 7.

M/s S & Co., a sole proprietary concern is converted into a company, Sid Co. Ltd. with effect from November 29, 2023. The written down value of assets as on April 1, 2023 are as follows:

Items	Rate of Depreciation	WDV as on 1 April, 2023
Building	10%	₹ 3,50,000
Furniture	10%	₹ 50,000
Plant & Machinery	15%	₹ 2,00,000

Further, on 15-10-2023, M/s S & Co. purchased a plant for ₹ 1,00,000 (rate of depreciation 15%). After conversion, the company added another plant worth ₹ 50,000 (rate of depreciation 15%). Compute the depreciation available to (i) M/s S & Co. and (ii) Sid Co. Ltd. for the A.Y. 2024-25

Solution:

Computation of depreciation on assets if there were no succession

Particulars	Building	Furniture	Plant & Machinery
Rate of depreciation	10%	10%	15%
W.D.V. as on 1/4/2023	3,50,000	50,000	2,00,000
Add: Purchase during the year	Nil	Nil	1,00,000*
	3,50,000	50,000	3,00,000
Less: Sale during the year	Nil	Nil	Nil
	3,50,000	50,000	3,00,000
Depreciation	35,000	5,000	37,500

It is assumed that the assessee is not entitled for additional depreciation.

* Without considering assets acquired after succession.** [(₹ 2,00,000 * 15%) + (₹ 1,00,000 * 15% * ½)]

Allocation of depreciation between sole proprietary concern and the successor company

The depreciation is to be allocated in the ratio of number of days the assets were used by the sole proprietary concern and the successor company.

Calculation of allowable depreciation to sole proprietary concern

Particulars	Amount
Depreciation on assets held as on 01/04/2023	
Assets are used by sole proprietary concern from 1/4/2023 to 28/11/2023 i.e. 242 days, hence depreciation shall be allowed for 242 days	
- Building (₹ 35,000 x 242/366)	23,142
- Furniture (₹ 5,000 x 242/366)	3,306
- Plant and Machinery (₹ 30,000 x 242/366)	19,836
Depreciation on newly acquired assets	
New asset has been used by it from 15/10/2023 to 28/11/2023 i.e. 45 days, hence depreciation shall be allowed for 45 days	
- Plant and Machinery (₹ 7,500 x 45/169)	1,997
Depreciation allowable u/s 32	**48,281**

Calculation of allowable depreciation to successor company

Particulars	Amount (₹)
Depreciation on assets held by sole-proprietary concern as on 01/04/2023	
Asset of sole proprietary concern used by the successor company from 29/11/2023 to 31/3/2024 i.e. 124 days, hence depreciation shall be allowed for 124 days	
- Building (₹ 35,000 x 124/366)	11,858
- Furniture (₹ 5,000 x 124/366)	1,694
- Plant and Machinery (₹ 30,000 x 124/366)	10,164
Depreciation on assets acquired by sole-proprietary concern during the year	
New asset has been used by it from 29/11/2023 to 31/03/2024 i.e. 124 days, hence depreciation shall be allowed for 124 days	
- Plant and Machinery (₹ 7,500 x 124/169)	5,503
After conversion	
Depreciation in respect of plant purchased by the successor company is fully allowable in the hands of successor company [50% of 15% on ₹ 50,000].	3,750
Total depreciation	**32,969**

Carry forward & Set off of losses on conversion of proprietary concern or partnership firm into company [Sec. 72A(6)]

Condition: Where -

- a firm is succeeded by a company fulfilling the conditions laid down in sec. 47(xiii); or
- a proprietary concern is succeeded by a company fulfilling conditions laid down in sec. 47(xiv).

Tax Treatment: The accumulated loss and unabsorbed depreciation of the predecessor firm or the proprietary concern, as the case may be, shall be deemed to be the loss or allowance for depreciation of the successor company for the purpose of previous year in which reorganisation of business was effected.

Taxpoint: Accumulated loss of such firm or concern can be carried forward for further 8 years.

Effect of non compliance of conditions given u/s 47(xiii) and (xiv)

If any of the conditions laid down in the sec. 47(xiii) or (xiv) are not complied with, the set off of loss or allowance of depreciation made in any previous year by the successor company shall be deemed to be the income of the company and chargeable to tax in the year in which such conditions are violated.

Conversion of Private Limited Company/ Unlisted Public Company into LLP

5.6

Transaction not regarded as transfer for the purpose of capital gain [Sec. 47(xiiib)]

Any transfer of -

a. a capital asset or intangible asset by a private company or unlisted public company[1] (hereafter referred to as the company) to a limited liability partnership (LLP); or

b. a share(s) held in the company by a shareholder as a result of conversion[2] of the company into a limited liability partnership (LLP)

shall not regarded as a transfer, if following conditions are satisfied:

i. All the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the LLP;

ii. All the shareholders of the company immediately before the conversion become the partners of the LLP and their capital contribution and profit sharing ratio in the LLP are in the same proportion as their shareholding in the company on the date of conversion;

iii. The shareholders of the company do not receive any consideration or benefit other than by way of share in profit and capital contribution in the LLP;

iv. The aggregate of the profit sharing ratio of the shareholders of the company in the LLP shall not be less than 50% at any time during the period of 5 years from the date of conversion;

v. The total sales, turnover or gross receipts in business of the company in any of the 3 previous years preceding the previous year in which the conversion takes place does not exceed ₹ 60 lakh;

vi. The total value of the assets as appearing in the books of account of the company in any of the 3 previous years preceding the previous year in which the conversion takes place does not exceed ₹ 5 crore; and

vii. No amount is paid (directly or indirectly) to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of 3 years from the date of conversion.

Withdrawal of exemption u/s 47(xiiib) [Sec. 47A(4)]

On violation of aforesaid conditions, exemption earlier allowed to the company or shareholder shall be withdrawn and amount of profits or gains arising from the transfer of such capital asset or intangible asset or share(s) not charged earlier shall be deemed to be the profits and gains chargeable to tax of the successor LLP or the shareholder (of predecessor company) for the previous year in which the requirements of sec. 47(xiiib) are violated.

[1] Private company or unlisted public company as per provisions of the Limited Liability Partnership Act, 2008

[2] Such conversion should be in accordance with the provisions of sec. 56 or 57 of the Limited Liability Partnership Act, 2008

Taxpoint

Withdrawal of exemption	The benefits availed shall be treated as deemed income
Year of taxability	The year in which condition u/s 47(xiiib) are violated.
Who will be liable to tax	For exemption available to the company: Successor LLP For exemption available to the shareholder: Such shareholder
Benefit of indexation	Available up to the year when succession took place.
Cost of acquisition of transferred asset in hands of the LLP	If conditions u/s 47(xiiib) are satisfied: Cost of asset in hands of the company If conditions u/s 47(xiiib) are not satisfied: Value at which such asset were transferred to the LLP at the time of conversion
Period of holding in hands of the LLP	In any circumstances, period of holding starts afresh. In other words, holding period of the previous owner cannot be considered.

Illustration 8.

Balance sheet of Handoo & Handoo (P) Ltd. as on 1/04/2023

Liabilities	Amount	Assets	Amount
Equity Share capital of ₹ 10 each	10,00,000	Land (acquired on 17/05/2007)	10,00,000
Reserves	30,00,000	(Market value ₹ 50,00,000)	
		Building (WDV as per IT Act)	13,00,000
		(Market value ₹ 30,00,000)	
		Machinery (WDV as per IT Act)	6,00,000
		(Market value ₹ 10,00,000)	
		Investments (acquired on 18/08/2008)	4,00,000
		(Market value ₹ 12,00,000)	
		Current Assets (Realizable)	7,00,000
	40,00,000		**40,00,000**

Additional information

a. The company converts itself into limited liability partnership (LLP) [as per conditions mentioned u/s 47(xiiib)] on the date of balance sheet.

b. All assets and liabilities of the company was transferred to the LLP. Further, it was also agreed that assets shall be transferred to the LLP at market value.

c. Total number of shareholders in the company: 4 (each holding 25% of equity shares capital and acquired at face value on 01-04-2001)

d. On 10-12-2023, the LLP has transferred land to Mr. Animesh for a consideration of ₹ 63,00,000.

Discuss tax treatment in hands of company, shareholder and LLP.

Solution:

Computation of capital gain for the A.Y. 2024-25 in the hands of Handoo & Handoo (P) Ltd.

Particulars	Land	Building	Machinery	Investment
Full value of consideration	50,00,000	30,00,000	10,00,000	12,00,000
Less: Indexed Cost of Acquisition				
[₹ 10,00,000 x 348 / 129]	26,97,674	-	-	-
[₹ 4,00,000 x 348 / 137]	-	-	-	10,16,058
Less: Cost of Acquisition	-	13,00,000	6,00,000	-
Long Term Capital Gain	23,02,326	-	-	1,83,942
Short Term Capital Gain	-	17,00,000	4,00,000	-

Note: Entire capital gain is exempt in hands of Handoo & Handoo (P) Ltd., if such conversion fulfills all the conditions given in sec.47(xiiib). However, if such conditions are not fulfilled at the time of conversion, then entire capital gain would be taxable in hands of the company. Further, if later on, such conditions are violated, then such capital gain shall be taxable in hands of the **Limited Liability Partnership in the year of such violation**.

Statement showing consideration received by a shareholder of the company

Land	₹ 50,00,000
Building	₹ 30,00,000
Machinery	₹ 10,00,000
Investment	₹ 12,00,000
Current Asset	₹ 7,00,000
Total worth available for 1,00,000 shares	₹ 1,09,00,000
To be received by each shareholder (₹ 1,09,00,000 x 25%)	₹ 27,25,000
- Received as Dividend [(₹ 30,00,000 x 25%]	₹ 7,50,000
- Received against shares	₹ 19,75,000

Computation of capital gain in hands of each Shareholder

Particulars	Amount
Full value of consideration	19,75,000
Less: Indexed Cost of Acquisition [(₹ 10,00,000 x 25%) x 348 / 100]	8,70,000
Long Term Capital Gain	**11,05,000**

Note: Entire capital gain is exempt in hands of shareholder, if such conversion fulfills all the conditions given in sec.47(xiiib). However, if such conditions are not fulfilled at the time of conversion, then entire capital gain would be taxable in hands of the shareholder. Further, if later on, such conditions are **violated**, then such capital gain shall be taxable in hands of the **shareholder in the year of such violation**. Further, dividend is separately taxable in hands of respective shareholder.

Computation of capital gain in hands of LLP (Sale of land)

Particulars	Amount
Full value of consideration	63,00,000
Less: Cost of Acquisition	10,00,000
Short Term Capital Gain	**53,00,000**

Allocation of depreciation in the year of conversion

Deduction for depreciation shall be apportioned between the company and the LLP in the ratio of the number of days for which the assets were used by them.

Carry forward & Set off of losses on conversion into Limited Liability Partnership [Sec. 72A(6A)]

Condition: Where a private company or unlisted public company is succeeded by a limited liability partnership fulfilling the conditions laid down in the proviso to sec.47(xiiib).

Tax Treatment: The accumulated loss and unabsorbed depreciation of the predecessor concern shall be deemed to be the loss or allowance for depreciation of the successor firm for the purpose of previous year in which reorganisation of business was effected.

Taxpoint: Accumulated loss of such firm or concern can be carried forward for further 8 years.

Effect of non compliance of conditions given u/s 47(xiiib)

If any of the conditions laid down in the sec. 47(xiiib) are not complied with, the set off of loss or allowance of depreciation made in any previous year by the successor firm shall be deemed to be the income of the firm and chargeable to tax in the year in which such conditions are violated.

Capital Gain on buy back of own securities [Sec. 46A]

Buy back of specified securities (other than shares) is a transfer for its holder and shall be treated as under:

Sale consideration	Amount received by a securityholder from the company.
Cost of acquisition/Cost of improvement	As usual
Taxable	In the year when such securities are purchased by the company.

Taxpoint*:* In case of buy back of shares, any income (or capital gain) in hands of shareholder is exempt u/s 10(34A). However, company (listed or unlisted) itself is liable to pay additional tax @ 20% (+SC + Cess) u/s 115QA.

Succession to business otherwise than on death [Sec. 170]

- Where a person carrying on any business or profession (such person hereinafter in this section being referred to as the predecessor) has been succeeded therein by any other person (hereinafter in this section referred to as the successor) who continues to carry on that business or profession,—
  a. the predecessor shall be assessed in respect of the income of the previous year in which the succession took place up to the date of succession;
  b. the successor shall be assessed in respect of the income of the previous year after the date of succession.
- However, when the predecessor cannot be found, the assessment of the income of the previous year in which the succession took place up to the date of succession and of the previous year preceding that year shall be made on the successor
- Further, where there is succession, the assessment or reassessment or any other proceedings, made or initiated on the predecessor during the course of pendency of such succession, shall be deemed to have been made or initiated on the successor
  - "Pendency" means the period commencing from the date of filing of application for such succession of business before the High Court or tribunal or the date of admission of an application for corporate insolvency resolution by the Adjudicating Authority u/s 5(1) of the Insolvency and Bankruptcy Code,

2016 and ending with the date on which the order of such High Court or tribunal or such Adjudicating Authority, as the case may be, is received by the Principal Commissioner or the Commissioner.

- When any sum payable under this section in respect of the income of such business or profession for the previous year in which the succession took place up to the date of succession or for the previous year preceding that year, assessed on the predecessor, cannot be recovered from him, the Assessing Officer shall record a finding to that effect and the sum payable by the predecessor shall thereafter be payable by and recoverable from the successor, and the successor shall be entitled to recover from the predecessor any sum so paid.
- Where any business or profession carried on by a Hindu undivided family is succeeded to, and simultaneously with the succession or after the succession there has been a partition of the joint family property between the members or groups of members, the tax due in respect of the income of the business or profession succeeded to, up to the date of succession, shall be assessed and recovered in the manner provided in section 171, but without prejudice to the provisions of this section.

Effect of order of tribunal or court in respect of business reorganization [Sec. 170A]

Filing of Modified Return

In a case of business reorganisation, where prior to the date of order of a High Court or tribunal or an Adjudicating Authority as defined in sec. 5(1) of the Insolvency and Bankruptcy Code, 2016 (hereinafter referred to as order in respect of business reorganisation), as the case may be, any return of income has been furnished by an entity to which such order applies u/s 139 for any assessment year relevant to the previous year to which such order applies, the successor shall furnish, within a period of 6 months from the end of the month in which the order was issued, a modified return in such form (ITR-A) and manner, as may be prescribed, in accordance with and limited to the said order.

Taxpoint

- Where the assessment or reassessment proceedings for an assessment year relevant to a previous year to which the order in respect of the business reorganisation applies,—
  a. have been completed on the date of furnishing of the modified return, the Assessing Officer shall pass an order modifying the total income of the relevant assessment year determined in such assessment or reassessment, in accordance with such order and taking into account the modified return so furnished;
  b. are pending on the date of furnishing of the modified return, the Assessing Officer shall pass an order assessing or reassessing the total income of the relevant assessment year in accordance with the order of the business reorganisation and taking into account the modified return so furnished.
- Save as otherwise provided in this section, in an assessment or reassessment made in respect of an assessment year, all other provisions of this Act shall apply and the tax shall be chargeable at the rate or rates as applicable to such assessment year.
- Business reorganisation means the reorganisation of business involving the amalgamation or demerger or merger of business of one or more persons.
- Successor means all resulting companies in a business reorganisation, whether or not the company was in existence prior to such business reorganisation.

Illustration 9.

Smile Ltd. is a wholly-owned subsidiary company of Happy Ltd., an Indian company. Smile Ltd. owns Plant-A and Plant-B (depreciation rate 40%, depreciated value of the block ₹ 3,00,000 on 1st April, 2023). Plant-B was purchased and put to use on 10th November, 2021 (cost being ₹ 70,000). Plant-B is transferred by Smile Ltd. to

Happy Ltd. on 14th December, 2023 for ₹ 20,000. It is put to use by Happy Ltd. on the same day. Happy Ltd. owns Plant-C on 1st April, 2023 (depreciation rate 40%, depreciated value ₹ 60,000). Find out the amount of depreciation in the hands of Smile Ltd. and Happy Ltd. for the assessment year 2024-25.

Solution:

Depreciation in the hands of Smile Ltd. for the assessment year 2024-25

Particulars	Amount (₹)
Depreciated value of the Plant A and B on 1st April, 2023	3,00,000
Less: Plant B transferred to Happy Ltd	20,000
WDV as on 31st March, 2024	2,80,000
Depreciation for the block P.Y.2023-24	1,12,000
WDV at the end of the year	**1,38,000**

Depreciation in the hands of Happy Ltd. for the assessment year 2024-25

Particulars	Amount (₹)
Depreciated value of the block on 1st April, 2023	60,000
Add: Actual Cost of Plant B acquired from Smile Ltd (See Note)	33,600
WDV as on 31st March, 2024	93,600
Depreciation on transferred asset [₹ 33,600* ½ * 40%]	6,720
Other Asset @ 40% of ₹ 60,000	24,000
Total Depreciation	**30,720**

Note: Actual Cost of Plant B in the hands of Happy Ltd.

Particulars	Amount (₹)
Actual Cost of Plant B in the hands of Smile Ltd on Nov 10, 2021	70,000
Less: Depreciation for P.Y 2021-22 (1/2 of 40% of ₹ 70,000)	14000
Balance on April 1, 2022	56,000
Less: Depreciation for the P.Y.2022-23	22,400
Balance on April 1, 2023	**33,600**

Solved Case:

Laxmi Ltd transferred its Unit X to Amin Ltd. by way of slump sale on 31st December, 2023. The summarized balance sheet of Laxmi Ltd. as on that date is given below:

Liabilities	₹ in lakhs	Assets	₹ in lakhs
Share capital-paid up	2,000	Fixed Assets:	
Reserves and Surplus	950	Unit X	700
Liabilities:		Unit Y	900

Liabilities	₹ in lakhs	Assets	₹ in lakhs
Unit X	400	Unit Z	1,200
Unit Y	600	Other Assets:	
Unit Z	1,050	Unit X	650
		Unit Y	750
		Unit Z	800
	5,000		**5,000**

From the information given below compute the capital gain arising from slump sale of Unit X:

i. Cost inflation index for the financial year 2007-08 is 129 being the year in which the Unit X was established. The cost inflation index for the financial year 2023-24 is 348.

ii. The lump sum consideration received for transfer of Unit X is ₹ 1,100 lakhs.

iii. The fixed assets of Unit X includes a vacant land which was purchased in the financial year 2007-08 for ₹ 50 lakhs and it was revalued at ₹ 100 lakhs in the year 2023-24.

iv. Other fixed assets reflected in the balance sheet ₹ 600 (₹ 700 lakhs less value of land) represents WDV of the assets as per books of account. The WDV of these assets under the Income-tax Act is ₹ 200 lakhs

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be the networth of unit X?
2. What will be the nature of gain (loss) on such slump sale?
3. What will be the taxable income on such slump sale?

Solution:

Computation of Net worth of Unit X

Particulars	₹ in lakhs
Book value of non-depreciable asset	
Land - ignoring the revaluation amount	50
Other assets	650
Depreciable assets - as per WDV	200
	900
Less: Liabilities of Unit X	300
Net worth of Unit X	**600**

Computation of Capital gain on slump sale of Unit X

Particulars	₹ in lakhs
Sale consideration	1,100
Less: Net worth	600
Long-term capital gain arising on slump sale as the unit is operational since 2007	**500**

Exercise

Multiple Choice Questions

1. In case of amalgamation, eligible loss of amalgamating company shall be available to the amalgamated company for:
   a) Remaining tenure
   b) Such loss shall be treated as loss of the previous year in which amalgamation took place
   c) 5 years
   d) 3 years
2. In the year restructuring, depreciation shall be:
   a) available to the successor company fully
   b) apportioned between successor and predecessor on the basis of number of days
   c) available to the predecessor company fully
   d) None of the above

[Answer: 1 – B; 2 – B]

Short Essay Type Questions

1. Define amalgamation.
2. Analyse the effect of amalgamation on the shareholder of the amalgamating company.
3. Discuss the tax treatment in case of slump sale.

Comprehensive Numerical Problems

M/s. R. M/s. RST Co. a sole proprietary concern, was converted into a company w,e,f. 01-09-2023. Before the conversion, the sole proprietary concern had a block of Plant & Machinery (15%), whose WDV as on 1-4-2023 was ₹ 6,00,000. On 1st April itself, a new plant of the same block was purchased for ₹ 2,40,000. After the conversion, the company has purchased the same type of plant on 1-1-2024 for ₹ 3,20,000. Compute the depreciation that would be allocated between the concern & the company.

[Ans: ₹ 52,672 and ₹ 97,328]

Unsolved Case:

1. Padmaja Textiles Ltd., (PTL) has two separate divisions J and K. Division K was stated on 14-05-2013. The summarized financial position of the company as on 1st October, 2023 was as under:

	(₹ in lakhs)
Share capital	1,200
Reserves and surplus	500
Loan creditors:	
Division J	400

	(₹ in lakhs)
Division K	300
Total	**2,400**
Represented by	
Fixed assets:	
Division J	800
Division K	
Goodwill	30
Vacant Land (Purchased on 02.03.2015)	170
Plant and Machinery (WDV)	400
Current assets:	
Division J	550
Division K	450
Total	**2,400**

On 01.10.2023, Division K was acquired by VK Textile Pvt. Ltd., in a slump sale, the entire sale consideration of ₹ 310 lakhs being paid through RTGS.

The following additional information are available relating to the fixed assets of Division K:

i. All the plant and machinery were acquired 11 months back.

ii. The WDV of the plant and machinery of division K as per the Income-tax Act, 1961 was ₹ 350 lakhs.

iii. Apart from these, there are plant used in scientific research for which deduction had been availed u/s 35AD in the assessment year 2019-20. The fair market value of these items of plant is ₹ 12 lakhs.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be the networth of division K

   a. ₹ 6,80,000

   b. ₹ 7,00,000

   c. ₹ 10,00,000

   d. None of the above

2. What will be the nature of gain (loss) on such slump sale?

   a. Long term capital gain (loss)

   b. Short term capital gain (loss)

   c. Business profit (loss)

   d. None of the above

3. What will be the taxable income on such slump sale?

a. (₹ 3,90,000)

b. ₹ 3,90,000

c. (₹ 7,89,456)

d. None of the above

2. ABC Ltd. was amalgamated with XYZ Ltd. on 01.04.2023. All the conditions of Section 2(1B) were satisfied and amalgamation is within the meaning of Section 72A of Income-tax Act. ABC Ltd. has the following carried forward losses as assessed till the Assessment Year 2023-24

Particulars	₹ (in lakhs)
Speculative loss	4
Unabsorbed depreciation	18
Unabsorbed expenditure of capital nature on scientific research	2
Business loss (Non speculative)	120

XYZ Ltd. has computed a profit of ₹ 140 lakhs for the financial year 2023-24 before setting off eligible losses of ABC Ltd. but after providing depreciation at 15% per annum on ₹ 150 lakhs, being the consideration at which plant and machinery were transferred to XYZ Ltd. The written down value before depreciation as per income tax record of ABC Ltd. as on 31st March, 2023 was ₹ 100 lakhs. Above profit of XYZ Ltd. includes speculative profit of ₹ 10 lakhs.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. State the amount of addition required to be made on account of depreciation (excluding unabsorbed depreciation) while computing income of XYZ Ltd.

a. ₹ 9.75 lakhs

b. ₹ 12.75 crore

c. Nil

d. None of the above

2. What will be total income of XYZ Ltd?

a. ₹ 9.75 lakhs

b. ₹ 12.75 lakhs

c. ₹ 19.75 lakhs

d. None of the above

3. Kite & Co. (firm) had sold all its assets and liabilities on 31.03.2024 to ABC Co. (P) Ltd. for a lump sum consideration of ₹ 500 lakhs.

The Balance Sheet of Kite & Co. as on 31.03.2024 is as below:

Liabilities	₹ in lakhs	Assets	₹ in lakhs	
Capital	1,500	Fixed Assets:		
Unsecured loans	100	Plant & Machinery at WDV	300	
Bank borrowing	700	Land (At revalued figure)	1,200	1,500
Sundry Creditors	200	Current Assets:		
		Sundry Debtors	500	
		Cash & Bank balance	50	
		Loans & Advances	340	
		Closing stock	110	1,000
	2,500			**2,500**

Additional Information:

(1) The land was acquired in March, 2006 for ₹ 200 lakhs.

(2) WDV of plant & machinery under section 43(6) was ₹ 250 lakhs.

(3) Cost inflation index for the financial year 2005-06 was 117 and for 2023-24 is 348.

(4) Stock is overvalued by 10%.

(5) Loans and advances include ₹ 150 lakhs due from ABC Co. (P) Ltd.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be networth of the concern, if such transfer is treated as slump sale

    a. ₹ 440 lakhs

    b. ₹ 290 lakhs

    c. ₹ 490 lakhs

    d. None of the above

2. What will be the nature of such gain?

    a. Long term capital gain

    b. Short term capital gain

    c. Profits and Gains of Business or Profession

    d. None of the above

3. What will be tax liability?

    a. ₹ 12.48 lakhs

    b. ₹ 43.68 lakhs

c. ₹ 18.72 lakhs

d. None of the above

4. Company X is proposed to be merged with company Y. The following are the particulars of the former company:

Unabsorbed depreciation	₹ 50,00,000
Brought forward business loss (non-speculative)	₹ 80,00,000
Brought forward business loss (speculative)	₹ 10,00,000

On the basis of above information, answer the following

1. State the amount of unabsorbed depreciation and brought forward losses available to the company Y, If the merger is not amalgamation within the meaning of sec. 2(1B)

   a. Nothing shall be available

   b. Unabsorbed depreciation and brough forward non-speculative business loss will be available, however brough forward speculative business loss shall not be available

   c. Unabsorbed depreciation shall be available, however, brough forward non-speculative business loss and brough forward speculative business loss shall not be available

   d. Only brough forward speculative business loss shall be available

2. State the amount of unabsorbed depreciation and brought forward losses available to the company Y, If the merger is an amalgamation within the meaning of sec. 2(1B) but it does not fulfill the conditions given u/s 72A

   a. Nothing shall be available

   b. Unabsorbed depreciation and brough forward non-speculative business loss will be available, however brough forward speculative business loss shall not be available

   c. Unabsorbed depreciation shall be available, however, brough forward non-speculative business loss and brough forward speculative business loss shall not be available

   d. Only brough forward speculative business loss shall be available

3. State the amount of unabsorbed depreciation and brought forward losses available to the company Y, If the merger is an amalgamation within the meaning of sec. 2(1B) and also fulfill the conditions given u/s 72A

   a. Nothing shall be available

   b. Unabsorbed depreciation and brough forward non-speculative business loss will be available, however brough forward speculative business loss shall not be available

c. Unabsorbed depreciation shall be available, however, brough forward non-speculative business loss and brough forward speculative business loss shall not be available

d. Only brough forward speculative business loss shall be available

Reference

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Different Aspects of Tax Planning 6

This Module includes:

Different Aspects of Tax Planning

SLOB Mapped against the Module:

To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify and evalute the various managerial options
- Analyse and interpret the cost and benefit of such options
- Apply the skill in ascertaining best of available options

Introduction

6

"How can I reduce my tax liability?" is the question that goes through every taxpayer's mind. Tax liability can be reduced through proper tax planning. The obvious benefit of tax planning is to reduce tax liabilities, which by extension means the individual or the company retaining more money for their own needs. Businesses reducing their tax liability through tax planning can provide better returns to their investors and better wages to their employees. It can also spend the money otherwise payable as tax to increase working capital and thereby improve performance efficiency, or spend more on capital expansion and thereby expand market share.

Individuals applying tax planning will have more disposable income in their hands. Very often, tax planning provides individuals with money to spend for their personal benefit or enjoyment, and failure to apply tax planning may lead to such money being paid as tax.

Tax planning also provides an indirect benefit of allowing sound control over finances. It provides a valuable road map to planning finances in the most optimal manner. It allows for streamlining cash outflows, making a planned expenditure, and committing to an informed investment decision.

Reducing tax liability is not always a bad or illegal exercise. There are legitimate ways to reduce taxes through proper tax planning and such methods are always encouraged. But unfortunately, there is also a tendency to reduce taxes through illegal methods. They are not accepted practice and can invite problems. There are three methods that are commonly used by the taxpayers to reduce their tax liabilities:

- Tax Planning;
- Tax Avoidance; and
- Tax Evasion

The Apex Court in *McDowell & Co. Ltd. –vs.- CTO* (1985) has observed that "tax planning may be legitimate provided it is within the framework of the law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honorable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay tax honestly without resorting to subterfuges." In deciding whether a transaction is a genuine or colourable device, it is open for the tax authorities to go behind the transaction and examine the "substance" and not merely the "form".

Doctrine of form and substance in the context of tax planning

The following are certain principles enunciated by the Courts on the question as to whether it is the form or substance of a transaction, which will prevail in income-tax matters:

1. **Form of transaction is to be considered in case of genuine transactions:** It is well settled that when a transaction is arranged in one form known to the law, it will attract tax liability whereas, if it is entered into in another form which is equally lawful, it may not. Therefore, in considering whether a transaction attracts tax or not, the form of the transaction put through is to be considered and not the substance. This rule cannot naturally

apply where the transaction, as put through by the assessee, is not genuine but colourable or is a mere device. For here, the question is not one between 'form' and 'substance' but between appearance and truth. [Motor and General Stores (P) Ltd. -vs.- CIT (1967)]

2. **True legal relation is the crucial element for taxability:** A firm transferred its business assets to a company formed for its purposes. The same business was carried by the company consisting of the erstwhile partners as its shareholders. The Income-tax Officer sought to withdraw the depreciation allowed (the difference between the sale price and written-down value) on machinery. Tribunal and High Court has held that there was a change only in the form of ownership as persons behind both firm and company were the same. The Apex Court has held that it is open for the authorities to pierce the corporate veil and look behind the legal facade at the reality of the transaction. The taxing authority is entitled as well as bound to determine the true legal relation resulting from a transaction. The true legal relation arising from a transaction alone determines the taxability of a receipt arising from the transaction [CIT -vs.- B.M. Kharwar (1969) (SC)]

3. **Substance (i.e. actual nature of expense) is relevant and not the form:** Where the authorities are charged under the Act with the duty of determining the nature or purpose of and payment or receipt on the facts of a case, it is open to them to work at the substance of the matter and the formal aspect may be ignored.

- In the case of expenditure, the mere fact that the payment is made under an agreement does not preclude the department from enquiring into the actual nature of the payment [Swadeshi Cotton Mills Co. Ltd. -vs.- CIT (1967) (SC)].
- In order to determine whether a particular item of expenditure is of revenue or capital nature, the substance and not merely the form should be looked into. [Assam Bengal Cement Co. Ltd. -vs.- CIT (1955) (SC)]. Where the terms of a transaction are embodied in a document, it should not be construed only in its formal or technical aspect. While the words used should be looked at, too much importance should not be attached to the name or label given by the parties and the document should be interpreted so as to accord with the real intention of the parties as appearing from the instrument.
- Certain shares were held in the name of others, but the deceased was the real owner of the shares as was found with reference to evidence. The High Court had held that the shares were not includible in the estate of the deceased as they were not in his name. The Supreme Court pointed out that, in substance, the deceased was the owner though only beneficially and upheld the inclusion for estate duty purposes [CED -vs.- Aloke Mitra (1980)]

Formation of Tax Laws

Article 265 of the Constitution of India states that no tax shall be levied or collected except by authority. In Murthy Match Works case, it is stated that:

"It is well established that the modern State, in exercising its sovereign power of taxation, has to deal with complex factors relating to the objects to be taxed, the quantum to be levied, the conditions subject to which the levy has to be made, the social and economic policies which the tax is designed to subserve, and what not."

Though wide latitude is given to the legislature in the matter of levy of taxes, what is needed, firstly, is that the tax statute should be constitutionally valid to pass the muster of Article 14 of the Constitution of India.

Secondly, liability of tax depends upon the charging section. No tax is complete nor a charge can raise under a fiscal statutes unless the subject, the object and the quantum of tax are prescribed. In the case of State of Tamil Nadu –vs.- M K Kandaswami, the Apex Court has held that the essence of tax laws depends upon three inter-related and distinct concepts which are:

a. Who is a taxable person;

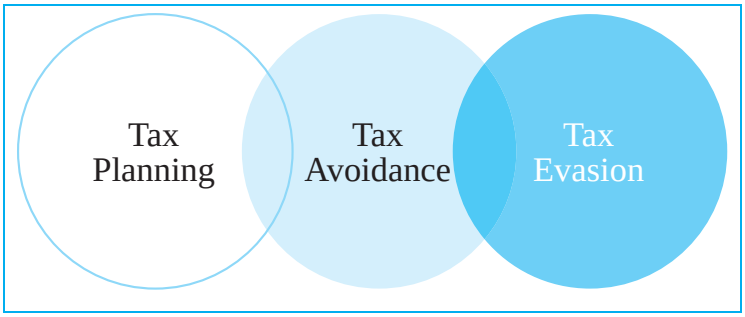
b. What is a taxable event; and

c. What is the subject matter of taxation.

Tax Planning, Tax Evasion and Tax Avoidance

6.1

Tax evasion is the illegal way to reduce tax liability by deliberately suppressing income or sales or by increasing expenses, etc., which results in the reduction of the total income of the assessee. Dishonest taxpayers try to reduce their taxes by concealing income, inflation of expenses, submitting misleading information, falsification of accounts, and willful violation of the provisions of the Income-tax Act. Such unethical practices often create problems for the tax evaders. Tax department not only imposes huge penalties but also initiate prosecution in such cases. It is illegal, both in script & moral. It is the cancer of modern society and work as a clog in the development of the nation. It is a grave problem in a developing country like ours as it leads to a creation of a 'resource crunch' for developmental activities of the State.



Tax avoidance is an exercise by which the assessee legally takes advantage, with malafide motive, of loopholes in the Act. Tax avoidance is minimizing the incidence of tax by adjusting the affairs in such a manner that although it is within the four corners of the laws, it is done with the purpose to defraud the revenue. It is a practice of dodging or bending the law without breaking it. It is a way to reduce tax liability by applying the script of law only. E.g. if A gives gift to his wife, the income from the asset gifted will be clubbed in the hand of A. But to avoid this clubbing provision "A" decides to give gift to B's wife and B reciprocates it by giving gift to A's wife. This is not tax planning but tax avoidance. Most of the amendments are aimed to curb such loopholes.

The Direct Taxes Enquiry Committee (Wanchoo Committee) has tried to draw a distinction between the two items in the following words.

"The distinction between 'evasion' and 'avoidance', therefore, is largely dependent on the difference in methods of escape resorted to. Some are instances of merely availing, strictly in accordance with law, the tax exemptions or tax privileges offered by the government. Others are maneuvers involving an element of deceit, misrepresentation of facts, falsification of accounting calculations or downright fraud. The first represents what is truly tax planning, the latter tax evasion. However, between these two extremes, there lies a vast domain for selecting a variety of methods which, though technically satisfying the requirements of law, in fact circumvent it with a view to eliminate or reduce tax burden. It is these methods which constitute "tax avoidance".

The Royal Commission on Taxation for Canada has explained the concept of tax avoidance as under:

"Tax Avoidance" will be used to describe every attempt by legal means to prevent or reduce tax liability which would otherwise be incurred, by taking advantage of some provisions or lack of provisions of law. It excludes fraud, concealment or other illegal measures.

The line of demarcation between tax avoidance and tax planning is very thin and blurred. There are two thoughts about tax avoidance –

a) As per first thought it is legal. Such thought is also supported by various judgments of the Supreme Court, some of them are as follows -

Helvering vs. Greggory (1934)

"Anyone may so arrange his affairs that his taxes shall be as low as possible. He is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes."

IRC vs. Duke of Westminster (1936)

"Taxpayer is entitled to so arrange his affairs that the tax under the appropriate Act is less than what otherwise it could be."

Inland Revenue Commissioners vs. Fishers Executors (1958)

"The highest in authority, have always recognized that the subject is entitled so to arrange his affairs as not to attract taxes imposed by the Crown, so far he can do so within the law, and that he may legitimately claim the advantage of any express terms or any omissions that he can find in his favour in taxing Act. In doing so, he neither comes under liability, nor incurs blame."

CIT vs. Raman & Co. (1968)

"Avoidance of tax liability by so arranging commercial affairs that the charge of tax is distributed, is not prohibited. A taxpayer may resort to a device to divert the income before it accrues or arises to him. Effectiveness of the device depends not upon considerations of morality, but on the operation of the Income-tax Act."

Smt. C. Kamala vs. CIT (1978)

"It is quite possible that when a transaction is entered into in one form known to law, the amount received under that transaction may attract liability under the Act and if it is entered into in another form which is equally lawful, it may not attract such tax liability. But when the assessee has adopted the latter one, it would not be open to the court to hold him liable for tax."

CWT vs. Arvind Narotham (1988)

"It is true that tax avoidance in an underdeveloped or developing economy should not be encouraged on practical as well as ideological grounds. One would wish….. that one could get the enthusiasm ….. that taxes are the price of civilization and one would like to pay that price to buy civilization. But the question which many ordinary taxpayers very often, in a country of shortages with ostentatious consumption and deprivation for the large masses, ask is, does he with taxes buy civilization or does he facilitate the waste and ostentation of the few. Unless ostentation and waste in Government spending are avoided or eschewed, no amount of moral sermons would change people's attitude to tax avoidance."

b) As per second thought it is not a legal way to reduce tax burden and it should be prohibited.

McDowell & Co. Ltd. vs Commercial Tax Officer (1985)

Supreme Court observed - "we think time has come for us to depart from Westminster principle….tax planning may be legitimate provided it is within the framework of law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honorable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the honestly without resorting to subterfuges."

CIT vs B.M. Kharwar (1969)

Supreme Court held – "the taxing authority is entitled and is indeed bound to determine the true legal relation resulting from a transaction. If the parties have chosen to conceal by a device the legal relation, it is open to the taxing authorities to unravel the device and to determine the true character of relationship. But the legal effect of a transaction cannot be displaced by probing into substance of the transaction."

Justice O. Chinnappa Reddy of Supreme Court has, while briefing the evil consequences of tax avoidance in Mc.Dowell & Co. Ltd. -vs.- CTO, observed that one such evil consequence is the ethics (or the lack of it) of transferring the burden of tax liability to the shoulders of the guideless, good citizens from those of artful dodgers. As regards the ethics of taxation, he observed:

"We now live in a welfare State whose financial needs, if backed by law, have to be respected and met. We must recognize that there is behind taxation laws as much moral sanction as behind any other welfare legislation and it is a pretence to say that avoidance of taxation is not unethical and that it stands on no less moral plane than honest payment of taxation".

A similar observation was made by Lord Chancellor in Latilla vs. Inland Revenue Commissioner (1943) 011 ITR (E.C) 0078:

"There is, of course no doubt that they are within their legal rights but that is no reason why their efforts, or those of the professional gentlemen who assist them in the matter, should be regarded as a commendable exercise of ingenuity or as a discharge of the duties of the good citizenship. On the contrary, one result of such methods, if they succeed, is of course to increase pro tanto the load of tax on the shoulder of the body of good citizens who do not desire or do not know how to adopt these maneuvers."

Tax Planning

6.2

Tax law reflects the complexity of modern life and the multitude of choices and options available to all taxpayers when legitimately seeking to structure their affairs. This necessary offer of options within tax legislation creates the opportunity for choice on the part of the tax payer and means that determining the right amount of tax (but no more) that they seek to pay does necessarily requires the exercise of judgement on occasion. So long as the exercise of that judgement seeks to ensure that the taxpayer makes choices that exercise options clearly allowed by law and that they do not exploit unintended loopholes created between laws then that process of a taxpayer choosing how to structure their affairs is the process of tax planning, which is a legitimate, proper and socially acceptable act.

Thus, tax planning is a systematic evaluation of finances and investments, to reduce the tax burden in a legitimate way. It involves understanding the tax implications of various cash inflows and outflows such as salary composition, property income, home loan, investments, sale or purchase of assets, gifts and interest-bearing deposits, to draw up an appropriate investment strategy that allows realization of financial goals while at the same time reducing tax liability to minimum.

It is a way to reduce tax liability by taking full advantages provided by the Act through various exemptions, deductions, rebates & relief. In other words, it is a way to reduce tax liability by applying script & moral of law. The two basic approaches of tax planning are:

1. **Reducing taxable income:** As a rule, higher the income or profit, higher the tax liability on such income or profit. Gross income is total profits or income from all sources, and taxable income is such gross income less adjustments allowable under various tax laws and other provisions. Such adjustments bases itself on the nature of income and expenditure. Opting for the income or expenditure heads that allows maximum set-offs from the gross income reduces taxable income, and by extension tax liability.

2. **Deferring payment of taxes to the extent possible:** An underestimated dimension of tax planning is timing investments and financial transactions so that the tax liability for such transactions arises at the farthest possible time. While this does not reduce the amount of tax payable, it delays tax outgo, thereby effectively providing interest-free cash on hand. Individuals may not need to resort to such a strategy, but delayed pay-out is valuable for small businesses that very often face cash flow difficulties.

   The goal of tax planning is to arrange your financial affairs so as to minimize your taxes. It is the planning so as to attract minimum tax liability or postponement of tax liability for the subsequent period by availing various incentives, concessions, allowance, rebates and relief provided in the Act.

Distinguish between Tax Planning, Tax Evasion, Tax Avoidance and Tax Management

6.3

Difference between tax planning, tax avoidance, tax evasion & tax management

Points of distinction	Tax planning	Tax Avoidance	Tax Evasion	Tax Management
Definition	It is a way to reduce tax liability by taking full advantages provided by the Act through various exemptions, deductions, rebates & relief.	It is an exercise by which the assessee legally takes advantage of the loopholes in the Act.	It is the illegal way to reduce tax liability by deliberately suppressing income or sale or by increasing expenses, etc., which results in reduction of total income of the assessee.	It is a procedure to comply with the provisions of the law.
Feature	Tax planning is a practice to follow the provisions of law within the moral framework.	Tax avoidance is a practice of bending the law without breaking it.	Tax evasion is illegal, both in script & moral.	It is implementation or execution part of taxation department of an organisation.
Object	To reduce tax liability by applying script & moral of law.	To reduce the tax liability to the minimum by applying script of law only	To reduce tax liability by applying unfair means.	To comply with the provisions of laws.
Approach	It is futuristic and positive in nature. The planning is made today to avail benefits in future.	It is futuristic but short term in nature, as loophole of the law will be corrected in future by amendments of the law.	It is concerned with past and applied after the liability of tax has arisen. It is done with negative approach to avail benefits by killing the moral of law.	It is a continuous approach, which is concerned with past (rectification, revisions etc.), present (filing of return, etc.) & future (corrective action).
Benefit	Generally, arises in long run.	Generally, arises in short run.	Generally, benefits do not arise but it causes penalty and prosecution.	Penalty, interest & prosecution can be avoided.
Treatment of Law	It uses benefits of the law.	It uses loopholes in the law.	It overrules the law.	It implements the law.
Practice	It is tax saving.	It is tax hedging.	It is tax concealment.	It is tax administration.
Need	It is desirable	It is avoidable	It is objectionable	It is essential.
Morality	It is moral in nature.	It is immoral in nature	It is illegal.	It is duty.

Objectives of Tax Planning

6.4

Tax planning is an exercise undertaken to minimize tax liability through the best use of all available allowances, deductions, exclusions, exemptions, etc. The objectives of tax planning cannot be regarded as offending any concept of the taxation laws and subjected to reprehension of reducing the inflow of revenue to the Government's coffer, so long as the measures are in conformity with the statue laws and the judicial expositions thereof. The basic objectives of tax planning are:

a. Reduction of Tax liability

Tax law provides multiple choices and options to taxpayers. This necessary offer of options within tax legislation creates the opportunity for choice on the part of the tax payer. However, due to lack of awareness of legal requirements, in many a cases, a taxpayer may suffer heavy taxation. Through proper tax planning and awareness, a tax payer may reduce such heavy tax burden.

b. Minimisation of litigation

In the matter of taxation, the tax payers will try to pay the least tax and on the other hand, the tax administrator will attempt to extract the maximum. This conflict behaviour may results into litigations. However, where proper tax planning is adopted by the tax payer in conformity with the provisions of the taxation laws, the incidence of litigation can be minimised. This saves him from the hardships and inconveniences caused by the unnecessary litigations.

c. Productive investment

A tax payer may reduce heavy tax burden through proper tax planning. Such reduction results into reduction in cash-outflow. In the days of credit squeeze and dear money conditions, even a rupee of tax decently saved may be taken as an interest-free loan from the Government, which perhaps, an assessee need not repay. Such retained cash can be utilised in other productive venture which also provide additional earning to the taxpayer. That means, proper tax planning is a measure of proper utilisation of available resources which in turn maximise the cash-inflow and minimise the tax burden.

d. Healthy growth of economy

The growth of a nation's economy is synonymous with the growth and prosperity of its citizens. In this context, a saving of earnings by legally sanctioned devices fosters the growth of both, because savings by dubious means lead to generation of black money, the evils of which are obvious. Conversely, tax-planning measures are aimed at generating white money having a free flow and generation without reservations for the overall progress of the nation. Tax planning assumes a great significance in this context.

e. Economic stability

Tax planning results in economic stability by way of:

(i) productive investments by the tax payers; and

(ii) harnessing of resources for national projects aimed at general prosperity of the national economy and reaping of benefits even by those not liable to pay tax on their incomes.

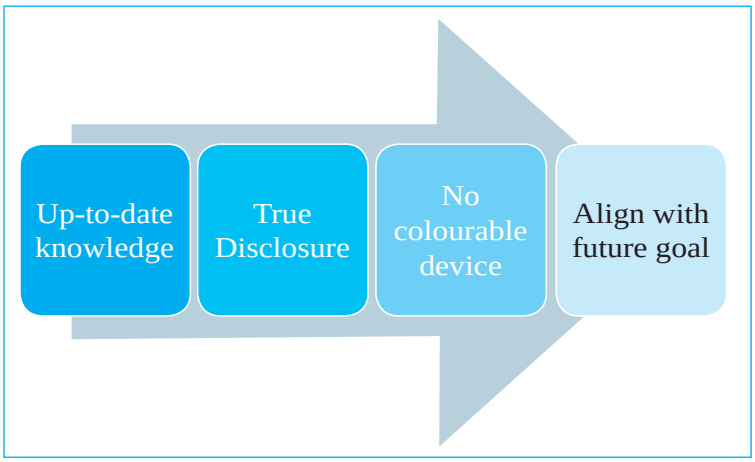
Essentials of Tax Planning

6.5

Fo

Following are the essentials of tax planning:

- Up-to-date Knowledge of tax laws alongwith circulars, notifications, clarifications and Administrative instructions issued by the CBDT.
- Disclosure of full and true material informatio
- Avoid sham transactions or make-believe transactions or colourable devices
- Foresight of future development or changes and enterprise's goal. The planning should be flexible enough to adjust statutory negation.

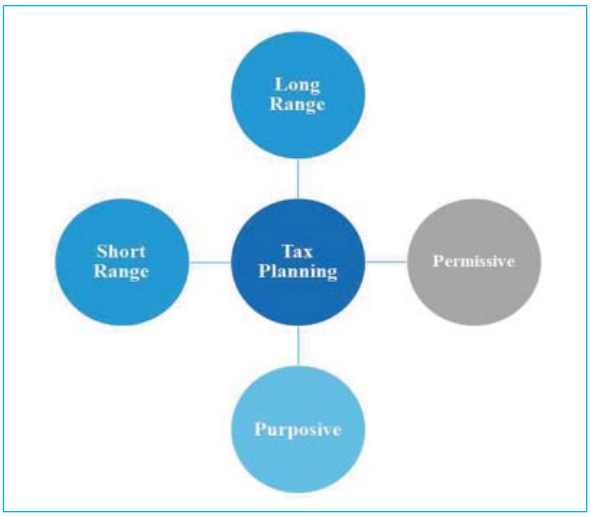


Types of Tax Planning

6.6

The tax planning exercise ranges from devising a model for specific transaction as well as for systematic corporate planning. These are:

(a) Short-range and long-range tax planning: Short-range planning refers to planning to achieve some specific or limited objective of particular fiscal year. E.g., an individual assessee whose income is likely to register unusual growth in particular year as compared to the preceding year, may plan to subscribe to the PPF/NSC's[1] within the prescribed limits in order to enjoy substantive tax relief. By investing in such a way, he is not making permanent commitment but is substantially saving in the tax. Long-range planning on the other hand, involves entering into activities, which may not pay-off immediately. E.g., when an assessee transfers his equity shares to his minor son, he knows that the Income from the shares will be clubbed with his own income. But clubbing would also cease after his son attains majority.



(b) Permissive tax planning: Permissive tax planning is tax planning under the express provisions of tax laws. Tax laws of our country offer many exemptions and incentives.

(c) Purposive tax planning: Purposive tax planning is based on the basis of circumvention of the law. The permissive tax planning has the express sanction of the Statute while the purposive tax planning does not carry such sanction. E.g., If an assessee manages his affairs in such a way that his income is taxable in hands of other person without attracting clubbing provision, such a plan would work in favour of the tax payer because it would increase his disposable resources.

1 If he has opted for old tax regime

Areas of Tax Planning

6.7

Some of the important areas where planning can be attempted in an organised manner are as under:

(a) Form of organisation/ownership pattern;

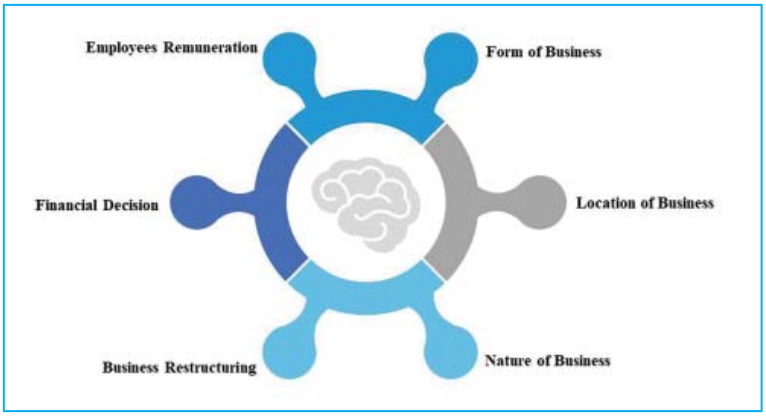
(b) Locational aspects;

(c) Nature of business.

(d) Tax planning in respect of corporate restructuring;

(e) Tax planning in respect of financial management;

(f) Tax planning in respect of employees remunerations;



(g) Tax planning in respect of specific managerial decisions;

(h) Tax planning in respect of Non-Residents

Form of organisation

A snapshot of features of different forms of business:

Particulars	Form of Business		
	Company	Firm or LLP	Sole proprietorship
Tax rates	Company is liable to pay @ 30% (in some cases at lower rate) + surcharge + cess @ 4%. Further, whatever amount of tax is paid by a company is not deemed to have been paid on behalf of the shareholders. Therefore, no rebate is allowed to shareholders.	Firm is liable to pay @ 30% + surcharge + cess @ 4%. Share of profit distributed to the partner is exempt from tax.	Sole proprietor is liable to tax at slab rate.

Particulars	Form of Business		
	Company	Firm or LLP	Sole proprietorship
Remuneration to owner-director	Remuneration to the persons who are managing the affairs of the company and also owning its shares is allowed	Remuneration to the working partners is allowed. However, such remuneration is subject to sec. 40(b)	Remuneration to owner of the business is not an allowable expenditure.
Distribution of income	Distributed income is taxable in hands of the shareholder	Share of profit distributed to the partner is exempt from tax.	NA
Specific business expenditure allowed	Certain expenditure is allowed only in hands of company assessee. E.g., expenditure covered u/s 36(1)(ix) are allowable only in hands of company assessee only.	Apart from sec. 40(b), no other provision contains such restriction.	Expenditure like interest on loan provided to the business by the owner or remuneration to proprietor is not an allowable expenses.
Different assessee	Company is treated as a separate assessee apart from its shareholders	Firm is treated as a separate assessee apart from its partners.	Proprietorship business is not treated as a separate assessee.
Decision making	Any important business matter required to be deal in proper meeting and requires a long procedure. Thus, decision on any important business matter can be delayed	Since partners of the firm meets more frequently, decision on any important business matter cannot be delayed	As owner is the only person to take decisions, thus decision on any important business matter cannot be delayed
Risk taking capacity	Once approved by the governing body, the chance of getting involved in risky activities is comparatively high.	The chance of getting involved in risky activities is very less because every important decision is made with the concurrence of all the partners.	The chance of getting involved in risky activities is depends on the owner's ability to take risk.
Raising of additional capital	Company can raise large capital by way of issuing shares to large number of public[1].	Capital can be raised by introducing new partner or by existing partners.	There is personal limitation is raising capital.
Loan-fund	Since the company has perpetual succession, lender is happy to lent money to company form of business.	Money can be raised by way of borrowings easily, in compared to sole-proprietorship business, because of number of partners and their joint and several liability to pay the debts of the firm, the lenders will be more interested in lending.	There is personal limitation in raising capital.
Limited liability	Shareholder is not liable to pay more than his shares amount.	Partners have unlimited liability, subject to certain case.	Proprietor have unlimited liability.

1 Not in case of private limited company.

Particulars	Form of Business		
	Company	Firm or LLP	Sole proprietorship
Liability of owner	Owners are not liable for act of governing body.	Partners are liable for act of another partner	N.A.
Size of business	In case of public company, there is no such limitation.	Partnership can be formed up to maximum number of 20 partners. Thus, it is not suitable for large scale business.	It is not suitable for large scale business.

Locational Aspects

There are certain locations which are given special tax treatment. Some of these are as under:

a. Unit located in special economic zone is eligible for exemption u/s 10AA for several numbers of years.

b. In respect of certain undertakings in North-Eastern States is eligible for deduction u/s 80-IE.

c. In respect of unit located in SEZ deduction is available u/s 80-LA

Nature of Business

There are certain businesses which are granted special tax treatment. Some of them are as follows:

– Tea Development Account, Coffee Development Account and Rubber Development Account [Section 33AB].

– Site restoration fund [Section 33ABA].

– Specified business eligible for deduction of Capital Expenditure [Section 35AD].

– Special reserve created by a financial corporation under Section 36(1)(viii).

– Special provision for deduction in the case of business for prospecting for mineral oil [Sections 42 and 44BB].

– Special provisions for computing profits and gains of business on presumptive basis [Section 44AD].

– Special provisions in the case of business of plying, hiring or leasing goods carriages [Section 44AE].

– Special provisions in the case of shipping business in the case of non-residents [Section 44B].

– Special provisions in the case of business of operation of aircraft [Section 44BBA].

– Special provisions in the case of certain turnkey power projects [Section 44BBB].

– Special provisions in the case of royalty income of foreign companies [Section 44D].

– Special provisions in case of royalty income of non-residents [Section 44DA].

– Certain income of offshore Banking Units and international Financial Service Centre [Section 80-LA].

– Profit and gains of industrial undertakings or enterprises engaged in infrastructure development, etc.

– Profits and gains from the business of collecting and processing of bio-degradable waste [Section 80JJA].

– Special tax rate under Sections 115A, 115AB, 115AC, 115AD, 115B, 115BBA, 115BAC, 115BB, 115BA, 115D, etc.

Tax Planning relating to Corporate Restructuring

Corporate Restructuring is a process of redesigning one or more aspects of a corporate for achieving certain objectives. The objectives of restructuring may be achieving economies of scale or surviving in an adverse economic climate or restructuring of debt or for any other objectives. Such restructuring can be done through various tools. Some of them are as follow:

- Amalgamation
- Demerger
- Slump sale of business
- Buy back of shares
- Capital Reduction
- Conversion of debentures into shares
- Redemption of preference shares
- Conversion into company
- Conversion of an Indian branch of foreign company into an subsidiary company
- Conversion of company into LLP, etc.

Tax Planning relating to Financial Management Decisions

Fund can be obtained from various sources thus their procurement is always considered as a complex problem by a business organisation. Fund procured from different sources have different characteristics in terms of risk, cost and control. Some of the sources for funds for a business enterprise are:

Equity: The funds raised by the issue of equity shares are the best from the risk point of view for the firm, since there is no question of repayment of equity capital except when the firm is under liquidation. From the tax point of view, dividends are an appropriation of profit, thus the same is not allowed as an expense under the Income Tax Act.

Debentures: Debentures as a source of funds are comparatively cheaper than the shares because of their tax advantage. The interest the company pays on a debenture is tax deductible.

In this regards, following sections are relevant:

- Amortisation of preliminary expenses [Sec. 35D]
- Interest on borrowed capital [Sec. 36(1)(iii)]
- Actual cost of assets [Sec. 43(1)]
- General Deductions [Sec. 37]
- Depreciation [Sec. 32]
- Tax on distribution of profit [Sec. 115-O]

Capital Structure

The optimum capital structure is a mix of equity capital and debt funds. Following should be considered in this regard:

a) Interest on debt fund is allowed as deduction as it is a business expenditure. Therefore, it may increase the rate of return on owner's equity.

b) Dividend on equity fund is not allowed as deduction as it is the appropriation of profit.

c) The cost of raising owner's fund is treated as capital expenditure therefore not allowed as deduction. However, if conditions of sec. 35D is satisfied then such cost can also be amortized.

d) The cost of raising debt fund is treaded as revenue expenditure.

Lease or Buy

When a person needs an asset for his business purposes, he has to decide whether the asset should be purchased or taken on lease. Following should be considered in this regard:

a) Lease rental can be claimed as deduction as revenue expenditure. However, depreciation on leases asset is not allowed.

b) Depreciation on depreciable assets can be claimed as deduction u/s 32.

c) In case, the asset is purchased from the amount taken on loan, interest paid for the period after the asset is first put to use, the deduction on account of interest shall be claimed as revenue expenditure. However, interest paid for the period before the asset is first put to use shall be capitalized.

d) Any gain on transfer of capital asset is subject to capital gain. In this regard, it is to be noted that in case of depreciable asset, asset shall be merged in the respective block of asset.

Tax Planning relating to Employee's Remuneration

The following aspects should be considered:

a. The salary should not be a consolidated one and on the other hand, it should be divided into basic pay and several allowances as some of the allowance may be fully or partially exempt from tax.

b. There should be an option to the employee for commuted pension up to the maximum limit permissible in the Act as it is exempt from tax to certain specific limit

c. There should be a provision for encashment of leave on retirement as it is exempt from tax up to a prescribed limit

d. The employer's contribution to the provident fund should be atleast upto12% of the salary as the same is exempt from tax. However, upper cap should be kept in mind.

e. Perquisites are preferable to fixed allowances as the lower valuation of many perquisites helps in the reduction of tax liability

f. Commission payable should be based on turnover and it must form part of the salary. This will help in reducing the incidence of tax in respect of House Rent Allowance, etc.

g. The component of the salary should be available as deduction while computing business income of the employer.

*These are illustrative aspects

Tax Planning relating to Non Resident

Some of the important aspects, which should be considered:

a. Meaning of non-resident as per sec. 6

b. Scope of income of non-resident – Sec. 5

c. Income deemed to be accrued or arise in India – Sec. 9

d. Various exemptions available u/s 10

e. Presumptive income in case of certain business – Sec. 44B, 44BBA, etc.

f. Deduction in respect of head office expenditure – Sec. 44C

g. Special tax treatment of income covered u/s 115A, 115AB, etc.

h. Method of computation of capital gain in certain cases of non-resident – Sec. 48

i. Special provision relating to non-resident Indians – Sec. 115C to Sec. 115-I

j. Provision of Double Tax Avoidance Agreement

k. Applicability of GAAR

Organisation Tax Planning Cells

6.8

Various organisations have separate tax planning departments to plan their transactions with a view to attracting the least incidence of tax. Organisation of such a cell can be justified on the following grounds:

a. **Complexity and volume of work:** Where the volume of tax work to be handled is large and highly complex, then it is required to appoint a special tax expert along with the required staff.

b. **Separate Documentation:** Documentation is an indispensable ingredient of tax management. An assessee has to keep reliable, complete and updated documentation for all the relevant tax files so that the documentary evidence can be made available at a short notice whenever it is required. In absence thereof, an assessee may lose a case for want of proper documentary evidence. Not only that the company has to maintain proper account books, records, vouchers, bills, correspondence and agreements, etc. as a part of tax management. In the case of new industrial undertaking it is better to keep separate accounts for the same.

c. **Data Collection:** The staff concerned with taxation has to collect and keep on collecting data relating to latest circulars, case laws, rules and provisions, and other government notifications to keep abreast of the current developments.

d. **Integration:** Tax planner should be consulted by all the departments of the company to know the impact of taxation on their decisions. It would be necessary to integrate and properly link all the departments of the company with the tax planning department.

e. **Constant Monitoring:** In order to obtain the intended tax benefits, persons connected with tax management should ensure compliance of all the pre-requisites, like procedures, rules etc. Besides, there should be constant monitoring, so that all the tax obligations are discharged and penal consequences avoided.

f. **Developing Tax effective Alternatives:** Tax laws provide various options for entering into a transaction. A tax planner could guide management in taking important decisions, by considering varieties of alternatives and choices.

g. **Take advantage of variance allowances and deductions:** An expert tax manager has to keep track of the provisions relating to various allowances, deductions, exemptions, and rebates so as to initiate tax planning measures.

Illustration 1.

Naresh, who is neither a director nor has a substantial interest in any company, is offered employment by Freewheel Ltd., Mumbai with the following two alternatives:

Particulars	I	II
Basic pay	66,000	66,000
Bonus	9,000	9,000
Education allowance for 2 children	30,200	-
Education facility for 2 children in school maintained by employer	-	30,200
Sweeper allowance	10,000	-
Sweeper facility	-	10,000
Entertainment allowance	6,000	-
Club facility	-	6,000
Transport allowance for personal use	1,800 pm	-
Free car (1200 cc) facility for performing journey between office to home and vice versa (car owned by employer)	-	12,000
Medical allowance	18,000	-
Medical bills reimbursement facility	-	18,000
Allowance for gas, electricity and water supply	4,500	-
Free gas, electricity and water supply (bills will be in the name of the employer)	-	4,500
Holiday home allowance	8,000	-
Holiday home facility	-	8,000
Lunch allowance	18,000	-
Free lunch (₹ 70 x 200 days + ₹ 80 x 50 days)	-	18,000
Diwali gift allowance	7,500	-
Gift on Diwali	-	7,500
A rent-free unfurnished home – lease rent	14,000	14,000

Which of the two alternatives Naresh should opt for on the assumption that both employer and employee will contribute 10% of salary towards unrecognized provident fund? Interest free loan of ₹ 20,000 will be given to him for purchasing household items. Assume that he has opted for old tax regime

Solution:

As both the options are yielding equivalent facilities, hence the option where tax liability can be minimized is the better choice for the assessee. Accordingly, computation of taxable salary of Naresh under both options are as under

Particulars	Working	Option 1		Option 2	
		Details	Amount	Details	Amount
Basic salary			66,000		66,000
Bonus			9,000		9,000
Allowances					
Children education allowance		30,200			
Less: Exemption u/s 10(14) Rule 2BB	100 x 2 x 12	2,400	27,800		

Particulars	Working	Option 1		Option 2	
		Details	Amount	Details	Amount
Transport allowance		21,600			
Less: Exemption u/s 10(14)		Nil	21,600		
Holiday home allowance			8,000		
Medical allowance			18,000		
Sweeper allowance			10,000		
Entertainment allowance			6,000		
Lunch allowance			18,000		
Gas, electricity & water allowance			4,500		
Diwali gift allowance			7,500		
Perquisites u/s 17(2)					
Rent free accommodation					
(Being minimum of the following):					
Rent paid by employer		14,000		14,000	
10% of salary*		19,640	14,000	7,500	7,500
Car facility for performing journey between office to home and vice versa	Exempted				Nil
Education facility				30,200	
Less: Exempted				24,000	6,200
Interest free loan exempted up to ₹ 20,000			Nil		Nil
Sweeper facility					10,000
Club facility					6,000
Holiday home facility					8,000
Medical facility					18,000
Gift	7,500 – 5,000				2,500
Gas, electricity & water facility					4,500
Free lunch facility	(20x200)+(30x50)				5,500
Gross Taxable Salary			2,10,400		1,43,200
Less: Standard Deduction u/s 16(ia)			50,000		50,000
Taxable Salary			**1,60,400**		**93,200**

* Salary for the purpose of -

Particulars	Rent free accommodation	
	Option 1	Option 2
Basic	66,000	66,000
Bonus	9,000	9,000
Children education allowance	27,800	-
Transport allowance	21,600	-
Holiday home allowance	8,000	-
Medical allowance	18,000	-

Particulars	Rent free accommodation	
	Option 1	Option 2
Sweeper Allowance	10,000	-
Entertainment allowance	6,000	-
Lunch allowance	18,000	-
Gas, electricity & water allowance	4,500	-
Diwali gift allowance	7,500	-
Total	1,96,400	75,000

Note: Contribution to URPF is not taxable.

Conclusion: Option 2 is better.

Illustration 2.

Star Gas Ltd. commenced operations of the business of laying and operating a cross-country natural gas pipeline network for distribution on 1st April, 2023. The company incurred capital expenditure of ₹ 1,490 lakh (including the cost of financial instrument ₹ 2 lakh) during the period January to March, 2023 exclusively for the above business and capitalized the same in its books of account as on 1st April, 2023.

Further, during the financial year 2023-24, it has incurred capital expenditure of ₹ 6,600 lakh (including the cost of land ₹ 1,100 lakh) exclusively for the above business. Compute the amount of deduction u/s 35AD for the A.Y. 2024-25, assuring that the company has fulfilled all the conditions specified in sec. 35AD**.**

Solution:

Computation of the Amount of Deduction under Section 35AD for the Assessment Year 2024-25

Particulars	₹ in lakh
Capital expenditure incurred during the Year (excluding cost of land) [₹ 6,600 lakh – ₹ 1,100 lakh]	5,500
Capital expenditure incurred prior to commencement of business & capitalized (excluding cost of Financial Instrument) [₹ 1,490 lakh – ₹ 2 lakh]	1,488
Total Deduction u/s 35AD	6,988

Illustration 3.

Lucent Ltd. purchased machinery on 1st April, 2023 for ₹ 10 crores by availing loan facility from the bank. The machine was put to use in effective production on 1st February, 2024. The interest on the loan works out to 12% per annum. Advise Lucent Ltd. on the treatment of interest payment made on this loan and depreciation allowable for the previous year 2023-24. You may assume that this is the only machine in its block.

Solution:

Computation of Depreciation

Particulars	Amount (in Crore)	Amount (In Crore)
Block: Plant & Machinery (Rate 15%)		
W.D.V. as on 1/4/2023		Nil
Add: Purchase	10	

Interest on loan upto Jan. 2024 (₹ 10 cr x 12% x 10/12)	1	11
		11
Depreciation [₹ 11 cr. * 15% * ½]		0.825

Interest cost from Feb 2024 shall be allowed as deduction u/s 36(1)(iii).

Illustration 4.

P Ltd. owns two undertakings. Undertaking-A is eligible for deduction u/s 80-IA and Undertaking-B are not eligible for such deduction. The date of commencement of operation in both the undertaking is 14th September, 2023. The profits earned by both the undertaking are as under:

Previous Year	Undertaking-A (₹ in Lakhs)	Undertaking-B (₹ in Lakhs)
2023-24	(–) 6	(–) 4
2024-25	(–) 4	10
2025-26	5	9
2026-27	8	6
2027-28	9	(–) 3

Calculate total income of P Ltd. for last three assessment years.

Solution:

In the given case, the entire loss of the undertaking A has been set-off under Sections 70 & 72 till the A.Y 2026-27

Assessment Year	Unit A	Unit B	GTI	Carried forward losses
2024-25	- 6	- 4	Nil	-10
2025-26	- 4	10	Nil	-4
2026-27	5	9	10	Nil
2027-28	8	6	14	Nil
2028-29	9	- 3	6	Nil

There is no loss brought forward for earlier years for the Assessment Year 2027-28 and subsequent year. However, to compute profit eligible for tax holidays u/s 80-IA, it is assumed that the undertaking is the only unit owned by P. Ltd. Consequently, deduction u/s 80-IA is as under:

Computation of Total Income

Particulars	A.Y. 2026-27	A.Y. 2027-28	A.Y. 2028-29
Profit from Unit A	5	8	9
Add: Profit from Unit B	9	6	-3
Gross Total Income (a)	14	14	6
Less: Deduction u/s 80-IA			
Current year profit of Unit A	5	8	9
Less: Notional B/F loss from earlier years	-10	-5	Nil
Balance	-5	3	9
Deduction U/S 80-IA @ 100% (b)	Nil	3	6 (Restricted to GTI)
Total Income [(a)-(b)]	14	11	Nil

Illustration 5.

Mr. A owned two residential house for his own residential purpose, details of which are as follows –

Particulars	House 1	House 2
Gross Annual value	4,00,000	5,00,000
Municipal tax (paid)	2,000	10,000
Interest on loan taken for construction of house	20,000	25,000

On 1/4/2023, Mr. A gifted ₹ 25,00,000 to her wife. Out of such money, she acquired a house property for her own residential purpose. The new house has a gross municipal value of ₹ 2,50,000. She paid a corporation tax of ₹ 2,000. Compute income from house property of Mr. & Mrs. A. (Assume that Mrs. A does not own any other property). Assume that he has opted for old tax regime

Solution:

Computation of income from house property of Mr. A for the A.Y. 2024-25

Particulars	Amount
Self-occupied house properties	
Net Annual Value	Nil
Less: Deduction u/s	
24(b) Interest on loan [₹ 25,000 + ₹ 20,000]	45,000
	(45,000)
Add: Income of Mrs. A clubbed u/s 64(1)(iv)	Nil
Income from house property	**(45,000)**

Computation of income from house property of Mrs. A for the A.Y. 2024-25

Particulars	Amount
Self-occupied house	
Net Annual Value	Nil
Less: Deduction u/s	
24(b) Interest on loan	Nil
	Nil
Less: Income clubbed u/s 64(1)(iv) with the income of Mr. A	Nil
Income from house property	**Nil**

Illustration 6.

Sure Success Ltd. wants to acquire an asset costing ₹ 1,00,000. It has two options are available, the first one is buying the asset by taking a loan repayable in five installments of ₹ 20,000 each with 14% interest per annum. The second is leasing the asset for which the annual lease rental charge is ₹ 30,000 up to 5 years. The lessor charges 1% as a processing fee in the first year. Assume the internal rate of return to be 10%. The present value factors are:—

Year	1	2	3	4	5
P/V Factor	.909	.826	.751	.683	.621

Assuming that the payments are made at the end of the year, suggest which alternative is better for the company. The rate of depreciation is 15% while tax rate is 33.22%.

Solution:

Cost of Ownership

Year	Instalment	Interest	Depreciation	Tax Benefit	Net Outflow	P/V	Net
	(a)	(b)	(c)	(d) = (b+c)*33.22%	(a+b-d)		
1	20,000	14,000	15,000	9,634	24,366	.909	22,151
2	20,000	11,200	12,750	7,956	23,244	.826	19,210
3	20,000	8,400	10,838	6,391	22,009	.751	16,536
4	20,000	5,600	9,212	4,921	20,679	.683	14,124
5	20,000	2,800	7,830	3,531	19,269	.621	11,965
Total							**83,985**

It is assumed that salvage value is Nil after 5 years.

Cost of Lease

Year	Lease	Tax Benefit	Net Outflow	P/V	Net
	(a)	(b)	(a-b)		
0	1,000	332	668	1	668
1	30,000	9,966	20,034	.909	18,211
2	30,000	9,966	20,034	.826	16,557
3	30,000	9,966	20,034	.751	15,052
4	30,000	9,966	20,034	.683	13,683
5	30,000	9,966	20,034	.621	12,440
Total					**76,611**

Since net present value in case of lease is less; hence lease is benefited.

Illustration 7.

Specify whether the following acts can be considered as an act of (i) Tax management; or (ii) Tax planning; or (iii) Tax evasion:

a. X has paid the premium of ₹ 72,000 for Life Insurance Policy so as to reduce Total Income.

b. X has installed an air conditioner costing ₹ 60,000 at his residence but shows as it is fitted in a factory. This is with the objective to claim depreciation.

c. Y Ltd maintains registers of tax deductions affected by it to enable timely compliance.

d. Z ltd issues a credit note for ₹ 36,000 for brokerage payable to A, who is the son of G, managing director of the company. The purpose is to reduce Z ltd. income and increase A's income from ₹ 18,000 to ₹ 54,000.

e. A is a working partner in ABC Firm. In such a capacity, he is entitled to a salary of ₹ 7,500 per month. He treats this as salary instead of business income.

f. A is using a motor car for his personal purposes, but charges as business expenditure.

g. X always pays advance tax on time

h. Y sold his residential house and purchased another residential house to claim exemption u/s 54

i. X had Fixed deposit interest amounting to ₹ 15,000 but did not disclose this amount in his Income Tax Return

j. Y had Saving deposit interest amounting to ₹ 5,000, he disclosed this amount under other sources and claimed deduction u/s 80TTA

Solution:

(a) Tax planning;
(b) Tax evasion;
(c) Tax management;
(d) Tax evasion;
(e) Tax evasion;
(f) Tax evasion;
(g) Tax management;
(h) Tax planning;
(i) Tax evasion;
(j) Tax planning.

Soved Case 1:

A business entity requires ₹ 50 lakhs for expansion of business. The entity has two options

Particulars	Option 1	Option 2	Option 3
	(₹)	(₹)	(₹)
Equity Share of ₹ 10 each	40,00,000	30,00,000	30,00,000
12% Debentures	10,00,000	10,00,000	20,00,000
18% Loan from Bank		10,00,000	

Expected rate of return is 15% (before tax). Tax Rate is 31.2% (including cess).

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be the profit after tax in Option 1?
2. What will be the profit after tax in Option 2?
3. What will be the profit after tax in Option 3?
4. Which option is better?

Solution:

Particulars	Option 1	Option 2	Option 3
Share Capital	40,00,000	30,00,000	30,00,000
12% Debentures	10,00,000	10,00,000	20,00,000
18% loan from Bank	—	10,00,000	
EBIT	7,50,000	7,50,000	7,50,000
Cost to Company			
Debenture Interest	1,20,000	1,20,000	2,40,000
Interest on loan from Bank	—	1,80,000	--
Net Profit before tax and dividend	6,30,000	4,50,000	5,10,000
Tax Payable @ 31.2%	1,96,560	1,40,400	1,59,120
Profit after tax	4,33,440	3,09,600	3,50,880
Return on capital	**10.84%**	**10.32%**	**11.70%**

Option 3 is better as in this option return on capital is maximum

Exercise

Multiple Choice Questions

1. Countries that employ explicit policies designed to attract international trade oriented activities by minimization of taxes and reduction or elimination of other restrictions on business operations is described as _____.

   A. Tax Havens
   B. Tax Planning
   C. Tax Evasion
   D. Tax Management

2. A is using a motor car for his personal purposes, but charges as business expenditure.

   This is the case of

   A. Tax Avoidance
   B. Tax Planning
   C. Tax Evasion
   D. Tax Management

[Answer: 1 – A; 2 - C]

Short Essay Type Questions

1. State the difference between tax planning, tax evasion and tax avoidance.
2. What are the objectives of tax planning?
3. Describe the various type of tax planning.

Comprehensive Numerical Problems

XYZ Ltd. needs a component in an assembly operation. It is contemplating the proposal to either make or buy the aforesaid component.

1. If the company decides to make the product itself, then it would need to buy a second hand machine for ₹8 lakh which would be used for 5 years. Manufacturing costs in each of the five years would be ₹12 lakh, ₹14 lakh, ₹16 lakh, ₹20 lakh and ₹25 lakh respectively. The relevant depreciation rate is 15%. The machine will be sold for ₹1 lakh at the end of the 5th year. Capital loss is of no use
2. If the company decides to buy the component from a supplier the component would cost ₹18 lakh, ₹20 lakh, ₹22 lakh, ₹28 lakh and ₹34 lakh respectively in each of the five year.

The relevant discounting rate and tax rate are 14% and 32.445% respectively. Should XYZ Ltd. make the component or buy from outside?

[Ans. Make option is better]

Unsolved Case:

Virat Ltd. is a widely held company. It is currently considering a major expansion of its production facilities and the following alternative are available:

Particulars	Alt-1	Alt-2	Alt-3
	(₹)	(₹)	(₹)
Share capital	50,00,000	20,00,000	10,00,000
14% Debentures	—	20,00,000	15,00,000
18% Loan from Bank	—	10,00,000	25,00,000

EBIT will be ₹ 15,00,000/-. Tax Rate is 31.2%. Rate of dividend of the company since 1995 has not been less than 22% and date of dividend declaration is 30th June every year.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be the profit after tax in Alternate 1?
   a. ₹ 10,32,000
   b. ₹ 7,15,520
   c. ₹ 5,77,920
   d. None of the above
2. What will be the profit after tax in Alternate II?
   a. ₹ 10,32,000
   b. ₹ 7,15,520
   c. ₹ 5,77,920
   d. None of the above
3. What will be the profit after tax in Alternate III?
   a. ₹ 10,32,000
   b. ₹ 7,15,520
   c. ₹ 5,77,920
   d. None of the above
4. Out of these 3 alternatives, which one is better
   a. Alternative I
   b. Alternative II
   c. Alternative III
   d. All are at par

Reference

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

CBDT and Other Authorities 7

This Module includes:

CBDT and Other Authorities

SLOB Mapped against the Module:

To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify the various income-tax authorities
- Appreciate the power of various income-tax authorities

Income Tax Authorities [Sec. 116]

7.1

CBDT AND OTHER AUTHORITIES

a. the Central Board of Direct Taxes constituted under the Central Boards of Revenue Act, 1963
b. Principal Directors General of Income-tax or Principal Chief Commissioners of Income-tax,
c. Directors-General of Income-tax or Chief Commissioners of Income-tax,
d. Principal Directors of Income-tax or Principal Commissioners of Income-tax,
e. Directors of Income-tax or Commissioners of Income-tax or Commissioners of Income-tax (Appeals),
f. Additional Directors of Income-tax or Additional Commissioners of Income-tax or Additional Commissioners of Income-tax (Appeals),
g. Joint Directors of Income-tax or Joint Commissioners of Income-tax or Joint Commissioners of Income-tax (Appeals),
h. Deputy Directors of Income-tax or Deputy Commissioners of Income-tax or Deputy Commissioners of Income-tax (Appeals),
i. Assistant Directors of Income-tax or Assistant Commissioners of Income-tax,
j. Income-tax Officers,
k. Tax Recovery Officers,
l. Inspectors of Income-tax

Taxpoint

- As per sec. 2(7A), Assessing Officer means the Assistant Commissioner or Deputy Commissioner or Assistant Director or Deputy Director or the Income-tax Officer who is vested with the relevant jurisdiction by virtue of directions or orders, and the Additional Commissioner or Additional Director or Joint Commissioner or Joint Director who is directed to exercise or perform all or any of the powers and functions conferred on, or assigned to, an Assessing Officer under this Act.
- As per sec. 2(9A), Assistant Commissioner means a person appointed to be an Assistant Commissioner of Income-tax or a Deputy Commissioner of Income-tax u/s 117(1)
- As per sec. 2(15A), Chief Commissioner means a person appointed to be a Chief Commissioner of Income-tax or a Principal Chief Commissioner of Income-tax u/s 117(1)
- As per sec. 2(16), Commissioner means a person appointed to be a Commissioner of Income-tax or a Director of Income-tax or a Principal Commissioner of Income-tax or a Principal Director of Income-tax u/s 117(1)
- As per sec. 2(21), Director General or Director means a person appointed to be a Director General of Income-tax or a Principal Director General of Income-tax or, as the case may be, a Director of Income-tax or a Principal Director of Income-tax, u/s 117(1), and includes a person appointed to be an Additional Director of Income-tax or a Joint Director of Income-tax or an Assistant Director or Deputy Director of Income-tax
- As per sec. 2(28C), Joint Commissioner means a person appointed to be a Joint Commissioner of Income-tax or an Additional Commissioner of Income-tax u/s 117(1).
- As per sec. 2(28CA), Joint Commissioner (Appeals) means a person appointed to be a Joint Commissioner of Income-tax (Appeals) or an Additional Commissioner of Income-tax (Appeals) u/s 117(1)
- As per sec. 2(28D), Joint Director means a person appointed to be a Joint Director of Income-tax or an Additional Director of Income-tax u/s 117(1).

Appointment of Income-tax Authorities [Sec. 117]

7.2

Appointment of income-tax authorities [Sec. 117]

1. The Central Government may appoint such persons as it thinks fit to be income-tax authorities.
2. The Central Government may authorise the Board, or a Principal Director General or Director-General, a Principal Chief Commissioner or Chief Commissioner or a Principal Director or Director or a Principal Commissioner or Commissioner to appoint income-tax authorities below the rank of an Assistant Commissioner or Deputy Commissioner.
3. An income-tax authority authorised in this behalf by the Board may appoint such executive or ministerial staff as may be necessary to assist it in the execution of its functions.

All these appointments can be made subject to the rules and orders of the Central Government.

Central Board of Direct Taxes (CBDT) 7.3

The Central Board of Direct Taxes is a statutory authority functioning under the Central Board of Revenue Act, 1963. The officials of the Board in their ex-officio capacity also function as a Division of the Ministry dealing with matters relating to levy and collection of direct taxes.

The Central Board of Revenue as the apex body of the Department, charged with the administration of taxes, came into existence as a result of the Central Board of Revenue Act, 1924. Initially the Board was in charge of both direct and indirect taxes. However, when the administration of taxes became too unwieldy for one Board to handle, the Board was split up into two, namely the Central Board of Direct Taxes and Central Board of Excise and Customs with effect from 1.1.1964. This bifurcation was brought about by constitution of two Boards u/s 3 of the Central Board of Revenue Act, 1963.

The Central Board of Direct Taxes consists of a Chairman and following six Members: -

1. Chairman
2. Member (Income-tax)
3. Member (Legislation & Computerisation)
4. Member (Personnel & Vigilance)
5. Member (Investigation)
6. Member (Revenue)
7. Member (Audit & Judicial)

Power of CBDT

1. **Instructions to subordinate authorities [Sec. 119(1)]**

   The Board may, from time to time, issue such orders, instructions and directions to other income-tax authorities as it may deem fit for the proper administration of this Act. Such authorities and all other persons employed in the execution of this Act shall observe and follow such orders, instructions and directions of the Board

   Exception

   No such orders, instructions or directions shall be issued—

   - So as to require any income-tax authority to make a particular assessment or to dispose of a particular case in a particular manner; or
   - So as to interfere with the discretion of the Joint Commissioner (Appeals) or Commissioner (Appeals) in the exercise of his appellate functions.

However, the Board can issue administrative instructions.

2. **Issue General or Special orders to subordinates [Sec. 119(2)(a)]**

The Board may issue from time to time general or special orders to its subordinate subject to the following features:

(a) If it considers it necessary or expedient to do so, for the purpose of proper and efficient management of the work of assessment and collection of revenue.

(b) Such order may be issued whether by way of relaxation of any of the provisions of sec. 115P, 115S, 139, 143, 144, 147, 148, 154, 155, 158BFA, 201(1A), 210, 211, 234A, 234B, 234C, 234E, 234F, 270A, 271, 271C, 271CA and 273 or otherwise.

(c) Such orders may be in respect of any class of incomes or class of cases

(d) Such order must not be prejudicial to the assessee.

(e) Such order acts as guidelines, principles or procedures to be followed by other income-tax authorities in the work relating to assessment or collection of revenue or the initiation of proceedings for the imposition of penalties;

(f) Any such order may, if the Board is of the opinion that it is necessary in the public interest so to do, be published and circulated in the prescribed manner for general information.

3. **Admit application or claim after expiry of time limit [Sec. 119(2)(b)]**

(a) The Board may, by general or special order, admit an application or claim for any exemption, deduction, refund or any other relief under this Act after the expiry of the period specified under this Act for making such application or claim.

(b) Such order can be issued by the Board, if it considers it desirable or expedient to do so, for avoiding genuine hardship in any case or class of cases.

(c) Such order can be issued to any income-tax authority except the Joint Commissioner (Appeals) or Commissioner (Appeals).

4. **Relaxation in requirement of the provisions of Chapter IV or Chapter VIA [Sec. 119(2)(c)]**

- The Board may, by general or special order, relax any requirement contained in any of the provisions of Chapter IV (Sec.14 to 59) or Chapter VIA (Sec.80A to 80U), where the assessee has failed to comply with any requirement specified in such provision for claiming deduction thereunder.
- Reasons for issuing such order are to be specified therein;
- The Board can issue such order if it considers it desirable or expedient to do so for avoiding genuine hardship in any case or class of cases;
- Such order can be issued subject to the following conditions:

  a) the default in complying with such requirement was due to circumstances beyond the control of the assessee; and

  b) the assessee has complied with such requirement before the completion of assessment in relation to the previous year in which such deduction is claimed.

Note: The Central Government shall cause every order issued under this clause to be laid before each House of Parliament.

5. **Control over income-tax authorities [Sec. 118]**

The Board may, by notification in the Official Gazette, direct that any income-tax authority or authorities specified in the notification shall be subordinate to such other income-tax authority or authorities as may be specified in such notification.

Note:

An order, circular, instruction or direction issued u/s 119 cannot override the provisions of the Act.

Taxpayer's Charter [Sec. 119A]

The Board shall adopt and declare a Taxpayer's Charter and issue such orders, instructions, directions or guidelines to other income-tax authorities as it may deem fit for the administration of such Charter.

Jurisdiction of Income-tax Authorities [Sec. 120]

7.4

- Income-tax authorities shall exercise all or any of the powers and perform all or any of the functions assigned to such authorities in accordance with directions of the Board
- The directions of the Board may authorise any other income-tax authority to issue orders in writing for the exercise of the powers and performance of the functions by any of its subordinate.
- The Board or other authorised income-tax authority may have regard to any one or more of the following criteria:
  a) territorial area;
  b) persons or classes of persons;
  c) incomes or classes of income; and
  d) cases or classes of cases.
- The Board may, by general or special order, and subject to such conditions, restrictions or limitations as may be specified therein:
  a. authorise any Principal Director General or Director General or Principal Director or Director to perform such functions of any other income-tax authority as may be assigned to him by the Board;
  b. empower the Principal Director General or Director General or Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner to issue orders in writing that the powers and functions assigned to, the Assessing Officer in respect of any specified area or persons or classes of persons or incomes or classes of income or cases or classes of cases, shall be exercised or performed by an Additional Commissioner or an Additional Director or a Joint Commissioner or a Joint Director; and
- Where it is considered necessary or appropriate for the proper management of the work, jurisdiction with more than one income tax authority in relation to any case may be conferred or assigned.
- The Board may direct that for the purpose of furnishing of the return of income or the doing of any other act or thing under this Act or any rule made thereunder by any person or class of persons, the income-tax authority exercising and performing the powers and functions in relation to the said person or class of persons shall be such authority as may be specified in the notification.

Jurisdiction of Assessing Officers [Sec. 124]

7.5

1. Where the Assessing Officer has been vested with jurisdiction over any area, within the limits of such area, he shall have jurisdiction:

In respect of any person carrying on a business or profession	If the place at which such person carries on business or profession is situate within the area, or where his business or profession is carried on in more places than one if the principal place of his business or profession is situate within the area
In respect of any other person	Person residing within the area

2. Where a question arises as to whether an Assessing Officer has jurisdiction to assess any person, the question shall be determined by the Principal Director General or Director General or the Principal Chief Commissioner or Chief Commissioner or the Principal Commissioner or Commissioner.

3. In case, where the question is one relating to areas within the jurisdiction of different Principal Directors General or Directors General or Principal Chief Commissioners or Chief Commissioners or Principal Commissioners or Commissioners, by the Principal Directors General or Directors General or Principal Chief Commissioners or Chief Commissioners or Principal Commissioners or Commissioners concerned or, if they are not in agreement, by the Board or by such Principal Director General or Director General or Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner as the Board may notify.

4. No person shall be entitled to call in question the jurisdiction of an Assessing Officer:

   a. where he has made a return u/s 139(1), after the expiry of 1 month from the date on which he was served with a notice u/s 142(2) or 143(2) or after the completion of the assessment, whichever is earlier.

   b. where he has made no such return, after the expiry of the time allowed by the notice u/s 142(1) or 148 for the making of the return or by the notice under the first proviso to sec. 144 to show cause why the assessment should not be completed to the best of the judgment of the Assessing Officer, whichever is earlier.

   c. where an action has been taken u/s 132 or 132A, after the expiry of 1 month from the date on which he was served with a notice u/s 153A or 153C or after the completion of the assessment, whichever is earlier.

5. Where an assessee calls in question the jurisdiction of an Assessing Officer, then the Assessing Officer shall, if not satisfied with the correctness of the claim, refer the matter for determination (as given in point 2 and 3) before the assessment is made.

6. Every Assessing Officer shall have all the powers conferred by or under this Act on an Assessing Officer in respect of the income accruing or arising or received within the area, if any, over which he has been vested with jurisdiction.

Power to Transfer Cases [Sec. 127]

7.6

- The Principal Director General or Director General or Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may transfer any case from one or more Assessing Officers subordinate to him (whether with or without concurrent jurisdiction) to any other Assessing Officer or Assessing Officers (whether with or without concurrent jurisdiction) also subordinate to him.
  - Such power shall be exercised after:
    a) giving the assessee a reasonable opportunity of being heard in the matter wherever it is possible to do so.
    b) recording his reasons for doing so.
- Where the Assessing Officer or Assessing Officers from whom the case is to be transferred and the Assessing Officer or Assessing Officers to whom the case is to be transferred are not subordinate to the same Principal Director General or Director General or Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner:

  a. where the Principal Directors General or Directors General or Principal Chief Commissioners or Chief Commissioners or Principal Commissioners or Commissioners to whom such Assessing Officers are subordinate are in agreement, then the Principal Director General or Director General or Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner from whose jurisdiction the case is to be transferred may pass the order.
     - Such power shall be exercised after:
       i) giving the assessee a reasonable opportunity of being heard in the matter wherever it is possible to do so.
       ii) recording his reasons for doing so.

  b. where such authorities are not in agreement, the order transferring the case may be passed by the Board or any other notified higher authority

- No opportunity of being heard to be given to the assessee where the transfer is from any Assessing Officer (whether with or without concurrent jurisdiction) to any other Assessing Officer (whether with or without concurrent jurisdiction) and the offices of all such officers are situated in the same city, locality or place.
- The transfer of a case may be made at any stage of the proceedings, and shall not render necessary the re-issue of any notice already issued by the Assessing Officer from whom the case is transferred.
  - Case, in relation to any person whose name is specified in any order or direction issued thereunder, means all proceedings under this Act in respect of any year which may be pending on the date of such order or direction or which may have been completed on or before such date, and includes also all proceedings under this Act which may be commenced after the date of such order or direction in respect of any year.

Succession of Income-tax Authority [Sec. 129]

7.7

- Whenever in respect of any proceeding under this Act an income-tax authority ceases to exercise jurisdiction and another income tax authority exercises jurisdiction.
- The income-tax authority so succeeding may continue the proceeding from the stage at which the proceeding was left by his predecessor.

Opportunity of being re-heard

The assessee may demand that before -

- Such succeeding authority reopens previous proceeding or any part thereof; or
- any order of assessment is passed against him,

- he must be given an opportunity of being re-heard.

Faceless Jurisdiction of Income-tax Authorities [Sec. 130]

7.8

The Central Government may notify a scheme for the purposes of:

a. exercise of all or any of the powers and performance of all or any of the functions conferred on, or, as the case may be, assigned to income-tax authorities by or under this Act as referred to in sec. 120; or

b. vesting the jurisdiction with the Assessing Officer as referred to in sec. 124; or

c. exercise of power to transfer cases u/s 127; or

d. exercise of jurisdiction in case of change of incumbency as referred to in sec. 129,

so as to impart greater efficiency, transparency and accountability by—

i. eliminating the interface between the income-tax authority and the assessee or any other person, to the extent technologically feasible;

ii. optimising utilisation of the resources through economies of scale and functional specialisation;

iii. introducing a team-based exercise of powers and performance of functions by two or more income-tax authorities, concurrently, in respect of any area or persons or classes of persons or incomes or classes of income or cases or classes of cases, with dynamic jurisdiction.

Faceless Approval or Registration [Sec. 293D]

7.9

The Central Government may make a scheme, for the purposes of granting approval or registration, as the case may be, by income-tax authority under any provision of the Act, so as to impart greater efficiency, transparency and accountability by:

a. eliminating the interface between the income-tax authorities and the assessee or any other person to the extent technologically feasible;

b. optimising utilisation of the resources through economies of scale and functional specialisation;

c. introducing a team-based grant of approval or registration, with dynamic jurisdiction.

Exercise

Multiple Choice Questions

1. CBDT means
   A) Central Board of Direct Tax
   B) Central Board of Double Tax
   C) Central Bank of Direct Tax
   D) None of the above

2. Sec. 130 deals with
   A) Faceless jurisdiction of the income-tax authority
   B) Jurisdiction of the income-tax authority
   C) Jurisdiction of the CBDT
   D) None of the above

[Answer: 1 – A, 2 – A]

Short Essay Type Questions

1. State the power of the Central Board of Direct Taxes.
2. State the provision u/s 127 relating to power to transfer cases.

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

E-commerce Transaction and Liability in Special Cases

8

This Module includes:

8.1 Equalisation Levy

8.2 Tonnage Tax Scheme [Sec. 115V to Sec. 115VZC]

8.3 Legal Representatives [Sec. 159]

8.4 Executors [Sec. 168]

8.5 Representative Assessee [Sec. 160]

8.6 Company in Liquidation [Sec. 178]

8.7 Miscellaneous Provisions

E-commerce Transaction and Liability in Special Cases

SLOB Mapped against the Module:

To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.

Module Learning Objectives:

After studying this module, the students will be able to -

- Understand and identify the situation where provisions are applicable
- Compute tax liability in these cases
- Appreciate the various compliance required to be done

Equalisation Levy

8.1

With the expansion of information and communication technology, the supply and procurement of digital goods and services have undergone exponential expansion everywhere, including India. The digital economy is growing at 10% per year, significantly faster than the global economy as a whole.

Currently in the digital domain, business may be conducted without regard to national boundaries and may dissolve the link between an income-producing activity and a specific location. From a certain perspective, business in digital domain doesn't seem to occur in any physical location but instead takes place in the nebulous world of "cyberspace." Persons carrying business in digital domain could be located anywhere in the world. Entrepreneurs across the world have been quick to evolve their business to take advantage of these changes. It has also made it possible for the businesses to conduct themselves in ways that did not exist earlier, and given rise to new business models that rely more on digital and telecommunication network, do not require physical presence, and derives substantial value from data collected and transmitted from such networks.

These new business models have created new tax challenges. The typical direct tax issues relating to e-commerce are the difficulties of characterizing the nature of payment and establishing a nexus or link between a taxable transaction, activity and a taxing jurisdiction, the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes. The digital business fundamentally challenges physical presence-based permanent establishment rules. If permanent establishment (PE) principles are to remain effective in the new economy, the fundamental PE components developed for the old economy i.e. place of business, location, and permanency must be reconciled with the new digital reality.

The Organization for Economic Cooperation and Development (OECD) has recommended, in Base Erosion and Profit Shifting (BEPS) project under Action Plan 1, several options to tackle the direct tax challenges which include modifying the existing Permanent Establishment (PE) rule to include that where an enterprise engaged in fully de-materialized digital activities would constitute a PE if it maintained a significant digital presence in another country's economy. It further recommended a virtual fixed place of business PE in the concept of PE i,e creation of a PE when the enterprise maintains a website on a server of another enterprise located in a jurisdiction and carries on business through that website. It also recommended to impose of a final withholding tax on certain payments for digital goods or services provided by a foreign e-commerce provider or imposition of a equalisation levy on consideration for certain digital transactions received by a non-resident from a resident or from a non-resident having permanent establishment in other contracting state.

Considering the potential of new digital economy and the rapidly evolving nature of business operations it is found essential to address the challenges in terms of taxation of such digital transactions as mentioned above. In order to address these challenges, Chapter VIII of the Finance Act, 2016[1], titled "Equalisation Levy", provides for an equalisation levy of 6 % of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment ('PE') in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India. Different provisions thereof are discussed below:

1 The equalization levy would come into effect from 01-06-2016 [Notification dated 27-05-2016]

A. Charge of equilisation levy on specified services [Sec. 165]

Equalisation levy shall be payable @ 6% of the consideration for any specified service received or receivable by a person, being a non-resident from:

i. a person resident in India and carrying on business or profession; or

ii. a non-resident having a permanent establishment in India.

- Specified service means
  a) online advertisement,
  b) any provision for digital advertising space or any other facility or service for the purpose of online advertisement and
  c) any other notified service – Sec. 164(i)
- Online means a facility or service or right or benefit or access that is obtained through the internet or any other form of digital or telecommunication network – Sec. 164(f)

Taxpoint

These provisions extend to the whole of India.

Exception

The equalisation levy shall not be charged, where:

a) the consideration received or receivable for specified services shall not include the consideration, which are taxable as royalty or fees for technical services in India, read with the agreement notified u/s 90 or 90A of the Income-Tax Act.

b) the non-resident providing the specified service has a permanent establishment in India and the specified service is effectively connected with such permanent establishment;

c) the aggregate amount of consideration for specified service received or receivable in a previous year from resident in India or from a non-resident having a permanent establishment in India, does not exceed ₹ 1,00,000; or

d) the payment for the specified service by the person resident in India, or the permanent establishment in India is not for the purposes of carrying out business or profession.

Examples

1. Vikash has advertised on Facebook to expand his business. He has to pay ₹ 2,00,000 in the previous year 2023-24 to Facebook for the advertising services availed. In this case, Vikash will deduct 6% of ₹ 2,00,000 i.e., ₹ 12,000, and pay the balance ₹ 1,88,000 to Facebook.

2. Ashok has advertised on Facebook to promote his business of baking. He is required to pay ₹ 20,000 in the previous year 2023-24 to Facebook for the advertising services availed. In this case, since during the financial year annual payments did not exceed ₹ 1,000,00, Ashok is not liable to deduct equalisation levy.

Collection and recovery of equalisation levy on specified services [Sec. 166]

Who is liable to deduct equalisation levy:

Every person, being a resident and carrying on business or profession or a non-resident having a permanent establishment in India (hereafter in this Chapter referred to as assessee) shall deduct the equalisation levy u/s 165 from the amount paid or payable to a non-resident in respect of the specified service.

Rate of levy: 6%

Threshold limit: Such deduction shall be made if the aggregate amount of consideration for specified service in a previous year exceeds ₹ 1,00,000.

Time limit for depositing the levy to the credit of the Central Government: The equalisation levy so deducted during any calendar month shall be paid by every assessee to the credit of the Central Government by the 7th day of the month immediately following the said calendar month.

Consequences of failure to deduct equalisation levy: Any assessee who fails to deduct the levy shall be (even though not deducted) liable to pay the levy to the credit of the Central Government in accordance with the aforesaid provisions.

B. Charge of equalisation levy on e-commerce supply of services [Sec. 165A]

Equalisation levy shall be charged @ 2% of the amount of consideration received or receivable by an e-commerce operator from e-commerce supply or services made or provided or facilitated by it—

a. to a person resident in India; or

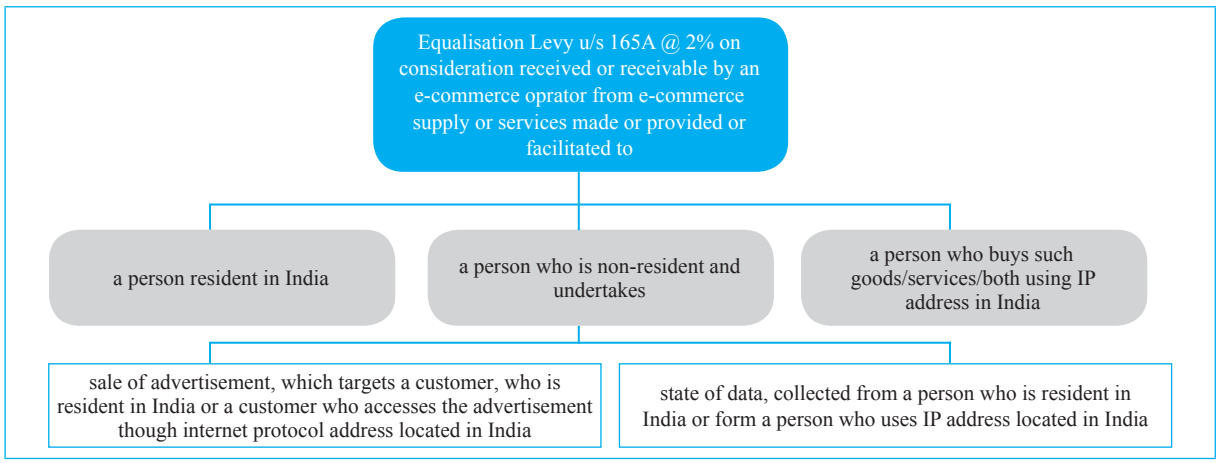
b. to a non-resident in the specified circumstances; or

- "Specified circumstances" mean—

  i. sale of advertisement, which targets a customer, who is resident in India or a customer who accesses the advertisement though internet protocol address located in India; and

  ii. sale of data, collected from a person who is resident in India or from a person who uses internet protocol address located in India

c. to a person who buys such goods or services or both using internet protocol address located in India.



Taxpoint

- Consideration received or receivable from e-commerce supply or services shall include:

  i. consideration for sale of goods irrespective of whether the e-commerce operator owns the goods, so, however, that it shall not include consideration for sale of such goods which are owned by a person resident in India or by a permanent establishment in India of a person non-resident in India, if sale of such goods is effectively connected with such permanent establishment.

ii. consideration for provision of services irrespective of whether service is provided or facilitated by the e-commerce operator, so, however, that it shall not include consideration for provision of services which are provided by a person resident in India or by permanent establishment in India of a person non-resident in India, if provision of such services is effectively connected with such permanent establishment.

- e-commerce operator means a non-resident who owns, operates or manages digital or electronic facility or platform for online sale of goods or online provision of services or both;
- e-commerce supply or services means:
  - i. online sale of goods owned by the e-commerce operator; or
  - ii. online provision of services provided by the e-commerce operator; or
  - iii. online sale of goods or provision of services or both, facilitated by the e-commerce operator; or
  - iv. any combination of activities listed in clause (i), (ii) or clause (iii);
  - Online sale of goods and online provision of services shall include one or more of the following online activities:
    - a. acceptance of offer for sale; or
    - b. placing of purchase order; or
    - c. acceptance of the purchase order; or
    - d. payment of consideration; or
    - e. supply of goods or provision of services, partly or wholly

Exception

The equalisation levy shall not be charged:

a. the consideration received or receivable for e-commerce supply or services shall not include the consideration, which are taxable as royalty or fees for technical services in India, read with the agreement notified u/s 90 or 90A of the Income-Tax Act.

b. where the e-commerce operator making or providing or facilitating e-commerce supply or services has a permanent establishment in India and such e-commerce supply or services is effectively connected with such permanent establishment;

c. where the equalisation levy is leviable u/s 165 [i.e. A supra]; or

d. sales, turnover or gross receipts, as the case may be, of the e-commerce operator from the e-commerce supply or services made or provided or facilitated is less than ₹ 2 crore during the previous year.

Examples:

1. ABC Inc. a non-resident is operating an electronic or digital platform, whereby services of enabling online meeting for various participants is being provided. The platform of ABC Inc. is being used for online webinars/ meetings, etc. by Indian customers who are availing such services by paying annual/monthly charges. In this case, ABC Inc. is an e-commerce operator and online provision of services of enabling webinars/meetings by the said company will fall within the meaning of "e-commerce supply or services".

2. DEF, a UK-based company, approaches GHI which is a US-based company, targeting Indian customers at large, for placing advertisements of its food products on the digital platform of GHI. In this case, GHI will be liable to pay equalisation levy @ 2% of the consideration received by it from DEF.

3. XYZ, UK based Company, an e-commerce operator, collects data from an Indian resident person and further sells such data collected to KLM, a France-based company. In this case, XYZ selling the data collected from an Indian resident will be liable to pay equalisation levy @ 2% on the amount of consideration received by it from the KLM.

Collection and recovery of equalisation levy on e-commerce supply or services [Sec. 166A]

The equalisation levy u/s 165A shall be paid by every e-commerce operator to the credit of the Central Government quarterly as per following time schedule:

Date of ending of the quarter of financial	Due date of payment
30th June	7th July
30th September	7th October
31st December	7th January
31st March	31st March

Furnishing of Statement [Sec. 167]

- Every assessee or ecommerce operator shall, within 30th June immediately following the financial year, prepare and deliver to the Assessing Officer (or to any other authority or agency authorised by the Board), a statement in Form 1, verified in such manner and setting forth such particulars as may be prescribed, in respect of all specified services or e-commerce supply or services during such financial year.
- *Revised Statement*: An assessee or ecommerce operator who has not furnished the statement within aforesaid time or having furnished such statement, notices any omission or wrong particular therein, may furnish a statement or a revised statement, as the case may be, at any time before the expiry of 2 years from the end of the financial year in which the specified services or e-commerce supply or services was provided or facilitated.
- *Notice by the Assessing Officer*: Where any assessee or ecommerce operator fails to furnish the statement within 30th June immediately following the financial year, the Assessing Officer may serve a notice upon such assessee or ecommerce operator requiring him to furnish the statement in the prescribed form, verified in the prescribed manner and setting forth such particulars, within 30 days from the date of service of the notice.

Processing of Statement [Sec. 168]

Statement furnished u/s 167 shall be processed in the following manner:

a. the equalisation levy shall be computed after making the adjustment for any arithmetical error in the statement;

b. the interest, if any, shall be computed on the basis of sum deductible or payable as computed in the statement;

c. the sum payable by, or the amount of refund due to, the assessee shall be determined after adjustment of the interest against any amount paid u/s 166 or 166A or 170 and any amount paid otherwise by way of tax or interest;

d. an intimation shall be prepared or generated and sent to the assessee or ecommerce operator specifying the sum determined to be payable by, or the amount of refund due to, him; and

e. the amount of refund due to the assessee or ecommerce operator shall be granted to him.

Time limit

No intimation shall be **sent** after the expiry of 1 year from the end of the financial year in which the statement or revised statement is furnished.

Taxpoint

For the purposes of processing of statements, the Board may make a scheme for centralised processing of such statements to expeditiously determine the tax payable by, or the refund due to, the assessee or ecommerce operator.

Rectification of mistake [Sec. 169]

- With a view to rectifying any mistake apparent from the record, the Assessing Officer may amend any intimation issued u/s 168, within **1 year** from the end of the financial year in which the intimation sought to be amended was issued.
- The Assessing Officer may make an amendment to any intimation either *suo motu* or on any mistake brought to his notice by the assessee or ecommerce operator.
- An amendment to any intimation, which has the effect of increasing the liability of the assessee or ecommerce operator or reducing a refund, shall not be made unless the Assessing Officer has given notice to the assessee of his intention so to do and has given the assessee or ecommerce operator a reasonable opportunity of being heard.
- Where any such amendment to any intimation has the effect of enhancing the sum payable or reducing the refund already made, the Assessing Officer shall make an order specifying the sum payable by the assessee or ecommerce operator and the provisions of this Chapter shall apply accordingly.

Interest on Delayed payment of equalisation levy [Sec. 170]

Every assessee or ecommerce operator, who fails to credit adequate equalisation levy to the account of the Central Government within specified period, shall pay simple interest @ 1% of such levy for every month or part of a month by which such crediting of the tax is delayed.

Penalty

Penalties provisions are as under:

Sec.	Nature of default	Amount of Penalty
171(a)	Fails to deduct the equalisation levy u/s 165	Equal to the amount of equalisation levy
171(aa)	Fails to pay the equalisation levy u/s 165A	
171(b)	Fails to pay levy, after deduction, to the credit of the Central Government	₹ 100 for every day during which the failure continues subject to maximum of amount failed to pay
172	Failure to furnish statement as required u/s 172	₹ 100 for every day during which the failure continues

- No penalty shall be imposable:
  1. If the assessee proves to the satisfaction of the Assessing Officer that there was reasonable cause for the said failure.
  2. Without giving reasonable opportunity of being heard to the assessee or ecommerce operator [Sec. 173].

- An assessee or ecommerce operator aggrieved by an order imposing penalty may appeal to the Commissioner of Income-tax (Appeals) within 30 days from the date of receipt of the order in Form 3. It shall be accompanied with fees of ₹ 1,000/-. The provisions relating to appeals are in line with that of the Income-tax Act, 1961. [Sec. 174]
- Similarly, appeals can be filed before the ITAT against the order of the Commissioner (Appeals) in Form 4 within 60 days from the date on which the order sought to be appealed against is received by the assessee (or ecommerce operator) or by the Commissioner. In case appeal before the ITAT is filed by the assessee, it should be accompanied with fees of ₹ 1,000/- [Sec. 175]

Punishment for false statement [Sec. 176]

If a person makes a false statement in any verification or delivers an account or statement, which is false, and which he either knows or believes to be false, or does not believe to be true, he shall be punishable with imprisonment for a term which may extend to 3 years and with fine.

Taxpoint:

- An offence punishable above shall be deemed to be non-cognizable.
- No prosecution shall be instituted against any person for any offence except with the previous sanction of the Chief Commissioner of Income-tax [Sec. 177].

Application of Certain provisions of Income-tax Act [Sec. 178]

The provisions of sec. 120, 131, 133A, 138, 156, Chapter XV and sec. 220 to 227, 229, 232, 260A, 261, 262, 265 to 269, 278B, 280A, 280B, 280C, 280D, 282 and 288 to 293 of the Income-tax Act shall so far as may be, apply in relation to equalisation levy, as they apply in relation to income-tax.

Tonnage Tax Scheme [Sec. 115V to Sec. 115VZC]

8.2

To make the Indian shipping industry more competitive, a tonnage tax scheme for taxation of shipping profits was introduced. Some of the basic features of the tonnage tax scheme are as follows:-

- It is a scheme of presumptive taxation whereby the notional income arising from the operation of a ship is determined based on the tonnage of the ship.
- The notional income is taxed at the normal corporate rate applicable for the year.
- Tax is payable even if there is a loss in an year.
- A company may opt for the scheme and once such option is exercised, there is a lock in period of 10 years. If a company opts out, it is debarred from re-entry for 10 years.
- Since this is a preferential regime of taxation, certain conditions like creation of reserves, training etc. are required to be met.
- A company may be expelled in certain circumstances.

A company owning at least one qualifying ship may join. A qualifying ship is one with a minimum tonnage of 15 tons and having a valid certificate. Certain types of ships like fishing vessels, pleasure crafts etc. are excluded in terms of sec. 115V-D. The business of operating qualifying ships is to be considered a separate business and separate accounts are to be maintained. Sec. 115VG gives the manner of computation of the daily tonnage income which when multiplied by the number of days the ship operated, will give the annual tonnage income from the ship. A company owning at least 1 ship may charter in ships subject to certain limits for the purpose of operation. Relevant shipping income, which replaces the actual income from the operations, is defined in sec. 115 V-I. Sec. 115VJ gives the treatment of common costs.

A company opting for the scheme is not allowed any set-off of loss nor is any depreciation allowed. However, both loss and depreciation are deemed to have been allowed and notional adjustments are made against the relevant shipping income. Although depreciation is not allowed, it is necessary to bifurcate the qualifying ships and non-qualifying ships at the time a company joins the scheme. Sec. 115VK lays down the method for allocating the written down value amongst qualifying and non-qualifying ships. Any income from transfer of qualifying assets is treated in the same manner as for any other business asset in terms of sec. 115VN.

The profits from the business of operating qualifying ships will not be taken into consideration for the purpose of MAT as per sec. 115V-O.

Sec. 115VP lays down the procedure for the option and the manner of granting approval. Sec. 115VQ lays down that once a company opts for the scheme, the option remains in force for 10 years except in certain circumstances. Sec. 115VS provides for the circumstances in which the tonnage tax company is prohibited from opting for the scheme. Such prohibition is for a period of 10 years. Sec. 115VT, 115VU, 115VS and 115VW lay down the conditions for the applicability of the scheme. In terms of sec. 115VT, a tonnage tax company has to create a reserve of at least 20% of its book profits to be utilized for the purpose of acquisition of new ships. As per sec. 115VU a tonnage tax

company has to comply with a minimum training requirement in accordance with the guidelines to be issued by the DG (Shipping). The company will be expelled if the training requirements are not met for 5 consecutive years. Sec. 115VV lays down the limit of 49% for chartering in. In terms of sec. 115VW, maintenance of separate books of account and the audit of the same is compulsory for a company opting for the scheme. Sec. 115VX lays down the details regarding valid certificate which indicates the net tonnage of ships. Sec. 115VY and 115VZ provide for the contingencies of amalgamation and demerger. Sec. 115VZB enjoins upon a company not to abuse the preferential tax regime and sec. 115VZC provides for expulsion of a company in case of abuse

Few of the provisions are discussed here in below:

Computation of profits and gains from the business of operating qualifying ships [Sec. 115VA]

In the case of a company, the income from the business of operating qualifying ships, may, **at its option**, be computed in accordance with the provisions of this Chapter and such income shall be deemed to be the profits and gains of such business chargeable to tax under the head "*Profits and gains of business or profession*".

Taxpoint

- **Operating ships [Sec. 115VB]**

  A company shall be regarded as operating a ship if it operates any ship whether owned or chartered by it and includes a case where even a part of the ship has been chartered in by it in an arrangement such as slot charter, space charter or joint charter.

  However, a company shall not be regarded as the operator of a ship, which has been chartered out by it on bareboat charter-cum-demise[1] terms or on bareboat charter[2] terms for a period exceeding 3 years.

  - Bareboat charter means hiring of a ship for a stipulated period on terms which give the charterer possession and control of the ship, including the right to appoint the master and crew;
  - Bareboat charter-cum-demise means a bareboat charter where the ownership of the ship is intended to be transferred after a specified period to the company to whom it has been chartered;

- **Qualifying ship [Sec. 115VD]**

  A ship is a qualifying ship if:

  a. it is a sea going ship or vessel of 15 net tonnage or more;
     - Seagoing ship means a ship if it is certified as such by the competent authority of any country.

  b. it is a ship registered under the Merchant Shipping Act, 1958 or a ship registered outside India in respect of which a licence has been issued by the Director-General of Shipping u/s 406 or section 407 of the Merchant Shipping Act, 1958; and

  c. a valid certificate in respect of such ship indicating its net tonnage is in force,—

  In nutshell, qualifying ship means a sea-going ship having valid certificate

  - but does not include—

  i. Factory ships;
     - Factory ship includes a vessel providing processing services in respect of processing of the fishing produce.

  ii. Pleasure crafts;
     - Pleasure craft means a ship of a kind whose primary use is for the purposes of sport or recreation.

iii. Harbour and river ferries;

iv. A seagoing ship or vessel if the main purpose for which it is used is the provision of goods or services of a kind normally provided on land;

v. Off-shore installations;

vi. Fishing vessels

vii. a qualifying ship, which is used as a fishing vessel for a period of more than 30 days during a previous year.

Qualifying company [Sec. 115VC]

A company is a qualifying company if:

(a) it is an Indian company;

(b) the place of effective management of the company is in India;

Place of effective management of the company means:

(i) the place where the board of directors of the company or its executive directors, as the case may be, make their decisions; or

(ii) in a case where the board of directors routinely approve the commercial and strategic decisions made by the executive directors or officers of the company, the place where such executive directors or officers of the company perform their functions.

(c) it owns at least one qualifying ship; and

(d) the main object of the company is to carry on the business of operating ships.

Manner of computation of income under tonnage tax scheme [Sec. 115VE]

- A tonnage tax company (means a qualifying company in relation to which tonnage tax option is in force) engaged in the business of operating qualifying ships shall compute the profits from such business under the tonnage tax scheme.
- The business of operating qualifying ships giving rise to income [referred to in sec. 115V-I(1)] shall be considered as a separate business (hereafter referred to as the tonnage tax business) distinct from all other activities or business carried on by the company.
- The profits shall be computed separately from the profits and gains from any other business.
- The tonnage tax scheme shall apply only if an option to that effect is made in accordance with the provisions of section 115VP.
- Where a company engaged in the business of operating qualifying ships is not covered under the tonnage tax scheme or, has not made an option to that effect, as the case may be, the profits and gains of such company from such business shall be computed in accordance with the other provisions of this Act.

Tonnage income [Sec. 115VF]

The tonnage income shall be computed in accordance with sec. 115VG and the income so computed shall be deemed to be the profits chargeable under the head "Profits and gains of business or profession" and the relevant shipping income referred to in sec. 115V-I(1) shall not be chargeable to tax.

Computation of tonnage income [Sec. 115VG]

The tonnage income of a tonnage tax company for a previous year shall be the aggregate of the tonnage income of each qualifying ship computed in accordance with the following provisions:

- The tonnage income of each qualifying ship shall be the daily tonnage income of each such ship multiplied by:
  (a) the number of days in the previous year; or
  (b) the number of days in part of the previous year in case the ship is operated by the company as a qualifying ship for only part of the previous year.
- Daily tonnage income of a qualifying ship shall be:

Qualifying ship having net tonnage	Amount of daily tonnage income
Upto 1,000	₹ 70 for each 100 tons
Exceeding 1,000 but not more than 10,000	₹ 700 plus ₹ 53 for each 100 tons exceeding 1,000 tons
Exceeding 10,000 but not more than 25,000	₹ 5,470 plus ₹ 42 for each 100 tons exceeding 10,000 tons
Exceeding 25,000	₹ 11,770 plus ₹ 29 for each 100 tons exceeding 25,000 tons

- The tonnage shall be rounded off to the nearest multiple of 100 tons and for this purpose
  - any tonnage consisting of kilograms shall be ignored and thereafter;
  - if such tonnage is not a multiple of 100, then,
  - if the last figure in that amount is 50 tons or more, the tonnage shall be increased to the next higher tonnage which is a multiple of 100; or
  - if the last figure is less than 50 tons the tonnage shall be reduced to the next lower tonnage which is a multiple of 100.
- No deduction or set off shall be allowed in computing the tonnage income under this Chapter.

Relevant shipping income [Sec. 115V-I]

- The relevant shipping income of a tonnage tax company means:
  (i) its profits from core activities;
  (ii) its profits from incidental activities
- Where the aggregate of incomes from incidental activities exceeds ¼% of the turnover from core activities, such excess shall not form part of the relevant shipping income for the purposes of this Chapter and shall be taxable under the other provisions of this Act.
- The **core activities** of a tonnage tax company shall be:
  (i) its activities from operating qualifying ships; and
  (ii) other ship-related activities mentioned as under:—
    A. shipping contracts in respect of—
      (a) earning from pooling arrangements;
        - Pooling arrangement means an agreement between two or more persons for providing services through a pool or operating one or more ships and sharing earnings or operating profits on the basis of mutually agreed terms.
      (b) contracts of affreightment
        - Contract of affreightment means a service contract under which a tonnage tax company agrees to transport a specified quantity of specified products at a specified rate, between designated loading and discharging ports over a specified period.

B. specific shipping trades, being,—

(a) on-board or on-shore activities of passenger ships comprising of fares and food and beverages consumed on board;

(b) slot charters, space charters, joint charters, feeder services, container box leasing of container shipping.

- The **incidental activities** shall be the activities which are incidental to the core activities and which may be prescribed for the purpose.
- Where a tonnage tax company operates any ship, which is not a qualifying ship, the income attributable to operating such non-qualifying ship shall be computed in accordance with the other provisions of this Act.
- Where any goods or services held for the purposes of tonnage tax business are transferred to any other business carried on by a tonnage tax company or *vice versa* and the consideration for such transfer as recorded in the accounts of the tonnage tax business does not correspond to the market value of such goods or services as on the date of the transfer, then, the relevant shipping income under this section shall be computed as if the transfer, in either case, had been made at the market value of such goods or services as on that date.
- Where it appears to the Assessing Officer that, owing to the close connection between the tonnage tax company and any other person, or for any other reason, the course of business between them is so arranged that the business transacted between them produces to the tonnage tax company more than the ordinary profits which might be expected to arise in the tonnage tax business, the Assessing Officer shall, in computing the relevant shipping income of the tonnage tax company for the purposes of this Chapter, take the amount of income as may be reasonably deemed to have been derived therefrom.
- In case the relevant shipping income of a tonnage tax company is a loss, then, such loss shall be ignored for the purposes of computing tonnage income.

General exclusion of deduction and set off, etc. [Sec. 115VL]

In computing the tonnage income of a tonnage tax company for any previous year (hereafter in this section referred to as the "relevant previous year") in which it is chargeable to tax in accordance with this Chapter:

- Every loss, allowance or deduction referred to sec. 30 to 43B had been given full effect to for that previous year;
- No loss referred to in sec. 70(1) or 70(3) [long term capital loss] or 71(1) or 71(2) or 72(1) or 72A(1), in so far as such loss relates to the business of operating qualifying ships of the company, shall be carried forward or set off where such loss relates to any of the previous years when the company is under the tonnage tax scheme;
- No deduction shall be allowed under Chapter VI-A in relation to the profits and gains from the business of operating qualifying ships; and
- In computing the depreciation allowance u/s 32, the written down value of any asset used for the purposes of the tonnage tax business shall be computed as if the company has claimed and has been actually allowed the deduction in respect of depreciation for the relevant previous year.

Exclusion of loss [Sec. 115VM]

- Section 72 shall apply in respect of any losses that have accrued to a company before its option for tonnage tax scheme and which are attributable to its tonnage tax business, as if such losses had been set off against the relevant shipping income in any of the previous years when the company is under the tonnage tax scheme.
- The losses shall not be available for set off against any income other than relevant shipping income in any previous year beginning on or after the company exercises its option u/s 115VP.

Exclusion from section 115JB [Sec. 115VO]

The book profit or loss derived from the activities of a tonnage tax company, referred to in sec. 115VI(1), shall be excluded from the book profit of the company for the purposes of sec. 115JB. In other words, MAT provisions are not applicable.

Legal Representatives [Sec. 159]

8.3

- Where a person dies, his legal representatives shall be liable to pay any sum which the deceased would have been liable to pay if he had not died, in the like manner and to the same extent as the deceased.
- The liability of a legal representative is limited to the extent to which the estate is capable of meeting the liability.
- However, every legal representative shall be personally liable for any tax payable by him in his capacity as legal representative if, while his liability for tax remains undischarged, he creates a charge on or disposes of or parts with any assets of the estate of the deceased, which are in, or may come into, his possession, but such liability shall be limited to the value of the asset so charged, disposed of or parted with.
- For the purpose of making an assessment (including an assessment, reassessment or recomputation u/s 147) of the income of the deceased and for the purpose of levying any sum in the hands of the legal representative in accordance with the above provisions:

  (a) any proceeding taken against the deceased before his death shall be deemed to have been taken against the legal representative and may be continued against the legal representative from the stage at which it stood on the date of the death of the deceased;

  (b) any proceeding which could have been taken against the deceased if he had survived, may be taken against the legal representative; and

  (c) all the provisions of this Act shall apply accordingly.
- The legal representative of the deceased shall be deemed to be an assessee.

Taxpoint:

- In the year of death of the assessee, there are two assessment (i) upto date of death, sec. 159 is applicable; (ii) after the date of death, sec. 168 or other sections are applicable.
- Representative u/s 159 and Executors u/s 168 may be same person.
- In case of death of the karta of HUF, HUF continues with to exist with changed composition and karta, hence section 159 is not applicable in case of death of karta. However, sec. 159 is applicable on the individual income of the karta.

Executors [Sec. 168]

8.4

- The income of the estate of deceased person shall be chargeable to tax in the hands of the executor:

  (a) if there is only one executor, then, as if the executor were an individual; or

  (b) if there are more executors than one, then, as if the executors were an association of persons;

  and for the purposes of this Act, the executor shall be deemed to be resident or non-resident according as the deceased person was a resident or non-resident during the previous year in which his death took place.

- The assessment of an executor shall be made separately from any assessment that may be made on him in respect of his own income.
- Separate assessments shall be made on the total income of each completed previous year (or part thereof) as is included in the period from the date of the death to the date of complete distribution to the beneficiaries of the estate according to their several interests.
- In computing the total income of any previous year, any income of the estate of that previous year distributed to (or applied to the benefit of) any specific legatee of the estate during that previous year shall be excluded; but the income so excluded shall be included in the total income of the previous year of such specific legatee.
- Executor includes an administrator or other person administering the estate of a deceased person.
- An executor in respect of tax paid or payable by him shall be recovered by him from the estate or from the beneficiaries [Sec. 169]

Representative Assessee [Sec. 160]

8.5

Representative assessee means:

	In respect of the income	Representative Assessee
	of a non-resident specified in Sec. 9(1)	Agent of the non-resident, including a person who is treated as an agent u/s 163
	of a minor, lunatic or idiot	A guardian or manager who is entitled to receive or is in receipt of such income on behalf of such minor, lunatic or idiot.
	which is received by ➢ the Court of Wards; ➢ the Administrator-General; ➢ the Official Trustee; or ➢ any receiver or manager, appointed by or under any order of a court on behalf of or for the benefit of any person.	Such – ➢ Court of Wards; ➢ Administrator-General; ➢ Official Trustee; or ➢ Receiver or Manager
	which is received by trustee [appointed under a trust declared by a duly executed instrument in writing whether testamentary or otherwise (including any valid wakf deed)] on behalf of or for the benefit of any person	Such trustee or trustees
	which is received receives or entitled to receive by trustee (appointed under an oral trust) on behalf of or for the benefit of any person	Such trustee or trustees

Taxpoint: Every representative assessee shall be deemed to be an assessee.

Liability of representative assessee [Sec. 161]

- Every representative assessee shall be subject to the same duties, responsibilities and liabilities as if the income were income received by or accruing to or in favour of him beneficially. Any assessment shall be deemed to be made upon him in his representative capacity only, and the tax shall be levied upon and recovered from him in like manner and to the same extent as it would be leviable upon & recoverable from the person represented by him.
- Where any person is, in respect of any income, assessable in the capacity of a representative assessee, he shall not, in respect of that income, be assessed under any other provision of this Act.
- Further refer Private Trust

Right of representative assessee to recover tax paid [Sec. 162]

- Every representative assessee who, as such, pays any sum under this Act, shall be entitled to recover the sum so paid from the person on whose behalf it is paid, or to retain out of any moneys that may be in his possession or may come to him in his representative capacity, an amount equal to the sum so paid.
- Any representative assessee who apprehends that he may be assessed as a representative assessee, may retain out of any money payable by him to the person on whose behalf he is liable to pay tax (hereinafter in this section referred to as the principal), a sum equal to his estimated liability.
- In the event of any disagreement between the principal and such representative assessee, such representative assessee may secure from the Assessing Officer a certificate stating the amount to be so retained pending final settlement of the liability, and the certificate so obtained shall be his warrant for retaining that amount.
- The amount recoverable from such representative assessee at the time of final settlement shall not exceed the amount specified in such certificate, except to the extent to which such representative assessee may, at such time, have in his hands additional assets of the principal.

Direct assessment or recovery not barred [Sec. 166]

Nothing shall prevent either the direct assessment of the person on whose behalf or for whose benefit income therein referred to is receivable or the recovery from such person of the tax payable in respect of such income.

Remedies against property in cases of representative assessee [Sec. 167]

The Assessing Officer shall have the same remedies against all property of any kind vested in or under the control or management of any representative assessee as he would have against the property of any person liable to pay any tax, and in as full and ample a manner, whether the demand is raised against the representative assessee or against the beneficiary direct.

Company in Liquidation [Sec. 178]

8.6

- **Every person:**

  a. who is the liquidator of any company which is being wound-up, whether under the orders of a court or otherwise; or

  b. who has been appointed the receiver of any assets of a company, (hereinafter referred to as the liquidator) shall, within 30 days after he has become such liquidator, give notice of his appointment as such to the Assessing Officer who is entitled to assess the income of the company.

- The Assessing Officer shall, after making such inquiries or calling for such information as he may deem fit, notify to the liquidator within 3 months from the date on which he receives notice of the appointment of the liquidator the amount which, in the opinion of the Assessing Officer, would be sufficient to provide for any tax which is then, or is likely thereafter to become, payable by the company.

- The liquidator:

  a. shall not, without the leave of the Chief Commissioner or Commissioner, part with any of the assets of the company or the properties in his hands until he has been notified by the Assessing Officer (*as above*); and

  b. on being so notified, shall set aside an amount equal to the amount notified and, until he so sets aside such amount, shall not part with any of the assets of the company or the properties in his hands.

- However, the liquidator can part with for:

  1. The purpose of the payment of the tax payable by the company or

  2. The purpose of making any payment to secured creditors whose debts are entitled under law to priority of payment over debts due to Government on the date of liquidation or

  3. The purpose of meeting such costs and expenses of the winding-up of the company as are in the opinion of the Chief Commissioner or Commissioner reasonable.

- If the liquidator fails to give the notice or fails to set aside such amount or parts with any of the assets of the company or the properties in his hands in contravention of above provisions, he shall be personally liable for the payment of the tax which the company would be liable to pay.

  - However, the personal liability of the liquidator shall be restricted to the notified amount.

- Where there are more liquidators than one, the obligations and liabilities attached to the liquidator under this section shall attach to all the liquidators jointly and severally.

- The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other law for the time being in force except the provisions of the Insolvency and Bankruptcy Code, 2016.

Liability of directors of private company [Sec. 179]

Where any tax due from a private company -

- in respect of any income of any previous year; or
- from any other company in respect of any income of any previous year during which such other company was a private company cannot be recovered, then, every person who was a director of the private company at any time during the relevant previous year shall be jointly and severally liable for the payment of such tax. However, no such director shall be liable if he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company.

Taxpoint: Tax Due includes penalty, interest or any other sum payable under the Act.

Miscellaneous Provisions

8.7

Exceptions to the general rule that income of a Previous Year is taxed in its Assessment Year

Assessment of persons leaving India [Sec. 174]

- When it appears to the Assessing Officer that any individual may leave India during the current assessment year or shortly after its expiry **and** that he has no present intention of returning to India, the total income of such individual for the period from the expiry of the previous year for that assessment year up to the probable date of his departure from India shall be chargeable to tax in that assessment year.
- The total income of each completed previous year or part of any previous year included in such period shall be chargeable to tax at the rate or rates in force in that assessment year, and separate assessments shall be made in respect of each such completed previous year or part of any previous year.
- The Assessing Officer may estimate the income of such individual for such period or any part thereof, where it cannot be readily determined in the manner provided in this Act.
- For the purpose of making an assessment, the Assessing Officer may serve a notice upon such individual requiring him to furnish, within such time, not being less than 7 days, as may be specified in the notice, a return in the same form and verified in the same manner as a return u/s 142(1)(*i*), setting forth his total income for each previous year and his estimated total income for any part of the previous year and the provisions of this Act shall, so far as may be, and subject to the provisions of this section, apply as if the notice were a notice issued u/s 142(1)(i).

Assessment of AOP or BOI or artificial juridical person formed for shorter period [Sec. 174A]

- Where it appears to the Assessing Officer that any AOP or BOI or an artificial juridical person, formed for a particular purpose is likely to be dissolved in the assessment year in which such AOP, etc. was formed or immediately after such assessment year, the total income of such association, etc. for the period from the expiry of the previous year for that assessment year up to the date of its dissolution shall be chargeable to tax in that assessment year.
- Proceedings (as given in sec. 174 in the case of persons leaving India) shall be applicable.

Assessment of persons likely to transfer property to avoid tax [Sec. 175]

- If it appears to the Assessing Officer during any current assessment year that any person is likely to charge, sell, transfer, dispose of or otherwise part with any of his assets with a view to avoiding payment of any liability under the provisions of this Act, the total income of such person for the period from the expiry of the previous year for that assessment year to the date when the Assessing Officer commences proceedings under this section shall be chargeable to tax in that assessment year
- Proceedings (as given in sec. 174 in the case of persons leaving India) shall be applicable.

Discontinued business [Sec. 176]

- Where any business or profession is discontinued in any assessment year, the income of the period from the expiry of the previous year for that assessment year up to the date of such discontinuance may, at the ***discretion*** of the Assessing Officer, be charged to tax in that assessment year.
- The total income of each completed previous year or part of any previous year included in such period shall be chargeable to tax at the rate or rates in force in that assessment year, and separate assessments shall be made in respect of each such completed previous year or part of any previous year.
- Any person discontinuing any business or profession shall give to the Assessing Officer notice of such discontinuance within 15 days thereof.
- Where any business is discontinued in any year, any sum received after the discontinuance shall be deemed to be the income of the recipient and charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the person who carried on the business had such sum been received before such discontinuance. [Sec. 176(3A)]
- Where any profession is discontinued in any year on account of the cessation of the profession by, or the retirement or death of, the person carrying on the profession, any sum received after the discontinuance shall be deemed to be the income of the recipient and charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the aforesaid person had it been received before such discontinuance. [Sec. 176(4)]
- Where an assessment is to be made under the provisions of this section, the Assessing Officer may serve on the person whose income is to be assessed or, in the case of a firm, on any person who was a partner of such firm at the time of its discontinuance or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice u/s 142(1)(*i*) and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued u/s 142(1)(i).

Association dissolved or business discontinued [Sec. 177]

- Where any business or profession carried on by an association of persons has been discontinued or where an association of persons is dissolved, the Assessing Officer shall make an assessment of the total income of the association of persons as if no such discontinuance or dissolution had taken place, and all the provisions of this Act, including the provisions relating to the levy of a penalty or any other sum chargeable under any provision of this Act shall apply, so far as may be, to such assessment.
- If the Assessing Officer or the Commissioner (Appeals) in the course of any proceeding under this Act in respect of any such association of persons is satisfied that the association of persons was guilty of any of the acts specified in Chapter XXI (i.e., *penalties*), he may impose or direct the imposition of a penalty in accordance with the provisions of that Chapter.
- Every person who was at the time of such discontinuance or dissolution a member of the association of persons, and the legal representative of any such person who is deceased, shall be jointly and severally liable for the amount of tax, penalty or other sum payable, and all the provisions of this Act, so far as may be, shall apply to any such assessment or imposition of penalty or other sum.
- Where such discontinuance or dissolution takes place after any proceedings in respect of an assessment year have commenced, the proceedings may be continued against above persons from the stage at which the proceedings stood at the time of such discontinuance or dissolution, and all the provisions of this Act shall, so far as may be, apply accordingly.

Mode of taking or accepting certain loans, deposits and specified sum [Sec. 269SS]

No person shall take or accept from any other person (herein referred to as the depositor), any loan or deposit or any specified sum, otherwise than by an account payee cheque or account payee bank draft or use of electronic clearing system through a bank account or through other prescribed electronic modes, if:

a) the amount of such loan or deposit or specified sum or the aggregate amount of such loan, deposit and specified sum; or

b) on the date of taking or accepting such loan or deposit or specified sum, any loan or deposit or specified sum taken or accepted earlier by such person from the depositor is remaining unpaid (whether repayment has fallen due or not), the amount or the aggregate amount remaining unpaid; or

c) the amount or the aggregate amount referred to in (a) together with the amount or the aggregate amount referred to in (b), is ₹ 20,000 or more.

Taxpoint

- Loan or deposit means loan or deposit of money.
- Specified sum means any sum of money receivable, whether as advance or otherwise, in relation to transfer of an immovable property, whether or not the transfer takes place.
- However, in the case of any deposit or loan where,—
  a. such deposit is accepted by a primary agricultural credit society or a primary co-operative agricultural and rural development bank from its member; or
  b. such loan is taken from a primary agricultural credit society or a primary co-operative agricultural and rural development bank by its member
  - then, the limit of ₹ 20,000 shall be increased to ₹ 2,00,000

Exception 1

The provisions shall not apply to any loan or deposit or specified sum taken or accepted from, or any loan or deposit or specified sum taken or accepted by:

a. the Government;

b. any banking company, post office savings bank or co-operative bank;

c. any corporation established by a Central, State or Provincial Act;

d. any Government company as defined in sec. 2(45) of the Companies Act, 2013;

e. such other notified institution, association or body or class of institutions, associations or bodies.

Taxpoint: The reasons for notifying such institution, etc. should be recorded in writing

Exception 2

The provisions shall not apply to any loan or deposit or specified sum, where both, receiver and giver, are having agricultural income and neither of them has any income chargeable to tax

Penalty [Sec. 271D]

If a person takes or accepts any loan or deposit or specified sum in contravention of the provisions of sec. 269SS, he shall be liable to pay, by way of penalty, a sum equal to the amount of the loan or deposit or specified sum so taken or accepted. Such penalty shall be imposed by the Joint Commissioner.

Mode of undertaking transactions [Sec. 269ST]

No person shall receive an amount of ₹ 2,00,000 or more:

a. in aggregate from a person in a day; or

b. in respect of a single transaction; or

c. in respect of transactions relating to one event or occasion from a person,

otherwise than by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account or through other prescribed electronic modes.

Exception

The provisions shall not apply to:

i. any receipt by:
   a) Government;
   b) any banking company, post office savings bank or co-operative bank;

ii. transactions of the nature referred to in sec. 269SS

iii. such other persons or class of persons or receipts, which the Central Government may notify.

- The Central Government vide Notification No. 28/2017 dated 05-04-2017 & 57/2017 dated 03-07-2017 has specified following receipt on which the provision is not applicable:
  a) receipt by a business correspondent on behalf of a banking company or co-operative bank, in accordance with the guidelines issued by the Reserve Bank of India;
  b) receipt by a white label automated teller machine operator from retail outlet sources on behalf of a banking company or co-operative bank, in accordance with the authorisation issued by the Reserve Bank of India under the Payment and Settlement Systems Act, 2007
  c) receipt from an agent by an issuer of pre-paid payment instruments, in accordance with the authorisation issued by the Reserve Bank of India under the Payment and Settlement Systems Act, 2007
  d) receipt by a company or institution issuing credit cards against bills raised in respect of one or more credit cards;
  e) receipt which is not includible in the total income u/s 10(17A)
  f) receipt by any person from any banking company, post office savings bank or co-operative bank;

Clarification vide Circular No. 22/2017 dated 03-07-2017

In respect of receipt in the nature of repayment of loan by Non-Banking Financial Companies (NBFCs) and Housing Finance Companies (HFCs), the receipt of one instalment of loan repayment in respect of a loan shall constitute a 'single transaction' as specified in sec. 269ST(b) and all the instalments paid for a loan shall not be aggregated for the purposes of determining applicability of the provisions sec. 269ST.

Penalty [Sec. 271DA]

If a person receives any sum in contravention of the provisions of sec. 269ST, he shall be liable to pay, by way of penalty, a sum equal to the amount of such receipt. However, no penalty shall be imposable if such person proves that there were good and sufficient reasons for the contravention.

Taxpoint: Such penalty shall be imposed by the Joint Commissioner.

Mode of repayment of certain loans or deposits [Sec. 269T]

No branch of a banking company or a co-operative bank and no other company or co-operative society and no firm or other person shall repay any loan or deposit made with it or any specified advance received by it otherwise than by an account payee cheque or account payee bank draft drawn in the name of the person who has made the loan or deposit or paid the specified advance, or by use of electronic clearing system through a bank account if:

a. the amount of the loan or deposit or specified advance together with the interest, if any, payable thereon, or

b. the aggregate amount of the loans or deposits held by such person with the branch of the banking company or co-operative bank or, as the case may be, the other company or co-operative society or the firm, or other person either in his own name or jointly with any other person on the date of such repayment together with the interest, if any, payable on such loans or deposits, or

c. the aggregate amount of the specified advances received by such person either in his own name or jointly with

any other person on the date of such repayment together with the interest, if any, payable on such specified advances,

- is ₹ 20,000 or more:

Taxpoint:

- Loan or deposit means any loan or deposit of money which is repayable after notice or repayable after a period and, in the case of a person other than a company, includes loan or deposit of any nature.
- Specified advance means any sum of money in the nature of advance, by whatever name called, in relation to transfer of an immovable property, whether or not the transfer takes place.
- Where the repayment is by a branch of a banking company or co-operative bank, such repayment may also be made by crediting the amount of such loan or deposit to the savings bank account or the current account (if any) with such branch of the person to whom such loan or deposit has to be repaid.
- However, in the case of any deposit or loan where,—

  a. such deposit is paid by a primary agricultural credit society or a primary co-operative agricultural and rural development bank to its member; or

  b. such loan is repaid to a primary agricultural credit society or a primary co-operative agricultural and rural development bank by its member

  - then, the limit of ₹ 20,000 shall be increased to ₹ 2,00,000

Exception

The provision of this section shall not apply to repayment of any loan or deposit or specified advance taken or accepted from:

i. Government;

ii. any banking company, post office savings bank or co-operative bank;

iii. any corporation established by a Central, State or Provincial Act;

iv. any Government company;

v. such other notified institution, association or body or class of institutions, associations or bodies.

Taxpoint: The reasons for notifying such institution, etc. should be recorded in writing

Penalty [Sec. 271E]

If a person repays any loan or deposit or specified advance referred to in sec. 269T otherwise than in accordance with the provisions of that section, he shall be liable to pay, by way of penalty, a sum equal to the amount of the loan or deposit or specified advance so repaid.

Taxpoint: Such penalty shall be imposed by the Joint Commissioner.

Acceptance of payment through prescribed electronic modes [Sec. 269SU]

Applicable to: Person carrying on business having total sales / turnover / gross receipts in excess of ₹ 50 crores during the immediately preceding previous year.

Compliance: Such person is required to provide facility for accepting payment through prescribed electronic modes, in addition to the facility for other electronic modes, of payment, if any, being provided by such person

Penalty: If such person fails to provide such facility then he is liable to pay penalty of ₹ 5,000 for every day during which such failure continues – [Sec. 271DB]

Taxpoint:

- No such penalty shall be imposable if such person proves that there were good and sufficient reasons for such failure.
- Such penalty shall be imposed by the Joint Commissioner of Income-tax

Service of notice when family is disrupted or firm, etc., is dissolved [Sec. 283]

- After a finding of total partition has been recorded by the Assessing Officer u/s 171 in respect of any Hindu family, notices under this Act in respect of the income of the Hindu family shall be served on the person who was the last manager of the Hindu family, or, if such person is dead, then on all adults who were members of the Hindu family immediately before the partition.
- Where a firm or other association of persons is dissolved, notices under this Act in respect of the income of the firm or association may be served on any person who was a partner (not being a minor) or member of the association, as the case may be, immediately before its dissolution.

Service of notice in the case of discontinued business [Sec. 284]

Where an assessment is to be made u/s 176, the Assessing Officer may serve on the person whose income is to be assessed, or, in the case of a firm or an association of persons, on any person who was a member of such firm or association at the time of its discontinuance or, in the case of a company, on the principal officer thereof, a notice containing all or any of the requirements which may be included in a notice u/s 139(2), and the provisions of this Act shall, so far as may be, apply accordingly as if the notice were a notice issued under that section.

Submission of statement by a non-resident having liaison office [Sec. 285]

Every person, being a non-resident having a liaison office in India set up in accordance with the guidelines issued by the Reserve Bank of India under the Foreign Exchange Management Act, 1999, shall, in respect of its activities in a financial year, prepare and deliver to the Assessing Officer having jurisdiction, within 60 days from the end of such financial year, a statement in Form – 49C and containing such particulars as may be prescribed.

Furnishing of information or documents by an Indian concern in certain cases [Sec. 285A]

Where any share of, or interest in, a company or an entity registered or incorporated outside India derives, directly or indirectly, its value substantially from the assets located in India, as referred to in *Explanation 5* to sec. 9(1)(i) and such company or, as the case may be, entity, holds, directly or indirectly, such assets in India through, or in, an Indian concern, then, such Indian concern shall, for the purposes of determination of any income accruing or arising in India u/s 9(1)(i), furnish within the prescribed period to the prescribed income-tax authority the information or documents, in such manner (Form – 49D), as may be prescribed

Submission of statements by producers of cinematograph films [Sec. 285B]

Any person carrying on the production of a cinematograph film or engaged in any specified activity, or both, during the financial year, shall, in respect of such production or specified activity, furnish within the prescribed period, a statement in the prescribed form to the prescribed income-tax authority in the prescribed manner, containing particulars of all payments of over ₹50,000 in the aggregate made by him or due from him to each such person as is engaged by him in such production or specified activity.

"Specified Activity" means any event management, documentary production, production of programmes for telecasting on television or over the top platforms or any other similar platform, sports event management, other performing arts or any other notified activity

Publication of information respecting assessees in certain cases [Sec. 287]

- If the Central Government is of opinion that it is necessary or expedient in the public interest to publish the names of any assessees and any other particulars relating to any proceedings or prosecutions under this Act in respect of such assessees, it may cause to be published such names and particulars in such manner as it thinks fit.
- No publication under this section shall be made in relation to any penalty imposed under this Act until the time for presenting an appeal to the Commissioner (Appeals) has expired without an appeal having been presented or the appeal, if presented, has been disposed of.
- In the case of a firm, company or other association of persons, the names of the partners of the firm, directors,

managing agents, secretaries and treasurers, or managers of the company, or the members of the association, as the case may be, may also be published if, in the opinion of the Central Government, the circumstances of the case justify it.

Appearance by registered valuer in certain matters [Sec. 287A]

Any assessee who is entitled or required to attend before any income-tax authority or the Appellate Tribunal in connection with any matter relating to the valuation of any asset, otherwise than when required u/s 131 to attend personally for examination on oath or affirmation, may attend by a registered valuer.

Appearance by authorised representative [Sec. 288]

Any assessee who is entitled or required to attend before any income-tax authority or the Appellate Tribunal in connection with any proceeding under this Act otherwise than when required u/s 131 to attend personally for examination on oath or affirmation, may, subject to the other provisions of this section, attend by an authorised representative.

- Authorised representative means a person authorised by the assessee in writing to appear on his behalf, being:
  - i. a person related to the assessee in any manner, or a person regularly employed by the assessee; or
  - ii. any officer of a Scheduled Bank with which the assessee maintains a current account or has other regular dealings; or
  - iii. any legal practitioner who is entitled to practise in any civil court in India; or
  - iv. an accountant; or
  - v. any person who has passed any accountancy examination recognised in this behalf by the Board; or
    - The following accountancy examinations are recognised [Rule 50]:
      - a. The National Diploma in Commerce awarded by the All-India Council for Technical Education under the Ministry of Education, New Delhi, provided the diploma-holder has taken Advanced Accountancy and Auditing as an elective subject for the Diploma Examination.
      - b. Government Diploma in Company Secretaryship awarded by the Department of Company Affairs, under the Ministry of Industrial Development and Company Affairs, New Delhi.
      - c. Final Examination of the Institute of Company Secretaries of India, New Delhi.
      - d. The Final Examination of the Institute of Cost and Works Accountants of India constituted under the Cost and Works Accountants Act, 1959
      - e. The Departmental Examinations conducted by or on behalf of the Central Board of Direct Taxes for Assessing Officers, Class I or Group 'A', Probationers, or for Assessing Officers, Class II or Group 'B', Probationers, or for promotion to the post of Assessing Officers, Class II or Group 'B', as the case may be.
      - f. The Revenue Audit Examination for Section Officers conducted by the Office of the Comptroller and Auditor General of India.]
  - vi. any person who has acquired such educational qualifications as the Board may prescribe for this purpose; or
    - A degree in Commerce or Law conferred by any of the following Universities are prescribed as educational qualifications [Rule 51]:
      - a. Any Indian University
      - b. Rangoon University.
      - c. English and Welsh Universities: The Universities of Birmingham, Bristol, Cambridge, Durham, Leeds, Liverpool, London, Manchester, Oxford, Reading, Sheffield and Wales.

d. Scottish Universities: The Universities of Aberdeen, Edinburgh, Glasgow and St. Andrews.

e. Irish Universities: The Universities of Dublin (Trinity College), the Queen's University, Belfast and the National University of Dublin.

f. Any Pakistan University incorporated by any law for the time being in force.

vii. any person who, before the coming into force of this Act in the Union territory of Dadra and Nagar Haveli, Goa, Daman and Diu, or Pondicherry, attended before an income-tax authority in the said territory on behalf of any assessee otherwise than in the capacity of an employee or relative of that assessee.

viii. any other person as may be prescribed

- Accountant means a chartered accountant as defined in the Chartered Accountants Act, 1949 who holds a valid certificate of practice, but does not include [except for the purposes of representing the assessee]:

a. in case of an assessee, being a company, the person who is not eligible for appointment as an auditor of the said company in accordance with the provisions of sec. 141(3) of the Companies Act, 2013; or

b. in any other case:

i. the assessee himself or in case of the assessee, being a firm or association of persons or Hindu undivided family, any partner of the firm, or member of the association or the family;

ii. in case of the assessee, being a trust or institution, any person referred to in sec. 13(3)(a), (b), (c) and (cc);

iii. the person who is competent to verify the return u/s 139 in accordance with the provisions of sec. 140;

iv. any relative of any of aforesaid persons;

v. an officer or employee of the assessee;

vi. an individual who is a partner, or who is in the employment, of an officer or employee of the assessee;

vii. an individual who, or his relative or partner:

I. is holding any security of, or interest in, the assessee

- The relative may hold security or interest in the assessee of the face value not exceeding ₹ 1,00,000

II. is indebted to the assessee

- The relative may be indebted to the assessee for an amount not exceeding ₹ 1,00,000;

III. has given a guarantee or provided any security in connection with the indebtedness of any third person to the assessee.

- The relative may give guarantee or provide any security in connection with the indebtedness of any third person to the assessee for an amount not exceeding ₹ 1,00,000;

viii. a person who, whether directly or indirectly, has business relationship with the assessee of such nature as may be prescribed;

➢ Business relationship shall be construed as any transaction entered into for a commercial purpose, other than,:

a) commercial transactions which are in the nature of professional services permitted to be rendered

by an auditor or audit firm under the Act and the Chartered Accountants Act, 1949 and the rules or the regulations made under those Acts;

b) commercial transactions which are in the ordinary course of business of the company at arm's length price - like sale of products or services to the auditor, as customer, in the ordinary course of business, by companies engaged in the business of telecommunications, airlines, hospitals, hotels and such other similar businesses – [Rule 51A]

ix. a person who has been convicted by a court of an offence involving fraud and a period of 10 years has not elapsed from the date of such conviction.

- No person shall be qualified to represent an assessee:

Person, who has been	Disqualification for
Dismissed or removed from Government service after 01-04-1938	All times
Convicted of an offence connected with any income-tax proceeding or on whom a penalty has been imposed under this Act, other than a penalty imposed on him u/s 271(1)(ii) or 272A(1)(d)	Such time as the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner may by order determine
An insolvent	The period during which the insolvency continues
Convicted by a court for an offence involving fraud	A period of 10 years from the date of conviction

- If any person who is a legal practitioner or an accountant is found guilty of misconduct in:

a. his professional capacity by any authority entitled to institute disciplinary proceedings against him, an order passed by that authority shall have effect in relation to his right to attend before an income-tax authority as it has in relation to his right to practise as a legal practitioner or accountant, as the case may be;

b. connection with any income-tax proceedings by the Chief Commissioner or Commissioner having requisite jurisdiction may direct that he shall thenceforth be disqualified to represent an assessee

- Such order or direction shall be subject to the following conditions:

a. no such order or direction shall be made in respect of any person unless he has been given a reasonable opportunity of being heard;

b. any person against whom any such order or direction is made may, within 1 month of the making of the order or direction, appeal to the Board to have the order or direction cancelled; and

c. no such order or direction shall take effect until the expiration of 1 month from the making thereof, or, where an appeal has been preferred, until the disposal of the appeal.

- Relative in relation to an individual, means:

a. spouse of the individual;

b. brother or sister of the individual;

c. brother or sister of the spouse of the individual;

d. any lineal ascendant or descendant of the individual;

e. any lineal ascendant or descendant of the spouse of the individual;

f. spouse of a person referred to in (b) to (e);

g. any lineal descendant of a brother or sister of either the individual or the spouse of the individual.

Exercise

Multiple Choice Questions

1. As per section 178(3), the _____ of a company has to intimate the tax authority before he parts with any of the assets of the company or the properties in his hands and has to set aside the amount if any intimated to him by the tax authorities.
   A. Managing Director
   B. Manager
   C. Chartered Accountant
   D. Liquidator
2. Equalisation levy shall be payable @ __
   A. 6%
   B. 5%
   C. 2%
   D. None of the above

[Answer:1 – D, 2 – A]

Short Essay Type Questions

1. When equalisation levy is applicable?
2. Write a brief note on tonnage tax scheme.
3. Who is termed as representative assessee u/s 160?
4. What is the duty of the liquidator u/s 178?

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Income Computation and Disclosure Standards (ICDS)

9

This Module includes:

Income Computation and Disclosure Standards (ICDS)

SLOB Mapped against the Module:

1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
2. To acquire knowledge of various compliance related provisions of taxation laws and attain skills for their proactive compliance in business operations to avoid any eventual risk exposure.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify the applicability of the standards
- Understand the requirement of the standards
- Analyse the impact of such standards in computing income and tax liability
- Appreciate the various disclosures.

Introduction

9

…. for the purposes of ascertaining profits and gains, the ordinary principles of commercial accounting should be applied, so long as they do not conflict with any express provision of the relevant statutes.

Croom-Johnson, J

Commissioners of Inland Revenue -vs.- Cock, Russell & Co. Ltd.

In exercise of the powers conferred by sec. 145(2), the Central Government has notified (vide Notification No. 87/2016 dated 29-09-2016) the income computation and disclosure standards (ICDS). The rationale behind issuing ICDS is to lessen the uncertainty of alternative accounting treatment due to flexibility offered by Accounting Standards (AS) & also to reduce litigation that crops up when the stand taken by income-tax authorities is not in alignment with the AS

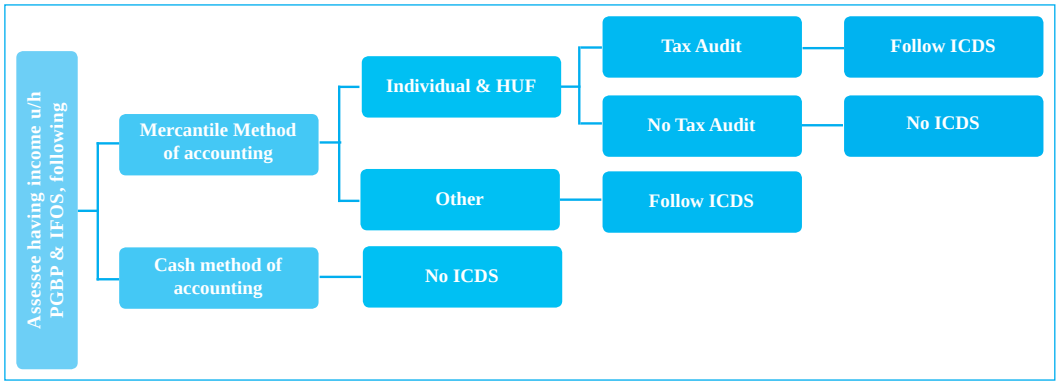
Applicability

The standards are required to be followed:

- by all assessee (other than an individual or a Hindu undivided family who is not required to get his accounts of the previous year audited u/s 44AB)
- who follows the mercantile system of accounting,
- for the purposes of computation of income chargeable to income-tax under the head "Profits and gains of business or profession" or "Income from other sources".

Taxpoint

- The standards are not for the purpose of maintenance of books of account. The standards are for computation of income under aforesaid heads of income only.
- In case of conflict between the provision of the Income-tax Act and ICDS, the provision of the Act shall prevail to that extent.



ICDS

9.1

Following ICDS have been notified:

ICDS	Name of the ICDS	Corresponding	
		AS	Ind-AS
ICDS I	Accounting Policies	1	1 & 8
ICDS II	Valuation of Inventories	2	2
ICDS III	Construction Contracts	7	11
ICDS IV	Revenue Recognition	9	18
ICDS V	Tangible Fixed Assets	10	16
ICDS VI	Effects of change in Foreign Exchange Rates	11	21
ICDS VII	Government Grants	12	20
ICDS VIII	Securities	13	32
ICDS IX	Borrowing Costs	16	23
ICDS X	Contingent Assets	29	37

ICDS I: Accounting Policies

9.2

Accounting Policies

- Accounting policies adopted by a person shall be such so as to represent a true and fair view of the state of affairs and income of the business, profession or vocation.

  Taxpoint: Accounting policies should be such that discloses 'true and fair view' and not —'true and correct'.

- The treatment and presentation of transactions and events shall be governed by their substance and not merely by the legal form.

- Marked to market loss or an expected loss shall not be recognised unless the recognition of such loss is in accordance with the provisions of any other Income Computation and Disclosure Standard.

Fundamental Accounting Assumptions

- The fundamental accounting assumptions i.e., Going Concern, Consistency and Accrual are assumed as followed. No specific disclosure is required, if these assumptions are followed, however, if such assumption are not followed, the fact shall be disclosed.

  Taxpoint: ICDS does not recognize materiality as an accounting policy

Change in Accounting Policies

- An accounting policy shall not be changed without reasonable cause.

  Taxpoint: The word 'reasonable cause' is not defined in the ICDS

Disclosure of Accounting Policies

- All significant accounting policies adopted by a person shall be disclosed.

- Any change in an accounting policy which has a material effect shall be disclosed (with quantum of the effect, if ascertainable). Where such amount is not ascertainable, the fact shall be indicated.

- Disclosure of accounting policies or of changes therein cannot remedy a wrong or inappropriate treatment of the item.

Comparative study of ICDS with respective AS

Basis of difference	AS 1	ICDS I
Concept of Prudence	Provision is made for all known liabilities and losses on best estimate basis	Marked to market (MTM) loss or an expected loss shall not be recognised unless permitted by any other ICDS
	Anticipated profits are not recognized	ICDS silent on recognition of anticipated profits
Materiality	Materiality should be considered while selecting and applying accounting policy	Concept of Materiality is not recognized in ICDS
Change in accounting policy	Change in accounting policy permitted if (a) required by statute; (b) required for compliance of AS; (c) change results in more appropriate presentation of financial statements	Accounting policies shall not be changed without a "reasonable cause"
Disclosure of change in accounting policy	Required in period of change, if impact is not material in current period but material in later periods	Required in period of change and also required in first year in which change has material effect, if impact is not material in current period but material in later periods.

ICDS II: Valuation of Inventories

9.3

Scope

- This Standard shall be applied for valuation of inventories, except
  - i. Work-in-progress arising under 'construction contract'
  - ii. Work-in-progress which is dealt with by other Standard
  - iii. Shares, debentures and other financial instruments held as stock-in-trade[3]
  - iv. Producers' inventories of livestock, agriculture and forest products, mineral oils, ores and gases to the extent that they are measured at net realisable value
  - v. Machinery spares, which can be used only in connection with a tangible fixed asset and their use is expected to be irregular[4]

Measurement

- Inventories shall be valued at cost, or net realisable value, whichever is lower.
  - *Net realisable value* is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.
  - In case of dissolution of a partnership firm or association of person or body of individuals, notwithstanding whether business is discontinued or not, the inventory on the date of dissolution shall be valued at the net realisable value. The provision is contrary to law settled by the Apex court in the case of Sakti Trading Co.

Cost of Inventories

- Cost of inventories shall comprise of all costs of purchase, costs of services, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.
  - The *costs of purchase* shall consist of purchase price including duties and taxes, freight inwards and other expenditure directly attributable to the acquisition. Trade discounts, rebates and other similar items shall be deducted in determining the costs of purchase
  - The *costs of services* shall consist of labour and other costs of personnel directly engaged in providing the service including supervisory personnel and attributable overheads.
  - The *costs of conversion* of inventories shall include costs directly related to the units of production and a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods.

1 Refers ICDS on Securities
2 Refers ICDS on Tangible Fixed Assets

- Other costs shall be included in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.
- Interest and other borrowing costs shall not be included in the costs of inventories, unless they meet the criteria for recognition of interest as a component of the cost as specified in the Income Computation and Disclosure Standard on borrowing costs.
- In determining the cost of inventories, the following costs shall be excluded
  a. Abnormal amounts of wasted materials, labour, or other production costs;
  b. Storage costs, unless those costs are necessary in the production process prior to a further production stage;
  c. Administrative overheads that do not contribute to bringing the inventories to their present location and condition;
  d. Selling costs.

Cost Formulae

- The standard recognizes 3 cost formulae viz. (i) Specific Identification Method; (ii) First-in-First-Out Method (FIFO); (iii) Weighted Average Method

Change of Method of Valuation of Inventory

- The method of valuation of inventories once adopted by a person in any previous year shall not be changed without reasonable cause

Disclosure

- Following shall be disclosed:
  a. the accounting policies adopted in measuring inventories including the cost formulae used; and
  b. the total carrying amount of inventories and its classification appropriate to a person.

Comparative study of ICDS with respective AS

Basis of difference	AS 2	ICDS II
Valuation of service inventory	No specific provision	NA
Opening inventory	No specific provision	➢ Value of opening inventory of a business shall be the same as the value of inventory at the end of the immediately preceding financial year ➢ In case of commencement of business, Cost of inventory on the day of commencement of business will be opening inventory
Change in method of inventory valuation	Change permitted if (a) required by statute; (b) required for compliance of AS; (c) change results in more appropriate presentation of financial statements	Method of valuation once adopted shall not be changed without "reasonable cause"
Inventory valuation in case of certain dissolutions	No specific provision	In case of partnership firm, AOP or BOI inventory on the date of dissolution shall be valued at NRV, whether or not business is discontinued

ICDS III: Construction Contracts

9.4

Scope

- The Standard should be applied in determination of income for a construction contract of a contractor.
  - Construction contract is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use and includes:
    - (i) contract for the rendering of services which are directly related to the construction of the asset, for example, those for the services of project managers and architects;
    - (ii) contract for destruction or restoration of assets, and the restoration of the environment following the demolition of assets.
- Construction contracts are formulated in a number of ways which are classified as fixed price contracts and cost plus contracts.
  - Fixed price contract is a construction contract in which the contractor agrees to a fixed contract price, or a fixed rate per unit of output, which may be subject to cost escalation clauses.
  - Cost plus contract is a construction contract in which the contractor is reimbursed for allowable or otherwise defined costs, plus a mark up on these costs or a fixed fee.

Contract Revenue

- Contract revenue shall be recognised when there is reasonable certainty of its ultimate collection.
- Contract revenue shall comprise of:

a) the initial amount of revenue agreed in the contract, including retentions; and

- Retentions are amounts of progress billings which are not paid until the satisfaction of conditions specified in the contract for the payment of such amounts or until defects have been rectified.
- Progress billings are amounts billed for work performed on a contract whether or not they have been paid by the customer.

b) variations in contract work, claims and incentive payments:

i. to the extent that it is probable that they will result in revenue; and

ii. they are capable of being reliably measured.

Contract Costs

- Contract costs shall comprise of:
  a) costs that relate directly to the specific contract;
  b) costs that are attributable to contract activity in general and can be allocated to the contract;
  c) such other costs as are specifically chargeable to the customer under the terms of the contract; and
  d) allocated borrowing costs in accordance with the ICDS on Borrowing Costs.
- These costs shall be reduced by any incidental income, not being in the nature of interest, dividends or capital gains, that is not included in contract revenue.
- Costs that cannot be attributed to any contract activity or cannot be allocated to a contract shall be excluded from the costs of a construction contract.

Recognition of Contract Revenue and Expenses

- Contract revenue and contract costs associated with the construction contract should be recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the reporting date.
- The recognition of revenue and expenses by reference to the stage of completion of a contract is referred to as the percentage of completion method. Under this method, contract revenue is matched with the contract costs incurred in reaching the stage of completion, resulting in the reporting of revenue, expenses and profit which can be attributed to the proportion of work completed.

Changes in Estimates

- The percentage of completion method is applied on a cumulative basis in each previous year to the current estimates of contract revenue and contract costs. Where there is change in estimates, the changed estimates shall be used in determination of the amount of revenue and expenses in the period in which the change is made and in subsequent periods.

Disclosure

- A person shall disclose:
  a. the amount of contract revenue recognised as revenue in the period; and
  b. the methods used to determine the stage of completion of contracts in progress.
- A person shall disclose the following for contracts in progress at the reporting date:
  a. amount of costs incurred and recognised profits (less recognised losses) upto the reporting date;
  b. the amount of advances received; and
  c. the amount of retentions.

Comparative study of ICDS with respective AS

Basis of difference	AS 7	ICDS III
Recognition of contract revenue	Contract revenue is required to be recognized if it is possible to reliably measure the outcome of a contract	- The criteria of 'reliable measurement of outcome of contract' omitted – Recognized as per provision of ICDS – III

Basis of difference	AS 7	ICDS III
Retention money	Silent on treatment of accrual of income	Retention money is required to be considered as part of contract revenue and revenue to be recognized on POCM basis
Allowability of losses including probable / expected loss	Losses fully allowable irrespective of commencement, stage of completion and expected profits from other independent contracts	- Losses not allowable unless actually incurred and only on POCM basis - ICDS on accounting policies also does not permit recognition of foreseeable loss
Contract Work in progress recognition	Contract cost which relates to future activity shall be recognized as an asset only if recoverability is probable	Contract cost is to be recognized as an asset
Early stage of contract – Non-recognition of revenue	– Revenue is to be recognized only to the extent of recoverable costs – No profit is to be recognized during early stages of contract	Same as AS, however ICDS objectively defines early stage as not to exceed beyond 25%
Pre-construction incidental income	Contract cost may be reduced by any incidental income that is not included in contract revenue	Contract cost shall be reduced by any incidental income (except interest, dividend and capital gains) that is not included in contract revenue

ICDS IV: Revenue Recognition

9.5

Scope

- The Standard deals with the bases for recognition of revenue arising in the course of the ordinary activities of a person from:
  a) the sale of goods;
  b) the rendering of services;
  c) the use by others of the person's resources yielding interest, royalties or dividends.
- Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of a person from the sale of goods, from the rendering of services, or from the use by others of the person's resources yielding interest, royalties or dividends. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.
- The Standard does not deal with the aspects of revenue recognition which are dealt with by other ICDS.

Sale of Goods

- Revenue from sales transactions should be recognized when the following conditions are fulfilled -
  a) The seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer;
  b) The seller retains no effective control of the goods transferred to a degree usually associated with ownership;
  c) There is reasonable certainty of its ultimate collection.

Rendering of Services

- Revenue from service transactions shall be recognised by the percentage completion method.
- Under this method, revenue from service transactions is matched with the service transaction costs incurred in reaching the stage of completion, resulting in the determination of revenue, expenses and profit which can be attributed to the proportion of work completed.
- However, when services are provided by an indeterminate number of acts over a specific period of time, revenue may be recognised on a straight line basis over the specific period.
- Revenue from service contracts with duration of not more than 90 days may be recognised when the rendering of services under that contract is completed or substantially completed.

Interest

- Interest shall accrue on the time basis determined by the amount outstanding and the rate applicable.

- Interest on refund of any tax, duty or cess shall be deemed to be the income of the previous year in which such interest is received.
- Discount or premium on debt securities held is treated as though it were accruing over the period to maturity.

Royalty

- Royalties shall accrue in accordance with the terms of the relevant agreement and shall be recognised on that basis unless, having regard to the substance of the transaction, it is more appropriate to recognise revenue on some other systematic and rational basis.

Dividend

- Dividends are recognised in accordance with the provisions of the Act

Disclosure

- Following disclosures shall be made in respect of revenue recognition:
  a) in a transaction involving sale of goods, total amount not recognised as revenue during the previous year due to lack of reasonably certainty of its ultimate collection along with nature of uncertainty;
  b) the amount of revenue from service transactions recognised as revenue during the previous year;
  c) the method used to determine the stage of completion of service transactions in progress; and
  d) for service transactions in progress at the end of previous year:
     i. amount of costs incurred and recognised profits (less recognised losses) upto end of previous year;
     ii. the amount of advances received; and
     iii. the amount of retentions.

Comparative study of ICDS with respective AS

Basis of difference	AS 9	ICDS IV
Postponement of revenue recognition	Revenue recognition to be postponed if significant uncertainty exists on measurability and collect ability of revenue from sale of goods, rendering of services, interest, royalties and dividends	Revenue to be recognized only if there is reasonable certainty of its ultimate collection from sale of goods and rendering of services
Method of revenue recognition for service contracts	- Proportionate completion method or - Completed service contract method	- Mandatory to recognize revenue based on Percentage completion method - ICDS requires application of ICDS III on Construction contracts for recognition of such revenue on mutatis mutandis basis
Disclosure requirement	Disclose circumstances in which revenue recognition has been postponed pending significant uncertainties.	Disclosures for amounts not recognized as revenue due to lack of reasonable certainty of its ultimate collection along with nature of uncertainty

ICDS V: Tangible Fixed Assets

9.6

Scope

- This Income Computation and Disclosure Standard deals with the treatment of tangible fixed assets.
  - *Tangible fixed asset* is an asset being land, building, machinery, plant or furniture held with the intention of being used for the purpose of producing or providing goods or services and is not held for sale in the normal course of business.
  - Stand-by equipment and servicing equipment are to be capitalised. Machinery spares shall be charged to the revenue as and when consumed. When such spares can be used only in connection with an item of tangible fixed asset and their use is expected to be irregular, they shall be capitalised.

Components of Actual Cost

- The actual cost of an acquired tangible fixed asset shall comprise its purchase price, import duties and other taxes, excluding those subsequently recoverable, and any directly attributable expenditure on making the asset ready for its intended use. Any trade discounts and rebates shall be deducted in arriving at the actual cost.
- The cost of a tangible fixed asset may undergo changes subsequent to its acquisition or construction on account of:
  a. price adjustment, changes in duties or similar factors; or
  b. exchange fluctuation as specified in ICDS on the effects of changes in foreign exchange rates.
- Administration and other general overhead expenses are to be excluded from the cost of tangible fixed assets if they do not relate to a specific tangible fixed asset.
- The expenditure incurred on start-up and commissioning of the project, including the expenditure incurred on test runs and experimental production, shall be capitalised.

Self- constructed Tangible Fixed Assets

- In arriving at the actual cost of self-constructed tangible fixed assets, the same principles shall be followed.
- Cost of construction that relate directly to the specific tangible fixed asset and costs that are attributable to the construction activity in general and can be allocated to the specific tangible fixed asset shall be included in actual cost. Any internal profits shall be eliminated in arriving at such costs.

Non- monetary Consideration

- When a tangible fixed asset is acquired in exchange for another asset, the fair value of the tangible fixed asset so acquired shall be its actual cost.
  - *Fair value* of an asset is the amount for which that asset could be exchanged between knowledgeable, willing parties in an arm's length transaction

- When a tangible fixed asset is acquired in exchange for shares or other securities, the fair value of the tangible fixed asset so acquired shall be its actual cost.

Improvements and Repairs

- An Expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance is added to the actual cost.
- The cost of an addition or extension to an existing tangible fixed asset which is of a capital nature and which becomes an integral part of the existing tangible fixed asset is to be added to its actual cost. Any addition or extension, which has a separate identity and is capable of being used after the existing tangible fixed asset is disposed of, shall be treated as separate asset.

Valuation of Tangible Fixed Assets in Special Cases

- Where a person owns tangible fixed assets jointly with others, the proportion in the actual cost, accumulated depreciation and written down value is grouped together with similar fully owned tangible fixed assets.
- Where several assets are purchased for a consolidated price, the consideration shall be apportioned to the various assets on a fair basis.

Comparative study of ICDS with respective AS

Basis of difference	AS 10	ICDS V
Applicability	Fixed assets such as land, building, plant and machinery, vehicles, furniture and fittings, goodwill, patents, trademarks and designs, royalties and dividends	Tangible fixed assets being land, building, machinery, plant or furniture
Component of cost	'Cost' of fixed asset comprises its purchase price, non- refundable taxes and any directly attributable cost of bringing the asset to its working condition for its intended use. Trade discount and rebates will be deducted while computing cost.	It has similar definition to AS 10 but words used are 'actual cost' as compared to 'cost' in AS 10
Stand-by equipment and servicing equipment	AS acknowledges capitalization of stand-by equipment and servicing equipment as a normal practice but does not mandate it.	ICDS 'mandates' capitalization of stand-by equipment and servicing equipment
Machinery spares	- It is 'usually' charged to P&L a/c on consumption. - However, if spares are used only in connection with the item of fixed asset with irregular use then it 'may' be appropriate to capitalize	- It 'shall' be charged to P&L a/c on consumption - However, if spares are used only in connection with the item of fixed asset with irregular use then it 'shall' be capitalized

Basis of difference	AS 10	ICDS V
Asset acquired against non-monetary consideration	In case of acquisition of fixed asset in exchange for another asset, shares or other securities issued, cost of asset acquired should be recorded either at (a) fair market value of asset given up/shares or securities issued or (b) fair market value of asset acquired, whichever is more clearly evident	In case of acquisition of a tangible fixed asset in exchange for another asset, shares or other securities issued, actual cost of the tangible fixed asset shall be recorded at fair value of tangible fixed asset acquired
Assets acquired for consolidated price	Consolidated price to be apportioned to various assets on a fair basis as determined by competent valuers	Consolidated price shall be apportioned to various assets on a fair basis
Disclosure requirement	Gross and net book values at beginning and end of year showing additions, deletions and other movements, expenditure incurred in course of construction and revalued amount, if any	Description of assets/block of assets, depreciation rate and allowable depreciation, actual cost / opening WDV and closing WDV showing additions or deduction including adjustment for CENVAT, exchange difference and subsidy, grant or reimbursement

ICDS VI: Effects of Changes in Foreign Exchange Rates

9.7

Scope

- The Standard deals with:
  a. treatment of transactions in foreign currencies;
  b. translating the financial statements of foreign operations;
     - Foreign operations of a person is a branch, by whatever name called, of that person, the activities of which are based or conducted in a country other than India
  c. treatment of foreign currency transactions in the nature of forward exchange contracts.
     - Foreign currency transaction is a transaction which is denominated in or requires settlement in a foreign currency, including transactions arising when a person:
       a) buys or sells goods or services whose price is denominated in a foreign currency; or
       b) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or
       c) becomes a party to an unperformed forward exchange contract; or
       d) otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.
     - Forward exchange contract means an agreement to exchange different currencies at a forward rate, and includes a foreign currency option contract or another financial instrument of a similar nature.

Initial Recognition

- A foreign currency transaction shall be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction.
- An average rate for a week or a month that approximates the actual rate at the date of the transaction may be used for all transaction in each foreign currency occurring during that period. If the exchange rate fluctuates significantly, the actual rate at the date of the transaction shall be used.

Conversion at Last Date of Previous Year

- At last day of each previous year:
  a. foreign currency monetary items shall be converted into reporting currency by applying the closing rate;
     - Monetary items are money held and assets to be received or liabilities to be paid in fixed or determinable amounts of money. Cash, receivables, and payables are examples of monetary items;

b. non-monetary items in a foreign currency shall be converted into reporting currency by using the exchange rate at the date of the transaction.

- Non-monetary items are assets and liabilities other than monetary items. Fixed assets, inventories, and investments in equity shares are examples of non-monetary items;

c. non-monetary item being inventory which is carried at net realisable value denominated in a foreign currency shall be reported using the exchange rate that existed when such value was determined.

Forward Exchange Contracts

- Any premium or discount arising at the inception of a forward exchange contract shall be amortised as expense or income over the life of the contract. Exchange differences on such a contract shall be recognised as income or as expense in the previous year in which the exchange rates change. Any profit or loss arising on cancellation or renewal shall be recognised as income or as expense for the previous year.
- Premium, discount or exchange difference on contracts that are intended for trading or speculation purposes, or that are entered into to hedge the foreign currency risk of a firm commitment or a highly probable forecast transaction shall be recognised at the time of settlement.

Comparative study of ICDS with respective AS

Basis of difference	AS 11	ICDS VI
Revenue monetary items (like trade receivables, payables)	– Converted into reporting currency by applying the closing rate – Exchange difference recognized in P&L a/c	– Converted into reporting currency by applying the closing rate – Exchange difference recognized as income or expense subject to provisions of Rule 115
Revenue non-monetary items (e.g. Inventory)	*If item is carried at historical cost*: Reported at the exchange rate on the date of transaction *If item is carried at fair value*: Reported at the exchange rate that existed when the value was determined	Converted into reporting currency using the exchange rate at the date of the transaction
Capital monetary items relating to imported assets and domestic assets	Requires recognition in P&L A/c	– Requires recognition as income or expense subject to provisions of sec. 43A – No distinction recognized between capital and revenue items
Foreign operations	Foreign operation is a subsidiary, associate, joint venture or branch of the reporting enterprise, the activities of which are based or conducted in a country other than the country of the reporting enterprise	Foreign operations of a person is a branch, by whatever name called, of that person, the activities of which are based or conducted in a country other than India

Basis of difference	AS 11	ICDS VI
Integral foreign operation	– Same principles as for own assets and liabilities – Exchange differences are recognized in P&L A/c	– Subject to sec. 43A and Rule 115, similar to AS 11 – No distinction recognized between capital and revenue items
Non-integral foreign operations	– All assets & liabilities and income & expense items are translated at closing rates – Exchange differences are accumulated in Foreign Currency Translation Reserve (FCTR) A/c and to be taken to P&L a/c on disposal of non-integral foreign operations	– Similar to AS 11 except that, (subject to sec. 43A & Rule 115) resulting exchange differences are to be recognized as income or expense instead of accumulation in FCTR A/c – No distinction recognized between capital and revenue items
Forex derivatives for hedging purpose (Capital and revenue a/c)	– Premium/discount is amortized over life of contract – Restated on MTM basis at year end and difference is recognized in P&L – Profit/ loss on cancellation or renewal is also recognized in P&L	– Same as AS without distinguishing between contracts on capital account and revenue account (subject to sec. 43A applicable to imported assets)
Forex derivative for trading / speculation purposes / firm commitments /highly probable forecast transactions	– Forward contract is restated at year end on mark to market basis and difference is recognized in P&L – No amortization of premium/ discount	– Premium, discount or exchange difference shall be recognized at the time of settlement – No distinction recognized between contracts on capital account and revenue account
Forex derivatives not covered by ICDS VI (futures, interest rate swaps, etc)	– Not covered by AS 11 being a derivative contract covered by AS 30, 31 & 32 which are yet to be notified under Companies Act 2013 – Currently ICAI Guidance Note requires recognition of loss on MTM basis but gain to be ignored	– Forex derivatives not covered by ICDS VI. – ICDS I on accounting policies provides that MTM loss or an expected loss shall not be recognized unless permitted under other ICDS.

ICDS VII: Government Grants

9.8

Scope

- The Standard deals with the treatment of Government grants. The Government grants are sometimes called by other names such as subsidies, cash incentives, duty drawbacks, waiver, concessions, reimbursements, etc. but does not include Government participation in the ownership of the enterprise
  - Government refers to the Central Government, State Governments, agencies and similar bodies, whether local, national or international.
  - Government grants are assistance by Government in cash or kind to a person for past or future compliance with certain conditions. They exclude those forms of Government assistance which cannot have a value placed upon them and the transactions with Government which cannot be distinguished from the normal trading transactions of the person.

Recognition of Government Grants

- Government grants should not be recognised until there is reasonable assurance that (i) the person shall comply with the conditions attached to them, and (ii) the grants shall be received.
- Recognition of Government grant shall not be postponed beyond the date of actual receipt.

Treatment of Government Grants

Grant Relates to	Treatment
Depreciable fixed asset	The grant shall be deducted from the actual cost of the asset or from the written down value of block of assets
Non-depreciable asset requiring fulfillment of certain obligations	The grant shall be recognised as income over the same period over which the cost of meeting such obligations is charged to income
Not directly relatable to the asset acquired	Proportionate amount shall be deducted from the actual cost of the assets or shall be reduced from the written down value of block of assets to which the assets belonged to.
Receivable as compensation for expenses or losses incurred in a previous financial year or for the purpose of giving immediate financial support to the person with no further related costs	The grant shall be recognised as income of the period in which it is receivable
In other case	Grants shall be recognised as income over the periods necessary to match them with the related costs which they are intended to compensate

- The Government grants in the form of non-monetary assets, given at a concessional rate, shall be accounted for on the basis of their acquisition cost.

Refund of Government Grants

- The amount refundable in respect of a Government grant shall be applied first against any unamortised deferred credit remaining in respect of the Government grant. To the extent that the amount refundable exceeds any such deferred credit, or where no deferred credit exists, the amount shall be charged to profit and loss statement.
- The amount refundable in respect of a Government grant related to a depreciable fixed asset shall be recorded by increasing the actual cost or written down value of block of assets by the amount refundable. Where the actual cost of the asset is increased, depreciation on the revised actual cost or written down value shall be provided prospectively at the prescribed rate.

Disclosure

- Following disclosure shall be made in respect of Government grants:

  a. nature and extent of Government grants recognised during the previous year by way of deduction from the actual cost of the asset or assets or from the written down value of block of assets during the previous year;

  b. nature and extent of Government grants recognised during the previous year as income;

  c. nature and extent of Government grants not recognised during the previous year by way of deduction from the actual cost of the asset or assets or from the written down value of block of assets and reasons thereof; and

  d. nature and extent of Government grants not recognised during the previous year as income and reasons thereof.

Comparative study of ICDS with respective AS

Basis of difference	AS 12	ICDS VII
Recognition of grant	– On reasonable assurance of compliance of attached conditions and reasonable certainty of ultimate collection – Mere receipt of grant is not sufficient	– On reasonable assurance of compliance of attached conditions and reasonable certainty of ultimate collection – Recognition cannot be postponed beyond date of actual receipt
Grant in the nature of promoter's contribution	To be credited to capital reserve and to be treated as shareholders' funds	ICDS is silent on this category
Grants relatable to depreciable fixed assets	To be reduced from cost or recognized as deferred revenue by systematic credit to P&L A/c	To be reduced from cost of fixed asset [in line with Explanation 10 to sec. 43(1)]
Relatable to non-depreciable fixed assets	– To be credited as capital reserve, if no conditions attached to the grant – To be credited to P&L A/c over period of incurring cost of meeting conditions of grant	– To be considered as income on an upfront basis, if there are no conditions attached to grant – To be treated as income over period over which cost of meeting conditions is incurred

Basis of difference	AS 12	ICDS VII
Grants other than those covered above	Revenue grant to be credited as income or reduced from related expense	Grant to be treated as income over period over which cost of meeting conditions is incurred.
Compensation for expenses/ loss incurred or for giving immediate financial support	To be recognized as income in the year in which it is receivable	To be recognized as income in the year in which it is receivable
Disclosure requirement	Accounting policy adopted for grants including the method of presentation, extent of recognition in the financial statements, accounting of non-monetary assets given at concession/ free of cost	Requires disclosure of nature and extent of recognized as well as unrecognized grants. It also requires disclosure of reasons for non-recognition.

ICDS VIII: Securities

9.9

Scope

- This part of the Standard deals with securities held as stock-in-trade. However, this part of the Standard does not deal with:
  a. the bases for recognition of interest and dividends on securities;
  b. securities held by a person engaged in the business of insurance;
  c. securities held by mutual funds, venture capital funds, banks and public financial institutions formed under a Central or a State Act or so declared under the Companies Act, 1956 or the Companies Act, 2013
     - Securities shall have the meaning assigned to it in sec. 2(h) of the Securities Contracts (Regulation) Act, 1956 and shall include share of a company in which public are not substantially interested but shall not include derivatives.

Recognition and Initial Measurement of Securities

- A security on acquisition shall be recognised at actual cost i.e., its purchase price + acquisition charges such as brokerage, fees, tax, duty or cess.
- Where a security is acquired in exchange for other securities or other asset, the fair value of the security so acquired shall be its actual cost.
  - Fair value is the amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction.
- Where unpaid interest has accrued before the acquisition of an interest-bearing security and is included in the price paid for the security, the subsequent receipt of interest is allocated between pre-acquisition and post-acquisition periods; the pre-acquisition portion of the interest is deducted from the actual cost.

Subsequent Measurement of Securities

- At the end of any previous year, securities held as stock-in-trade shall be valued at actual cost initially recognised or net realisable value at the end of that previous year, whichever is lower.
- The comparison of actual cost initially recognised and net realisable value shall be done categorywise (viz., shares; debt securities; convertible securities; and any other securities) and not for each individual security.
- Securities not listed on a recognised stock exchange or listed but not quoted on a recognised stock exchange shall be valued at actual cost initially recognised.

Comparative study of ICDS with respective AS

Basis of difference	AS 13	ICDS VIII
Applicability	– AS applicable to accounting for investments – AS clarifies that principles applicable to 'current investments' can apply to securities held as stock-in-trade	ICDS is applicable to securities held as stock-in-trade
Security acquired against non-monetary consideration	In case of acquisition of securities in exchange for shares or other securities issued or another asset, cost of security acquired should be recorded either at (a) fair market value of securities issued or (b) fair market value of asset given up, whichever is more clearly evident	In case of acquisition of securities in exchange for other securities issued or another asset, actual cost of security acquired shall be recorded at fair value of security acquired
Year-end valuation of securities	Current investments to be valued at lower of cost or fair value either on individual investment basis or by category of investment but not on global basis.	– Securities should be valued at lower of cost or NRV. Comparison of cost and NRV shall be done category-wise. – Securities are classified under following categories (a) shares; (b) debt; (c) convertible securities; and (d) other securities
Opening value of securities	No specific provision	– Value of opening inventory of securities shall be the same as the value of securities at the end of the immediately preceding financial year – In case of commencement of business, Cost of security on the day of commencement of business will be opening value
Valuation of unlisted or thinly traded securities	No specific provision	Valuation of unlisted or thinly traded securities shall be valued at actual cost initially recognized
Ascertainment of cost	Cost formulae are the same as those specified in AS 2 (e.g. FIFO; average cost, etc.)	Cost which cannot be ascertained by specific identification shall be determined on the basis of FIFO method or weighted average formula.

ICDS IX: Borrowing Costs

9.10

Scope

- The Standard deals with treatment of borrowing costs. However, the Standard does not deal with the actual or imputed cost of owners' equity and preference share capital.
  - Borrowing costs are interest and other costs incurred by a person in connection with the borrowing of funds and include:
    a) commitment charges on borrowings;
    b) amortised amount of discounts or premiums relating to borrowings;
    c) amortised amount of ancillary costs incurred in connection with the arrangement of borrowings;
    d) finance charges in respect of assets acquired under finance leases or under other similar arrangements.

Recognition

- Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset shall be capitalised as part of the cost of that asset.
  - Qualifying asset means:
    a. land, building, machinery, plant or furniture, being tangible assets;
    b. know-how, patents, copyrights, trade marks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets;
    c. inventories that require a period of 12 months or more to bring them to a saleable condition.

Borrowing Costs Eligible for Capitalisation

- *Specific Borrowing*: The extent to which funds are borrowed specifically for the purposes of acquisition, construction or production of a qualifying asset, the amount of borrowing costs to be capitalised on that asset shall be the actual borrowing costs incurred during the period on the funds so borrowed.
- *Other than specific borrowing*: The amount of borrowing costs to be capitalised shall be computed in accordance with this formula: A × B / C

A Borrowing costs incurred during the previous year except on specific borrowings

B i. the average of costs of qualifying asset as appearing in the balance sheet of a person on the first day and the last day of the previous year

ii. in case the qualifying asset does not appear in the balance sheet of a person on the first day, half of the cost of qualifying asset; or

excluding the extent to which the qualifying assets are directly funded out of specific borrowings

iii. in case the qualifying asset does not appear in the balance sheet of a person on the last day of the previous year, the average of the costs of qualifying asset as appearing in the balance sheet of a person on the first day of the previous year and on the date of put to use or completion, as the case may be,

C the average of the amount of total assets as appearing in the balance sheet of a person on the first day and the last day of the previous year, other than assets to the extent they are directly funded out of specific borrowings

Commencement of Capitalisation

- The capitalisation of borrowing costs shall commence
  - In case of specific borrowing : from the date on which funds were borrowed
  - In case of other borrowing : from the date on which funds were utilised

Cessation of Capitalisation

- Capitalisation of borrowing costs shall cease:
  - In case of asset other than inventory — When such asset is first put to use
  - In case of inventory — When substantially all the activities necessary to prepare such inventory for its intended sale are complete.

Disclosure

- The following disclosure shall be made in respect of borrowing costs, namely:—

a) the accounting policy adopted for borrowing costs; and

b) the amount of borrowing costs capitalised during the previous year.

Comparative study of ICDS with respective AS

Basis of difference	AS 16	ICDS IX
Borrowing cost	Borrowing cost includes exchange difference to the extent that they are regarded as an adjustment to interest costs	Borrowing cost does not include exchange differences arising from foreign currency borrowings
Qualifying assets	Qualifying asset defined to be an asset which necessarily takes a substantia period of time to get ready for its intended use or sale	Qualifying assets means – Inventory that require a period of 12 months or more to bring them to a saleable condition – Specified tangible and intangible assets are qualifying assets (regardless of substantial period condition)

Basis of difference	AS 16	ICDS IX
Commencement and cessation of capitalization	Capitalisation will commence when all the three conditions are satisfied (a) incurrence of capital expenditure (b) incurrence of borrowing cost (c) construction activity is in progress and cessation from the date when asset is ready to use	*In case of specific borrowing:* Capitalization will commence from date of borrowing of funds and cessation from the date when asset is put to use *In case of general borrowing* Capitalization will commence from date of utilization of funds and cessation from the date when asset is put to use
Methodology of capitalization	*In case of specific borrowing:* Directly attributable to borrowing cost *In case of general borrowing:* Weighted average cost of borrowing applied to capital expenditure	*In case of specific borrowing:* Directly attributable to borrowing cost *In case of general borrowing:* Prorate borrowing cost allocation as per normative formulae
Income from temporary deployment of funds	Income from temporary deployment of unutilised funds from specific loans to be reduced from borrowing cost	No similar provision in ICDS
Suspension of capitalization	Capitalization of borrowing costs should be suspended during extended periods in which active development is interrupted	No similar provision in ICDS

ICDS X: Provisions, Contingent Liabilities and Contingent Assets

9.11

Scope

- The Standard deals with provisions, contingent liabilities and contingent assets, except those:
  a. resulting from financial instruments;
  b. resulting from executory contracts;
  c. arising in insurance business from contracts with policyholders; and
  d. covered by another ICDS.
    - **Provision** is a liability which can be measured only by using a substantial degree of estimation.
    - **Liability** is a present obligation of the person arising from past events, the settlement of which is expected to result in an outflow from the person of resources embodying economic benefits.
    - **Obligating event** is an event that creates an obligation that results in a person having no realistic alternative to settling that obligation.
    - **Contingent liability** is:
      a. a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the person; or
      b. a present obligation that arises from past events but is not recognised because:
        A. it is not reasonably certain that an outflow of resources embodying economic benefits will be required to settle the obligation; or
        B. a reliable estimate of the amount of the obligation cannot be made.
    - *Contingent asset* is a possible asset that arises from past events the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the person.
    - *Executory contracts* are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent.
    - *Present obligation* is an obligation if, based on the evidence available, its existence at the end of the previous year is considered reasonably certain.

Recognition

Provisions

- A provision shall be recognised when:
  a. a person has a present obligation as a result of a past event;

b. it is reasonably certain that an outflow of resources embodying economic benefits will be required to settle the obligation; and

c. a reliable estimate can be made of the amount of the obligation.

- No provision shall be recognised for costs that need to be incurred to operate in the future. It is only those obligations arising from past events existing independently of a person's future actions, that is the future conduct of its business, that are recognised as provisions.

Contingent Liabilities

- A person shall not recognise a contingent liability.

Contingent Assets

- A person shall not recognise a contingent asset. Contingent assets are assessed continually and when it becomes reasonably certain that inflow of economic benefit will arise, the asset and related income are recognised in the previous year in which the change occurs.

Measurement

- The amount recognised as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the previous year. The amount of a provision shall not be discounted to its present value.

Reimbursements

- Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement shall be recognised when it is reasonably certain that reimbursement will be received if the person settles the obligation. The amount recognised for the reimbursement shall not exceed the amount of the provision.
- Where a person is not liable for payment of costs in case the third party fails to pay, no provision shall be made for those costs.
- An obligation, for which a person is jointly and severally liable, is a contingent liability to the extent that it is expected that the obligation will be settled by the other parties.

Review

- Provisions shall be reviewed at the end of each previous year and adjusted to reflect the current best estimate. If it is no longer reasonably certain that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision should be reversed.

Use of Provisions

- A provision shall be used only for expenditures for which the provision was originally recognised.

Disclosure

- Following disclosure shall be made in respect of each class of provision:

a) a brief description of the nature of the obligation;

b) the carrying amount at the beginning and end of the previous year;

c) additional provisions made during the previous year, including increases to existing provisions;

d) amounts used, that is incurred and charged against the provision, during the previous year;

e) unused amounts reversed during the previous year; and

f) the amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.

Comparative study of ICDS with respective AS

Basis of difference	AS 29	ICDS X
Onerous executory contracts	– Includes onerous executory contracts within its scope – Upfront recognition of liabilities required under onerous contracts	Onerous executory contracts excluded from the scope of ICDS
Recognition of provision	Provision shall be recognized when it is "probable" that an outflow of economic resources will be required to settle an obligation	Provision shall be recognized when it is "reasonably certain" that an outflow of economic resources will be required to settle an obligation
Recognition of reimbursement claims	Reimbursement claims are recognized when the realization of related income is "virtually certain"	Reimbursement claims are recognized when the realization of related income is "reasonably certain"
Meaning of obligation	Clarifies that obligations may be legally enforceable and may also arise from normal business practice, custom and a desire to maintain good business relations or act in an equitable manner.	No specific guidance on meaning of 'obligation

Clarifications Issued by CBDT [Circular 10/2017 dated 23-03-2017

Question 1:

Preamble of ICDS-I states that this ICDS is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purposes of maintenance of books of accounts. However, Para 1 of ICDS I states that it deals with significant accounting policies. Accounting policies are applied for maintenance of books of accounts and preparing financial statements. What is the interplay between ICDS-I and maintenance of books of accounts?

Answer:

As stated in the Preamble, ICDS is not meant for maintenance of books of accounts or preparing financial statements. Persons are required to maintain books of accounts and prepare financial statements as per accounting policies applicable to them. For example, companies are required to maintain books of account and prepare financial statements as per requirements of Companies Act 2013. The accounting policies mentioned in ICDS-I being fundamental in nature shall be applicable for computing income under the heads "Profits and gains of business or profession" or "Income from other sources".

Question 2:

Certain ICDS provisions are inconsistent with judicial precedents. Whether these judicial precedents would prevail over ICDS?

Answer:

The ICDS have been notified after due deliberation and after examining judicial views for bringing certainty on the issues covered by it. Certain judicial pronouncements were pronounced in the absence of authoritative guidance on these issues under the Act for computing Income under the head "Profits and gains of business or profession" or Income from other sources. Since certainty is now provided by notifying ICDS u/s 145(2), the provisions of ICDS shall be applicable to the transactional issues dealt therein in relation to assessment year 2017-18 and subsequent assessment years.

Question 3:

Does ICDS apply to non-corporate taxpayers who are not required to maintain books of account and/or those who are covered by presumptive scheme of taxation like sections 44AD, 44AE, 44ADA, 44B, 44BB, 44BBA, etc. of the Act?

Answer:

ICDS is applicable to specified persons having income chargeable under the head 'Profits and gains of business or profession' or 'Income from other sources'. Therefore, the relevant provisions of ICDS shall also apply to the persons computing income under the relevant presumptive taxation scheme. For example, for computing presumptive income of a partnership firm u/s 44AD of the Act, the provisions of ICDS on Construction Contract or Revenue recognition shall apply for determining the receipts or turnover, as the case may be.

Question 4:

If there is conflict between ICDS and other specific provisions of the Income-tax rules, 1962 ('the Rules') governing taxation of income like rules 9A, 9B etc. of the Rules, which provisions shall prevail?

Answer:

ICDS provides general principles for computation of income. In case of conflict, if any, between the provisions of Rules and ICDS, the provisions of Rules, which deal with specific circumstances, shall prevail.

Question 5:

lCDS is framed on the basis of accounting standards notified by Ministry of Corporate Affairs (MCA) vide Notification No. GSR 739(E) dated 7 December 2006 u/s 211(3C) of erstwhile Companies Act 1956. However, MCA has notified in February 2015 a new set of standards called 'Indian Accounting Standards' (Ind-AS). How will ICDS apply to companies which adopted Ind-AS?

Answer:

ICDS shall apply for computation of taxable income under the head "Profit and gains of business or profession" or "Income from other sources" under the Income Tax Act. This is irrespective of the accounting standards adopted by companies i.e. either Accounting Standards or Ind-AS.

Question 6:

Whether ICDS shall apply to computation of Minimum Alternate Tax (MAT) u/s 115JB of the Act or Alternate Minimum Tax (AMT) under section 115JC of the Act?

Answer:

MAT u/s 115JB of the Act is computed on 'book profit' that is net profit as shown in the Profit and Loss Account prepared under the Companies Act subject to certain specified adjustments. Since, the provisions of ICDS are applicable for computation of income under the regular provisions of the Act, the provisions of ICDS shall not apply for computation of MAT.

AMT u/s 115JC of the Act is computed on adjusted total income which is derived by making specified adjustments to total income computed as per the regular provisions of the Act. Hence, the provisions of ICDS shall apply for computation of AMT.

Question 7:

Whether the provisions of ICDS shall apply to Banks, Non-banking financial institutions, Insurance companies, Power sector, etc.?

Answer:

The general provisions of ICDS shall apply to all persons unless there are sector specific provisions contained in the ICDS or the Act. For example, ICDS VIII contains specific provisions for banks and certain financial institutions and Schedule I of the Act contains specific provisions for Insurance business.

Question 8:

Para 4(ii) of ICDS-I provides that Market to Market (MTM) loss or an expected loss shall not be recognized unless the recognition is in accordance with the provisions of any other ICDS. Whether similar consideration applies to recognition of MTM gain or expected incomes?

Answer:

Same principle as contained in ICDS-I relating to MTM losses or an expected loss shall apply *mutatis mutandis* to MTM gains or an expected profit.

Question 9:

ICDS-I provides that an accounting policy shall not be changed without 'reasonable cause'. The term 'reasonable cause' is not defined. What shall constitute 'reasonable cause'?

Answer:

Under the Act, 'reasonable cause' is an existing concept and has evolved well over a period of time conferring desired flexibility to the tax payer in deserving cases.

Question 10:

Which ICDS would govern derivative instruments?

Answer:

ICDS -VI (subject to para 3 of ICDS-VIII) provides guidance on accounting for derivative contracts such as forward contracts and other similar contracts. For derivatives, not within the scope of ICDS-VI, provisions of ICDS-I would apply.

Question 11:

Whether the recognition of retention money, receipt of which is contingent on the satisfaction of certain performance criterion is to be recognized as revenue on billing?

Answer:

Retention money, being part of overall contract revenue, shall be recognised as revenue subject to reasonable certainty of its ultimate collection condition contained in para 9 of ICDS-III on Construction contracts.

Question 12:

Since there is no specific scope exclusion for real estate developers and Build-Operate-Transfer (BOT) projects from ICDS IV on Revenue Recognition, please clarify whether ICDS-III and ICDS-IV should be applied by real estate developers and BOT operators. Also, whether ICDS is applicable for leases.

Answer:

At present there is no specific ICDS notified for real estate developers, BOT projects and leases. Therefore, relevant provisions of the Act and ICDS shall apply to these transactions as may be applicable.

Question 13:

The condition of reasonable certainty of ultimate collection is not laid down for taxation of interest, royalty and dividend. Whether the taxpayer is obliged to account for such income even when the collection thereof is uncertain?

Answer:

As a principle, interest accrues on time basis and royalty accrues on the basis of contractual terms. Subsequent non-recovery in either cases can be claimed as deduction in view of amendment to sec. 36(1)(vii). Further, the provision of the Act (e.g. sec. 43D) shall prevail over the provisions of ICDS.

Question 14:

Whether ICDS is applicable to revenues which are liable to tax on gross basis like interest, royalty and fees for technical services for non-residents u/s. 115A of the Act?

Answer:

Yes, the provisions of ICDS, shall also apply for computation of these incomes on gross basis for arriving at the amount chargeable to tax.

Question 15:

Para 8 of ICDS-V states expenditure incurred on commissioning of project, including expenditure incurred on test runs and experimental production shall be capitalized. It also states that expenditure incurred after the plant has begun commercial production i.e., production intended for sale or captive consumption shall be treated as revenue expenditure. What shall be the treatment of expense incurred after the conduct of test runs and experimental production but before commencement of commercial production?

Answer:

As clarified in Para 8 of ICDS- V, the expenditure incurred till the plant has begun commercial production, that is, production intended for sale or captive consumption, shall be treated as capital expenditure.

Question 16:

What is the taxability of opening balance as on 1st day of April 2016 of Foreign Currency Translation Reserve (FCTR) relating to non-integral foreign operation, if any, recognised as per Accounting Standards (AS) II?

Answer:

FCTR balance as on 1 April 2016 pertaining to exchange differences on monetary items for non-integral operations, shall be recognised in the previous year relevant for assessment year 2017-18 to the extent not recognised in the income computation in the past.

Question 17:

For subsidy received prior to 1st day of April 2016 but not recognised in the books pending satisfaction of related conditions and achieving reasonable certainty of receipt, how shall the same be recognised under ICDS on or after 1st day of April 2016?

Answer:

Para 4 of ICDS- VII read with Para 5 to Para 9 of ICDS- VII provides for timing of recognition of government grant. The transitional provision in Para 13 of ICDS-VII provides that a government grant which meets the recognition criteria on or after 1st day of April 2016 shall be recognised in accordance with ICDS- VII. All government grants actually received prior to 1st day of April 2016 shall be deemed to have been recognised on its receipt in accordance with Para 4(2) of ICDS-VII and accordingly will be outside the transitional provision and therefore the government grants received on or after 1st day of April 2016 and for which recognition criteria provided in Para 5 to Para 9 of ICDS-VII is also satisfied thereafter, the same shall be recognised as per the provisions of ICDS- VII. The grants received prior to 1st day of April 2016 shall continue to be recognised as per the law prevailing prior to that date.

E.g. if out of total subsidy entitlement of ₹ 10 Crore, an amount of ₹ 6 Crore is recognised in the books of accounts till 31st day of March 2016 and recognition of balance ₹ 4 Crore is deferred pending satisfaction of related conditions and/or achieving reasonable certainty of receipt. The balance amount of ₹ 4 Crore will be taxed in the year in which related conditions are met and reasonable certainty is achieved. If these conditions are met over two years, the amount of ₹4 Crore shall be taxed over the period of two years. The amount of ₹ 6 Crore for which recognition criteria were met prior to 1st day of April 2016 shall not be taxable post 1st day of April 2016.

But if the subsidy is already received prior to 1st day of April 2016, Para 13 of ICDS-VII shall not apply even if some of the related conditions are met on or after 1st April 2016. This is in view of Para 4(2) of ICDS- VII which provides that Government grant shall not be postponed beyond the date of actual receipt. Such grants shall continue to be governed by the provisions of law applicable prior to 1st day of April 2016.

Question 18:

If the taxpayer sells a security on the 30th day of April 2017. The interest payment dates are December and June. The actual date of receipt of interest is on the 30th day of June 2017 but the interest on accrual basis has been accounted as income on the 31st day of March 2017. Whether the taxpayer shall be permitted to claim deduction of such interest i.e. offered to tax but not received while computing the capital gain?

Answer:

Yes, the amount already taxed as interest income on accrual basis shall be taken into account for computation of income arising from such sale.

Question 19:

Para 9 of ICDS-VIII on securities requires securities held as stock-in-trade shall be valued at actual cost initially recognised or net realisable value (NRV) at the end of that previous year, whichever is lower. Para 10 of Part-A of ICDS-VIII requires the said exercise to be carried out category wise. How the same shall be computed?

Answer:

For subsequent measurement of securities held as stock-in-trade, the securities are first aggregated category wise. The aggregate cost and NRV of each category of security are compared and the lower of the two is to be taken as carrying value as per ICDS- VIII. This is illustrated below:

Security	Category	Cost	NRV	Lower of cost or NRV	ICDS Value
A	Share	100	75	75	
B	Share	120	150	120	
C	Share	140	120	120	
D	Share	200	190	190	
	Total	**560**	**535**	**505**	**535**
E	Debt Security	150	160	150	
F	Debt Security	105	90	90	
G	Debt Security	125	135	125	
H	Debt Security	220	230	220	
	Total	**600**	**615**	**585**	**600**
Securities Total		**1160**	**1150**	**1090**	**1135**

Question 20:

There are specific provisions in the Act read with Rules under which a portion of borrowing cost may get disallowed under sections like 14A, 43B, 40(a) (i), 40(a)(ia), 40A(2)(b), etc. of the Act. Whether borrowing costs to be capitalized under ICDS-IX should exclude portion of borrowing costs which gets disallowed under such specific provisions?

Answer:

Since specific provisions of the Act override the provisions of ICDS, it is clarified that borrowing costs to be considered for capitalization under ICDS IX shall exclude those borrowing costs which are disallowed under specific provisions of the Act. Capitalization of borrowing cost shall apply for that portion of the borrowing cost which is otherwise allowable as deduction under the Act.

Question 21:

Whether bill discounting charges and other similar charges would fall under the definition of borrowing cost?

Answer:

The definition of borrowing cost is an inclusive definition. Bill discounting charges and other similar charges are covered as borrowing cost.

Question 22:

How to allocate borrowing costs relating to general borrowing as computed in accordance with formula provided under Para 6 of ICDS-IX to different qualifying assets?

Answer:

The capitalization of general borrowing cost under ICDS-IX shall be done on asset- by-asset basis.

Question 23:

What is the impact of Para 20 of ICDS X containing transitional provisions?

Answer:

Para 20 of ICDS - X provides that all the provisions or assets and related income shall be recognised for the previous year commencing on or after 1st day of April 2016 in accordance with the provisions of this standard after taking into account the amount recognised, if any, for the same for any previous year ending on or before 31st day of March, 2016.

The intent of transitional provision is that there is neither 'double taxation' of income due to application of ICDS nor there should be escape of any income due to application of ICDS from a particular date. This is explained as under

Provision required as per ICDS on 31 March 2017 for items brought forward from 31st day of March 2016 ... (A)	INR 3 Crores
Provisions as per ICDS for FY 2016-17 ... (B)	INR 5 Crores
Total gross provision … (C) = (A) + (B)	INR 8 Crores
Less: Provision already recognised for computation of taxable income in FY 2016-17 or earlier ... (D)	INR 2 Crores
Net provisions as per ICDS in FY 2016-17 to be recognised as per transition provision… (E) = (C) – (D)	INR 6 Crores

Question 24:

Expenditure on most post-retirement benefits like provident fund, gratuity, etc. are covered by specific provisions. There are other post-retirement benefits offered by companies like medical benefits. Such benefits are covered by AS-15 for which no parallel ICDS has been notified. Whether provision for these liabilities are excluded from scope of ICDS X?

Answer:

It is clarified that provisioning for employee benefit which are otherwise covered by AS 15 shall continue to be governed by specific provisions of the Act and are not dealt with by ICDS-X.

Question 25:

ICDS-I requires disclosure of significant accounting policies and other ICDS requires specific disclosures. Where is the taxpayer required to make such disclosures specified in ICDS?

Answer:

Net effect on the income due to application of ICDS is to be disclosed in the Return of income. The disclosures required under ICDS shall be made in the tax audit report in Form 3CD. However, there shall not be any separate disclosure requirements for persons who are not liable to tax audit.

Miscellaneous Provisions

9.12

Method of accounting in certain cases [Sec. 145A]

Valuation of stock

- The valuation of inventory shall be made at lower of actual cost or net realisable value computed in accordance with the ICDS.
- The valuation of purchase and sale of goods or services and of inventory shall be adjusted to include the amount of any tax, duty, cess or fee (by whatever name called) actually paid or incurred by the assessee to bring the goods or services to the place of its location and condition as on the date of valuation. Such tax, duty, etc. shall include all such payment notwithstanding any right arising as a consequence to such payment.
- The inventory being securities not listed on a recognised stock exchange, or listed but not quoted on a recognised stock exchange with regularity from time to time, shall be valued at actual cost initially recognised in accordance with the ICDS.
- The inventory being securities other than above, shall be valued at lower of actual cost or net realisable value in accordance with the ICDS
- The inventory being securities held by a scheduled bank or public financial institution shall be valued in accordance with the ICDS after taking into account the extant guidelines issued by the Reserve Bank of India in this regard.
- The comparison of actual cost and net realisable value of securities shall be made category-wise.

Taxation of foreign exchange fluctuation [Sec. 43AA]

Any gain (or loss), being computed in accordance with the ICDS, arising on account of any change in foreign exchange rates shall be treated as income (or loss).

Taxpoint:

- Such gain or loss shall arise in respect of all foreign currency transactions, including those relating to:
  i. monetary items and non-monetary items;
  ii. translation of financial statements of foreign operations;
  iii. forward exchange contracts;
  iv. foreign currency translation reserves[3]
- The provision of sec. 43AA is not applicable in respect of cases covered u/s 43A (like computation of actual cost of the asset, etc)

3 ICDS is not dealing with foreign currency translation reserves.

Loss as per ICDS [Sec. 36(1)(xviii)]

Marked to market loss or other expected loss as computed in accordance with the ICDS shall be allowed.

Computation of income from construction and service contracts [Sec. 43CB]

The profits and gains arising from a construction contract or a contract for providing services shall be determined on the basis of percentage of completion method in accordance with the ICDS.

Taxpoint:

- Profits and gains arising from a contract for providing services:

Case	Method
Contract for providing services with duration of not more than 90 days	Project completion method
A contract for providing services involving indeterminate number of acts over a specific period of time	Straight line method

- For the purpose of percentage of completion method:
  - the contract revenue shall include retention money;
  - the contract costs shall not be reduced by any incidental income in the nature of interest, dividends or capital gains.

Exercise

Multiple Choice Questions

1. ICDS VIII deals with
   A. Government Grants
   B. Revenue recognition
   C. Construction Contract
   D. Securities
2. ICDS is applicable in case of income under the head:
   A. Profits and gains from Business or Profession
   B. Capital Gains
   C. Income from House Property
   D. All heads of income

[Answer: 1 – D; 2 – A]

Short Essay Type Questions

1. Write a brief note of ICDS I.
2. State the disclosure requirements of ICDS III.

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Black Money Act, 2015 10

This Module includes:

10.1 Introduction to Black Money Act

10.2 Highlights of Black Money Act

Black Money Act, 2015

SLOB Mapped against the Module:

To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify the applicability of the provisions
- Understand the requirement of the provisions
- Analyse the impact of such provisions in computing income and tax liability
- Appreciate the various disclosures and procedure.

Introduction to Black Money Act

10.1

An Act to make provisions to deal with the problem of the Black money that is undisclosed foreign income and assets, the procedure for dealing with such income and assets and to provide for imposition of tax on any undisclosed foreign income and asset held outside India and for matters connected therewith or incidental thereto.

Highlights of Black Money Act

10.2

Chargeability

The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 had been introduced in the Parliament on 20-03-2015 which thereafter received President's assent on 26th May 2015 and notified in the month of July 2015.

The Act extends to the whole of India and provides that tax @ 30% shall be charged on every assessee for every assessment year in respect of total undisclosed foreign income and asset of the previous year – [Sec. 3]

Taxpoint

- Assessee means a person, being a resident other than not ordinarily resident in India within the meaning of sec. 6(6) of the Income-tax Act, by whom tax in respect of undisclosed foreign income and assets, or any other sum of money, is payable under this Act and includes every person who is deemed to be an assessee in default under this Act – [Sec. 2(2)]
- Previous year means:
  a) the period beginning with the date of setting up of a business and ending with the date of the closure of the business or the 31st day of March following the date of setting up of such business, whichever is earlier;
  b) the period beginning with the date on which a new source of income comes into existence and ending with the date of closure of the business or the 31st day of March following the date on which such new source comes into existence, whichever is earlier;
  c) the period beginning with the 1st day of the financial year and ending with the date of discontinuance of the business other than business referred to in (b) or dissolution of an unincorporated body or liquidation of a company, as the case may be; or
  d) the period of 12 months commencing on the 1st day of April of the relevant year in any other case,
  - and which immediately precedes the assessment year [Sec. 2(9)]
- Undisclosed asset located outside India means an asset (including financial interest in any entity) located outside India, held by the assessee in his name or in respect of which he is a beneficial owner, and he has no explanation about the source of investment in such asset or the explanation given by him is in the opinion of the Assessing Officer unsatisfactory [Sec. 2(11)]
- Undisclosed foreign income and asset means the total amount of undisclosed income of an assessee from a source located outside India and the value of an undisclosed asset located outside India, referred to in section 4, and computed in the manner laid down in section 5 [Sec. 2(12)]
- An undisclosed asset located outside India shall be charged to tax on its value in the previous year in which such asset comes to the notice of the Assessing Officer.

- Value of an undisclosed asset means the fair market value of an asset (including financial interest in any entity) determined in such manner as may be prescribed.

Scope of total undisclosed foreign income and asset [Sec. 4]

- The total undisclosed foreign income and asset of any previous year of an assessee shall be:

  a) the income from a source located outside India, which has not been disclosed in the return of income furnished u/s 139 of the Income-tax Act;

  b) the income, from a source located outside India, in respect of which a return is required to be furnished u/s 139 of the Income-tax Act but no return of income has been furnished u/s 139 of the Income-tax Act; and

  c) the value of an undisclosed asset located outside India.

- Any variation made in the income from a source outside India in the assessment or reassessment of the total income of any previous year, of the assessee under the Income-tax Act in accordance with the provisions of section 29 to section 43C (Profits and gains of business or profession) or section 57 to section 59 (Income from other sources) or section 92C (Transfer pricing) of the said Act, **shall not** be included in the total undisclosed foreign income.

- To avoid double taxation, the income included in the total undisclosed foreign income and asset under this Act shall not form part of the total income under the Income-tax Act.

Computation of total undisclosed foreign income and asset [Sec. 5]

- In computing the total undisclosed foreign income and asset of any previous year of an assessee:

  - No deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee, whether or not it is allowable in accordance with the provisions of the Income-tax Act.

  - Any income,—

    a) which has been assessed to tax for any assessment year under the Income-tax Act prior to the assessment year to which this Act applies; or

    b) which is assessable or has been assessed to tax for any assessment year under this Act,

shall be reduced from the value of the undisclosed asset located outside India, if, the assessee furnishes evidence to the satisfaction of the Assessing Officer that the asset has been acquired from the income which has been assessed or is assessable, as the case may be, to tax.

- The amount of deduction in case of an immovable property shall be the amount which bears to the value of the asset as on the first day of the financial year in which it comes to the notice of the Assessing Officer, the same proportion as the assessable or assessed foreign income bears to the total cost of the asset.

Illustration 1.

A house property located outside India was acquired by an assessee in the previous year 2009-10 for ₹ 50 lakh. Out of the investment of ₹ 50 lakh, ₹ 20 lakh was assessed to tax in the total income of the previous year 2009-10 and earlier years. Such undisclosed asset comes to the notice of the Assessing Officer in the year 2021-22. If the value of the asset in the year 2021-22 is ₹ 1 crore, the amount chargeable to tax shall be ₹ 60,00,000 i.e.:

₹ 1,00,00,000 – (₹ 20,00,000 / ₹ 50,00,000) = ₹ 60,00,000

Tax Mangement

Tax authorities [Sec. 6]

- The income-tax authorities shall be the tax authorities for the purposes of this Act.
- Every such authority shall exercise the powers and perform the functions of a tax authority under this Act in respect of any person within his jurisdiction.
- The jurisdiction of a tax authority under this Act shall be the same as he has under the Income-tax Act
- The tax authority having jurisdiction in relation to an assessee who has no income assessable to income-tax under the Income-tax Act shall be the tax authority having jurisdiction in respect of the area in which the assessee resides or carries on its business or has its principal place of business.

Change of incumbent [Sec. 7]

The tax authority who succeeds another authority as a result of change in jurisdiction or for any other reason, shall continue the proceedings from the stage at which it was left by his predecessor. The assessee in such a case may be given an opportunity of being heard, if he so requests in writing, before passing any order in his case.

Assessment [Sec. 10]

- The Assessing Officer may, on receipt of an information from an income-tax authority or any other authority under any law for the time being in force or on coming of any information to his notice, serve on any person, a notice requiring him, on the specified date, to produce such accounts or documents or evidence as the Assessing Officer may require for the purposes of this Act.
  - No separate return is required to be filed under this Act
  - There is no time limit for issuance of the aforesaid notice. The Assessing Officer may issue such notice any time on the basis of information.
- The Assessing Officer may, from time to time, serve further notices requiring the production of such other accounts or documents or evidence as he may require.
- The Assessing Officer may make such inquiry, as he considers necessary, for the purpose of obtaining full information in respect of undisclosed foreign income and asset of any person for the relevant financial year or years.
- The Assessing Officer, after considering such accounts, documents or evidence, as he has obtained, and after taking into account any relevant material which he has gathered and any other evidence produced by the assessee, shall by an order in writing, assess the undisclosed foreign income and asset and determine the sum payable by the assessee.
- Such order shall be made within 2 years from the end of the financial year in which the notice was issued by the Assessing Officer [Sec. 11]
- **Best Judgment Assessment:** If any person fails to comply with all the terms of the notice, the Assessing Officer shall, after taking into account all the relevant material which he has gathered, make the assessment of undisclosed foreign income and asset to the best of his judgment and determine the sum payable by the assessee. [Sec. 10(4)]
  - Before making such an assessment, an opportunity of being heard is required to be given to the assessee.
- Aggrieved with the order of the Assessing Officer, the assessee may file appeal or rectification petition or revision petition (which are in line with the Income-tax Act)

	Income-tax Act	Black Money Act
Rectification	Sec. 154	Sec. 12
Notice of Demand	Sec. 156	Sec. 13
Appeals to Commissioner (Appeals)	Sec. 246A to 250	Sec. 15 to 17
Appeals to Tribunal	Sec. 252 to 255	Sec. 18
Appeals to High Court	Sec. 260A	Sec. 19
Appeals to the Supreme Court	Sec. 261	Sec. 21
Revision	Sec. 263 / 264	Sec. 23 / 24
Recovery of Tax	Sec. 220	Sec. 30
Tax Recovery Officer	Sec. 222 to 232	Sec. 31 to 39
Interest	Sec. 234 to 234C	Sec. 40
Power regarding discovery, inspection, etc.	Sec. 131	Sec. 8

- **Liability of manager of a company [Sec. 35]**

  Every person being a manager at any time during the financial year shall be jointly and severally liable for the payment of any amount due under this Act in respect of the company for the financial year, if the amount cannot be recovered from the company.

  However, if the manager proves that non-recovery cannot be attributed to any neglect, misfeasance or breach of duty on his part in relation to the affairs of the company, then aforesaid provision shall not be applied.

- **Joint and several liability of participants [Sec. 36]**

  Every person, being a participant in an unincorporated body at any time during the financial year, or the representative assessee of the deceased participant, shall be jointly and severally liable, along with the unincorporated body, for payment of any amount payable by the unincorporated body under this Act and all the provisions of this Act shall apply accordingly.

  However, if the partner of LLP proves that non-recovery cannot be attributed to any neglect, misfeasance or breach of duty on his part in relation to the affairs of the partnership, then aforesaid provision shall not be applied.

  - Participant means—

    a. a partner in relation to a firm; or

    b. a member in relation to an association of persons or body of individuals [Sec. 2(7)]

Penalties & Prosecutions

Provision relating to penalties and prosecutions are enumerated here in below:

Nature of default	Sec.	Penalty	Sec.	Prosecution
Fails to disclose foreign income and asset	41	300% of tax u/s 10	51(1)	3 years to 10 years[1]
Fails to furnish return of income before expiry of the relevant assessment year[2]	42	₹ 10 lakh		
Fails to disclose foreign asset or income in the return of income[2]	43	₹ 10 lakh	50	6 months to 10 years[1]

Nature of default	Sec.	Penalty	Sec.	Prosecution
Attempt to evade payment of tax, interest and penalty	44	Tax in arrear	51(2)	3 years to 10 years
Failure to: a) answer any question put to him by a tax authority b) sign any statement made by him in the course of any proceedings which a tax authority may legally require him to sign; c) attend or produce books of account or documents at the place or time, at certain place and time in response to summons issued u/s 8	45	₹ 50,000 to ₹ 2,00,000		
Makes a statement or delivers an account or statement which is false			52	6 months to 10 years[1]
Abets or induces another person to make and deliver an account or a statement or declaration which is false			53	6 months to 10 years[1]
Second and subsequent offences			58	3 years to 10 years[3]

[1.] with fine

[2.] However, no penalty shall be levied, if assessee fails to report bank accounts with maximum balance upto ₹5,00,000 at any time during the previous year

[3.] Fine of ₹ 5 lakh to ₹ 1 crore

Taxpoint:

- No penalty order shall be passed after the expiry of 1 year from the end of the financial year in which the notice for imposition of penalty is issued u/s 46 [Sec. 47]
- A person shall not be prosecuted against for an offence except with the sanction of the Principal Commissioner or Commissioner or the Commissioner (Appeals), as the case may be.
- An order imposing a penalty shall be made with the approval of the Joint Commissioner, if:
  - the penalty exceeds ₹ 1,00,000 and the tax authority levying the penalty is in the rank of Income-tax Officer; or
  - the penalty exceeds ₹ 5,00,000 and the tax authority levying the penalty is in the rank of Assistant Commissioner or Deputy Commissioner.
- **Congnizance of offence:** No court inferior to that of a metropolitan magistrate or a magistrate of the First Class shall try any offence under this Act. – Sec. 80
- No suit shall be brought in any civil court to set aside or modify any proceeding taken or order made under this Act. – Sec. 82(1)
- No prosecution, suit or other proceeding shall lie against the Government or any officer of the Government, for anything in good faith done or intended to be done, under this Act -Sec. 82(2)

Other Provisions

- **Rounding off**

  a. The amount of undisclosed foreign income and asset computed shall be rounded off to the nearest multiple of ₹ 100.

  b. Any amount payable or receivable by the assessee shall be rounded off to the nearest multiple of ₹ 10.

- **Agreement with foreign countries or specified territories [Sec. 73]**

  The Central Government may enter into an agreement with the Government of any other country:

  a. for exchange of information for the prevention of evasion or avoidance of tax on undisclosed foreign income chargeable under this Act or under the corresponding law in force in that country, or investigation of cases of such evasion or avoidance;

  b. for recovery of tax under this Act and under the corresponding law in force in that country.

Taxpoint:

- The Central Government may enter into an agreement with the Government of any specified territory outside India
- The Central Government may, by notification, make such provisions as may be necessary for implementing the agreements
- Any specified association in India may enter into an agreement with any specified association in the specified territory outside India and the Central Government may by notification make such provisions as may be necessary for adopting and implementing such agreement.

Exercise

Multiple Choice Questions

1. The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 extends to
   A. Whole of India
   B. Whole of India excluding Jammu and Kashmir
   C. Whole of India excluding Jammu and Kashmir and Arunachal Pradesh
   D. None of the above
2. The rate of tax provided by the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 is
   A. 30%
   B. 60%
   C. 50%
   D. None of the above

[Answer: 1 – A, 2 – A]

Short Essay Type Questions

1. How to compute total undisclosed foreign income and asset u/s 5 of the Black Money Act?
2. State the amount of penalty u/s 41 of the Black Money Act for failure to disclose foreign money and asset.

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

Case Study 11

This Module includes:

11.1 Discussion on Various Cases

Case Study

SLOB Mapped against the Module:

1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify the issue before the judiciary
- Understand, analyse, and interpret the decision of the judiciary
- Appreciate the applicability of such decision in the given scenario

Discussion on Various Cases

11.1

Siemens Public Communications Network Ltd -vs.- CIT (2016) (SC)

Voluntary subsidies paid by a holding company, to protect the capital investment, to its loss-making subsidiary is capital receipt in the hands of the recipient

The subvention received by the Assessee - Company from its parent company in Germany in a situation where the assessee–company was making losses has been treated to be a revenue receipt by the Assessing Officer. Though the first Appellate Authority and the ITAT has reversed the said finding. However, the High Court has restored the view taken by the Assessing Officer referring the decisions of Apex Court in Sahney Steel & Press Works Ltd., Hyderabad -vs.- CIT (1997) 7 SCC 764 and CIT -vs.- Ponni Sugars and Chemicals Limited (2008) 9 SCC 337.

In these cases, the Apex Court has held that unless the grant-in-aid received by an Assessee is utilized for acquisition of an asset, the same must be understood to be in the nature of a revenue receipt.

However, the aforesaid view tends to overlook the fact that in both Ponni Sugars and Sahney Steel the subsidies received were in the nature of grant-in-aid from public funds and not by way of voluntary contribution by the parent Company as in the present cases. Further, the voluntary payments made by the parent Company to its loss making Indian company can also be understood to be payments made in order to protect the capital investment of the Assessee Company. Thus, it was held that the payments made to the Assessee Company by the parent Company for Assessment Years in question cannot be held to be revenue receipts.

Earlier, the same view has also been held in CIT -vs.- Handicrafts and Handlooms Export Corporation of India Ltd. (Delhi)

Susham Singla -vs.- CIT (2016)(P&H)

Annual value of the properties like the ones in the case in hand which are more than one, owned by the assessee and which admittedly remained vacant throughout the previous year would not be assessed u/s 23(1)(c) but u/s 23(1)(a)

A search was conducted upon a Jeweller Group and the appellant-assessee being related to that Group, was also subjected to such search, on the basis of which, a notice was issued to him as to why deemed income by determining annual value of properties may not be added to his income (excluding one house property which was treated as self-occupied) as appellant-assessee is found to be the owner of 3 more properties. In the return, assessee had not shown any deemed income from them, notional rent was determined and after providing the statutory deductions, added to the appellant-assessee's income. Such addition at the hands of the Assessing Officer was challenged by the appellant-assessee considering that there is no chargeability of rent which cannot be realized according to sec. 23(1)(c).

Since the properties, which had been assessed to tax, had not been let out and had remained vacant in the respective previous years, no annual value for them could be determined u/s 23(4) and it was urged that as per the provisions of sec. 23(1)(c), the annual value of such properties had to be taken as `Nil'.

Section 23(1) has three sub sections which are as under:

Sec. 23(1)(a) provides that the annual value of any property shall be deemed to be the sum for which the property might reasonably be expected to let from year to year.

Sec. 23(1)(b) provides that where any property or any part of such property is let and the actual rent received or receivable by the owner in respect thereof is in excess of the sum, which the property might reasonably be expected to let from year to year, then the annual value of such property would be the actual amount so received or receivable.

Section 23(1)(c) is to the effect that where any property or part of such property is let but remained vacant during the whole or any part of the previous year and owing to such vacancy, the actual rent received or receivable is less than the sum, which such property might reasonably be expected to yield on being let out, then the amount so received or receivable would be the annual value of the property.

Section 23(2) is to the effect that where the property consists of a house or part of a house, which is in the occupation of the owner for the purposes of his own residence or could not actually be occupied by him for the reason that on account of his employment, business or profession, he had to reside at other places in a building, which is not owned by him, in that situation, the annual value of such house or part of the house is required to be taken as `Nil'.

According to Section 23(4)(a), where the property referred to in Section 23(2) consists of more than one house, then Section 23(2) is to apply only in respect of one of such houses and Section 23(4)(b) provides that the annual value of the house or houses, other than the house in respect of which the assessee had exercised an option under Section 23(4)(a) shall be determined under Section 23(1) as if such house or houses had been let.

It is held that sec. 23(1)(b) and (c) would apply only to those properties which were actually let out and for which rent was actually received or receivable by the assessee. These provisions deal with the concept of real income and not notional income. Thus, the annual value of the properties like the ones in the case in hand which are more than one, owned by the assessee and which admittedly remained vacant throughout the previous year would not be assessed u/s 23(1)(c) but u/s 23(1)(a). The annual value would, therefore, be determined notionally.

Further it is to be noted that Special Leave Petition in this regard is dismissed by the Apex Court.

Pr. CIT -vs.- U. K. Paints India Pvt. Ltd (2016) (Delhi)

Provisions of sec. 14A cannot be invoked by the Assessing Officer by rejecting the suo-moto disallowances made by assessee, without assigning any reasons.

During the relevant Assessment Year, the assessee's return had reported tax exempt income of over ₹ 25 crores. The Assessing Officer framed the assessment after applying disallowance u/s 14A in respect of this exempt income and without accepting the proferred disallowance of ₹ 7.5 lakhs made by the assessee. The order was rectified u/s 154 wherein AO merely clarified that the amount of ₹ 7.5 lakh offered was not 'taken into consideration' at the time of passing the order u/s 143(3). The Assessing Officer, therefore, reduced that amount from the figure of the determined disallowance. Commissioner (Appeals) was of the opinion that the rejection of ₹ 7.5 lakh was valid and restored the matter for fresh computation to the Assessing Officer. The Tribunal held that the Assessing Officer can proceed to make an independent determination of the disallowance under Rule 8D read with sec. 14(2) after recording his satisfaction about the amount and the reasons thereof offered by the assessee voluntarily u/s 14A.

The High Court considered the reasons for disallowance, the method of computation adopted by the Assessing Officer and the various submissions made by Revenue. The High Court also went through the order of the ITAT in appellant's own case, where the ITAT had observed "there is no iota of doubt to the effect that intention behind using the expression "in relation to" in sec. 14A is to encompass not only the direct but also the indirect expenditure which has any relation to the exempt income."

The High Court observed that the principle of disallowance is stated in Section 14A(1) and Section 14A(2) prescribes the mode or methodology for the disallowance and the steps for its calculation. Unlike the other part of the statute which decree or enjoin the actual methodology and are substantive, Parliament deemed it appropriate to leave it to the rule making authority to prescribe the methodology, i.e. computation. For instance, what are taxable and in what proportion and the principles applicable are embedded in the statute in certain provisions, such as Sections 28 to 43 and Sections 80A to 80HHC when it comes to deductions. Instead of adopting that mode, the Parliament thought it appropriate to leave the mode to the rule making authority.

The High Court held that the opinion of the Assessing Officer in the latter part [of Section 14A(2)] is to be based upon an appraisal of objective material relating to the assessee's voluntary disallowance of amounts and in addition if in the course of assessment, the assessing Officer enquires from the assessee about the amounts spent, which are to be disallowed, and the assessee in fact discloses a larger amount (than the one given in the return), it is still incumbent upon the Assessing Officer to enquire into such larger amounts and determine whether it has nexus with expenditure relatable to exempt income to attract sec. 14A(1).

It is to be noted that sec. 14A(2) states that "… if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under this Act"

Raj Dadarkar & Associates -vs.- ACIT (2017) (SC)

Income from the sub-licensing of property is taxable as house property income and not business income

The Maharashtra Housing and Developing Authority (MHADA) had constructed buildings. However, there was a reservation for Municipal retail market on the plot on which MHADA had constructed. Therefore, MHADA handed over the ground floor [stilt portion] of the above said buildings to Market Department of Municipal Corporation Greater Bombay (MCGB). In 1993, the Markets Department of the MCGB auctioned the property on a monthly license [stallage charges] basis to run the municipal market. The assessee participated in the auction and was the successful bidder. Accordingly, MCGB handed over possession of the market portion to the assessee. The premises allotted to the assessee was a bare structure, on stilts, that is, a pillar/column, sans even four walls. In terms of the auction, it was the assessee who had to make the entire premises fit to be used a market, including the construction of walls, construction of entire common amenities such as toilet blocks, etc. Accordingly, after taking possession of the premises, the assessee spent a substantial amount on additions/alternations of the entire premises, including demolishing the existing platform and, thereafter, reconstructing the same according to the new plan sanctioned by the MCGB. The assessee constructed 95 shops and 30 stalls of different carpet areas on the premises under the market name 'S Shopping Centre'. The assessee also obtained, in terms of the conditions of the auction, the necessary registration certificate for running a business under the Shop and Establishment Act and other licenses/ permissions from MCGB and other Government and semi-Government bodies for carrying on trading activities on the said premises. The assessee was responsible for day-to-day maintenance, cleanliness and upkeep of the market premises. The appellant also had to incur/pay water charges, electricity charges, taxes and repair charges

The assessee collected the following types of receipts from the sub-licensees:

- Compensation from sub-licensees [same rate of stallage charges and on the same terms and condition as given to the assessee by the MCGB]
- Leave and license fees
- Service Charges for providing various services, including security charges, utilities, etc.

The assessee filed the returns of income offering the income from the aforesaid shops and stalls sub-licensed by it as business income. The Assessing Officer computed the income from the shops, and the stalls under head 'Income from House Property'. The Commissioner (Appeals) allowed the appeal of the appellant and reversed the action of the respondent. However, the Tribunal reversed the order of the Commissioner (Appeals) and confirmed the action

of the Assessing Officer. Aggrieved by the Tribunal's order, the assessee filed an appeal before the High Court. The High Court dismissed the appeal filed by the assessee.

On appeal, the Apex Court has held that wherever there is an income from leasing out of premises and collecting rent, normally such an income is to be treated as income from house property, in case provisions of sec. 22 are satisfied with primary ingredient that the assessee is the owner of the said building or lands appurtenant thereto. 'Owner of the house property' is defined in sec. 27 which includes certain situations where a person not actually the owner shall be treated as the deemed owner of a building or part thereof.

The assessee is held to be 'deemed owner' of the property in question by virtue of sec. 27. Merely because there is an entry in the object clause of the business showing a particular object, would not be the determinative factor to arrive at a conclusion that the income is to be treated as income from business. Such a question would depend upon the circumstances of each case. The Tribunal being the last forum insofar as factual determination is concerned, the findings have attained finality. The Tribunal held that the service charges received were inseparable from the basic charges of rent. Also, it was undisputed that the assessee did not undertake any systematic or organized activity of providing services to the occupiers, which can constitute receipt as business income for the assessee.

It was for the assessee to produce sufficient material on record to show that its entire income or substantial income was from letting out of the property which was the principal business activity of the assessee. Reliance placed by the assessee on the judgments in Chennai Properties & Investments Ltd. (2015) 14 SCC 793 (SC) and Rayala Corporation (P) Ltd. T (2016) 15 SCC 201 (SC) would be of no avail. In Chennai Properties & Investments Ltd., the entire income of the appellant was through letting out of the two properties it owned and there was no other income of the assessee except the income from letting out of the said properties, which was the business of the assessee.

Palam Gas Service -vs.- CIT (2017) (SC)

Provision of sec. 40(a)(ia) covers the cases where the amount is actually paid.

The assessee is engaged in the business of purchase and sale of LPG cylinders. During the relevant assessment year, assessee received freight payments of ₹ 32 lakhs from Indian Oil Corporation (IOC) with whom the assessee had entered into main contract for carriage of LPG. The transportation of LPG was done through three truck-owners, to whom a total freight payment of ₹ 20 lakhs was made. As per the Assessing Officer, since the assessee has sub-contracted the transportation to these three persons within the meaning of sec. 194C, he was liable to deduct tax on ₹ 20 lakhs. The Assessing Officer thus disallowed these expenses u/s 40(a)(ia). On appeal, the Commissioner (Appeals) & the ITAT upheld the order of the Assessing Officer. On further appeal, the High Court too ruled in favour of the Revenue.

The Apex Court rejects assessee's plea that since the word used in sec. 40(a)(ia) is 'payable', no disallowance can be made where the freight charges had been paid during the year. The Apex Court acknowledges that grammatically, it may be accepted that the two words, i.e. 'payable' and 'paid', denote different meanings, but held that "when the entire scheme of obligation to deduct the tax at source and paying it over to the Central Government is read holistically, it cannot be held that the word 'payable' occurring in sec. 40(a)(ia) refers to only those cases where the amount is yet to be paid and does not cover the cases where the amount is actually paid." The Apex Court remarks that if the provision is interpreted in the manner suggested by appellant-assessee, "then even when it is found that a person, like the appellant, has violated the provisions of Chapter XVIIB .., he would still go scot free."

Maneklal Agarwal -vs.- DCIT (2017)(SC)

Higher rentals received from third party sub-lessees taxable in the hands of the first lessor where the lease is shown to be sham

The assessee had leased out his property to his own family members for a nominal rent, who in turn had sub-leased

it to third parties on much higher rental values. The tax authorities, at both assessment and first appellate levels, held that such sub-letting income was subject to tax in the hands of the assessee only. Upon further appeal, the order of the Commissioner (Appeals) was upheld by the Tribunal with a directive to consider municipal valuation as basis of income so charged to tax. The tax department challenged the order passed by the Tribunal before the Andhra Pradesh & Telangana High Court. The High Court allowed the revenue's appeal and dismissed the assessee appeals on the ground that the nature of lease executed by the assessee was proved to be bogus as a fact by the Tribunal, leading to a conclusion that the net rental value would be chargeable to tax in the hands of the assessee.

Aggrieved by the High Court's order, the assessee filed an appeal with the Supreme Court. The Supreme Court observed that the assessee had devised a structure to show lesser income in his hands by entering into a lease agreement with his wife, son, and daughter-in-law at very nominal rates and allowing such family members to sub-let the property at a much higher rental value. The Supreme Court relied on its own decision in ITO -vs.- Ch. Atchaiah (1996) AIR 993, where it had held that the Assessing Authority has the right to tax the 'right person'. In the instant case, given the finding of fact that the first lease transaction was bogus, the assessee was found to be the 'right person', making it permissible for the revenue to tax the said rental income in the hands of the assessee. To avoid double taxation of the same income, the Supreme Court further held that the assessee's relatives could seek redressal of the taxation of income at their hands in appropriate proceedings.

CIT -vs.- Smt. Sarika Jain (2017)(All)

ITAT wasn't competent to make addition under different section if it wasn't subject matter of appeal

The assessee was a partner in a firm, wherein he introduced certain amount of capital. Notice u/s 148 was issued to the assessee to explain the source of such capital. In reply to the said notice, the assessee submitted that she had received gift of certain amounts from 2 persons. The gifts were received through banking channel. In order to prove the aforesaid gift transactions, gift deeds were also produced before the authorities. The statement of the two donors were also recorded u/s 131 and they proved the factum of the gift. The Assessing Officer has held that gifts were not genuine as these were held to be unnatural and aforesaid amounts were added as undisclosed income of assessee u/s 68. On appeal, the Commissioner (Appeals) affirmed the said order. On further appeal, the Tribunal, held that the addition made by the Assessing Officer u/s 68 and sustained by the Commissioner (Appeals) could not be sustained. However, the Tribunal proceeded to add the aforesaid amount as the income of the assessee u/s 69-A.

Sec. 254(1) provides that the Appellate Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit.

The High Court has held that the use of the word 'thereon' is important and it reflects that the Tribunal has confined itself to the questions, which are arising or are subject matter in the appeal and it cannot be travelled beyond the same. The power to pass such orders as the Tribunal thinks fit can be exercised only in relation to the matter that arises in the appeal and it is not open to the Tribunal to adjudicate any other question or an issue, which is not in dispute and which is not the subject matter of the dispute in appeal. When said income could not be added u/s 68 and Tribunal was not competent to make said addition u/s 69A entire order of the Tribunal stand vitiated in law. Accordingly, the Tribunal was not competent to make any addition u/s 69A and as the same was not subject matter of the appeal before it.

Purnima Advertising Agency Pvt Ltd -vs.- DCIT (2017)(Guj)

Higher tax demand u/s 206AA cannot be raised on account of an incorrect PAN mentioned in the TDS return

The taxpayer is a company registered under the Companies Act and is engaged in the business of advertisement. During the year under consideration, the taxpayer has made payments to various recipients, on which the taxpayer has deducted tax at 2%. While filing TDS returns for the second and third quarters there was an inadvertent error

since the PAN of one deductee was wrongly mentioned. There was a typographical error while putting details in TDS statement. The taxpayer had not immediately noticed this error. During the course of processing TDS returns, the Assessing Officer (AO) found that the PAN indicated by the taxpayer in the declaration did not match with the actual PAN of the deductee. The PAN provided in the TDS return did not belong to that deductee and, therefore, in terms of sec. 206AA(6)2, it would have the effect as if the deductee has not furnished the PAN to the deductor and the effect of provisions of sec. 206AA(1)3 is applicable. The AO held that the taxpayer who was required to deduct tax at the rate of 20% had deducted the same at the rate of 2%. Therefore, the AO raised a demand for the remaining tax after adjusting such tax deducted.

Section 200(3) of the Act refers to the requirement of filing a TDS statement. This provision though does not refer to any mechanism for correction of such a statement, sec. 200A(1) specifically refers to a TDS statement or a correction statement. Thus, clearly leaving the possibility of correcting a declaration once made by the taxpayer. Sec. 200A(1)(a)(iii) permits the tax authority to make an adjustment of an incorrect claim, apparent from any information in the statement.

Neither the statute nor the department completely rules out the possibility of a genuine and bona fide typographical or even mechanical error. Looking to a large number of TDS statements and entries in such statements, it would be impossible to process individual claims of corrections, whether they are based on bona fide mistakes or otherwise. The taxpayer relied on the notification wherein tax department has formulated the scheme. This notification contains detailed provisions for the processing of TDS statements. It also refers to a correction of the TDS statement. The scheme authorises the director general to specify the procedures and processes for the effective functioning of the cell where such declarations would be processed which includes the receipt of the corrected TDS statement.

Even as per the tax department, the online system permits corrections limited to two alphabetical and two numerical errors in the PAN number. Such limited permission to correct is sought to be justified on two grounds. One is that if the error is genuine and bona fide in feeding the PAN number, it is unlikely that a typographical error would travel beyond such characters and the second is that looking to the millions of statements and entries being filed by the taxpayers across the country, it would open the flood gates, if corrections are permitted without any limit.

Once the tax department recognises the possibility of errors and also makes provisions for making corrections, it would be wholly illogical to limit such corrections on arithmetical working out of only two alphabets or two numeric being found incorrect requiring change. An error in feeding an entry or a number may have multiple origins from the typographical error of data entry operation to mechanical failures or through pure oversight referring to one column of PAN instead of another while filling up and uploading the statement. It is not necessary nor possible to envisage different situations under which such errors could crop-up and need not necessarily be confined to limited figures on the letters of the PAN being incorrect.

It is entirely one thing to suggest that the tax department would not accept any change once certain entries are uploaded, or at any rate no change would be permissible beyond a certain date. However, it is entirely another thing to suggest that the corrections may be permitted but should be limited to a number of characters where correction is needed.

In the present case, Section 200A of the Act itself refers to correction TDS statement. The intimation sent to the taxpayer of the shortfall in TDS also referred to the possibility of correction but limited it to certain characters. In the instant case, the deductee has already discharged its full tax liability. If the full effect of the tax department's decision is allowed, the deductee would not get the benefit of 2% of tax deducted by the deductor and already deposited with the government. Since the PAN does not match, the deductor would pay additional 18% which although styled in the name of TDS, would be additional to what deductee would have paid by way of tax to the department.

In the present case, with the payee having already discharged its tax liability independently, such an amount would remain in government coffers not accounted for by anyone's tax liability. Further, the tax department's contention

was that the incorrect PAN could be corrected as long as a mismatch is up to two alphabets and two numeric characters are incorrect.

The decision to limit the correction to limited characters is a policy decision which should be based on logical parameters. Nevertheless, putting the limitation of permitting corrections of only four characters has no rationale relation.

Accordingly, it has been held that the decision of the tax department in not permitting the taxpayer to correct the PAN of the deductee in the TDS statement was not acceptable. The tax department shall verify the taxpayer's claim of actual deduction of tax at the prescribed rate in the case of deductee, verify that the PAN sought to be corrected by the taxpayer belongs to the said deductee and that the tax was actually deposited in the case of such a deduction.

CIT -vs.- Equinox Solution Pvt. Ltd (2017)(SC)

If an undertaking is sold as a running business with all assets and liabilities for a slump price, no part of the consideration can be attributed to depreciable assets and assessed as a short-term capital gain u/s 50(2)

Assessee company was engaged in the business of manufacturing sheet metal components at Ahmedabad, sold his entire business in one go with all its assets and liabilities to another company and claimed the sale to be of 'slump sale' in the nature of long term capital gains as the undertaking was owned by assessee for almost 6 years. The Assessing Officer rejecting assessee's contention held that it was covered u/s 50(2) and framed assessment accordingly. On appeal, the Commissioner (Appeals) allowed assessee's claim of deduction. On further appeals before ITAT and High Court, assessee succeeded.

The Apex Court observed that sec. 50(2) would apply to any block of assets transferred which assessee was using in running of his business. The Apex Court, however, opined that where the entire running business with assets and liabilities stood transferred in one go, such sale could not be treated as short-term capital assets and is in the nature of LTCG.

The Apex Court upheld assessee's claim relying upon coordinate bench ruling in Artex Manufacturing Co. and Bombay High Court ruling in Premier Automobiles Ltd. wherein similar view was taken

Mcdowell & Company ltd -vs.- CIT (2017)(SC)

Deemed income u/s 41(1) of the amalgamating company should be reduced from the loss to be set off u/s 72A by the amalgamated company

Assessee company took over the sick company - HPL ('amalgamating company') through the scheme of amalgamation. HPL owed a lot of money to banks and financial institutions. In its books of accounts, the interest which had accrued on the loans given by such financial companies were shown as the money payable on account of interest to the said banking companies and was reflected as expenditure on that count. As the interest payable was treated as expenditure, benefit thereof was taken in the assessment orders made. Under certain circumstances and on fulfillment of conditions laid down u/s 72A, the company which takes over the sick company is allowed to set off losses of the amalgamated company as its own losses. After amalgamation, the assessee has taken such benefit.

The banks which had advanced loans to HPL agreed to waive off the interest which had accrued prior to certain date. Since, interest was claimed as expenditure by HPL in its returns. On the waiver of this interest, it became income in terms of sec. 41(1) of the Act. In the return filed by the assessee, the assessee claimed set off of the accumulated loses which it had taken over from HPL by virtue of the provisions contained in sec. 72A of the Act. The Assessing Officer treated the aforesaid income at the hands of the assessee herein and adjusted the same from the accumulated loses. The assessment order was drawn accordingly. The assessment was upheld by the Commissioner(Appeals). However, in further appeal, the ITAT held that the aforesaid income u/s 41(1) of the Act was not at the hands of the assessee herein but it may be treated as income of the HPL and since HPL was a

different assessee and a different entity, the assessee herein was not liable to pay any taxes on the said income. Later on, the High Court reverse the order of the Tribunal

The Apex Court held that waiver of liability due by amalgamating company after amalgamation is taxable in the hands of the amalgamated company u/s 41(1) as when the assessee is allowed the benefit of the accumulated losses while computing those loses, the income which accrued to it had to be adjusted and only thereafter net losses could have been allowed to be set off by the assessee company.

Shankar Dalal & others -vs.- CIT (2017)(Bom.)

Provisions of local land laws should be considered while determining the land as agricultural land.

In the return of income, the assessee has declared that gain on sale of agricultural land is exempt since the land does not constitute "Capital Assets" as defined u/s 2(14). The Assessing Officer passed an order denying exemption giving reasons that land did not constitute agricultural land since no agricultural operations were carried out regularly and same was sold to a company engaged in the business of development of infrastructure activity. The Assessing Officer also ruled that though the land was located beyond the specified limits from the municipal limits i.e. beyond 8 kms, yet it was to be treated as capital asset. On appeal, Commissioner (Appeals) held the land as agricultural land and exempts capital gain. The Tribunal upon re-inspection held that "To the extent the land is actually used for dry crop, the land has to be regarded to be an agricultural land the balance 4/5th of the land could not be regarded to be the agricultural land".

Bombay High Court reverses ITAT order, and held that "merely because the assessees could not produce and utilize the land fully by employing labour, and/or unable to give the crop statements should not have been the criteria" The Court held that the Revenue fell in error in not considering the provisions of local land laws, as activities performed by assessee on the land were recognised as 'agricultural' activities under the Local land law.

Mother Hospital (P) Ltd -vs.- CIT (2017)(SC)

A lessee cannot be said to be the "owner" for purposes of claiming depreciation and the lessee is entitled to depreciation on the cost of construction incurred by him but not on the cost incurred by the owner and reimbursed by the lessee

A partnership firm had been constituted by 'M' and his family members. The said firm owned a land. The purpose of the partnership firm was to run a super speciality hospital and, accordingly, the firm started construction of the hospital building. Thereafter, an agreement was entered into between the firm and the company by which it was agreed that the firm would complete the construction of the building and hand over possession of the same on completion, on the condition that the entire cost of construction of the building would be borne by the assessee company. The assessee-company filed its return in which it claimed depreciation on the building part of the said property. The Assessing Officer rejected the claim of depreciation and added back the same.

Building which was constructed by the firm belonged to the firm. The title in case of immovable property cannot pass when its value is more than ₹ 100/- unless it is executed on a proper stamp paper and is also duly registered with the sub-Registrar. Nothing of the sort took place. In the absence thereof, it could not be said that the assessee had become the owner of the property.

Further, the Court held that it is only when assessee holds a lease right or other right of occupancy and any capital expenditure is incurred by it on construction or renovation or improvement of building, assessee would be entitled to depreciation to extent of such expenditure incurred. However, where construction is carried out by owner-lessor and expenditure is only reimbursed by assessee-lessee, Explanation 1 to section 32(1) would not come to aid of assessee.

Rajesh Kumar Aggarwal -vs.- CIT (2017)(Delhi)

Exemption u/s 54F can be granted in revision u/s 264

The assessee for assessment year 2009-10 had claimed a set off of capital gains from sale towards house property as against capital losses and the loss in respect of shares. The set off was not permitted. In the meanwhile, the assessee had purchased new property, apparently with the intention of seeking the benefit u/s 54F. The original property was sold on 20.06.2008; the new property was purchased in July, 2008. However, the benefit of sec. 54F was not claimed when the return was filed on 30.09.2009. The assessment order disallowed the set off. This resulted in a capital gain. By then, the time to file the revised return had elapsed and the assessment was completed. The assessee filed the revision petition u/s 264 of the Act. The Commissioner rejected the assessee's revision petition stating that no documentary evidences whatsoever were filed by the assessee during the course of assessment proceedings with regard to cost of improvement made by him in the Property. Further, the assessee has also failed to bring on record reasons that prevented him from filing the copies of so called valuation report before the AO. Thus, the valuation report now filed by the assessee is a self serving document without any corroboratory evidences. As regards the claim of deduction u/s 54F, the assessee has not claimed the same in his return. Further, it has also never been raised by him during the course of assessment proceedings.

Section 264 in its operative part states that the (Principal Commissioner or) Commissioner may, either of his own motion or on an application by the assessee for revision, call for the record of any proceeding under this Act in which any such order has been passed and may make such inquiry or cause such inquiry to be made and, subject to the provisions of this Act, may pass such order thereon, not being an order prejudicial to the assessee, as he thinks fit.

The phraseology adopted by the provision is of the widest amplitude. The term "any such order as he thinks fit" is only qualified by subject to provisions of this Act. Therefore, unless there is a direct impediment to the power u/s 264 (exercisable by the Commissioner) which inhibits the grant of relief, it is per se admissible. The impediment may be in the form of a substantive provision which might place a time limit, to the grant of such relief or it may be otherwise. In the present case, the concerned provision sec. 54F, does not per se contain any such impediment. Therefore, as far as the text of the provision goes, this Court is of the opinion that there is no bar in the grant of the relief despite the assessee apparently having missed the bus and having committed the mistake.

Pr. CIT -vs.- Ramgopal Minerals (2017)(Kar)

No cessation of liability even if creditors were untraceable but evidences of payments to them were produced

In course of assessment, the Assessing Officer made addition to assessee's income u/s 41(1) in respect of cessation/ remission of trading liability of various transporters who transported the minerals for the assessee stating that the assessee had failed to produce these transporters/trade creditors before the authority, despite the summons issued to them. On further appeal, the Tribunal completely set aside the additions made by the revenue. On further appeal, High Court held that in legal parlance, merely because the creditor could not be traced on the date when the verification was made, same is not a ground to conclude that there was cessation of the liability.

Cessation of the liability has to be cessation in law, of the debt to be paid by the assessee to the creditor. The debt is recoverable even if the creditor has expired, by the legal heirs of the deceased creditor. Under the circumstances, in the present case, it can hardly be said that the liability had ceased. If the liability had not ceased or the benefit was not taken by the assessee in respect of such trade liability, the conditions precedent were not satisfied for invoking sec. 41(1).

Tribunal has clearly recorded the evidence and findings of facts in favour of the respondent-assessee that the assessee has produced the documentary evidence in the form of ledger accounts and proof of payments made through bank channel and PAN numbers also.

Burden of the Revenue to summon such creditors or transporters for establishing that the liability has ceased could not be shifted upon the respondent-assessee.

There is no perversity in the same so as to give rise to any substantial question of law arising in the present case, requiring consideration u/s 260A

CIT -vs.- Vinzas Solutions India (P.) Ltd (2017) (Mad)

Payment made by the dealer for outright purchase of software is not tantamount to "royalty"

The respondent-assessee was a dealer in computer software, having purchased the same from various companies. During the course of assessment proceedings, a disallowance was effected in terms of sec. 40(a)(ia) by the Assessing Officer on the ground that consideration for purchase was of the nature of 'royalty' under Explanation 4 and 5 of section 9(1)(vi) and tax ought to have been deducted at source in accordance with the provisions of section 194J. On appeal, CIT(A) affirmed the order of the Assessing Officer. On appeal, Tribunal reversed the order of CIT(A).

The term "'royalty' normally connotes the payment made by a person who has exclusive right over a thing for allowing another to make use of that thing which may be either physical or intellectual property or thing. The exclusivity of the right in relation to the thing for which royalty is paid should be with the grantor of that right. Mere passing of information concerning the design of a machine which is a tailor-made to meet the requirement of a buryer does not by itself amount to transfer of any right of exclusive user, so as to render the payment made therefor being regarded as 'royalty. There is a difference between a transaction of sale of a 'copyrighted article' and one of 'copyright' itself.

The provisions of sec. 9(1)(vi) as a whole, would stand attracted in the case of the latter and not the former. Explanations 4 and 7 relied by the authorities would thus have to be read and understood only in that context and cannot be expanded to bring within its fold transaction beyond the realm of the provision.

CIT -vs.- Subhash Vinayak Supnekar (2016) (Bom.)

Investment can be made out of advance received under sale agreement for sec. 54EC relief

The assessee entered into an agreement to sell for the subject property on 21-2-2006 and the sale deed was executed on 5-4-2007. The assessee had invested an amount of ₹ 50 lakhs from the advance received under the agreement to sale in the Rural Electrification Corporation Ltd. bonds on 2-2-2007. Assessing Officer as well as CIT(A) held that the assessee was not entitled to the benefit of section 54EC as the amount was invested in the bonds prior to the sale of the subject property on 5-4-2007. The Tribunal, however, held that even when an assessee made investment in bonds as required under section 54EC on receipt of advance as per the agreement to sell, still it was entitled to claim the benefit of section 54EC. Hight Court affirmed the order of the tribunal

Ian Peter Morris -vs.- ACIT (2016) (SC)

Interest u/s 234B & 234C does not apply on salary income

The appellant–assessee along with three others had promoted a Company. The said Company was acquired by one Synergy Credit Corporation Limited (the Acquirer Company). The appellant was offered the position of Executive Director in the Acquirer Company. Further, a Non-Compete Agreement was signed between the appellant–Assessee and the Acquirer Company imposing a restriction on the appellant from carrying on any business of Computer Software development and marketing for a period of five years for which the appellant–Assessee was paid a sum of ₹ 21,00,000/-. The question that arose in the proceedings commencing with the Assessment Order is whether the aforesaid amount of ₹ 21 lakhs is on account of 'salary' or the same is a 'capital receipt'. The High Court in the order under appeal took the view that the said amount is 'salary amount' on which interest would be chargeable/leviable u/s 234B and 234C.

However, the High Court's ruling to levy interest u/s 234B & 234C on this income was challenged in appeal. The Supreme Court held that on perusal of the relevant provisions of Chapter VII of the Act, against salary, a deduction, at the requisite rate at which income tax is to be paid by the person entitled to receive the salary, is required to be made by the employer failing which the employer is liable to pay simple interest thereon. In cases where receipt is by way of salary, deductions u/s 192 of the Act are required to be made. No question of payment of advance tax under Part 'C' of Chapter VII of the Act can arise in cases of receipt by way of 'salary'. Therefore, interest obligations u/s 234B and 234C would have no application to the present situation since the High Court has already decided that the non-Compete Agreement was by way of salary. The Apex Court thereby modified the order, deleting interest u/s 234B & 234C.

Pr. CIT -vs.- Bharat Heavy Elect. Ltd. (2016) (P&H)

Usual clauses in contract involving payments for construction, erection & commissioning etc of plants involving inputs from technical personnel do not constitute "payments for technical services" attracting TDS obligations u/s 194J

Post TDS inspection u/s 133A of the Act, the AO found that the company had made payments to five contractors in respect of various contracts and deducted tax in respect thereof u/s 194C of the Act, whereas, all the contracts involved the provision of professional and technical services which fell within the ambit of the provisions of sec. 194J of the Act and not u/s 194C.

The question, therefore, was whether the amounts paid under the contracts constitute fees for professional or technical services attracting sec. 194J or whether they constitute payments to contractors attracting the provisions of sec. 194C?

The High Court held that testing, pre-commissioning, commissioning and post commissioning are required to be carried out by a contractor to satisfy the customer that the work has been executed in a proper manner; that the equipment has been installed as required and that its performance meets the parameters specified in the contract. The personnel that are required to test and commission the plant and equipment perform their functions not under a contract for the supply of technical services to the customer, but to satisfy the customer on behalf of the contractor that the plant and equipment has been duly supplied as per the contractual specifications.

Indeed, this entire exercise would require the deployment of technical personnel, but what is important to note is that the technical personnel are deployed not for and on behalf of the customer, but for and on behalf of the contractor itself with a view to ensuring that the contractor has supplied the equipment as per the contractual specifications. The contract entered did not involve the supply of professional or technical services within the meaning of sec. 194J

CIT vs. Greenfield Hotels & Estates Pvt. Ltd (2016)(Bom.)

Where Revenue accepts decision of a Court/Tribunal on an issue of law, not challenging it in appeal, then a subsequent decision following the earlier cannot be challenged

The revenue was in appeal against the tribunal's order of having made provisions of section 50C inapplicable to transfer of land & building, being a leasehold property. It was brought to the notice of the court that the Revenue had not preferred any appeal against the decision of the Tribunal in a like case where facts were similar and it could be inferred that it had been accepted.

The High Court followed decisions of the court in DIT -vs.- Credit Agricole Indosuez 377 ITR 102 and the Apex Court in UOI -vs.- Satish P. Shah 249 ITR 221, which laid down the salutary principle that where the Revenue has accepted the decision of the Court/Tribunal on an issue of law and not challenged it in appeal, then a subsequent decision following the earlier decision cannot be challenged.

Further, it was not the Revenue's case before the court that there were any distinguishing features either in facts or in law in the present appeal from that arising in the earlier case. In the above view, the question as framed by the Revenue did not give rise to any substantial question of law and accordingly, was not entertained

ADIT -vs.- E-Funds IT Solution Inc (2017) (SC)

Outsourcing services provided by E-Funds Corporation, USA to its Indian affiliate does not constitute Permanent Establishment under the India-USA Tax Treaty

E-Funds Corporation ("**E-Funds US**") is a company incorporated in the USA and part of a group which is engaged in the business of electronic payments, ATM management service, decision support & risk management and similar professional services.

E-Funds US and its group company, E-Funds IT Solutions Group Inc ("**E-Funds IT US**") entered into contracts with their clients in the US, for the provision of Information Technology Enabled Services ("**ITES**"). These contracts were assigned or sub-contracted to e-Funds International India Private Limited ("**E-Funds India**"), an indirect subsidiary of E-Funds US in India, for execution. Under the terms of the agreements between E-Funds India and the two US entities, E-Funds India provided support services to E-Funds US and E-Funds IT US, which in turn enabled them to render services to their clients. The Assessing Officer ("**AO**"), relying upon the Functions, Assets and Risks Analysis ("**FAR Analysis**") performed in relation to E-Funds US and E-Funds India, observed that:

- E-Funds US allowed E-Funds India to use its technology and infrastructure for provision of IT enabled services for free;
- E-Funds US even undertook marketing activities for E-Funds India and the latter did not bear any significant risks in the overall services;

In light of this, the AO concluded that:

- E-Funds India was a fixed place PE of E-Funds US and E-Funds IT US in India since the US entities had a fixed place in India through which they were carrying on their own business.
- Thus, the income attributable to E-Funds US and E-Funds IT US, which was not included in the income earned by E-Funds India, was to be taxed in India.

This view was upheld by the Commissioner (Appeals) ("**CIT(A)**") who concluded that in addition to a fixed place PE, there also existed a service PE and an agency PE. On appeal, the findings of CIT(A) in relation to the existence of fixed place PE and a service PE were affirmed by the Income Tax Appellate Tribunal ("**Tribunal**"). The Tribunal did not rule on the existence of an agency PE as arguments on that ground had not been furthered by the Income Tax Department ("**Revenue**"). The findings of all the above authorities were set aside by the Delhi High Court ("**High Court**"), which ruled that E-Funds India did not constitute a PE of E-Funds US or E-Funds IT US in India. Aggrieved by the ruling of the High Court, the Revenue preferred an appeal before the Supreme Court.

The Supreme Court, after hearing all contentions put forth by the parties, arrived at the following conclusions:

1. **Determination of Fixed Place PE**

   The Supreme Court relied on its previous decision in Formula One World Championship Ltd vs. CIT to hold that a fixed place would constitute a PE of a non-resident only when such fixed place was "at the disposal" of that non-resident. A fixed place would be treated as being "at the disposal" of a non-resident enterprise when that enterprise has right to use the said place and has control thereupon. Merely having access to such a place, for the purposes of business, would not suffice. Control should be of a considerable amount and usually control would be present where the foreign entity can employ the place of business at its discretion.

In the present case, the Supreme Court noted that neither E-Funds US nor E-Funds IT US had a physical premise in India at its disposal nor did they have control over use of E-Funds India's premises for their business.

It further observed that the finding of the lower authorities regarding the existence of a PE, was based mainly on the fact that the business of the US entities was being outsourced to a 100% subsidiary in India and this resulted in a PE. On this aspect, the Supreme Court affirmed the observations of the High Court to the effect that a subsidiary of a foreign parent carrying on business in the source State does not by itself create a PE in the source State. The High Court had observed that close association between the entities or interactions or transactions between them were not appropriate tests to determine the existence of a PE. It had further held that neither the assigning of a contract nor sub-contracting, nor provision of intangible software free of cost would be relevant in determining a PE. Moreover, even if the foreign entities had reduced their expenditure by transferring the business to the Indian subsidiary, it would not by itself create a fixed place PE.

All of these observations were affirmed by the Supreme Court, which noted that it was "fundamentally erroneous" to say that merely by contracting with a 100% subsidiary, a PE would be created. In any event, E-Funds India had only rendered back office support services to both US entities, and as such, it could not be said that the business of either US entity had been carried on through E-Funds India.

On that basis, the Supreme Court held that the outsourcing of work by E-Funds US and E-Funds IT US to India would not result in the creation of a fixed place PE of E-Funds US or E-Funds IT US in India.

2. Determination of Service PE

Article 5(2)(l) of the India – US Tax Treaty provides that a service PE would be constituted in India where a US enterprise furnished services within India through employees or other personnel. The Revenue had argued that personnel engaged by E-Funds India for the provision of support services to E-Funds US and E-Funds IT US were de facto working under the control of the US entities, and as such, constituted a service PE of the US entities in India.

On facts, the Court observed that none of the customers of E-Funds US or E-Funds IT US were located in India, or receiving services in India. As such, the primary requirement that services be furnished "within India" had not been satisfied. On that basis, the Court did not go into the question of control over the personnel engaged by E-Funds India. In any event, E-Funds India merely undertook auxiliary operations that facilitated the provisioning of the main service (i.e. ITES) by E-Funds US and E-Funds IT US abroad. As such it could not be stated that a service PE had been created in India in terms of the India – US Tax Treaty.

3. Determination of Agency PE

On the question of whether a E-Funds India could be said to constitute the agency PE of E-Funds US and E-Funds IT US, the Supreme Court agreed with the view of the High Court that since the Revenue had not raised the argument of agency PE before the Tribunal or the High Court, it could not be raised at the level of the Supreme Court. In any event, it was observed that an agency PE could only be constituted in terms of Article 5(4) of the India – US Tax Treaty. Since the tests under Article 5(4) had not been satisfied with respect to E-Funds India, no agency PE could be said to have been constituted.

4. Mutual Agreement Procedure

In the present case, the competent authorities of India and the US had initiated proceedings under the Mutual Agreement Procedure ("**MAP**") article of the India – US Tax Treaty and had entered into an agreement as to attribution of profits between the US entities and E-Funds India. The Revenue contended that the PE issue stood determined owing to certain statements made in the MAP Settlement Agreement to the effect that the US entities had PEs in India. It was argued that these statements should continue to remain applicable to the E-Funds Group as there had been no subsequent change in the factual position of the Group.

On this point, the Court had concluded that MAP proceedings had been initiated on a without prejudice basis and that the existence of a PE was a question of law that needed to be determined purely on merits. Referring to Paragraph 3.6 of the OECD Manual on MAP Procedure, the Supreme Court observed that it was "very clear" that a MAP Settlement Agreement was time and case specific and could not be considered precedent for subsequent years. Thus, statements made in a MAP Settlement Agreement for a previous year could not be used in determining PE status for a subsequent year.

Merely holding a subsidiary in India which provides services to the parent, would not constitute a fixed place PE. A subsidiary would have to conform to the principles required to be considered a PE, and only if they are satisfied, would it be considered as a PE

R.B Shreeram Durgaprasad -vs.- CIT (2016) (Bom.)

Penalty order is illegal and without jurisdiction if it was passed during pendency of assessment proceeding

Certain addition was made to assessee income in reassessment proceedings. The assessee filed appeal before the Tribunal against such addition. The Assessing Officer levied penalty u/s 271(1)(c) upon assessee, while the appeal was pending before the tribunal. On reference, the assessee contended that in terms of section 275(1) (a), penalty proceedings could not have been initiated pending appeal before the Tribunal.

The High Court ruled in favor of the assessee by contending that the language of section 275(1)(a) clearly shows that the order imposing penalty cannot be passed if the appeal against basic order of assessment is pending before the competent superior authority. Here, though 1st appellate authority had disposed of the appeal, further appeal of assessee before the Tribunal was very much pending. The order imposing penalty, therefore, appears to be premature and, therefore, illegal and without jurisdiction. The notices for initiation of those proceedings are during the pendency of appeal before the Tribunal. Essential ingredients of section 275(1) are clearly not in contemplation of notice issuing authority on these dates. The form or language of these notices shows clear nonapplication of mind in this respect. It is obvious that such notices initiating the penalty proceedings could not have been issued before order of the Tribunal.

Hightension Switchgears Pvt Ltd -vs.- CIT (2016) (Kolkata)

No TDS on transportation charges reimbursed by buyer if seller is liable to pay such charges to GTA

During the year 2006-07, a seller had sold certain goods to the assessee(buyer). Under the contract of sale, the seller was bound to send the goods to the buyer and to pay the transportation charges to the GTA (Goods Transport Agency). It was, however, entitled to recover the transportation charges from the buyer. The assessee reimbursed the freight component to the seller and claimed deduction of the same. The Tribunal held that the assessee was liable to deduct tax at source as per section 194C in respect of freight component. Since the assessee had failed to deduct tax at source in respect thereof, the lower authorities were justified in disallowing the freight component as per section 40(a)(ia). Assessee on further appeal to High Court.

The High Court ruled in favour of the assessee by contending that even assuming that the supplier in transporting the goods to the assessee acted as an agent of the assessee and the assessee has reimbursed the freight charges to the supplier, who in turn has paid to the concerned transporter as held by the Tribunal is conceptually correct, no other conclusion is possible. The agent being the supplier in the instant case has admittedly paid to the transporter and has also deducted tax at source. When the agent has complied with the provision, the principal cannot be visited with penal consequences. For one payment there could not have been two deductions. Moreover, when a person acts through another, in law, he acts himself

CIT -vs.- Anil Kumar & Co. (2016) (Kar.)

No addition could be made on estimated basis without rejecting books of account of assessee

The assessee was a partnership firm carrying on the business as cotton merchants and commission agents. The assessee filed its return of income for the AY 2006-2007, declaring total income of INR NIL. On such return being selected for scrutiny assessment order came to be framed under section 143(3) after issuing notice and hearing the assessee. The AO noticed that the gross profit declared by the assessee for the earlier assessment years and the present assessment year were at variance and as such the gross profit was adopted at 4 per cent of the total turnover. On appeal, the Commissioner(Appeals) concluded that differential gross profit of Rs.5.99 lakhs was to be sustained as against gross profit of Rs. 32.44 lakhs made by the Assessing Officer. On further appeal, the Tribunal allowed the appeal of the assessee and deleted the addition made by the Commissioner (Appeals) on gross profit. On further, appeal to High Court.

The tribunal has rightly held that when the books of account of the assessee had not been rejected and assessment having not been framed u/s 144, the A.O and the Commissioner(Appeals) were in error in resorting to an estimation of income and such exercise undertaken by them was not sustainable. Section 145(3) lays down that the Assessing Officer can proceed to make assessment to the best of his judgment under section 144 only in the event of not being satisfied with the correctness of the accounts produced by the assessee. In the instant case the Assessing Officer has not rejected the books of account of the assessee. To put it differently the Assessing Officer has not made out a case that conditions laid down in section 145(3) are satisfied for rejection of the books of account. Thus, when the books of account are maintained by the assessee in accordance with the system of accounting, in the regular course of his business, same would form the basis for computation of income. In the instant case it is noticed that neither the Assessing Officer nor the Commissioner (Appeals) have rejected the books of account maintained by the assessee in the course of the business. As such tribunal has rightly rejected or set aside the partial addition made by Assessing Officer for arriving at gross profit and sustained by the Commissioner (Appeals) and rightly held that entire addition made by the Assessing Officer was liable to be deleted. The said finding is based on sound appreciation of facts and it does not give rise for framing substantial question of law.

CIT -vs-. Kotak Securities Ltd (2016) (SC)

Transaction charge paid to BSE isn't 'FTS' as BSE isn't providing customized services to members

By the impugned order dated 21st October, 2011 passed in the aforesaid appeal, the High Court of Bombay has held that the transaction charges paid by a member of the Bombay Stock Exchange to transact business of sale and purchase of shares amounts to payment of a fee for 'technical services' rendered by the Bombay Stock Exchange. Therefore, under the provisions of Section 194J of the Income Tax Act, 1961 (for short "the Act"), on such payments TDS was deductible at source. The said deductions not having been made by the appellant - assessee, the entire amount paid to the Bombay Stock Exchange on account of transaction charges was not deducted in computing the income chargeable under the head "profits and gains of business or profession" of the appellant - assessee for the Assessment Year in question i.e. 2005-2006. This is on account of the provisions of Section 40(a)(ia) of the Act. Notwithstanding the above, the Bombay High Court held that in view of the apparent understanding of both the assessee and the Revenue with regard to the liability to deduct TDS on transaction charges paid to the Bombay Stock Exchange right from the year 1995 i.e. coming into effect of Section 194J till the Assessment Year in question, benefit, in the facts of the case, should be granted to the appellant - assessee and the disallowance made by the Assessing Officer under Section 40(a)(ia) of the Act must be held to be not correct

The Apex Court ruled in favor of the assessee by contending that "we hold that the view taken by the Bombay High court that the transaction charges paid to the Bombay Stock Exchange by its members are for 'technical services' rendered is not an appropriate view. Such charges, really, are in the nature of payments made for facilities provided by the Stock Exchange. No TDS on such payments would, therefore, be deductible under Section 194J of the Act ".

IVRCL-KBL (JV) -va.- ACIT (2016) (Andhra Pradesh)

Credit of TDS won't be denied to a contractor even if entire work has been sub-contracted to others

The assessee was a joint-venture executing civil contract works. It was awarded contracts by the Irrigation Department of the State Government. The assessee gave said contracts subsequently on sub-contract basis to one of its constituents without any margin. The assessee filed its return claiming refund of tax deducted at source from bills paid by the State Government. The assessing authority contended that as no real work was carried on by the assessee, no income had accrued to it and therefore , credit for TDS was not allowable in the hands of the assessee in terms of Rule 37BA (2)(i) of the income tax rules,1962.

The High Court ruled in favour of the assessee by contending that there are two distinct and independent contracts. There is no privity of contract between the government and the constituent of the assessee i.e. sub-contractor. The rights and obligations under the first contract are only that of the Government and the assessee; and those, in the second contract, are only that of the assessee and the sub-contractor. The contractual obligation, to execute the work for the Government, is that of the assessee joint venture alone, and not that of the constituent member of the JV i.e. the sub-contractor. It is evident, therefore, that the contractual receipts under the first contract is only that of the assessee; and the income, arising out of the said contract, is assessable only in their hands, and not in the hands of the sub-contractor. The High Court set aside the order passed by the AO and directed to determine the quantum of credit for TDS which the assessee is entitled to and refund the amount so computed to assessee in accordance with law

CIT -vs.- Priya Blue Industries (P) Ltd (2016) (Guj)

Finished products obtained from ship breaking activity are usable as such and hence, are not 'waste and scrap' though commercially known as scrap, thus provision of TCS is not applicable.

The assessee-company, engaged in ship breaking activity, sold old and used plates, wood etc. It did not produce any document or papers to show collection of tax at source on sale of such items and payment thereof to the credit of the Central Government nor was certificate in Form No.27C produced. The Assessing Officer observed that such items were in the nature of scrap and therefore, the assessee is liable to collect tax at source from the buyers of scrap. Accordingly, demand u/s 201(1) alongwith interest u/s 201(1A) was raised. The assessee claimed that such items are usable as such, and are hence not 'scrap', thus, provisions relating to collection of tax at source is not applicable.

The Commissioner (Appeals) observed that the assessee was engaged in ship breaking activity and the products obtained from the activity were finished products which constituted sizable chunk of production done by the ship breakers. The Commissioner (Appeals) agreed with the assessee that such products though commercially known as 'scrap' were definitely not "waste and scrap". The Tribunal firstly recorded a list of items sold by the assessee from the ship breaking activity. It found that the assessee collected and paid tax, for seven items, but did not collect tax at source on certain items viz. old and used plates; non-excisable (exempted) goods like wood etc. It observed that the 'waste and scrap' must be from manufacture or mechanical working of material which is definitely not usable as such because of breakage, cutting up, wear and other reasons. Since the assessee is engaged in ship breaking activity, these items/products are finished products obtained from such activity which are usable as such and hence, are not 'waste and scrap' though commercially known as scrap. Accordingly, the Tribunal also decided the issue in favour of the assessee.

On further appeal, the High Court concurred with the view of the Tribunal.

CIT -vs.- M/s Thyssen Krupp Industries Private Ltd (2015)(Bom)

An Adjustment with respect to transfer pricing has to be confined to transactions with Associated Enterprises and cannot be made with respect to transactions with unrelated third parties

The assessee is in the business of execution of turnkey contracts involving design, manufacture, supply, erection and commissioning of sugar plants, cement plants, etc. During the subject Assessment Year, the assessee entered into international transactions with its Associated Enterprises (AE), as well as transactions with independent parties. The TPO proposed an addition on account of enhancement of profit margin on all transactions of the assessee. Aggrieved by the order, assessee filed an appeal with ITAT. The tribunal held that only transactions entered into by an assessee with its AE are subject to transfer pricing adjustment and not otherwise. Thus, allowing the assessee's appeal before it. Aggrieved by the order, the revenue filed an appeal with High Court.

The High Court dismisses revenue appeal by contending that as per Chapter X of the Act, redetermination of the consideration is to be done only with regard to income arising from International Transactions on determination of ALP. The adjustment which is mandated is only in respect of International Transaction and not transactions entered into by assessee with independent unrelated third parties, therefore this adjustment is beyond the scope and ambit of Chapter X of the Act.

Berger Paints India Ltd. -vs.- CIT (2017) (SC)

Securities premium shall not be considered as a part of the capital employed for the purpose of sec. 35D.

The appellant is a Limited Company engaged in the business of manufacture and sale of various kinds of paints. A notice was issued by the A.O. to the appellant (assessee) under Section 143(2) of the Act which called upon the appellant to explain as to on what basis the appellant had claimed in the return a deduction under the head "preliminary expenses" amounting to Rs.7,03,306/- being 2.5% of the "capital employed in the business of the company" under Section 35D of the Act. The appellant (assessee) replied to the notice. The appellant (assessee) contended therein that it had issued shares on a premium which, according to them, was a part of the capital employed in their business. The appellant, therefore, contended that it was on this basis, it claimed the said deduction and was, therefore, entitled to claim the same under Section 35D of the Act. The A.O. did not agree with the explanation given by the appellant. He was of the view that the expression "capital employed in the business of the company" did not include the "premium amount" received by the appellant on share capital. The Commissioner (Appeals) has deleted the addition. However, the Tribunal reversed the view taken by the Commissioner (Appeals). The High Court concurred with the Tribunal.

The Apex Court observed that if the intention of the Legislature were to treat the amount of "premium" collected by the Company from its shareholders while issuing the shares to be the part of "capital employed in the business of the company", then it would have been specifically said so in the Explanation (b) of sub-section (3) of Section 35D of the Act. It was, however, not said. Non-mentioning of the words does indicate the legislative intent that the Legislature did not intend to extend the benefit of Section 35D to such sum.

The company's accounts do not show the reserve and surplus as a part of its issued, subscribed and paid up capital. It is taken as part of share holders fund but the same was not a part of the issued, subscribed and paid up capital of the Company

Similarly, Companies Act which deals with the "issue of shares at premium and discount" requires a company to transfer the amount so collected as premium from the shareholders and keep the same in a separate account called "securities premium account". It does not anywhere says that such amount be treated as part of capital of the company employed in the business for one or other purpose.

Thus, securities premium shall not be considered as a part of the capital employed for the purpose of sec. 35D.

National Travel Services -vs.- CIT (2018) (SC)

Section 2(22)(e) gets attracted inasmuch as a loan has been made to a shareholder, who is the beneficial owner of shares holding not less than 10% of the voting power in the Company.

A reading of the amended definition would indicate that, after 31.05.1987, a "shareholder" is now a person who is the beneficial owner of shares holding not less than 10% of the voting power of the Company. After amendment of year 1988 carried out in section 2(22)(e), in order to invoke provisions of said section, 'shareholder' has only to be a person who is beneficial owner of shares.

One cannot be a registered owner and beneficial owner in the sense of a beneficiary of a trust or otherwise at the same time. It is clear therefore that the moment there is a shareholder, who need not necessarily be a member of the Company on its register, who is the beneficial owner of shares, the Section gets attracted without more. To state, therefore, that two conditions have to be satisfied, namely, that the shareholder must first be a registered shareholder and thereafter, also be a beneficial owner is not only mutually contradictory but is plainly incorrect.

Also, what is important is the addition, by way of amendment, of such beneficial owner holding not less than 10% of voting power. This is another indicator that the amendment speaks only of a beneficial shareholder who can compel the registered owner to vote in a particular way.

PCIT -vs.- Tejua Rohitkumar Kapadia (2018) (SC)

Purchases cannot be treated as bogus u/s 69 if

a. they are duly supported by bills;

b. all payments are made by account payee cheques;

c. the supplier has confirmed the transactions;

d. there is no evidence to show that the purchase consideration has come back to the assessee in cash;

e. the sales out of purchases have been accepted; and

f. the supplier has accounted for the purchases made by the assessee and paid taxes thereon

CIT -vs.- Vasisth Chay Vyapar Limited (2018) (SC)

In case of NBFCs, income from NPAs would be taxable on receipt basis

The assessee, an NBFC, had advanced certain Inter-Corporate Deposits (ICD) to another company. As no interest could be received on such deposits for more than six months, in terms of directions given by the Reserve Bank of India (RBI), the taxpayer treated the said ICDs as NPA and did not offer interest income on ICDs.

However, the tax officer imputed interest on said ICDs to income of the assessee by applying mercantile system of accounting. The tax officer contended that RBI directives could not override the provisions of the Act.

The CIT(A) affirmed the order of the tax officer. On further appeal, the Income Tax Appellate Tribunal (ITAT) held in favour of the taxpayer and deleted the addition made by the AO.

The Delhi HC held in favour of the assessee that income in the hands of NBFCs is to be recognised as per the RBI prudential norms regardless of the fact even if they deviate from the mercantile system of accounting. The Hon'ble SC confirmed the order of Delhi HC and accordingly, rejected Revenue's appeal against the order of the Delhi HC.

Honda Siel Cars India Ltd. -vs.- CIT (2017) (SC)

Technical fee paid under a technical collaboration agreement for setting up a joint venture company in India is to be treated as capital expenditure, if upon termination of the agreement, the joint venture would come to an end

The assessee, Honda Siel Cars India Ltd., is a joint venture company between Honda Motors, a Japanese company and Siel Ltd., an Indian company. The assessee and Honda Motors entered into a technical collaboration agreement (TCA) on May 21, 1996 under which a technical fee of 30.5 million USD was payable by the assessee in five equal

instalments on a yearly basis. Under the TCA, Honda Motors had to provide manufacturing facilities, know-how, technical information, information regarding intellectual property rights to the assessee which the assessee was entitled to exploit only as a licensee, without any proprietary rights. The assessee treated the technical fees as revenue while the Revenue authorities contended that it is capital in nature.

The Apex Court held that, in this case, technical fee is capital in nature since upon termination of TCA, the joint venture itself would come to an end. It is further held that if limited rights to use technical know-how is obtained for a limited period for improvising the existing business, the expenditure is revenue in nature. However, if technical know-how is obtained for setting up a new business, the know-how is a capital expenditure.

Director, Prasar Bharati -vs.- CIT (2018) (SC)

Payment made by the Prasar Bharati Doordarshan Kendra to various accredited advertising agencies to secure more business was in the nature of commission liable to TDS u/s 194H

The appellant, 'Prasar Bharati Doordarshan Kendra', was functioning under the Ministry of Information and Broadcasting of Government of India. In the course of business activities which included running of TV channels, the appellant had been regularly telecasting advertisements of several advertising agencies.

With a view to have better regulation of the practice of advertising, the appellant entered into an agreement with various advertising agencies. As per the agreement, in order to receive the status of 'accredited' agencies, the said agencies had to make an application to the appellant and in return they were allowed to telecast advertisement of several consumer products manufactured by several companies on the appellant's TV channel. One of the stipulations in the said agreement was that the appellant would pay commission of 15% to the agency which the agency was allowed to retain from the revenue generated from the telecasting of advertisements.

The AO held that since the payments made by the appellant to the agencies were in the nature of commission, the provisions of sec. 194H were attracted and the appellant defaulted in not deducting the TDS on such payments.

On further appeal before the Apex Court, it was argued by the appellant that the relationship between appellant and the accredited agencies was not that of principal and agent and it was rather in the nature of principal-to-principal. It was further argued that in terms of agreement, the agencies purchased the air time from the appellant and sold it in the market to their customers after retaining 15% commission given to them by the appellant and therefore, the transaction cannot be regarded as being in between principal and agent.

The Apex Court considered the agreements entered into by the appellant with the accredited agencies and discussed the provisions of sec. 194H of the Act and held that the provisions of sec. 194H are applicable to the appellant because the payments made by the appellant pursuant to the agreement in question were in the nature of payment made by way of "commission" and, therefore, the appellant was under statutory obligation to deduct the income tax at the time of credit or/and payment to the payee.

The conclusion of the High Court is clear from the undisputed facts emerging from the record of the case because the agreement itself has used the expression "commission" in all relevant clauses; Second, there is no ambiguity in any clause and no complaint was made to this effect by the appellant; Third, the terms of the agreement indicate that both the parties intended that the amount paid by the appellant to the agencies should be paid by way of "commission" and it was for this reason, the parties used the expression "commission" in the agreement; Fourth, keeping in view the tenure and the nature of transaction, it is clear that the appellant was paying 15% to the agencies by way of "commission" but not under any other head; Fifth, the transaction in question did not show that the relationship between the appellant and the accredited agencies was principal to principal rather it was principal and Agent; Sixth, it was also clear that payment of 15% was being made by the appellant to the agencies after collecting money from them and it was for securing more advertisements for them and to earn more business from the advertisement agencies; Seventh, there was a clause in the agreement that the tax shall be deducted at source

on payment of trade discount; and lastly, the definition of expression "commission" in the Explanation appended to Sec. 194H being an inclusive definition giving wide meaning to the expression "commission", the transaction in question did fall under the definition of expression "commission" for the purpose of attracting rigor of Sec. 194H of the Act.

Once it is held that the provisions of Sec. 194H apply to the transactions, it is obligatory upon the appellant to have deducted the income tax while making payment to the advertisement agencies. The non-compliance of sec. 194H by the assessee attracts the rigor of sec. 201 which provides for consequences of failure to deduct or pay the tax as provided u/s 194H of the Act.

The appellant had relied on the decision of the Allahabad High Court in the case of Jagran Prakashan Ltd. -vs.- DCIT (TDS) (2012) 345 ITR 288, which was distinguished by the Apex Court on the fact that in the case of Jagran Prakasan Ltd. the parties did not have any agreement like the one in the present case. Accordingly, the appellant's case was dismissed.

Tooltech Global Engineering P. Ltd. vs. ACIT (2015) (Bom)

Chapter X of the Act, is an anti-avoidance measure and not an anti-evasion measure. The object of the Transfer Pricing Officer is to put a stop to capital erosion and transfer of profits from one taxable territory to another taxable territory.

The assessee had granted certain loans to its associated enterprises (AE) on which no interest was charged. The AO was of the opinion that the granting of loans to AE is an international transaction. After so holding the AO worked out interest income thereon to determine the Arm's Length Price. The said order was affirmed by the Tribunal. The assessee challenged the said order in appeal before the Hon'ble High Court.

The primary contention of the assessee before the Hon'ble High Court was that by virtue of reworking interest on loans granted to AE the AO / Department has sought to tax notional or hypothetical income and not real income and as per the provisions of the Income-tax Act, 1961 only real income could have been taxed and therefore the addition as regards notional interest income was not sustainable.

The Hon'ble High Court dismissed the appeal holding that, Chapter X of the Act, is an anti-avoidance measure and not an anti-evasion measure. It is not premised on the basis that the transactions entered into between the parties suffers from under/over invoicing. The value of the transactions is brought in line with the consideration which would pass between two independent parties i.e. non-related / non-associated enterprises, by legislative mandate. It was further held that the Legislature has introduced special provisions in respect of International Transactions to bring the income to tax having regard to Arm's Length Price (ALP). In such case, the parties are obliged to establish the ALP of the International Transactions entered into between the two AE to bring to tax the real income i.e. the correct price of the transactions, shorn of, the price arrived at on account of relationship. It means the real income on application of a new measure. The object of the Transfer Pricing Officer is to put a stop to capital erosion and transfer of profits from one taxable territory to another taxable territory.

Renault Nissan Automotive India Private Ltd. -vs.- DRP & Others (2018) (Madras)

Cryptic order passed/ directions issued by the DRP without application of mind, simply accepting the TPO's order, without independent reasoning and findings, is liable to be set aside.

The TPO rejected the overseas tested party approach adopted by the assessee and the economic adjustments claimed by the assessee and proposed TP adjustment. The assessee-filed objection before the DRP against the draft assessment order incorporating the adjustment made by the TPO. The DRP issued directions to the AO, which in effect, accepted the conclusion arrived by the TPO in toto.

The assessee filed the writ petition before the High Court against the said directions of the DRP primarily

contending that the DRP had passed the order in total non-application of mind to the objections raised by the assessee. It contended that the DRP was not justified in rejecting the objections and confirming the TPO's order simply by stating that it was in agreement with the findings rendered by the TPO without any detailed discussions and independent findings on each issue.

The Court held that perusal of the DRP's order clearly indicated that apart from extracting objections raised by the Petitioner and the relevant portion of the TPO's order dealing with such objection, the DRP had not further discussed anything on the said objection in detail as to how the objections raised by the assessee could not be sustained or as to how the findings rendered by the TPO on such issue had to be accepted.

Noting that sec. 144C(5) r.w.s. 144C(6) contemplates that DRP shall issue directions only after inter alia considering objections raised by the assessee, evidences filed by assessee etc., the Court held that issuance of such directions could not be made mechanically or as an empty formality. It held that, on the other hand, the DRP had to issue directions only after considering the above stated materials and such consideration must be apparent on the face of the order.

It thus held that, in absence of independent reasoning and finding, the DRP had passed a cryptic order without application of mind.

Accordingly, it set aside the DRP's order and directed it to pass a fresh order after considering the objections raised by the assessee in detail and giving independent reasons and findings.

PCIT -vs.- IVen Interactive Limited (SC) (2019)

Mere mentioning of the new address in the return of income without specifically intimating the A.O. with respect to change of address and without getting the PAN database changed, is not enough and sufficient.

Notices u/s 143(2) are issued on selection of case generated under automated system of the Department which picks up the address of the assessee from the database of the PAN. Therefore, the change of address in the database of PAN is must. Following are the implications of the verdict:

a) It is important to get the address in PAN database updated.

b) If this is not done, the A.O. would be right in sending notice u/s 143(2) on the old address and you cannot escape by claiming you didn't receive the notice on your new address.

c) Without PAN updation, you cannot claim that the notices u/s 143(2) & 142(1) were not served upon you as you never received those notices and the subsequent notices served and received by you were beyond the period of limitation prescribed under proviso to sec. 143 of the 1961 Act.

d) In the absence of any intimation to the A.O. with respect to change in address, the A.O. was justified in issuing the notice at the address available as per the PAN database.

The Peerless General Finance And Investment Company Ltd. -vs.- CIT (SC) (2019)

Receipts of subscriptions pursuant to collective investment schemes is to be treated as capital receipts even if it is shown as income in books of accounts

Assessee-company has floated various schemes which require subscribers to deposit certain amounts by way of subscriptions in its hands, and, depending upon the scheme in question, these subscribed amounts at the end of the scheme are ultimately repaid with interest. The scheme at hand also contains forfeiture clauses as a result of which if, mid-way, a certain amount is forfeited, then the said amount would immediately become income in the hands of the assessee. Assessing Officer treated these amounts as income inasmuch as under the accounting system followed by the assessee, these amounts were credited to the profit and loss account for the years in question as income. It was held what was clear, even on general principle, was that subscriptions were received in the years in question

from the public at large under a collective investment scheme, and these subscriptions were never at any point of time forfeited. This being the case, and surrendered certificates not being the subject-matter of the appeal, it was clear that even on general principles, deposits by way of amounts pursuant to these investment schemes made by subscribers which had never been forfeited could only be stated to be capital receipts. The "theoretical" aspect of the present transaction was that assessee treated subscription receipts as income. The reality of the situation, however, was that the business aspect of the matter, when viewed as a whole, lead inevitably to the conclusion that the receipts in question were capital receipts and not income.

P. P. Mahatme, POA Lorna Margaret Pinto -vs.- ACIT (Bombay) (2019)

No transfer on Family settlement amongst family members in context of 'preexisting right'

A family settlement which is a settlement amongst family members in the context of their 'preexisting right' is not a "transfer". Such a settlement only defines a preexisting joint interest as a separate interest. However, if there is no preexisting right, the family arrangement constitutes a "transfer". Merely because dispute involved some family members and such dispute is ultimately settled by filing consent terms, the same cannot be styled as a family arrangement or family settlement so as to hold that the consideration received as a result of such settlement, does not constitute capital gain.

PCIT -vs.- State Bank of India (Bombay)(2019)

Genuine contributions to unapproved and unrecognized funds allowable as deduction

Assessee claimed deduction of expenditure of ₹ 50 lakhs towards contribution to a fund created for the health care of the retired employees. Revenue argued that such fund not being one recognized under Section 36(1)(iv) or (v), claim of expenditure was hit by the provisions of sec. 40A(9). It was held the very purpose of insertion of sec. 40A(9) was to restrict the claim of expenditure by the employers towards contribution to funds, trust, association of persons etc. which was wholly discretionary and did not impose any restriction or condition for expanding such funds which had possibility of misdirecting or misuse of such funds after the employer claimed benefit of deduction thereof. In plain terms, this provision was not meant to hit genuine expenditure by an employer for the welfare and the benefit of the employees. Thus, assessee was entitled for deduction.

CIT -vs.- NCR Corporation Pvt. Ltd (Kar) (2020)

Whether ATM can be considered as computer and charged higher rate of depreciation?

The Karnataka High Court held that so long as functions of computers are performed with other functions and other functions are dependent on the functions of the computer, ATMs are to be treated as computers and are entitled to higher rate of depreciation

UOI -vs.- UAE Exchange Centre (SC) (2020)

Activities carried out by Liaison Office (LO) are preparatory and auxiliary and hence the LO doesn't constitute a permanent establishment under India

Facts

- The Assessee was a limited company incorporated in the United Arab Emirates (UAE). It was engaged in offering, among others, remittance services for transferring amounts from UAE to various places in India.
- The Assessee had set up its first liaison office in Cochin, India in January, 1997 and thereafter, in Chennai, New Delhi, Mumbai and Jalandhar in India. The activities carried on by the Assessee from the said liaison offices were stated to be in conformity with the terms and conditions prescribed by the Reserve Bank of India.
- The entire expenses of the liaison offices in India were met exclusively out of funds received from UAE through normal banking channels. The liaison offices undertake no activity of trading, commercial or industrial. The

Assessee had no immovable property in India otherwise than by way of lease for operating the liaison offices. No fee/ commission was charged or received in India by any of the liaison offices for services rendered in India. The remittance services were offered by the Assessee to Non-Resident Indians in UAE. The contract pursuant to which the funds were handed over by the Non-Resident Indian to the Assessee in UAE was entered between the Assessee and the Non-Resident Indian remitter in UAE.

- However, the revenue was of the view that income shall be deemed to accrue in India from the activity carried out by the liaison offices of the Assessee in India under Article 5 and Article 7 of the tax treaty.

Held

- Article 5, deals with and defines the "Permanent Establishment" as 'A fixed place of business through which the business of an enterprise is wholly or partly carried on is regarded as a Permanent Establishment. The term "Permanent Establishment" would include the specified places referred to in clause 2 of Article 5'.
- In the present facts of the case, it was not in dispute that the place from where the activities were carried on by the assessee in India was a liaison office and would, therefore, be covered by the term Permanent Establishment in Article 5(2).
- However, Article 5(3) of the tax treaty opens with a non- obstante clause and also contains a deeming provision. It predicates that notwithstanding the preceding provisions of the concerned Article, which would mean clauses 1 and 2 of Article 5, it would still not be a Permanent Establishment, if any of the clauses in Article 5(3) are applicable.
- In present facts of the case, the crucial activities were of downloading particulars of remittances through electronic media and then printing cheques/ drafts drawn on the banks in India, which, in turn, were couriered or dispatched to the beneficiaries in India, in accordance with the instructions of the Non-Resident Indian remitter.
- While doing so, the liaison office of the Assessee in India remained connected with its main server in UAE and the information residing thereat was accessed by the liaison office in India for the purpose of remittance of funds to the beneficiaries in India by the Non-Resident Indian remitters. These were combination of virtual and physical activities unlike the virtual activity of funds being remitted by telegraphic transfer through banking channels.
- Further, the Reserve Bank of India had agreed for establishing a liaison office of the respondent at Cochin, initially for a period of three years to enable the Assessee to (i) respond quickly and economically to inquiries from correspondent banks with regard to suspected fraudulent drafts; (ii) undertake reconciliation of bank accounts held in India; (iii) act as a communication centre receiving computer (via modem) advices of mail transfer T.T. stop payments messages, payment details etc., originating from respondent's several branches in UAE and transmitting to its Indian correspondent banks; (iv) printing Indian Rupee drafts with facsimile signature from the Head Office and counter signature by the authorised signatory of the Office at Cochin; and (v) following up with the Indian correspondent banks. These were the limited activities which the Assessee was permitted to carry on within India.
- Thus, the office in India was not permitted to undertake any other activity of trading, commercial or industrial, or to enter into any business contracts in its own name without prior permission of the Reserve Bank of India. The liaison office of the Assessee in India could not even charge commission/ fee or receive any remuneration or income in respect of the activities undertaken by the liaison office in India.
- Therefore, from the onerous stipulations specified by the Reserve Bank of India, it could be safely concluded, as opined by the Hon'ble High Court, that the activities of the liaison office(s) of the Assessee in India were in the nature of preparatory or auxiliary character.

- Hence, the same being "of preparatory or auxiliary character" by virtue of Article 5(3)(e) of the tax treaty, the fixed place of business (liaison office) of the Assessee in India otherwise a Permanent Establishment, was deemed to be expressly excluded from being so. And since by a legal fiction it was deemed not to be a Permanent Establishment of the Assessee in India, it was not amenable to tax liability in terms of Article 7 of the tax treaty.

Yum! Restaurants (Marketing) Private Limited -vs.- CIT (SC) (2020)

Doctrine of mutuality is not applicable in case of a commercial concern and arrangement

Yum! Restaurants (Marketing) Private Limited which is the appellant company is a fully owned subsidiary of YRIPL. Purpose of the organisation is that of cost advertisement and promotion to the franchised (economies). The Secretariat for Industrial Assistance approved this purpose. However, few conditions were laid down with regard to the functioning of the Appellant company. The Appellant was obligated to operate as a non-profit entity. And this non- profit entity was based on the principle of Mutuality.

Thereafter, the Yum! Restaurants (Marketing) Private Limited got into a Tripartite Operating Agreement in furtherance of the approval. The agreement was between the Appellant company, YRIPL and the franchises. As per the agreement the Appellant company received 5% of Gross sales as a fixed contribution for the purpose of Advertising and Other Promotional activities as a mutual benefit to the franchises & the parent company as well.

After the Assessment Year, the assessee(the Appellant) filled the returns as NIL for income stating its mutual character of this non-profit entity. This was not accepted by the Assessing Officer. The Commissioner of the Income Tax department upheld this decision explaining that the rejection was on the basis of the undesirable Commercialityin the activities undertaken by the Appellant company. Thus, making the surplus liable to tax.

The Income Tax Appellate Tribunal held that the essentials of a Doctrine of Mutuality are not fulfilled thus there is no basis to the arguments made by the assessee. The Delhi High Court also upheld this view.

The Apex Court has held that if the realization of money by the taxpayer from both members as well as non-members was in the course of the same activity and is tainted with commerciality, then the test of mutuality is not met. Where the participants did not have the right to participate in surplus or were not entitled to get back the unspent portion of their respective contributions, then this was also held to be against the concept of mutuality. In such cases, the income earned inter-se was held to be chargeable to income tax. The doctrine of mutuality bestows a special status to qualify for exemption from tax liability. It is a settled proposition of law that exemptions are to be put to strict interpretation. The Assessee having failed to fulfil the stipulations and to prove the existence of mutuality, the question of extending exemption from tax liability to the Assessee, that too at the cost of public exchequer, does not arise.

Navin Jolly -vs.- ITO (Kar) (2020)

Multiple independent residential units in same building can be treated as one residential unit for section 54F Exemption and usage of the property has to be considered in determining whether it is a residential property or a commercial property

The assessing officer vide order held that the assessee owns nine residential flats in his name and that he is deriving the income from the residential flats and declared the same under the head income from house property and is not eligible to claim exemption by invoking proviso (a)(i) and (b) to sec. 54F(1). The ITAT while dismissing the appeal by the assessee said, "it is immaterial as to how the assessee utilized the residential units and whether these residential units are used for commercial purposes or residential purposes, so long as these units were recognized as residential units. Therefore, it was held that the assessee cannot claim the benefit of exemption u/s 54F of the Act."

The Hon'ble High Court has held that assessee is entitled to the benefit of exemption u/s 54F though the assessee owns more than one apartment of 500 square feet in the same building and it has to be treated as one residential unit.

PCIT -vs.- Open Solutions Software Services (Del) (2020)

Whether Transactional Net Margin Method does not require functional similarity between tested party and comparables?

The grievance of the Appellant is against the exclusion of four comparables introduced by the Transfer Pricing Officer ('TPO') for benchmarking the international transaction of rendition of software services by the Respondent.

From the exposition of law in Rampgreen Solutions Pvt. Ltd. -vs.- CIT and the other judgments, it is clear that even while applying the TNM method, comparables cannot be picked on the basis of broad classification under various heads, and that the actual functional profile of the comparable must be similar, if not same, to that of the taxpayer-assessee. In comparability analysis, the business environment; demand and supply of the services; assets employed, and, competence to provide different services are factors which would have a material bearing on the profitability of the entities and, therefore, regard must be had to such factors.

In the application of the TNM method, broad similarity in the domain of services is not enough and the overall FAR analysis of the comparable sought to be used must be similar with the taxpayer-assessee. On a perusal of the impugned order passed by the ITAT, present Court finds that none of the comparables have been excluded solely on the ground of high turnover. The primary reason for excluding the four comparables in question is on account of the dissimilarity in the overall profile of the said comparables with the Respondent-assessee.

In view of the above, it emerges that none of the comparables have been excluded on the ground of high turnover alone. The test of functional similarity applied by the Tribunal is in consonance with the legal position. Therefore, there is no merit in the contentions urged by the Revenue. Equally meritless is the contention of the Revenue regarding the bar to challenge the comparables after the acceptance of the filters. The filters are applied to narrow down the search to find the comparables that are closest to the assessee. The use of filters has to be necessarily validated from the annual reports. Since the TPO would have to do this exercise on the basis of the actual data in the report of the comparables, he would surely have the freedom to adopt or reject the comparables. It cannot held that merely because a comparable clears the filters, its inclusion in the list of comparables is immune to challenge by the assessee. The appeal is dismissed.

DIT -vs.- Samsung Heavy Industries Co Ltd (SC) (2020)

Project Office undertaking non-core activities in India does not constitute Permanent Establishment

Taxpayer, a non-resident company incorporated in South Korea, was awarded a turnkey contract by Oil and Natural Gas Corporation (ONGC) for carrying out the work involving surveys, design, engineering, procurement, fabrication, installation and modification of existing facilities; and start-up and commissioning of entire facilities of an oil and gas rig (Project) at north-west of Mumbai. The taxpayer, after seeking approval from Reserve Bank of India (RBI), setup a PO in Mumbai which would act as 'communication channel' between the taxpayer and ONGC in respect of the Project. The taxpayer undertook entire activities (as required under the Project) from outside India and later the rig platforms were brought to Mumbai for installation at the Project site. In its Indian tax return, the taxpayer disclosed a loss of INR 2.35mn which had been incurred on account of the activities carried out in India.

However, the tax officer, after examining the terms of agreement of Project, concluded that the project was a single indivisible turnkey project whose work was wholly executed by the PO which constitute a PE in India and thus consequently profits (attributed at the rate of 25% of the revenue) arising from such project would be taxable in India. The Dispute Resolution Panel (DRP) as well as Mumbai Tax Tribunal affirmed the findings of the tax

officer. Further, the Tribunal observed that the onus lies on the taxpayer to prove that the activities of PE are of preparatory and auxiliary in nature. Upon further appeal, the Hon'ble Uttarakhand High Court (HC) held that the question relating to whether the PO opened at Mumbai cannot be said to be a "Permanent Establishment" within the meaning of Article 5 of the Tax Treaty would be of no consequence. The HC then held that there was no finding or justification on record that 25% of the gross revenue of the taxpayer outside India was attributable to the business carried out by the PO.

Revenue Authorities filed an appeal before the Apex Court (SC) against the HC order. The Apex court observed that when it comes to 'fixed place' PE under the Tax Treaty, the condition precedent for applicability of Article 5(1) of the Tax Treaty and there by constituting PE is that there should be a place 'through which the business of an enterprise' is wholly or partly carried on. Further, the profits of the foreign enterprise are taxable in India only if the said enterprise carries on its core business (through a PE) in India. Further, SC perused the documents that were relied upon by Tribunal and made the following observations:

- Board Resolution shows that the PO was established to coordinate and execute 'delivery documents in connection with construction of offshore platform modification of existing facilities for ONGC'. Tribunal's finding that PO was involved in core activity of execution of the Project is perverse.
- Tribunal ignored facts submitted by the taxpayer which established that no expenditure was incurred by PO in India and that only 2 employees (having no technical qualification) were engaged to perform non-core activities.
- Tribunal's finding that the onus to establish that PO does not constitute a PE is on taxpayer, is against the SC decision in case of E-Funds IT Solution Inc.

Basis the above observations, SC held that taxpayer's PO in Mumbai did not constitute a Fixed Place PE in India. SC also affirmed the stand taken by the taxpayer that on the facts of the case, PO in Mumbai would fall within exclusionary Article 5(4)(e) of Tax Treaty as PO is only an auxiliary office meant to act as a liaison office between taxpayer and ONGC.

DCIT -vs.- Pepsi Foods Ltd (2021) 433 ITR 295 (SC)

Would automatic vacation of stay order upon expiry of extended period of stay of 365 days be valid, where the delay in disposing of the appeal is not attributable to the assessee?

The third proviso to sec. 254(2A) provides that where the appeal filed before the Appellate Tribunal is not disposed of within the period of stay or extended period of stay granted by the Tribunal, the order of stay shall stand vacated after the expiry of 365 days, even if the delay in disposing of the appeal is not attributable to the assessee.

The Apex Court observed that the Appellate Tribunal, wherever possible, has to hear and decide appeals within a period of four years from the end of the financial year in which such appeal is filed. It is only when a stay is granted by the Appellate Tribunal, the appeal is required to be disposed of within 365 days. So far as the disposal of an appeal by the Appellate Tribunal is concerned, this is a directory provision. However, the condition of automatic vacation of stay on expiry of the period becomes mandatory so far as the assessee is concerned.

The Apex Court also pointed out that the said proviso would result in the automatic vacation of a stay upon the expiry of 365 days, even if the Appellate Tribunal could not take up the appeal in time for no fault of the assessee. Further, vacation of stay in favour of the Department would ensue even if the Department is itself responsible for the delay in hearing the appeal. In this sense, the proviso is manifestly arbitrary being a provision which is capricious, irrational and disproportionate so far as the assessee is concerned.

Accordingly, the Apex Court held that the third proviso to sec. 254(2A) has to be read without the word "even" and the word "not" after the words "delay in disposing of the appeal". Thus, any order of stay shall stand vacated after the expiry of the period or periods mentioned in the section, only if the delay in disposing of the appeal is attributable to the assessee.

Engineering Analysis Centre of Excellence P. Ltd -vs.- CIT and Another (2021) (SC)

Would the amounts paid by resident Indian end-users / distributors to non-resident computer software manufacturers / suppliers, as consideration for the use/resale of the computer software through End-User Licence Agreement (EULAs) / distribution agreements, be considered as payment of royalty for the use of copyright in the computer software? If yes, is it liable for deduction of tax at source u/s 195?

The Apex Court observed that as per the definition given in Explanation 2(v) to sec. 9(1)(vi), "royalty" means consideration for, inter alia, the transfer of all or any rights (including the granting of a licence), in respect of any copyright, literary, artistic or scientific work. As per Explanation 4 thereto, such transfer of all or any rights includes transfer of all or any right for use or right to use a computer software (including the granting of a licence). As per the meaning assigned in the DTAA with Singapore, for example, "royalty" means payment of any kind received as consideration for "the use of, or the right to use, any copyright" of a literary, artistic or scientific work. The meaning of royalty in India's DTAA with other countries like Australia, Canada, France, Italy, USA, Netherlands, Sweden, Taiwan, Japan, China etc. is similar if not identical.

The Apex Court observed the following four categories of cases, in which the distribution agreements and end-user licence agreements did not create any interest or right to such distributors or end-users, which would amount to the use of or right to use any copyright:

a. where computer software is purchased directly by an end-user, resident in India, from a foreign, non-resident supplier or manufacturer.

b. where resident Indian companies acting as distributors or resellers, purchase computer software from foreign, non-resident suppliers or manufacturers and then, resell the same to resident Indian end-users.

c. where the distributor happens to be a foreign, non-resident vendor, who, after purchasing software from a foreign, non-resident seller, resells the same to resident Indian distributors or end-users.

d. where computer software is affixed onto hardware and is sold as an integrated unit/equipment by foreign, non-resident suppliers to resident Indian distributors or end-users.

In all the above cases, the Apex Court has held that the amount paid by resident Indian end-users or distributors to non-resident computer software manufacturers or suppliers, as consideration for the resale or use of the computer software through end-user licence agreements or distribution agreements, is not royalty for the use of copyright in the computer software.

The provisions contained in the Income-tax Act, 1961 [namely, section 9(1)(vi) read along with Explanations 2 and 4 thereof], which deal with royalty, not being more beneficial to the assessees, have no application in the facts of these cases. Consequently, the consideration paid to the non-resident computer software manufacturers or suppliers would not be chargeable to tax India. Hence, no tax is required to be deducted at source u/s 195.

As per section 90(2), the provisions of the Income-tax Act, 1961 will apply only to the extent they are more beneficial to the assessee, in a case where India has entered into a DTAA with the other country. In this case, since the provisions under the DTAA are more beneficial, the taxability of the payment would be determined as per the meaning of royalty assigned under the DTAAs.

PCIT -vs.- Dr. Ranjan Pai (2021) 431 ITR 250 (Kar)[1]

Can bonus shares received by shareholders be taxable under the head 'Income from other sources' as per the provisions of sec. 56(2)(x), as they are received without consideration?

The issue of bonus shares by capitalization of reserves is merely a reallocation of the company's funds. There is no inflow of fresh funds or increase in the capital employed, which remains the same. Thus, there is no addition or alteration to the profit-making apparatus and the total funds available with the company remain the same. On the other hand, when a shareholder gets bonus shares, the value of the original shares held by him goes down and the market value as well as intrinsic value of the two shares put together will be the same or nearly the same as the value of original share before the issue of bonus shares. Thus, any profit derived by the assessee shareholder on account of receipt of bonus shares is adjusted by depreciation in the value of equity shares originally held by him.

Accordingly, the High Court held that the bonus shares were not issued in order to evade any tax so to attract the provisions of sec. 56(2)(x). Hence, the provisions of sec. 56(2)(x) would not be attracted in the hands of the recipient shareholders on receipt of bonus shares.

CIT and another -vs.- Corporation Bank [2021] 431 ITR 554 (Kar)

Are the provisions of TDS u/s 194H attracted on payment made by the assessee-bank for services rendered by M/s. NFS, a network of shared ATMs in India?

National Financial Switch (NFS) is an ATM network which facilitates convenience banking. It links together the country's ATMs in a single network. The High Court observed that the relationship between the assessee-bank and National Financial Switch (NFS) is not of an agency but that of two independent parties on principal to principal basis. Therefore, the High Court held that the provisions of sec. 194H are not attracted on payment made by Corporation Bank, which issued the credit card, for payment gateway services provided by NFS.

CIT -vs.- Reliance Telecom Ltd (SC) (2021)

ITAT has no power to recall its order even if submissions were filed on merits

The Supreme Court held that the order passed by the ITAT recalling its earlier order is beyond the scope and ambit of the powers u/s 254(2). In exercise of powers u/s 254(2), the ITAT may amend any order passed by it to rectify any mistake apparent from the record only. The Tribunal cannot revisit its earlier order and go into detail on merits.

The powers u/s 254(2) are only to correct and/or rectify the mistake apparent from the record. Merely because the assessee might have filed detailed submissions, it does not confer jurisdiction upon the ITAT to pass the order de hors sec. 254(2).

In the instant case, a detailed order was already passed by the ITAT, which was held in favour of the revenue. Therefore, the said order could not have been recalled by ITAT in the exercise of powers u/s 254(2). If the assessee believed that the order passed by the ITAT was erroneous, either on facts or in law, the only remedy available was to prefer the appeal before the High Court.

Board of Control for Cricket in India -vs.- PCIT (2021)(Mum-Trib)

BCCI isn't engaged in commercial activities as funds generated from IPL are used for promoting cricket

The Mumbai Tribunal has allowed relief to BCCI and directed CIT to grant registration u/s 12A citing that BCCI is still promoting the game of cricket. The Court has ruled that the prime character of popularising cricket is not

1. This decision was rendered in the context of sec. 56(2)(vii); however, the underlying principle emanating therefrom applies with equal force in the context of the present provisions contained in sec. 56(2(x). Accordingly, the issue and decision has been presented with reference to sec. 56(2)(x).

lost just because a sports tournament is structured to make it more popular, resulting in more paying sponsorship and greater mobilisation of resources.

The Court rules that the basic character of popularising cricket is not lost just because a sports tournament is structured in such a manner to make it more popular, resulting in more paying sponsorship and greater mobilisation of resources.

It is indeed possible that the predominant object remains the promotion of cricket but that activity is done in a more effective and financially optimal manner. There is no conflict in the cricket becoming more popular and the cricket becoming more entertaining after the introduction of the IPL tournament.

As long as the object of promoting cricket remains intact, the assessee cannot be said to be not following the object of promoting cricket. It will not impact the eligibility of the assessee just because the operational model of a cricket tournament, whether IPL or any other tournament, is more entertaining, more economically viable, and provides economic opportunities to all those associated with that tournament.

All the funds available at the disposal of BCCI, including the additional funds generated by holding IPL tournaments, are employed for promoting cricket, and that matters. Improvising the game's rules, adding entertainment value, and making it economically attractive may be a purist's nightmare. Still, the same factors can also be viewed as radical and innovative ideas to popularise a game.

Therefore, the assessee is entitled to the continuance of its registration u/s 12A, and the order passed by the CIT stands quashed.

Kohinoor Indian (P.) Ltd. -vs.- ACIT (2021)(Amritsar-Trib)

'iPad' may have some computing functions, but it isn't a computer for higher depreciation

The Amritsar Tribunal has ruled that the predominant purpose of the iPad is communication, and it is not a computing device. Its main features are email, WhatsApp, Facetime calls, music, films, etc. Though the iPad may discharge some of the functions of computers, it is not a substitution for computers or laptops. In common parlance, the iPad is considered as communicating device with some additional features of a computer.

Further, apple stores do not sell the iPad as a computer device, but rather, it is selling it as communicating/ entertainment device. Another reason the iPad can be held as a communication device is it has an IMEI number. Though the assessee had denied having an IMEI number, no concrete records have been produced on record in this regard. Accordingly, ITAT held that the iPad is not a computer. Hence, depreciation is applicable at a lower rate.

PCIT -vs.- Tally Solutions (P.) Ltd. (2021) (Kar.)

Non-deduction of tax on the purchase of assets cannot take away the right to claim depreciation

The Karnataka High Court held that sec. 40(a)(i) and 40(a)(ia) provide for disallowance only in respect of expenditure, which is revenue in nature. Therefore, the provision does not apply to the assessee claiming depreciation, which is not an expenditure but an allowance.

The depreciation is not an outgoing expenditure, and therefore, provisions of sec. 40(a)(i) and 40(a)(ia) are not applicable. In the absence of any requirement of law for making a deduction of tax out of expenditure, which has been capitalised and no amount was claimed as revenue expenditure, no disallowance would be made.

It is also pertinent to note that depreciation is a statutory deduction available to the assessee on an asset, which is wholly or partly owned by it and used for business or profession. The depreciation is an allowance and not an expenditure, loss or trading liability.

Noida Cyber Park (P.) Ltd. -vs.- ITO (2021) (Delhi-Trib)

Section 50C is not applicable on the transfer of leasehold rights in land and building

The Delhi ITAT held that the expression 'land or building' in its coverage is quite distinct from the expression 'any right in land or building'. The legislature, in its wisdom, has used the expression 'land or building or both' in Section 50C, and not the expression 'any right in land or building'. Therefore, the express use of one expression would exclude the other.

The Hon'ble Supreme Court has supported these legal premises in the case of GVK Industries Ltd. -vs.- ITO [2011] (SC). Thus, transfer of leasehold rights does not warrant invoking sec. 50C as the said property is not of the nature covered by sec. 50C.

Aditya Balkrishna Shroff -vs.- ITO (2021) (Mum-Trib)

Gain received on personal loan due to forex fluctuation is a capital receipt not liable to tax

The Mumbai ITAT held that even before deciding whether the gain was of income nature, AO had proceeded to put the cart before the horse by deciding the head under which the income is to be taxed. He mixed up the concept of income with the concept of gains. In the case of Shaw Wallace & Co Ltd v. DCIT [2001] (Cal), the ITAT held that a capital receipt, in principle, is outside the scope of income chargeable to tax. A receipt cannot be taxed as income unless it is in the nature of a revenue receipt or is specifically brought within the ambit of income by way of specific provisions of the Income-tax Act.

AO had accepted that the transaction was in the capital field and proceeded to hold that income arising out of the loan transaction was required to be treated as interest or income from other sources. If the transaction is in the capital field, the question of its taxability does not arise unless there is a specific provision of bringing such a receipt to tax. In any case, where the loan was foreign currency-denominated and the amount advanced as loan, as also received back as repayment, was precisely the same, there was no question of interest component at all.

The benefit or gain received by the assessee was on account of foreign exchange fluctuation. Since the foreign exchange fluctuation was with respect to a transaction in the capital field, the foreign exchange fluctuation receipt itself turned out to be a capital receipt.

CIT (International Taxation) -vs.- Gracemac Corporation (Delhi)

Licensing of software products by Microsoft is not taxable in India as royalty

High court held that licensing of software products of Microsoft in the Territory of India by the Respondent was not taxable in India as Royalty under Section 9(1)(vi) of the Act read with Article 12 of the Indo US DTAA

The department approached the High Court contending that the Tribunal has failed to appreciate that the distribution model in the case of the respondent-assessee involved making of multiple copies of the software clearly indicating transfer of copyright.

The Court has relied on the decisions in EY Global Services Limited -vs.- ACIT and EYGBS (India) Private Limited -vs.- JCIT wherein the Apex Court has held that the payment received by EYGSL (UK) for providing access to computer software to its member firms of EY Network located in India, that is, EYGBS (India), does not amount to 'royalty' liable to be taxed in India under the provisions of the Income Tax Act, 1961 and the India-UK DTAA.

SAP Labs India Pvt. Ltd. -vs.- ITO [2023] 454 ITR 121 (SC)

Determination of ALP by the High Court

The Apex Court laid down the following with respect to the powers of High Court to consider the substantial question of law involving determination of ALP:

- While determining the ALP, the Tribunal has to follow the guidelines stipulated under Chapter X of the Income-tax Act, 1961, namely, sec. 92 to 92F and Rules 10A to 10E. Any determination of the ALP under Chapter X not in accordance with the relevant provisions of the Income-tax Act and Rules can be considered as perverse and it may be considered as a substantial question of law as perversity itself can be said to be a substantial question of law. Therefore, there cannot be any absolute proposition of law that in all cases where the Tribunal has determined the ALP, the same is final and cannot be the subject matter of scrutiny by the High Court in an appeal.
- When the determination of the ALP is challenged before the High Court, it is always open for the High Court to consider and examine whether the ALP has been determined while taking into consideration the relevant guidelines under the Act and the Rules.
- The High Court can also examine the question of comparability of two companies or selection of filters and examine whether the same is done judiciously and on the basis of the relevant material/evidence on record. The High Court can also examine whether the comparable transactions have been taken into consideration properly or not, i.e., to the extent as to whether non-comparable transactions are considered as comparable transactions or not.

Therefore, the view taken by the Karnataka High Court in the case of Softbrands India (P.) Ltd. that in the transfer pricing matters, the determination of the ALP by the Tribunal is final and cannot be subject matter of appeal under section 260A cannot be accepted. In an appeal challenging the determination of the arm's length price, it is always open for the High Court to examine in each case, within the parameters of section 260A, whether while determining the ALP, the guidelines laid down under the Income-tax Act and the Rules are followed or not and whether the determination of the ALP and the findings recorded by the Tribunal while determining the ALP are perverse or not.

CIT -vs.- Cognizant Technology Solutions of India Pvt. Ltd. (2023) 454 ITR 1 (SC)

Is deduction under section 10AA available in respect of foreign exchange gain solely relating to the export business of the assessee?

In order to allow deduction u/s 10AA, it has to be seen whether such benefit earned by the assessee was derived by virtue of export made by the assessee. The exchange value based on upward or downward of the rupee value is not in the hands of the assessee. The assessee does not determine the exchange value of the Indian rupee. But for the fact that, the assessee is an export house, there was no question of earning any foreign exchange. Therefore, when the fluctuation in foreign exchange rate was solely relatable to the export business of the assessee and the higher rupee value was earned by virtue of such exports carried out by the assessee, the deduction u/s 10AA would be available in respect of such foreign exchange gains.

CIT -vs.- Reliance Energy Ltd. (2022) 441 ITR 346 (SC)

Whether deduction u/s 80-IA has to be limited to the extent of the Income from Business or profession as per sec. 80AB or it has to be allowed to the extent of the profit of the eligible undertaking?

A plain reading of sec. 80AB shows that the provision pertains to determination of the quantum of deductible income in the "gross total income". Sec. 80AB cannot be read to be curtailing the width of sec. 80-IA. It is relevant to take note of sec. 80A(1) which stipulates that in computation of the "total income" of an assessee, deductions specified in sec. 80C to sec. 80U shall be allowed from his "gross total income". Sec. 80A(2) provides that the

aggregate amount of the deductions under Chapter VI-A shall not exceed the "gross total income" of the assessee. Thus, sec. 80AB which deals with determination of deductions under Part C of Chapter VI-A is with respect only to computation of deduction on the basis of "net income".

The import of sec. 80-IA is that the "total income" of an assessee is computed by taking into account the allowable deduction in respect of the profits and gains derived from the "eligible business". The scope of sec. 80-IA(5) is limited to determination of quantum of deduction u/s 80-IA(1) by treating "eligible business" as the "only source of income". Sub-section (5) cannot be pressed into service for reading a limitation of the deduction under sub-section (1) only to income under the head "Profits and gains of business and profession".

For the purpose of calculating profit-linked deduction under any section of Chapter VI-A, loss sustained in other divisions or units cannot be taken into account, as only profits from the eligible business have to be taken into account as if it was the only source of income. Profits and gains from eligible business cannot be reduced by the loss suffered in any other business owned by the assessee.

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

SECTION - B
INTERNATIONAL TAXATION

Double Taxation and Avoidance Agreements (DTAA)

12

This Module includes:

12.1 Types of DTAA

12.2 Models of DTAAs (OECD and UN)

12.3 Interlink of DTAAs with Section 90 of Income Tax Act. 1961

12.4 Overview of Articles in DTAAs

Double Taxation and Avoidance Agreements (DTAA)

SLOB Mapped against the Module:

1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.

Module Learning Objectives:

After studying this module, the students will be able to -

- Identify the income which are subject to double taxation
- Analyse the various articles of the treaty or convention
- Apply the provision of income tax to provide relief

Introduction

12

In home country, tax is an obligation, while in the host country, tax is a cost.

Every nation has a sovereign right to tax its residents/nationals on their global incomes. As a result, the income of a person can get taxed in both countries i.e. in the home country (country of his residence) as well the host country (country where income is generated) due to conflict of jurisdictions to tax. In such an environment, the benefits of international trade and competitive cost advantages would be lost. Double taxation is harmful for movement of capital, technology transfer, commerce, trade, and of course, people. In order to prevent the injury caused to international trade and commerce, Article 51 of the Indian Constitution has *inter-alia* provides that:

"The State shall endeavour to -

a. promote international peace and security;

b. maintain just and equitable relations between nations;

c. foster respect for international law and treaty obligations in the dealings of organised people with one another;

d. encourage settlement of international disputes by arbitration.

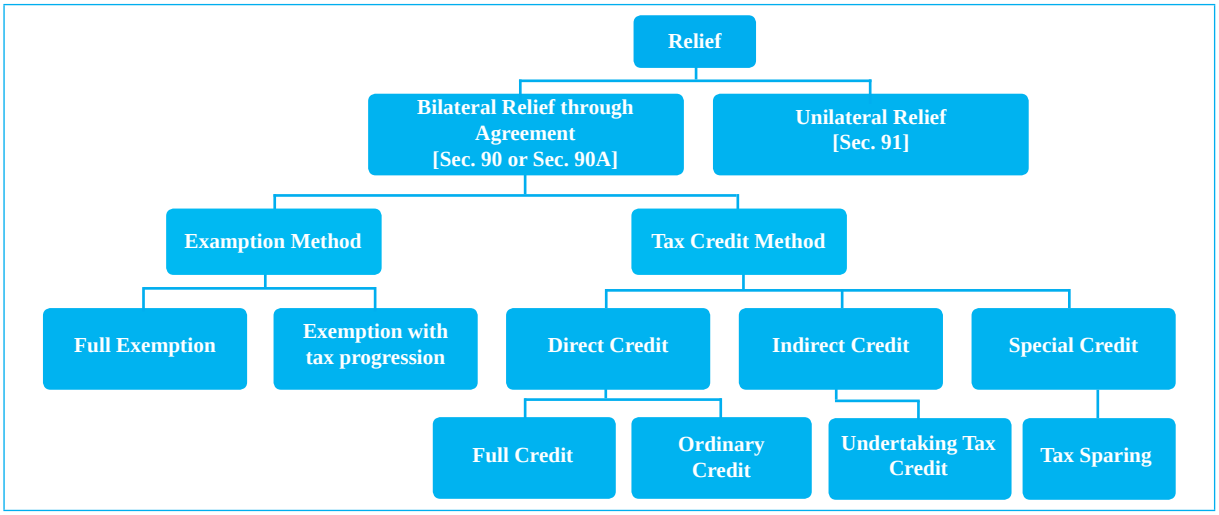
It is pertinent to note that entries 10 and 14 of list I of the seventh schedule confer the power on Parliament to legislate the treaties with foreign countries. Further, this power of Parliament has been delegated to the Central Government vide sec. 90 and 90A of the Income-tax Act, 1961.

Economic Double Taxation	Juridical Double Taxation
➢ Same income taxed in two or more country but in the hands of different taxpayers	➢ Two or more states levy taxes on same entity on same income for identical periods
➢ e.g. business profits and dividend in different countries	➢ Arises due to overlapping claims of tax jurisdictions
	➢ Tax treaties largely prevent / mitigate juridical double taxation

Generally, income is taxable on two basis viz. i) Source of income basis and ii) Residential Status basis, which results into double taxation of the same income of the person. Firstly, such income is taxed in the country in which such income is generated and again, the same income may be taxed on the basis of residential status of the person in another country. For instance, Mr. X, an ordinarily resident in India, earned bank interest of ₹ 1,00,000 on his money deposited into a bank located in US. In that case, such income is taxable in US on Source of income basis and again in India as he is an ordinarily resident India. In times when economies are going global and borders fading, double taxation is still one of the major obstacles to the development of inter-country economic relations. In order to prevent this hardship or to avoid double taxation, relief is provided to the tax-payer.

Such relief is provided by two ways:

- Bilateral Relief
- Unilateral Relief



Bilateral Relief

In this, the government of two countries enters into an agreement (known as 'treaties') to provide relief against double taxation of the same income. As per Article 2 of the Vienna Convention on Laws of Treaties, 1969, "Treaty"[1] means an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation. The relief is granted on the basis of the terms of such agreement. Generally, such an agreement provides relief through the following methods:

Exemption Method: In this method, one country provides an exemption to such type of income. Generally, the residence country gave up its right and the country of source is then given the exclusive right to tax such incomes.

a. Full Exemption Method

Under this method, income earned in the State of Source is fully exempt in the State of Residence.

b. Exemption with Progression

Under this method, income from the State of Source is considered by the State of Residence only for the rate purpose.

E.g., an Indian Company has earned income from Indian sources of ₹ 75 Lacs. Income from foreign sources (relief available as per exemption with progression method) is ₹ 35 Lacs. As per the provisions of the Act, in India, an additional surcharge of 7% is levied in addition to normal income-tax liability if the total income exceeds ₹ 1 crore and at the rate of 12% if income exceeds ₹ 10 crores. Therefore, in the present case, total income for rate purpose only will exceed ₹ 1 crore and accordingly, effective rate for tax would be after considering the additional surcharge of 7%. However, the income on which the effective rate (inclusive of surcharge) would apply will be ₹ 75 Lacs only.

1 Tax Treaties attempt to eliminate double taxation and try to achieve balance and equity. They aim at sharing of tax revenues by the concerned states on a rational basis. Tax treaties do not always succeed in eliminating Double Taxation, but contain the incidence to a tolerable level. Tax Treaties or DTAAs are also known as AADT (Agreements for Avoidance of Double Taxation), or DTCs (Double Tax Conventions). These terms are used interchangeably.

Mathematically, it would work in this way:

Particulars	Amount (₹)
Income from India	75,00,000
Income from a foreign county	35,00,000
Total Income	**1,10,00,000**
Tax on above @ 30%	33,00,000
Add: Surcharge @ 7%	2,31,000
Tax and surcharge	35,31,000
Add: HEC @ 4%	1,41,240
Tax, Surcharge and Cess [A]	**36,72,240**
Average rate of tax [₹ 36,72,240 / ₹ 1,10,00,000 × 100]	33.38%
Relief [₹ 35,00,000 × 33.38%] [B]	**11,68,440**
Tax, Surcharge and Cess [A - B]	**25,03,800**
Which effectively [₹ 75,00,000 × 30% × 107% × 104%]. If foreign income is not considered then tax on ₹ 75,00,000 would be calculated without considering surcharge, in that case, total income would not exceed the threshold limit applicable for charging surcharge.	

Credit Method: In this method, the resident remains liable in the country of residence on its global income, however as far as the quantum of tax liabilities is concerned credit or deduction for tax paid in the source country is given by the residence country against its domestic tax as if the foreign tax were paid to the country of the residence itself.

Taxpoint: In this type of relief, the mechanism for granting relief is provided in the agreement itself.

a. Full Credit

Total tax paid in the State of Source is allowed as credit against tax payable in the State of Residence.

b. Ordinary Credit

State of Residence allows credit of tax paid in the state of Source restricted to that part of income tax which is attributable to the income taxable in the state of Residence.

Example

- Mr. A is a resident of country X, went on 3 months assignment to Country Y
- Salary income of Mr. A is ₹ 24,00,000
- Of the above, Country Y taxed 3 months income of ₹ 6,00,000 @ 28%

Compute tax liability of Mr. A considering full credit method and ordinary credit method.

Solution:

Computation of tax liability of Mr. A

Particulars	Country X	Country Y
Total Income	24,00,000	6,00,000
Tax rate	Slab	28%
Tax on above before relief	**4,36,800**	**1,68,000**
Relief:		
Full Credit	**1,68,000**	
Ordinary Credit [Lower of the following]	**1,38,450**	
- Tax paid in country Y	1,68,000	
- Tax paid in country X [₹ 4,36,800 x ₹ 6,00,000 / ₹ 24,00,000]	1,09,200	

c. Tax Sparing

State of Residence allows credit for deemed tax paid on income which is otherwise exempt from tax in the State of Source.

Example

- A Ltd, the parent company, being located in Country X has a branch in Country Y
- Branch earns a profit of ₹ 10,00,000
- Country X taxes residents on global income @ 30%
- Tax rate in country Y is 25%. However, as a measure to promote economic development therein (like special economic zones), country Y is not levying any tax.
- DTAA between Country X-Y has tax sparing provisions.

Compute tax sparing if branch operates in a specified area and is not taxed in Y

Solution:

Computation of tax liability of A Ltd

Particulars	Country X	Country Y
Total Income	10,00,000	10,00,000
Tax on above before relief	**3,00,000**	**0**
Relief as per tax sparing provision		
Relief [₹ 10,00,000 x rate of tax in foreign country i.e., 25%]	**2,50,000**	
Tax Payable	**50,000**	**0**

Relief is available in country X deeming that tax has been paid in the country Y @ 25% though no tax has been paid in the country Y.

d. Underlying Tax Credit

Underlying tax credit method attempts to mitigate the economic double taxation. Economic double taxation occurs where the same income is taxed more than once in the hands of different person in the same tax jurisdiction. E.g., The profits earned by the corporates are taxed at their hand and the same is again taxed when

it is distributed to shareholders as dividend. Under underlying credit method, credit is allowed to resident not only for the taxes withheld against the dividend income but also for the taxes paid on the underlying profits out of which the said dividend is paid by a company in the overseas jurisdiction. However, underlying credit may only apply if satisfaction of substantial shareholding requirement is met.

Example

- A Ltd, the parent company, being located in Country X has a subsidiary B Ltd in Country Y
- B Ltd out of its profits of ₹ 10,00,000 paid dividend to A Ltd ₹ 1,00,000
- Other income of A Ltd is ₹ 11,00,000
- Dividend withholding tax rates in Country Y – 15%
- Tax rate in country Y is 25 % and in Country X it is 30%
- DTAA between Country X-Y has an underlying tax credit (UTC) provision

Solution

Computation of tax liability

Particulars	A Ltd	B Ltd
Total Income	12,00,000	10,00,000
Tax on above before relief	**3,60,000**	**2,50,000**
Less: Tax credit for withholding tax	15,000	0
Tax Liability without relief	3,45,000	
Relief as per underlying tax credit		
Relief [₹ 10,00,000 x rate of tax in foreign country i.e., 25%]	**2,50,000**	
Tax Payable after relief	**95,000**	**0**

Unilateral Relief

The aforesaid method depends on the bilateral activity of both the countries. However, no country will have such an agreement with every country in the world. To avoid double taxation in such cases, the country of the residence itself may provide relief on a unilateral basis.

Types of DTAA

12.1

[2]DTAA can be of two types, limited or comprehensive. Limited DTAA are those which are limited to certain types of incomes only e.g. DTAA between India and Pakistan is limited to shipping and aircraft profits only.

Comprehensive DTAAs are those which cover almost all types of incomes covered by any model convention.

2 Presently India have DTAA with more than 90 countries

Models of DTAAs (OECD and UN)

12.2

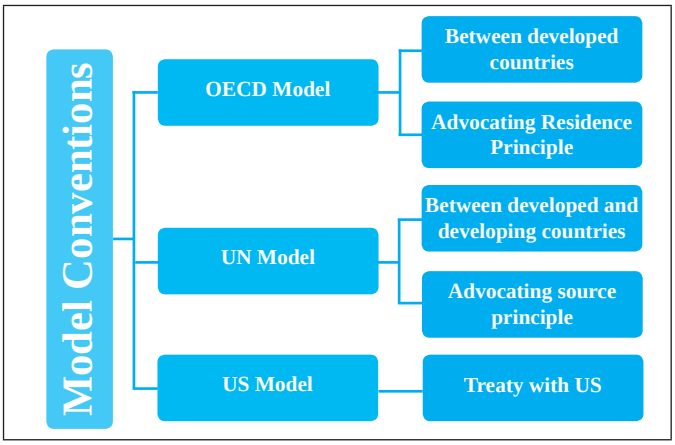
Global trade and commerce have made the world a single integrated market. In today's scenario, no country can claim that it is self-sufficient. This gives rise to import and export of goods and services. As and when the global trade started expanding its operations, economic transactions triggered tax provisions of various jurisdictions. In the absence of any agreement for avoidance of double taxation, the global business environment was affected. Therefore, a need was felt that there must be formulated a convention which would enable avoidance of double taxation. This led to series of model tax conventions by various bodies in different years.

Model tax treaties serve as the starting point (or can be termed as standard format) for negotiations between two countries. Although model treaties are not legally binding, their language often is incorporated verbatim (or with only minor alterations) in the text of bilateral treaties. However, sometimes they make changes as per their requirement and relationship with the other country.

Presently, the following are the model tax conventions which are in vogue –

a. Organisation for Economic Co-operation and Development (OECD) Model

The emergence of present form of OECD Model Convention can be traced back to 1927, when the Fiscal Committee of the League of Nations prepared the first draft of Model Form applicable to all countries. Since then, it has been revised several times and the latest being in the year 2017. OECD Model is essentially a model treaty between two developed nations. This model advocates residence principle, that is to say, it lays emphasis on the right of state of residence to tax the income.



b. United Nations (UN) Model

In 1968, the United Nations set up an Adhoc Group of Experts from various developed and developing countries to prepare a draft model convention between developed and developing countries. In 1980, this Group finalized the UN Model Convention in its present form. It has further been revised a number of times, the recent ones being in the year 2021. It gives more weight to the source principle as against the residence principle of the OECD Model. UN Model is designed to encourage flow of investments from the developed countries to developing countries. It takes into account sharing of tax-revenue with the country providing capital. Most of India's tax treaties are based on the UN Model.

c. US Model

The US Model convention was first published in 1976 and revised several times. US motel is used by the United States while entering into tax treaties with various country.

Articles in OECD Model and UN Model

In UN model, there are VII chapters which contains 31 articles whereas VII chapters of the OECD model contains 32 articles. List of articles are as under:

Article	OECD Model	UN Model
1	Person covered	Person covered
2	Taxes covered	Taxes covered
3	General definitions	General definitions
4	Resident	Resident
5	Permanent establishment	Permanent establishment
6	Income from immovable property	Income from immovable property
7	Business profits	Business profits
8	Shipping, inland waterways transport and air transport	Shipping, inland waterways transport and air transport (Alternative A & B)
9	Associated enterprise	Associated enterprise
10	Dividends	Dividends
11	Interest	Interest
12	Royalties	Royalties
12A	Fee for Technical Services	Fee for Technical Services
12B	--	Income from automated digital services
13	Capital Gains	Capital Gains
14	Deleted	Independent personal services
15	Income from employment	Dependent personal services
16	Directors' fees	Directors' fees and remuneration of top-level managerial officials
17	Entertainers and sportspersons	Artistes and sportspersons
18	Pensions	Pensions and Social Security Payments (Alternative A & B)
19	Government service	Government service
20	Students	Students
21	Other Income	Other Income
22	Capital	Capital
23A	Exemption method	Exemption method
23B	Credit method	Credit method
24	Non discrimination	Non discrimination
25	Mutual agreement procedure	Mutual agreement procedure (Alternative A & B)

Article	OECD Model	UN Model
26	Exchange of information	Exchange of information
27	Assistance in the collection of taxes	Assistance in the collection of taxes
28	Members of diplomatic missions and consular posts	Members of diplomatic missions and consular posts
29	Entitlement of benefits	Entitlement of benefits
30	Territorial extension	Entry in force
31	Entry in force	Termination
32	Termination	

In India, relief for the avoidance of double taxation is provided in both ways. Provisions relating thereto are enumerated here-in-below:

Interlink of DTAAs with Section 90 of Income Tax Act, 1961

12.3

Agreement with foreign countries [Sec. 90] [Bilateral Relief]

The Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India:

a. for the granting of relief in respect of—

   (i) income on which have been paid both income-tax under this Act and income-tax in that country or specified territory, as the case may be, or

   (ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory, as the case may be, to promote mutual economic relations, trade and investment, or

b. for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory, as the case may be, without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in the said agreement for the indirect benefit to residents of any other country or territory); or

c. for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory, as the case may be, or investigation of cases of such evasion or avoidance, or

d. for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory, as the case may be,

and may make such provisions as may be necessary for implementing the agreement.

Taxpoint

- **Applicability of DTAA**
  - Where the Central Government has entered into an agreement with the Government of any country or specified territory outside India for granting relief of tax or avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee. However, the provisions of Chapter X-A of the Act (i.e., GAAR) shall apply to the assessee even if such provisions are not beneficial to him.
  - **Example:** If as per DTAA with a foreign country, fee for technical services is to be taxed at the rate of 15% whereas it is taxable u/s 115A of the Act @ 10%, then it will be beneficial to apply sec. 115A. On the other hand, if as per the provision of DTAA, it is either not taxable or taxable at a rate lower than 10%, then DTAA is applicable.
  - Sections 4 and 5 of the Income-tax Act provide for taxation of global income of an assessee but this is subject to the provisions of an agreement entered into between the Central Government and the Government of a foreign country for avoidance of double taxation. In case of any conflict between the provisions of

the agreement and the Act, the provisions of the agreement would prevail over the Act in view of the provisions of sec. 90(2) [CIT v Kulandagan Chettiar (P V A L) (2004) (SC)] If any matter or income is not covered by the agreement, the Income-tax Act shall be applicable.

- When tax rate is determined under DTAA then tax rate prescribed therein shall have to be followed strictly without any additional taxes thereon in form of surcharge or education cess [DCIT -vs.- BOC Group Ltd. (2016) 156 ITD 402 (Mum) (Trib)]
- The charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.
- In case of a remittance to a country with which a Double Taxation Avoidance Agreement is in force, the tax should be deducted at the rate provided in the Finance Act of the relevant year or at the rate provided in the Double Taxation Avoidance Agreement, whichever is more beneficial to the assessee.
- If no tax liability is imposed under this Act, the question of relief does not arise [UOI vs Azadi Bachao Andolan (2003) (SC)]
- Relief cannot be granted unless the income which has been taxed in one of the contracting countries has also suffered tax in the other contracting country. Proof has to be provided of the income having suffered double taxation.

- **Tax Residency Certificate:** An assessee, not being a resident, to whom DTAA applies, shall not be entitled to claim any relief under such agreement unless a certificate of his being a resident in any country outside India or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory. Further, the assessee shall also provide such other documents and information, as may be prescribed.
  - Where the Government of the State certified that a person is a resident of that state or has a permanent establishment in the State, the certificate is binding on the other Government [UOI vs Azadi Bachao Andolan (2003) (SC)]
- **"Specified territory"** means any area outside India which may be notified[3] as such by the Central Government.
- **Meaning of the terms**
  - Where any term used in an agreement is defined under the said agreement, the said term shall have the same meaning as assigned to it in the agreement; and where the term is not defined in the said agreement, but defined in the Act, it shall have the same meaning as assigned to it in the Act and explanation, if any, given to it by the Central Government.
  - Further, any term used but not defined in the Act or in the agreement shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government.
  - Further, where any term is used in any agreement and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued, then, the meaning assigned to such term shall be deemed to have effect from the date on which the said agreement came into force.

3 Bermuda, British Virgin Islands, Cayman Islands, Gibraltar, Guernsey, Isle of Man, Netherlands Antilles, Macau, Hongkong and Sint Maarten

Illustration 1.

Mr. Ramesh, a resident Indian, has derived the following incomes for the previous year relevant to the A.Y. 2024-25:

a. Income from profession in India	₹ 12,44,000
b. Income from profession in country A (Tax paid in foreign country @ 5%)	₹ 4,50,000

Compute Indian tax liability of the assessee assuming that as per treaty between India and Country A, ₹ 4,50,000 is taxable in India. However foreign tax can be set off against Indian tax liability.

Solution:

Computation of total income and tax liability of Mr. Ramesh for the A.Y. 2024-25

Particulars	Amount
Income from profession in India	12,44,000
Income from profession in Country A	4,50,000
Gross Total Income	16,94,000
Less: Deduction u/ch. VIA	NA
Total income	16,94,000
Tax on above	2,08,200
Add: Health & Education cess	8,328
Tax and cess payable	2,16,528
Less: Relief u/s 90 [₹ 4,50,000 × 5%]	22,500
Tax payable in India (Rounded off u/s 288B)	**1,94,030**

Illustration 2.

Shri Anuj, an ordinarily resident in India, provides following details of his income for the previous year relevant to the A.Y. 2024-25

- Income from India ₹ 13,40,000
- Income from Country Z ₹ 12,00,000
- Investment in PPF ₹ 1,00,000

Further, it is to be noted that:

a) India has avoidance of double taxation agreement with Country Z. According to the said agreement, income is taxable in the country in which it is earned and not in the other country. However, in the other country, such income can be included for the purpose of computation of tax rate.

b) Foreign income has been taxed in Country Z @ 20%.

Compute Indian tax payable.

Solution:

Computation of total income and tax liability of Shri Anuj for the A.Y. 2024-25

Particulars	Amount
Income from India	13,40,000
Income from Country Z	12,00,000
Gross Total Income	25,40,000
Less: Deduction u/s 80C [Investment in PPF]	NA
Total income	**25,40,000**
Tax on above	4,62,000
Add: Health & Education cess	18,480
Tax and cess payable	4,80,480
Less: Relief u/s 90 [₹ 12,00,000 x 18.92%[1]]	2,27,040
Tax payable in India (Rounded off u/s 288B)	**2,53,440**

[1] Average rate of Indian tax = ₹ 4,80,480 / ₹ 25,40,000 x 100 = 18.92%

Adoption by Central Government of agreements between specified associations for double taxation relief [Sec. 90A]

Any specified association in India may enter into an agreement with any specified association in the specified territory outside India and the Central Government may, by notification in the Official Gazette, make such provisions as may be necessary for adopting and implementing such agreement—

a) for granting of relief in respect of—
   (i) income on which have been paid both income-tax under this Act and income-tax in any specified territory outside India; or
   (ii) income-tax chargeable under this Act and under the corresponding law in force in that specified territory outside India to promote mutual economic relations, trade and investment, or

b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that specified territory outside India, without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in the said agreement for the indirect benefit to residents of any other country or territory); or

c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that specified territory outside India, or investigation of cases of such evasion or avoidance, or

d) for recovery of income-tax under this Act and under the corresponding law in force in that specified territory outside India.

Notes

- **Specified association** means any institution, association or body, whether incorporated or not, functioning under any law for the time being in force in India or the laws of the specified territory outside India and which may be notified as such by the Central Government for the purposes of this section.
- Specified territory means any area outside India which may be notified as such by the Central Government for the purposes of this section.
- **Tax Residency Certificate:** An assessee, not being a resident, to whom DTA applies, shall not be entitled to claim any relief under such agreement unless a certificate of his being a resident in any country outside India

or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory. Further, the assessee shall also provide such other documents and information, as may be prescribed.

- **Meaning of the terms**
  - Where any term used in an agreement entered into is defined under the said agreement, the said term shall have the same meaning as assigned to it in the agreement; and where the term is not defined in the said agreement, but defined in the Act, it shall have the same meaning as assigned to it in the Act and explanation, if any, given to it by the Central Government.
  - Where any term is used in any agreement and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued, then, the meaning assigned to such term shall be deemed to have effect from the date on which the said agreement came into force.
- **GAAR:** Where a specified association in India has entered into an agreement with a specified association of any specified territory outside India and such agreement has been notified, for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee. However, the provisions of Chapter X-A of the Act (i.e., GAAR) shall apply to the assessee even if such provisions are not beneficial to him.

Certificate for claiming relief u/s 90 / 90A [Rule 21AB]

- For the purposes certificate discussed in sec. 90 and 90A, the following information shall be provided by an assessee in Form No. 10F:
  i. Status (individual, company, firm etc.) of the assessee;
  ii. Nationality (in case of an individual) or country or specified territory of incorporation or registration (in case of others);
  iii. Assessee's tax identification number in the country or specified territory of residence and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government of the country or the specified territory of which the asseessee claims to be a resident;
  iv. Period for which the residential status, as mentioned in the certificate, is applicable; and
  v. Address of the assessee in the country or specified territory outside India, during the period for which the certificate, as mentioned above, is applicable.
- The assessee may not be required to provide the information or any part thereof referred above, if the information is contained in the certificate.
- The assessee shall keep and maintain such documents as are necessary to substantiate the information and an income-tax authority may require the assessee to provide the said documents in relation to a claim by the said assessee of any relief under an agreement
- An assessee, being a resident in India, shall, for obtaining a certificate of residence for the purposes of an agreement referred to in sec. 90 and 90A, make an application in Form No. 10FA to the Assessing Officer.
- The Assessing Officer on receipt of an application and being satisfied in this behalf, shall issue a certificate of residence in respect of the assessee in Form No. 10FB.

Countries with which no agreement exists [Sec. 91] [Unilateral Relief]

If any person who is resident in India in any previous year proves that:

a) The income has accrued or arose during the previous year outside India (and which is not deemed to accrue or arise in India),

b) He has paid in any country income-tax on such income, by deduction or otherwise, under the law in force in that country

c) India does not have any agreement u/s 90 for the relief or avoidance of double taxation with that country

- then he shall be entitled to the deduction from the Indian income-tax payable by him

(i) of a sum calculated on such doubly taxed income at the average of Indian rate of tax or

(ii) of a sum calculated on such doubly taxed income at the average rate of tax of the said country,

- whichever is the lower, or at the Indian rate of tax if both the rates are equal.

Notes

a) The expression 'such doubly taxed income' really purports to indicate that it is only that portion of the income on which tax has been imposed and been paid by the assessee that is eligible for the double tax relief. Thus, where the foreign income which suffered tax in the foreign country was ₹ 88,535, and the income actually taxed in India after allowances and set off of losses (or deduction under chapter VIA) was ₹ 63,141, relief admissible would be calculated on ₹ 63,141 [CIT v. O.VR.SV.VR. Arunachalam Chettiar]

b) Relief u/s 91 is to be calculated on income country-wise and not on basis of aggregation or amalgamation of income of all foreign countries [CIT v. Bombay Burmah Trading Corpn. Ltd. (2003)]

c) No benefit is available on income which is deemed to accrue or arise in India, even though such income is doubly taxed.

Illustration 3.

Mr. Saha, a resident Indian, has derived the following incomes for the previous year relevant to the A.Y. 2024-25:

a.	Income from profession	₹ 3,74,000
b.	Royalty on books from foreign country Y (₹ 3,00,000 is eligible for deduction u/s 80QQB) (Tax paid in foreign country @ 20%)	₹ 5,00,000

Compute Indian tax liability, if he has opted for old regime, assuming that India does not have any agreement with country Y.

Solution:

Computation of total income and tax liability of Mr. Saha for the A.Y. 2024-25

Particulars	Amount
Income from profession	3,74,000
Royalty earned in country Y	5,00,000
Gross Total Income	8,74,000
Less: Deduction u/s 80QQB	3,00,000
Total income	5,74,000

Particulars	Amount
Tax on above	27,300
Add: Health & Education cess	1,092
Tax and cess payable	28,392
Average rate of tax [₹ 28,392 / ₹ 5,74,000 x 100]	4.95%
Rate of tax in country Y	20%
Relief u/s 91 [4.95%1 of ₹ 2,00,000]	9,900
Tax payable (Rounded off u/s 288B)	**18,490**

[1.] Indian average tax rate: 04.95% Foreign average tax rate: 20.00%

Relief u/s 91 is available at lower of aforesaid rate. i.e., 4.95%

Illustration 4.

Arvind, a textile merchant and resident Indian is doing business in India and abroad. During the previous year 2023-24, he disclosed the following information:

	₹
Income from business in India	27,00,000
Income from business in Country- A with which	
India does not have agreement for avoidance of double taxation	15,00,000
Income-tax levied by government in Country-A	5,00,000
Loss from business in Country-B with which also	
India does not have agreement for avoidance of double taxation	(4,00,000)
Contribution to public provident fund	1,50,000
Payment of life insurance premium on the life of his Father and mother	20,000

Compute the tax liability of Arvind for the assessment year 2024-25.

Solution:

Computation of total income and tax liability for the A.Y. 2024-25

Particulars	Amount
Income from business in India	27,00,000
Income from business in Country A	15,00,000
Income from business in Country B	(-) 4,00,000
Gross Total Income	38,00,000
Less: Deduction u/s 80C	NA
Total income	38,00,000
Tax on above	8,40,000
Add: Health & Education cess	33,600
Tax and cess payable	8,73,600

Particulars	Amount
Average rate of tax [₹ 8,73,600 / ₹ 38,00,000 x 100]	22.99%
Rate of tax in country A	33.33%
Relief u/s 91 [22.99%[1] of ₹ 15,00,000]	3,44,850
Tax payable (Rounded off u/s 288B)	**5,28,750**

[1] Indian average tax rate: 22.99% Foreign average tax rate: 33.33%

Relief u/s 91 is available at lower of the aforesaid rates i.e., 22.99%

Illustration 5.

Amar, an individual, resident of India, receives the following payments after TDS during the previous year 2023-24:

(i)	Professional fees on 17.08.2023	2,40,000
(ii)	Professional fees on 04.03.2024	1,60,000

Both the above services were rendered in country X on which TDS of ₹ 50,000 and ₹ 30,000 respectively has been deducted. He had incurred an expenditure of ₹ 2,40,000 for earning both these receipts / income. His income from other sources in India is ₹ 5,00,000 and he has made payment of ₹ 70,000 towards LIC. Compute the tax liability of Amar and also the relief u/s 91, if any, for A.Y.2024-25.

Solution:

Computation of total income and tax liability of Mr. Amar for the A.Y. 2024-25

Particulars	Amount	Amount
Income from profession from foreign	4,80,000	
Less: Expenses	2,40,000	2,40,000
Income from profession in India		5,00,000
Gross Total Income		7,40,000
Less: Deduction u/s 80C		NA
Total income		**7,40,000**
Tax on above		29,000
Add: Health & Education cess		1,160
Tax and cess payable		30,160
Average rate of tax [₹ 30,160 / ₹ 7,40,000 x 100]		4.08%
Rate of tax in Country X		16.67%
Relief u/s 91 [4.08%^ of ₹ 2,40,000]		9,792
Tax payable (Rounded off u/s 288B)		**20,370**

^ Relief u/s 91 is available at a lower rate i.e., 4.08%

Foreign Tax Credit [Rule 128]

An assessee, being a resident shall be allowed a credit for the amount of any foreign tax paid by him in a country or specified territory outside India, by way of deduction or otherwise, in the year in which the income corresponding to such tax has been offered to tax or assessed to tax in India, in the manner and to the extent as specified in this

rule.

Taxpoint:

- More than one year: In a case, where such foreign income is offered to tax in more than one year, credit of foreign tax shall be allowed across those years in the same proportion in which the income is offered to tax or assessed to tax in India.
- No credit for interest, etc.: The credit shall be available against the amount of tax, surcharge and cess payable under the Act but not in respect of any sum payable by way of interest, fee or penalty.
- No credit for disputed tax: No credit shall be available in respect of any amount of foreign tax or part thereof which is disputed in any manner by the assessee. However, the credit of such disputed tax shall be allowed for the year in which such income is offered to tax or assessed to tax in India if the assessee within 6 months from the end of the month in which the dispute is finally settled, furnishes evidence of settlement of dispute and an evidence to the effect that the liability for payment of such foreign tax has been discharged by him and furnishes an undertaking that no refund in respect of such amount has directly or indirectly been claimed or shall be claimed.

Meaning of Foreign Tax

In respect of	Foreign Tax
A country or specified territory with which India has entered into an agreement u/s 90 or 90A	Tax covered under the said agreement
Any other country or specified territory	Tax payable under the law of that country or specified territory in the nature of income-tax referred to in the Explanation to sec. 91 (i.e., "income-tax" in relation to any country includes any excess profits tax or business profits tax charged on the profits by the Government of any part of that country or a local authority in that country)

Taxpoint

The credit of foreign tax shall be the aggregate of the amounts of credit computed separately for each source of income arising from a particular country or specified territory outside India and shall be given effect to in the following manner:

- The credit shall be the lower of the tax payable under the Act on such income and the foreign tax paid on such income.
  - However, where the foreign tax paid exceeds the amount of tax payable in accordance with the provisions of the agreement for relief or avoidance of double taxation, such excess shall be ignored.
- The credit shall be determined by conversion of the currency of payment of foreign tax at the telegraphic transfer buying rate on the last day of the month immediately preceding the month in which such tax has been paid or deducted.

Tax Payable under MAT or AMT

- In a case where any tax is payable u/s 115JB or 115JC, the credit of foreign tax shall be allowed against such tax in the same manner as is allowable against any tax payable under the provisions of the Act other than the provisions of the said sections (hereafter referred to as the "normal provisions").
- Where the amount of foreign tax credit available against the tax payable u/s 115JB or 115JC exceeds the amount of tax credit available against the normal provisions, then while computing the amount of credit u/s

115JAA or 115JD in respect of the taxes paid u/s 115JB or 115JC, as the case may be, such excess shall be ignored.

Documents Required for Credit

Credit of any foreign tax shall be allowed on furnishing the following documents by the assessee within due date of furnishing return of income:

- a statement of income from the country or specified territory outside India offered for tax for the previous year and of foreign tax deducted or paid on such income in Form No.67 and verified in the manner specified therein;
- certificate or statement specifying the nature of income and the amount of tax deducted therefrom or paid by the assessee:
  - a) from the tax authority of the country or the specified territory outside India; or
  - b) from the person responsible for deduction of such tax; or
  - c) signed by the assessee:
    - The statement furnished and signed by the assessee shall be valid if it is accompanied by:
      - A. an acknowledgement of online payment or bank counter foil or challan for payment of tax where the payment has been made by the assessee;
      - B. proof of deduction where the tax has been deducted.

Taxpoint: Form No.67 shall also be furnished in a case where the carry backward of loss of the current year results in refund of foreign tax for which credit has been claimed in any earlier previous year or years.

Permanent Establishment (PE)

One of the important terms that occurs in all the Double Taxation Avoidance Agreements is the term 'Permanent Establishment' (PE) which has not been defined in the Income Tax Act. However as per the Double Taxation Avoidance Agreements, PE includes, a wide variety of arrangements i.e. a place of management, a branch, an office, a factory, a workshop or a warehouse, a mine, a quarry, an oilfield etc. Imposition of tax on a foreign enterprise is done only if it has a PE in the contracting state. Tax is computed by treating the PE as a distinct and independent enterprise.

Generally, in Indian context, the term permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on. The term "permanent establishment" shall also include:

a. a place of management;

b. a branch;

c. an office;

d. a factory;

e. a workshop;

f. a mine, an oil or gas well, a quarry or any other place of extraction of natural resources;

g. a warehouse in relation to a person providing storage facilities for others;

h. a farm, plantation or other place where agricultural, pastoral, forestry or plantation activities are carried on;

i. premises used as a sales outlet or for receiving or soliciting orders;

j. an installation or structure, or plant or equipment, used for the exploration for or exploitation of natural resources;

k. a building site or construction, installation or assembly project, or supervisory activities in connection with such a site or project, where that site or project exists or those activities are carried on (whether separately or together with other sites, projects or activities) for more than specified months (generally 6 months).

Exclusion

An enterprise shall not be deemed to have a permanent establishment merely by reason of :

a. the use of facilities solely for the purpose of storage or display of goods or merchandise belonging to the enterprise;

b. the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display;

c. the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

d. the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or of collecting information, for the enterprise; or

e. the maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information, for scientific research, or for similar activities which have a preparatory or auxiliary character, for the enterprise.

An enterprise of one of the Contracting States shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, a general commission agent or any other agent of an independent status, where that person is acting in the ordinary course of the person's business as such a broker or agent. However, when the activities of such a broker or agent are carried on wholly or principally on behalf of that enterprise itself or on behalf of that enterprise and other enterprises controlling, or controlled by or subject to the same common control as, that enterprise, the person will not be considered a broker or agent of an independent status within the meaning of this paragraph.

Taxation of Business Process Outsourcing Units in India

Taxation of IT-enabled Business Process Outsourcing Units in India as provided in the Circular 05/2004 dated 28-9-2004 are as under:

1. A non-resident entity may outsource certain services to a resident Indian entity. If there is no business connection between the two, the resident entity may not be a Permanent Establishment of the non-resident entity, and the resident entity would have to be assessed to income-tax as a separate entity. In such a case, the non-resident entity will not be liable under the Income-tax Act, 1961.

2. However, it is possible that the non-resident entity may have a business connection with the resident Indian entity. In such a case, the resident Indian entity could be treated as the Permanent Establishment of the non-resident entity. The tax treatment of the Permanent Establishment in such a case is under consideration in this circular.

3. During the last decade or so, India has seen a steady growth of outsourcing of business processes by non-residents or foreign companies to IT-enabled entities in India. Such entities are either branches or associated enterprises of the foreign enterprise or an independent Indian enterprise. Their activities range from mere procurement of orders for sale of goods or provision of services and answering sales related queries to the provision of services itself like software maintenance service, debt collection service, software development service, credit card/mobile telephone related service, etc. The non-resident entity or the foreign company will

be liable to tax in India only if the IT-enabled BPO unit in India constitutes its Permanent Establishment. The extent to which the profits of the non-resident enterprise is to be attributed to the activities of such Permanent Establishment in India has been under consideration of the Board.

4. A non-resident or a foreign company is treated as having a Permanent Establishment in India under Article 5 of the Double Taxation Avoidance Agreements entered into by India with different countries if the said non-resident or foreign company carries on business in India through a branch, sales office etc. or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts or regularly delivers goods or merchandise or habitually secures orders on behalf of the non-resident principal. In such a case, the profits of the non-resident or foreign company attributable to the business activities carried out in India by the Permanent Establishment becomes taxable in India under Article 7 of the Double Taxation Avoidance Agreements.

5. Paragraph 1 of Article 7 of Double Taxation Avoidance Agreements provides that if a foreign enterprise carries on business in another country through a Permanent Establishment situated therein, the profits of the enterprise may be taxed in the other country but only so much of them as is attributable to the Permanent Establishment. Paragraph 2 of the same Article provides that subject to the provisions of Paragraph 3, there shall in each contracting state be attributed to that Permanent Establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a Permanent Establishment. Paragraph 3 of the Article provides that in determining the profits of a Permanent Establishment there shall be allowed as deductions expenses which are incurred for the purposes of the Permanent Establishment including executive and general administrative expenses so incurred, whether in the State in which the Permanent Establishment is situated or elsewhere. What are the expenses that are deductible would have to be determined in accordance with the accepted principles of accountancy and the provisions of the Income-tax Act, 1961.

6. Paragraph 2 contains the central directive on which the allocation of profits to a Permanent Establishment is intended to be based. The paragraph incorporates the view that the profits to be attributed to a Permanent Establishment are those which that Permanent Establishment would have made if, instead of dealing with its Head Office, it had been dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market. This corresponds to the "arm's length principle". Paragraph 3 only provides a rule applicable for the determination of the profits of the Permanent Establishment, while paragraph 2 requires that the profits so determined correspond to the profit that a separate and independent enterprise would have made. Hence, in determining the profits attributable to an IT-enabled BPO unit constituting a Permanent Establishment, it will be necessary to determine the price of the services rendered by the Permanent Establishment to the Head office or by the Head office to the Permanent Establishment on the basis of "arm's length principle".

7. "Arm's length price" would have the same meaning as in the definition in sec. 92F(iii) of the Income-tax Act. The arm's length price would have to be determined in accordance with the provisions of sec. 92 to 92F of the Act.

Overview of Articles in DTAAs

12.4

Most of the world's income tax systems impose tax on the world-wide income of their residents and on profits with a source in the country where the income is derived by a non-resident. In the event of cross-border investments or business activities, two jurisdictions may wish to tax the same profits – the source country because the income is attributable to factors within that country and the residence country because all residents are taxed on their world-wide incomes. In the absence of any agreement between the source country and the residence country from which a cross-border investor or business is carried out, the source country would have primary taxing rights if only because it is in a position to extract the tax before the profits are repatriated to the residence country. Unless the residence country wished to double tax the income and in effect discourage any outward investment or business activities by its residents, it will have no choice but to forgo its claimed taxing rights and limit its tax to the difference, if any, between the tax rate imposed in the source country and that imposed in the residence country.

Wealthier countries, particularly OECD nations, very often enter into treaties with each other to divide taxing rights flowing from their competing claims to tax the same income. Treaties limit the source country's taxing rights, leaving more room for the country in which the investor or business is resident to tax the profits. Where two capital exporting nations enter into a tax treaty, the limitation of the source country's taxing rights has little overall impact as each jurisdiction will sacrifice to the other taxing rights of profits from cross-border investment and business. If one party to a treaty is a capital importing nation, the treaty will shift overall taxing rights (and tax revenue) from the poorer country to the richer country.

Country representatives commonly draw on two model treaties prepared by the OECD and UN respectively when negotiating tax treaties. The OECD treaty shifts more taxing powers to capital exporting countries while the UN treaty reserves more for capital importing countries.

Article-wise comparison of these two models are as under:

Para	OECD Model Tax Convention	UN Model Convention
Article 1 "Persons Covered"	This Convention shall apply to persons who are residents of one or both of the Contracting States.	
1	**Taxpoint:** Person is defined in article 3	
2	For the purposes of this Convention, income derived by or through an entity or arrangement that is treated as wholly or partly fiscally transparent under the tax law of either Contracting State shall be considered to be income of a resident of a Contracting State but only to the extent that the income is treated, for purposes of taxation by that State, as the income of a resident of that State.	
3	This Convention shall not affect the taxation, by a Contracting State, of its residents except with respect to the benefits granted under paragraph 3	This Convention shall not affect the taxation, by a Contracting State, of its residents except with respect to the benefits granted under 8

Para	OECD Model Tax Convention	UN Model Convention
	of Article 7, paragraph 2 of Article 9 and Articles 19, 20, 23 [A] [B], 24, 25 and 28.	paragraph 2 of Article 9, [paragraph 2 of Article 18 (Alternative A) or paragraph 3 of Article 18 (Alternative B)] and Articles 19, 20, [23 A or 23 B], 24, [25 (Alternative A) or 25 (Alternative B)] and 2
	Article 2 "Taxes Covered"	
1	This Convention shall apply to taxes on **income** and on **capital** imposed on behalf of a Contracting State or of its political subdivisions or local authorities, irrespective of the manner in which they are levied.	
2	There shall be regarded as taxes on income and on capital all taxes imposed on total income, on total capital, or on elements of income or of capital, including taxes on gains from the alienation of movable or immovable property, taxes on the total amounts of wages or salaries paid by enterprises, as well as taxes on capital appreciation. **Taxpoint** Tax imposed on the following are covered: ➢ Total income, ➢ Total capital, ➢ Elements of income or of capital, ➢ Gains from the alienation of movable or immovable property, ➢ Total amounts of wages or salaries paid by enterprises, ➢ Capital appreciation.	
3	The existing taxes to which the Convention shall apply are in particular: (a) (in State A): ..... (b) (in State B):	
4	The Convention shall apply also to any **identical** or **substantially similar taxes** which are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of **significant changes made to their tax law**.	
	Article 3 "General Definitions"	
1	For the purposes of this Convention, unless the context otherwise requires:	
1(a)	The term "person" includes an individual, a company and any other body of persons;	
1(b)	The term "company" means any body corporate or any entity that is treated as a body corporate for tax purposes; **Taxpoint:** It includes unincorporated entity like partnership firm, trust, etc.	
1(c)	The term "enterprise" applies to the carrying on of any business	--
	Taxpoint: Enterprise generally means a profit making entity including carrying on any professional activity.	

Para	OECD Model Tax Convention	UN Model Convention
1(d) of OECD Model and 1(c) of UN model	The terms "enterprise of a Contracting State" and "enterprise of the other Contracting State" mean respectively an enterprise carried on by a resident of a Contracting State and an enterprise carried on by a resident of the other Contracting State;	
1(e) of OECD Model and 1(d) of UN model	The term "international traffic" means any transport by a ship or aircraft except when the ship or aircraft is operated solely between places in a Contracting State and the enterprise that operates the ship or aircraft is not an enterprise of that State; **Taxpoint:** Further refer article 8	
1(f) of OECD Model and 1(e) of UN model	The term "competent authority" means: (i) (in State A): ..... (ii) (in State B): ..... **Taxpoint:** This definition enables each contracting States, to nominate one or more authorities as being competent authorities to handle issue relating to the convention.	
1(g) of OECD Model and 1(f) of UN model	The term "national", in relation to a Contracting State, means: (i) any individual possessing the **nationality or citizenship** of that Contracting State; and (ii) any legal person, partnership or association deriving its status as such from the laws in force in that Contracting State	The term "national" means: (i) any individual possessing the **nationality** of a Contracting State (ii) any legal person, partnership or association deriving its status as such from the laws in force in a Contracting State.
	Taxpoint: In UN Model, the word "citizenship" was excluded.	
1(h)	The term "business" includes the performance of professional services and of other activities of an independent character.	--
1(i) of OECD Model and 1(g) of UN Model	The term "recognised pension fund" of a State means an entity or arrangement established in that State that is treated as a separate person under the taxation laws of that State and: (i) that is established and operated exclusively or almost exclusively to administer or provide retirement benefits and ancillary or incidental benefits to individuals and that is regulated as such by that State or one of its political subdivisions or local authorities; or (ii) that is established and operated exclusively or almost exclusively to invest funds for the benefit of entities or arrangements referred to in subdivision (i).	
2	As regards the application of the Convention at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires or the competent authorities agree to a different meaning pursuant to the provisions of Article 25, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State.	

<table>
<tr><th>Para</th><th>OECD Model Tax Convention</th><th>UN Model Convention</th></tr>
<tr><td></td><td colspan="2">Taxpoint: If any term used under tax treaty is not defined there in then the meaning of that term can be adopted from tax laws of the relevant contracting states. However, where more than one meaning is given in the tax laws of a contracting State, the meaning which is provided for a particular provision for an issue, should be considered.</td></tr>
<tr><td colspan="3">Article 4 “Resident”</td></tr>
<tr><td>1</td><td>For the purposes of this Convention, the term “resident of a Contracting State” means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof as well as a recognised pension fund of that State. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.</td><td>For the purposes of this Convention, the term “resident of a Contracting State” means any person who, under the laws of that State, is liable to tax therein by reason of that person’s domicile, residence, place of incorporation, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof as well as a recognized pension fund of that State. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.</td></tr>
<tr><td>2</td><td colspan="2">Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:
a. He shall be deemed to be a resident only of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests);
b. If the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode;
c. If he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national;
d. If he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.
Taxpoint:
Tie-breaker rules, as the name suggests, serve to determine which of two countries should tax an individual as his/her country of residence, in case there is a “tie” on the matter between two countries.
WHICH COUNTRY’S PRESIDENT AM I?
PERMANENT HOSE
➢ In which country do you have a permanent home (Owned or Rented) available to you?
➢ If you have permanent home in more than one country, move to the next question
CENTER OF VITAL INTEREST
➢ In which country are your personal and economic relations closer?
➢ If the center of vital interest cannot be determined, move to the text questions</td></tr>
</table>

<table>
<tr><th>Para</th><th>OECD Model Tax Convention</th><th>UN Model Convention</th></tr>
<tr><td></td><td colspan="2">WHICH COUNTRY'S PRESIDENT AM I?
HABITUAL ABODE
➢ In which country do you have an habitual abode?
➢ If you have an habitual abode in neither of the countries, move to the next question
NATIONALITY
➢ In which country are you a national?
➢ If you are a national of both countries or of neither of them, move to the next question
COMPETENT AUTHORITY
➢ The residency will be determined by mutual agreement between both the countries 'competent authority'</td></tr>
<tr><td>3</td><td colspan="2">Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, the competent authorities of the Contracting States shall endeavour to determine by mutual agreement the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention, having regard to its place of effective management, the place where it is incorporated or otherwise constituted and any other relevant factors. In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by this Convention except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting States.
Taxpoint: This is tie-breaker rule for a person other than an individual.</td></tr>
<tr><td colspan="3">Article 5 "Permanent Establishment"</td></tr>
<tr><td>1</td><td colspan="2">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.</td></tr>
<tr><td>2</td><td colspan="2">The term "permanent establishment" includes especially:
a) a place of management;
b) a branch;
c) an office;
d) a factory;
e) a workshop, and
f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.</td></tr>
<tr><td>3</td><td>A building site or construction or installation project constitutes a permanent establishment only if it lasts more than 12 months.</td><td>The term "permanent establishment" also encompasses:
a. 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 6 months;</td></tr>
</table>

Para	OECD Model Tax Convention	UN Model Convention
		b. The **furnishing of services**, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only if activities of that nature continue within a Contracting State for a period or periods aggregating more than 183 days in any 12-month period commencing or ending in the fiscal year concerned.
4	Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include: a) the use of facilities solely for the purpose of **storage, display or delivery** of goods or merchandise belonging to the enterprise; b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of **storage, display or delivery**; c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise; d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity; f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e), provided that such activity or, in the case of subparagraph f), the overall activity of the fixed place of business, is of a preparatory or auxiliary character.	Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include: (a) The use of facilities solely for the purpose of **storage or display** of goods or merchandise belonging to the enterprise; (b) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of **storage or display**; (c) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise; (d) The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise; (e) The maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity; (f) The maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs (a) to (e), provided that such activity or, in the case of subparagraph (f), the overall activity of the fixed place of business, is of a preparatory or auxiliary character.
	Taxpoint: Para 4(a) and 4(b) of the UN model does not include the word "delivery"	

Para	OECD Model Tax Convention	UN Model Convention
4.1	Paragraph 4 shall not apply to a fixed place of business that is used or maintained by an enterprise if the same enterprise or a closely related enterprise carries on business activities at the same place or at another place in the same Contracting State and a. that place or other place constitutes a permanent establishment for the enterprise or the closely related enterprise under the provisions of this Article, or b. the overall activity resulting from the combination of the activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, is not of a preparatory or auxiliary character, provided that the business activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, constitute complementary functions that are part of a cohesive business operation.	Paragraph 4 shall not apply to a fixed place of business that is used or maintained by an enterprise if the same enterprise or a closely related enterprise carries on business activities at the same place or at another place in the same Contracting State and: a. that place or other place constitutes a permanent establishment for the enterprise or the closely related enterprise under the provisions of this Article, or b. the overall activity resulting from the combination of the activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, is not of a preparatory or auxiliary character, provided that the business activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, constitute complementary functions that are part of a cohesive business operation
5	Notwithstanding the provisions of paragraphs 1 and 2 but subject to the provisions of paragraph 6, where a person is acting in a Contracting State on behalf of an enterprise and, in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are a. in the name of the enterprise, or b. for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or c. for the provision of services by that enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if	Notwithstanding the provisions of paragraphs 1 and 2 but subject to the provisions of paragraph 7, where a person is acting in a Contracting State on behalf of an enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, if such a person: a. habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are i. in the name of the enterprise, or ii. for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or iii. for the provision of services by that enterprise,

Para	OECD Model Tax Convention	UN Model Convention
	exercised through a fixed place of business (other than a fixed place of business to which paragraph 4.1 would apply), would not make this fixed place of business a permanent establishment under the provisions of that paragraph.	unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business (other than a fixed place of business to which paragraph 4.1 would apply), would not make this fixed place of business a permanent establishment under the provisions of that paragraph; or b. the person does not habitually conclude contracts nor plays the principal role leading to the conclusion of such contracts, but habitually maintains in that State a stock of goods or merchandise from which that person regularly delivers goods or merchandise on behalf of the enterprise.
6	--	Notwithstanding the preceding provisions of this Article but subject to the provisions of paragraph 7, an insurance enterprise of a Contracting State shall, except in regard to re-insurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or insures risks situated therein through a person.
6 of OECD Model and 7 of UN Model	Paragraph 5 shall not apply where the person acting in a Contracting State on behalf of an enterprise of the other Contracting State carries on business in the first-mentioned State as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent within the meaning of this paragraph with respect to any such enterprise.	Paragraphs 5 and 6 shall not apply where the person acting in a Contracting State on behalf of an enterprise of the other Contracting State carries on business in the first-mentioned State as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent within the meaning of this paragraph with respect to any such enterprise.
	Taxpoint: In UN Model, provisions for both dependent agent and independent agent is discussed.	
7 of OECD Model and 8 of UN Model	The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.	

Para	OECD Model Tax Convention	UN Model Convention
8 of OECD Model and 9 of UN Model	For the purposes of this Article, a person or enterprise is closely related to an enterprise if, based on all the relevant facts and circumstances, one has control of the other or both are under the control of the same persons or enterprises. In any case, a person or enterprise shall be considered to be closely related to an enterprise if one possesses directly or indirectly more than 50 per cent of the beneficial interest in the other (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) or if another person or enterprise possesses directly or indirectly more than 50 per cent of the beneficial interest (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) in the person and the enterprise or in the two enterprises.	
	Article 6 "Income from Immovable Property"	
1 to 4	1. Income derived by a resident of a Contracting State from immovable property (including income from agriculture or forestry) situated in the other Contracting State may be taxed in that other State.	1. Income derived by a resident of a Contracting State from immovable property (including income from agriculture or forestry) situated in the other Contracting State may be taxed in that other State.
	2. The term "immovable property" shall have the meaning which it has under the law of the Contracting State in which the property in question is situated. The term shall in any case include property accessory to immovable property, livestock and equipment used in agriculture and forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources; ships and aircraft shall not be regarded as immovable property.	2. The term "immovable property" shall have the meaning which it has under the law of the Contracting State in which the property in question is situated. The term shall in any case include property accessory to immovable property, livestock and equipment used in agriculture and forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources; ships and aircraft shall not be regarded as immovable property.
	3. The provisions of paragraph 1 shall apply to income derived from the direct use, letting, or use in any other form of immovable property.	3. The provisions of paragraph 1 shall also apply to income derived from the direct use, letting, or use in any other form of immovable property.
	4. The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise.	4. The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise and to income from immovable property used for the performance of independent personal services

Para	OECD Model Tax Convention	UN Model Convention
	Article 7 "Business Profits"	
1	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 that are attributable to the permanent establishment in accordance with the provisions of paragraph 2 may be taxed in that other State.	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 attributable to a. that permanent establishment; b. sales in that other State of goods or merchandise of the same or similar kind as those sold through that permanent establishment; or c. other business activities carried on in that other State of the same or similar kind as those effected through that permanent establishment.
	Taxpoint: Principle of Force of Attraction (FOA) Rule The basic principle underlying the principle of FOA rule is that when an enterprise establishes a PE in another country, it brings itself within the jurisdiction of that country to such an extent that such another country acquires right to tax all profits that enterprise derives from their country, whether through the involvement of that PE or otherwise. Therefore, under the FOA rule, mere existence of PE in another country leads to all the profits, that can be said to be derived from that another country, being treated as taxable in that another country. In substance, such extended scope empowers the source country to tax profits of the enterprise also from the direct sale of similar goods/services in the source country, without involvement of the PE. Force of Attraction (FOA) in a way expands the rights of the source country to tax such business income of an enterprise. UN model, includes this rule.	
2	For the purposes of this Article and Article [23 A] [23 B], the profits that are attributable in each Contracting State to the permanent establishment referred to in paragraph 1 are the profits it might be expected to make, in particular in its dealings with other parts of the enterprise, if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the functions performed, assets used and risks assumed by the enterprise through the permanent establishment and through the other parts of the enterprise.	Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.
	Taxpoint: In order to allocate profits, OECD Model uses the term like functions performed, asset used and risk assumed. However, these terms are not used in the UN model.	

Para	OECD Model Tax Convention	UN Model Convention
3		In the determination of the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the business of the permanent establishment including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere. However, no such deduction shall be allowed in respect of amounts, if any, paid (otherwise than towards reimbursement of actual expenses) by the permanent establishment to the head office of the enterprise or any of its other offices, by way of royalties, fees or other similar payments in return for the use of patents or other rights, or by way of commission, for specific services performed or for management, or, except in the case of a banking enterprise, by way of interest on moneys lent to the permanent establishment. Likewise, no account shall be taken, in the determination of the profits of a permanent establishment, for amounts charged (otherwise than towards reimbursement of actual expenses), by the permanent establishment to the head office of the enterprise or any of its other offices, by way of royalties, fees or other similar payments in return for the use of patents or other rights, or by way of commission for specific services performed or for management, or, except in the case of a banking enterprise, by way of interest on moneys lent to the head office of the enterprise or any of its other offices.
3	Where, in accordance with paragraph 2, a Contracting State adjusts the profits that are attributable to a permanent establishment of an enterprise of one of the Contracting States and taxes accordingly profits of the enterprise that have been charged to tax in the other State, the other State shall, to the extent necessary to eliminate double taxation on these profits, make an appropriate adjustment to the amount of the tax charged on those profits. In determining such adjustment, the competent authorities of the Contracting States shall, if necessary, consult each other.	--

Para	OECD Model Tax Convention	UN Model Convention
4	--	In so far as it has been customary in a Contracting State to determine the profits to be **attributed to a permanent establishment** on the basis of an **apportionment** of the total profits of the enterprise to its various parts, nothing in paragraph 2 shall preclude that Contracting State from determining the profits to be taxed by such an apportionment as may be customary; the method of apportionment adopted shall, however, be such that the result shall be in accordance with the principles contained in this Article.
5	--	For the purposes of the preceding paragraphs, the profits to be **attributed to the permanent establishment** shall be determined by the same method year by year unless there is good and sufficient reason to the contrary
4 of OECD Model & 6 of UN Model	Where profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.	
	Article 8 "International Shipping and Air Transport"	
1	Profits of an enterprise of a Contracting State from the operation of ships or aircraft in international traffic shall be taxable only in that State.	**Alternative A** Profits of an enterprise of a Contracting State from the operation of ships or aircraft in international traffic shall be taxable only in that State.
2	The provisions of paragraph 1 shall also apply to profits from the participation in a pool, a joint business or an international operating agency.	The provisions of paragraph 1 shall also apply to profits from the participation in a pool, a joint business or an international operating agency
		Alternative B 1. Profits of an enterprise of a Contracting State from the operation of aircraft in international traffic shall be taxable only in that State.

Para	OECD Model Tax Convention	UN Model Convention
		2. Profits of an enterprise of a Contracting State from the operation of ships in international traffic shall be taxable only in that State unless the shipping activities arising from such operation in the other Contracting State are more than casual. If such activities are more than casual, such profits may be taxed in that other State. The profits to be taxed in that other State shall be determined on the basis of an appropriate allocation of the overall net profits derived by the enterprise from its shipping operations. The tax computed in accordance with such allocation shall then be reduced by ___ per cent. (The percentage is to be established through bilateral negotiations.) 3. The provisions of paragraphs 1 and 2 shall also apply to profits from the participation in a pool, a joint business or an international operating agency.
	Article 9 "Associated Enterprises"	
1	**Where:** a. an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the other Contracting State, or b. the same persons participate directly or indirectly in the management, control or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly	
2	Where a Contracting State includes in the profits of an enterprise of that State—and taxes accordingly—profits on which an enterprise of the other Contracting State has been charged to tax in that other State and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other State shall make an appropriate adjustment to the amount of the tax charged therein on those profits. In determining such adjustment, due regard shall be had to the other provisions of the Convention and the competent authorities of the Contracting States shall, if necessary, consult each other.	

Para	OECD Model Tax Convention	UN Model Convention
3	--	The provisions of paragraph 2 shall not apply where judicial, administrative or other legal proceedings have resulted in a final ruling that by actions giving rise to an adjustment of profits under paragraph 1, one of the enterprises concerned is liable to penalty with respect to fraud, gross negligence or wilful default.
	Article 10 "Dividends"	
1	Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.	
2	However, dividends paid by a company which is a resident of a Contracting State may also be taxed in that State according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed: a. 5% of the gross amount of the dividends if the beneficial owner is a company which holds directly at least 25% of the capital of the company paying the dividends throughout a 365 day period that includes the day of the payment of the dividend (for the purpose of computing that period, no account shall be taken of changes of ownership that would directly result from a corporate reorganisation, such as a merger or divisive reorganisation, of the company that holds the shares or that pays the dividend); b. 15 per cent of the gross amount of the dividends in all other cases. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of these limitations. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.	However, dividends paid by a company which is a resident of a Contracting State may also be taxed in that State and according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed: a. ___ % (the percentage is to be established through bilateral negotiations) of the gross amount of the dividends if the beneficial owner is a company which holds directly at least 25% of the capital of the company paying the dividends throughout a 365 day period that includes the day of the payment of the dividend (for the purpose of computing that period, no account shall be taken of changes of ownership that would directly result from a corporate reorganisation, such as a merger or divisive reorganisation, of the company that holds the shares or that pays the dividend); b. ___ % (the percentage is to be established through bilateral negotiations) of the gross amount of the dividends in all other cases. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of these limitations. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

Para	OECD Model Tax Convention	UN Model Convention
3	The term "dividends" as used in this Article means income from shares, "jouissance" shares or "jouissance" rights, mining shares, founders' shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident.	The term "dividends" as used in this Article means income from shares, "jouissance" shares or "jouissance" rights, mining shares, founders' shares or other rights, not being debt claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident.
4	The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident through a permanent establishment situated therein and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.	The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment or fixed base. In such case the provisions of Article 7 or Article 14, as the case may be, shall apply
5	Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other State may not impose any tax on the dividends paid by the company, except insofar as such dividends are paid to a resident of that other State or insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment situated in that other State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.	Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other State may not impose any tax on the dividends paid by the company, except in so far as such dividends are paid to a resident of that other State or in so far as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or a fixed base situated in that other State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.
	Article 11 "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, interest arising in a Contracting State may also be taxed in that State 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 10% of the gross amount of the interest. The competent authorities of the Contracting States shall by	However, interest arising in a Contracting State may also be taxed in that State 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 ___ % [the percentage is to be established through bilateral negotiations] of

Para	OECD Model Tax Convention	UN Model Convention
	mutual agreement settle the mode of application of this limitation.	the gross amount of the interest. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation
3	The term "interest" as used in this Article means income from debt claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment shall not be regarded as interest for the purpose of this Article.	
4	The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises through a permanent establishment situated therein and the debt-claim in respect of which the interest is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.	The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arises, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the debt claim in respect of which the interest is paid is effectively connected with a. such permanent establishment or fixed base, or with b. business activities referred to in (c) of paragraph 1 of Article 7. In such cases the provisions of Article 7 or Article 14, as the case may be, shall apply.
5	Interest shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment, then such interest shall be deemed to arise in the State in which the permanent establishment is situated.	Interest shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the indebtedness on which the interest is paid was incurred, and such interest is borne by such permanent establishment or fixed base, then such interest shall be deemed to arise in the State in which the permanent establishment or fixed base is situated.
6	Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the interest, having regard to the debt claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.	

Para	OECD Model Tax Convention	UN Model Convention
	Taxpoint: Special relationship means a. direct or indirect participation in the management, control and capital b. relatives	
	Article 12 "Royalties"	
1	Royalties arising in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in that other State.	Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State
2	--	However, royalties arising in a Contracting State may also be taxed in that State and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed ___% [the percentage is to be established through bilateral negotiations] of the gross amount of the royalties. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this limitation.
2 of OECD Model and 3 of UN Model	The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.	The term "royalties" as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, **or films or tapes used for radio or television broadcasting**, any patent, trademark, design or model, plan, secret formula or process, or **for the use of, or the right to use, industrial, commercial or scientific equipment** or for information concerning industrial, commercial or scientific experience.
3 of OECD Model and 4 of UN Model	The provisions of paragraph 1 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise through a permanent establishment situated therein and the right or property in respect of which the royalties are paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.	The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the royalties, being a resident of a Contracting State, carries on business in the other Contracting State in which the royalties arise, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the royalties are paid is effectively connected with (a) such permanent establishment or fixed base, or with (b) business activities referred to in

Para	OECD Model Tax Convention	UN Model Convention
		(c) of paragraph 1 of Article 7. In such cases the provisions of Article 7 or Article 14, as the case may be, shall apply.
5	--	Royalties shall be deemed to arise in a Contracting State when the payer is a resident of that State. Where, however, the person paying the royalties, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the liability to pay the royalties was incurred, and such royalties are borne by such permanent establishment or fixed base, then such royalties shall be deemed to arise in the State in which the permanent establishment or fixed base is situated.
4 of OECD Model and 6 of UN Model	Where by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties, having regard to the use, right or information for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.	
	Article 12A "Fees for Technical Services"	
1 to 7	--	1. Fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. 2. However, notwithstanding the provisions of Article 14 and subject to the provisions of Articles 8, 16 and 17, fees for technical services arising in a Contracting State may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the beneficial owner of the fees is a resident of the other Contracting State, the tax so charged shall not exceed ___ % of the gross amount of the fees [the percentage to be established through bilateral negotiations]. 3. The term "fees for technical services" as used in this Article means any payment in consideration for any service of a

Para	OECD Model Tax Convention	UN Model Convention
		managerial, technical or consultancy nature, unless the payment is made: (a) to an employee of the person making the payment; (b) for teaching in an educational institution or for teaching by an educational institution; or (c) by an individual for services for the personal use of an individual. 4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of fees for technical services, being a resident of a Contracting State, carries on business in the other Contracting State in which the fees for technical services arise through a permanent establishment situated in that other State, or performs in the other Contracting State independent personal services from a fixed base situated in that other State, and the fees for technical services are effectively connected with: (a) such permanent establishment or fixed base, or (b) business activities referred to in (c) of paragraph 1 of Article 7. In such cases the provisions of Article 7 or Article 14, as the case may be, shall apply. 5. For the purposes of this Article, subject to paragraph 6, fees for technical services shall be deemed to arise in a Contracting State if the payer is a resident of that State or if the person paying the fees, whether that person is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the obligation to pay the fees was incurred, and such fees are borne by the permanent establishment or fixed base.

Para	OECD Model Tax Convention	UN Model Convention
		6. For the purposes of this Article, fees for technical services shall be deemed not to arise in a Contracting State if the payer is a resident of that State and carries on business in the other Contracting State through a permanent establishment situated in that other State or performs independent personal services through a fixed base situated in that other State and such fees are borne by that permanent establishment or fixed base. 7. Where, by reason of a special relationship between the payer and the beneficial owner of the fees for technical services or between both of them and some other person, the amount of the fees, having regard to the services for which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the fees shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.
Article 12B "Income from Automated Digital Services"		
1	--	Income from automated digital services arising in a Contracting State, underlying payments for which are made to a resident of the other Contracting State, may be taxed in that other State.
2	--	However, subject to the provisions of Article 8 and notwithstanding the provisions of Article 14, income from automated digital services arising in a Contracting State 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 income is a resident of the other Contracting State, the tax so charged shall not exceed ___ % [the percentage is to be established through bilateral negotiations] of the gross amount of the payments underlying the income from automated digital services.

Para	OECD Model Tax Convention	UN Model Convention
3	--	The provisions of paragraph 2 shall not apply if the beneficial owner of the income from automated digital services, being a resident of a Contracting State, requests the other Contracting State where such income arises, to subject its qualified profits from automated digital services for the fiscal year concerned to taxation at the tax rate provided for in the domestic laws of that State. If the beneficial owner so requests, subject to the provisions of Article 8 and notwithstanding the provisions of Article 14, the taxation by that Contracting State shall be carried out accordingly. For the purposes of this paragraph, the qualified profits shall be 30% of the amount resulting from applying the profitability ratio of that beneficial owner's automated digital services business segment to the gross annual revenue from automated digital services derived from the Contracting State where such income arises. Where segmental accounts are not maintained by the beneficial owner, the overall profitability ratio of the beneficial owner will be applied to determine qualified profits. However, where the beneficial owner belongs to a multinational enterprise group, the profitability ratio to be applied shall be that of the business segment of the group relating to the income covered by this Article, or of the group as a whole in case segmental accounts are not maintained by the group, provided such profitability ratio of the multinational enterprise group is higher than the aforesaid profitability ratio of the beneficial owner. Where the segmental profitability ratio or, as the case may be, the overall profitability ratio of the multinational enterprise group to which the beneficial owner belongs is not available to the Contracting State in which the income from automated digital services arises, the provisions of this paragraph shall not apply; in such a case, the provisions of paragraph 2 shall apply.

Para	OECD Model Tax Convention	UN Model Convention
4	--	For the purposes of paragraph 3, "multinational enterprise group" means any "group" that includes two or more enterprises, the tax residence for which is in different jurisdictions. Further, for the purposes of paragraph 3, the term "group" means a collection of enterprises related through ownership or control such that it is either required to prepare Consolidated Financial Statements for financial reporting purposes under applicable accounting principles or would be so required if equity interests in any of the enterprises were traded on a public stock exchange.
5	--	The term "automated digital services" as used in this Article means any service provided on the Internet or another electronic network, in either case requiring minimal human involvement from the service provider.
6	--	The term "automated digital services" includes especially: (a) online advertising services; (b) supply of user data; (c) online search engines; (d) online intermediation platform services; (e) social media platforms; (f) digital content services; (g) online gaming; (h) cloud computing services; and (i) standardized online teaching services
7	--	The provisions of this Article shall not apply if the payments underlying the income from automated digital services qualify as "royalties" or "fees for technical services" under Article 12 or Article 12A as the case may be
8	--	The provisions of paragraphs 1, 2 and 3 shall not apply if the beneficial owner of the income from automated digital services, being a resident of a Contracting State, carries on business in the other Contracting State in which the income from automated digital services arises through a permanent establishment situated in that other State, or performs in the other Contracting State

Para	OECD Model Tax Convention	UN Model Convention
		independent personal services from a fixed base situated in that other State, and the income from automated digital services is effectively connected with: a. such permanent establishment or fixed base, or b. business activities referred to in para 1(c) of Article 7. In such cases the provisions of Article 7 or Article 14, as the case may be, shall apply
9	--	For the purposes of this Article and subject to paragraph 10, income from automated digital services shall be deemed to arise in a Contracting State if the underlying payments for the income from automated digital services are made by a resident of that State or if the person making the underlying payments for the automated digital services, whether that person is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the obligation to make the payments was incurred, and such payments are borne by the permanent establishment or fixed base.
10	--	For the purposes of this Article, income from automated digital services shall be deemed not to arise in a Contracting State if the underlying payments for the income from automated digital services are made by a resident of that State which carries on business in the other Contracting State through a permanent establishment situated in that other State or performs independent personal services through a fixed base situated in that other State and such underlying payments towards automated digital services are borne by that permanent establishment or fixed base.
11	--	Where, by reason of a special relationship between the payer and the beneficial owner of the income from automated digital services or between both of them and some other person, the amount of the payments underlying such income, having regard to the services for

Para	OECD Model Tax Convention	UN Model Convention
		which they are paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments underlying such income from automated digital services shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of this Convention.
	Article 13 "Capital Gains"	
1	Gains derived by a resident of a Contracting State from 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, including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise), may be taxed in that other State.	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 that an enterprise of a Contracting State that operates ships or aircraft in international traffic derives from the alienation of such ships or aircraft, or of movable property pertaining to the operation of such ships or aircraft, shall be taxable only in that State	
4	Gains derived by a resident of a Contracting State from the alienation of shares or comparable interests, such as interests in a partnership or trust, may be taxed in the other Contracting State if, at any time during the 365 days preceding the alienation, these shares or comparable interests derived more than **50%** of their value directly or indirectly from immovable property, as defined in Article 6, situated in that other State.	Gains derived by a resident of a Contracting State from the alienation of shares or comparable interests, such as interests in a partnership or trust, may be taxed in the other Contracting State if, at any time during the 365 days preceding the alienation, these shares or comparable interests derived more than **50%** of their value directly or indirectly from immovable property, as defined in Article 6, situated in that other State.
5	--	Gains, other than those to which paragraph 4 applies, derived by a resident of a Contracting State from the alienation of shares of a company, or comparable interests, such as interests in a partnership or trust, which is a resident of the other Contracting State, may be taxed in

Para	OECD Model Tax Convention	UN Model Convention
		that other State if the alienator, at any time during the 365 days preceding such alienation, held directly or indirectly at least ___ % (the percentage is to be established through bilateral negotiations) of the capital of that company or entity.
5 of OECD Model and 6 of UN Model	Gains from the alienation of any property, other than that referred to in aforesaid paragraphs shall be taxable only in the Contracting State of which the alienator is a resident.	Gains derived by a resident of a Contracting State from the alienation of a right granted under the law of the other Contracting State which allows the use of resources that are naturally present in that other State and that are under the jurisdiction of that other State, may be taxed in that other State.
7	--	Subject to paragraphs 4 and 5, gains derived by a resident of a Contracting State from the alienation of shares of a company, or comparable interests of an entity, such as interests in a partnership or trust, may be taxed in the other Contracting State if a. the alienator, at any time during the 365 days preceding such alienation, held directly or indirectly at least ___% [the percentage is to be established through bilateral negotiations] of the capital of that company or entity; and b. at any time during the 365 days preceding the alienation, these shares or comparable interests derived more than 50% of their value directly or indirectly from i. a property any gain from which would have been taxable in that other State in accordance with the preceding provisions of this Article if that gain had been derived by a resident of the first-mentioned State from the alienation of that property at that time, or ii. any combination of property referred to in subdivision (i).
8	--	Gains from the alienation of any property other than that referred to in paragraphs 1 to 7 shall be taxable only in the Contracting State of which the alienator is a resident.

Para	OECD Model Tax Convention	UN Model Convention
Article 14 "Independent Personal Services"		
1 & 2	Deleted	1. Income derived by a resident of a Contracting State in respect of professional services or other activities of an independent character shall be taxable only in that State except in the following circumstances, when such income may also be taxed in the other Contracting State: a. If he has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in that other Contracting State; or b. If his stay in the other Contracting State is for a period or periods amounting to or exceeding in the aggregate 183 days in any 12 months period commencing or ending in the fiscal year concerned; in that case, only so much of the income as is derived from his activities performed in that other State may be taxed in that other State. 2. The term "professional services" includes especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.
Article 15 "Income from Employment" [OECD Model] / "Dependent Personal Services" [UN Model]		
1	Subject to the provisions of Articles 16, 18 and 19, salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.	
2	Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if: a. The recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned; and	Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if: a. The recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned; and

Para	OECD Model Tax Convention	UN Model Convention
	b. The remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and c. The remuneration is not borne by a permanent establishment which the employer has in the other State.	b. The remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and c. The remuneration is not borne by a permanent establishment or **a fixed base** which the employer has in the other State.
3	Notwithstanding the preceding provisions of this Article, remuneration derived by a resident of a Contracting State in respect of an employment, as a member of the regular complement of a ship or aircraft, that is exercised aboard a ship or aircraft operated in international traffic, other than aboard a ship or aircraft operated solely within the other Contracting State, shall be taxable only in the first-mentioned State.	
	Article 16 "Directors' Fees"	
1	Directors' fees and other similar payments derived by a resident of a Contracting State in his capacity as a member of the board of directors of a company which is a resident of the other Contracting State may be taxed in that other State.	
2	--	Salaries, wages and other similar remuneration derived by a resident of a Contracting State in his capacity as an official in a top-level managerial position of a company which is a resident of the other Contracting State may be taxed in that other State.
	Article 17 "Entertainers and Sportspersons"	
1	Notwithstanding the provisions of Article 15, income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as a sportsperson, from that resident's personal activities as such exercised in the other Contracting State, may be taxed in that other State.	Notwithstanding the provisions of Articles 14 and 15, income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as a sportsperson, from his personal activities as such exercised in the other Contracting State, may be taxed in that other State.
2	Where income in respect of personal activities exercised by an entertainer or a sportsperson acting as such accrues not to the entertainer or sportsperson but to another person, that income may, notwithstanding the provisions of Article 15, be taxed in the Contracting State in which the activities of the entertainer or sportsperson are exercised.	Where income in respect of personal activities exercised by an entertainer or a sportsperson in his capacity as such accrues not to the entertainer or sportsperson himself but to another person, that income may, notwithstanding the provisions of Articles 7, 14 and 15, be taxed in the Contracting State in which the activities of the entertainer or sportsperson are exercised.
	Article 18 "Pensions" [OECD Model] / "Pensions and Social Security Payments" [UN Model]	
	Subject to the provisions of paragraph 2 of Article 19, pensions and other similar remuneration paid to a resident of a Contracting State in consideration of past employment shall be taxable only in that State.	**Alternative A** 1. Subject to the provisions of paragraph 2 of Article 19, pensions and other similar remuneration paid to a resident of a Contracting State in consideration of past employment shall be taxable only in that State.

Para	OECD Model Tax Convention	UN Model Convention
		2. Notwithstanding the provisions of paragraph 1, pensions paid and other payments made under a public scheme which is part of the social security system of a Contracting State or a political subdivision or a local authority thereof shall be taxable only in that State. **Alternative B** 1. Subject to the provisions of paragraph 2 of Article 19, pensions and other similar remuneration paid to a resident of a Contracting State in consideration of past employment may be taxed in that State. 2. However, such pensions and other similar remuneration may also be taxed in the other Contracting State if the payment is made by a resident of that other State or a permanent establishment situated therein. 3. Notwithstanding the provisions of paragraphs 1 and 2, pensions paid and other payments made under a public scheme which is part of the social security system of a Contracting State or a political subdivision or a local authority thereof shall be taxable only in that State.
Article 19 "Government Service"		
1	a. Salaries, wages and other similar remuneration paid by a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. b. However, such salaries, wages and other similar remuneration shall be taxable only in the other Contracting State if the services are rendered in that State and the individual is a resident of that State who: i. is a national of that State; or ii. did not become a resident of that State solely for the purpose of rendering the services.	a. Salaries, wages and other similar remuneration paid by a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. b. However, such salaries, wages and other similar remuneration shall be taxable only in the other Contracting State if the services are rendered in that other State and the individual is a resident of that State who: i. is a national of that State; or ii. did not become a resident of that State solely for the purpose of rendering the services.

Para	OECD Model Tax Convention	UN Model Convention
2	a. Notwithstanding the provisions of paragraph 1, pensions and other similar remuneration paid by, or out of funds created by, a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. b. However, such pensions and other similar remuneration shall be taxable only in the other Contracting State if the individual is a resident of, and a national of, that State.	a. Notwithstanding the provisions of paragraph 1, pensions and other similar remuneration paid by, or out of funds created by, a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. b. However, such pensions and other similar remuneration shall be taxable only in the other Contracting State if the individual is a resident of, and a national of, that other State.
3	The provisions of Articles 15, 16, 17 and 18 shall apply to salaries, wages, pensions, and other similar remuneration in respect of services rendered in connection with a business carried on by a Contracting State or a political subdivision or a local authority thereof.	
	Article 20 "Students"	
	Payments which a student or business apprentice who is or was immediately before visiting a Contracting State a resident of the other Contracting State and who is present in the first-mentioned State solely for the purpose of his education or training receives for the purpose of his maintenance, education or training shall not be taxed in that State, provided that such payments arise from sources outside that State.	Payments which a student or business trainee or apprentice who is or was immediately before visiting a Contracting State a resident of the other Contracting State and who is present in the first-mentioned State solely for the purpose of his education or training receives for the purpose of his maintenance, education or training shall not be taxed in that State, provided that such payments arise from sources outside that State.
	Article 21 "Other Income"	
1	Items of income of a resident of a Contracting State, wherever arising, not dealt with in the foregoing Articles of this Convention shall be taxable only in that State.	
2	The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Article 6, if the recipient of such income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein and the right or property in respect of which the income is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.	The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Article 6, if the recipient of such income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the right or property in respect of which the income is paid is effectively connected with such permanent establishment or fixed base. In such case the provisions of Article 7 or Article 14, as the case may be, shall apply

Para	OECD Model Tax Convention	UN Model Convention
3		Notwithstanding the provisions of paragraphs 1 and 2, items of income of a resident of a Contracting State not dealt with in the foregoing Articles of this Convention and arising in the other Contracting State may also be taxed in that other State.
	Taxation of Capital **Article 22 "Capital"**	
1	Capital represented by immovable property referred to in Article 6, owned by a resident of a Contracting State and situated in the other Contracting State, may be taxed in that other State.	
2	Capital represented by 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 may be taxed in that other State	Capital represented by 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 by 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 may be taxed in that other State.
3	Capital of an enterprise of a Contracting State that operates ships or aircraft in international traffic represented by such ships or aircraft, and by movable property pertaining to the operation of such ships or aircraft, shall be taxable only in that State	
4	All other elements of capital of a resident of a Contracting State shall be taxable only in that State. **Taxpoint:** In UN Model, it is also mentioned that the question of the taxation of all other elements of capital of a resident of a Contracting State is left to bilateral negotiations. Should the negotiating parties decide to include in the Convention an article on the taxation of capital, they will have to determine whether to use the wording of paragraph 4 as shown or wording that leaves taxation to the State in which the capital is located	
	Methods for the Elimination of Double Taxation **Article 23 A "Exemption Method"**	
1	Where a resident of a Contracting State derives income or owns capital which may be taxed in the other Contracting State, in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State or because the capital is also capital owned by a resident of that State), the first-mentioned State shall, subject to the provisions of paragraphs 2 and 3, exempt such income or capital from tax. **Taxpoint:** Where the exemption method is followed, doubly taxed income or capital shall be exempted in the resident State and it will be taxable in the source State.	
2	Where a resident of a Contracting State derives items of income which, in accordance with the provisions of Articles 10, 11 (in UN Model 12, 12A and 12B also) may be taxed in the other Contracting State, the first-mentioned State shall allow as a deduction from the tax on the income of that resident an amount equal to the tax paid in that other State. Such deduction shall not, however, exceed that part of the tax, as computed before the deduction is given, which is attributable to such items of income which may be taxed in that other State.	

Para	OECD Model Tax Convention	UN Model Convention
3	Where in accordance with any provision of the Convention income derived or capital owned by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital. **Taxpoint:** The doubly taxed income may be considered for rate purpose in the resident State.	
4	The provisions of paragraph 1 shall not apply to income derived or capital owned by a resident of a Contracting State where the other Contracting State applies the provisions of this Convention to exempt such income or capital from tax or applies the provisions of paragraph 2 of Article 10 or 11 to such income.	The provisions of paragraph 1 shall not apply to income derived or capital owned by a resident of a Contracting State where the other Contracting State applies the provisions of this Convention to exempt such income or capital from tax or applies the provisions of paragraph 2 of Article 10, 11, 12 or 12A, or the provisions of Article 12B, to such income; in the case where the other Contracting State does not exempt the income, the first-mentioned State shall allow the deduction of tax provided for by paragraph 2
	Article 23 B "Credit Method"	
1	Where a resident of a Contracting State derives income or owns capital which may be taxed in the other Contracting State, in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State or because the capital is also capital owned by a resident of that State), the first-mentioned State shall allow: a. as a deduction from the tax on the income of that resident an amount equal to the income tax paid in that other State; b. as a deduction from the tax on the capital of that resident, an amount equal to the capital tax paid in that other State. Such deduction in either case shall not, however, exceed that part of the income tax or capital tax, as computed before the deduction is given, which is attributable, as the case may be, to the income or the capital which may be taxed in that other State.	
2	Where, in accordance with any provision of this Convention, income derived or capital owned by a resident of a Contracting State is exempt from tax in that State, such State may nevertheless, in calculating the amount of tax on the remaining income or capital of such resident, take into account the exempted income or capital.	
	Article 24 "Non-Discrimination"	
1	Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.	

Para	OECD Model Tax Convention	UN Model Convention
2	Stateless persons who are residents of a Contracting State shall not be subjected in either Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of the State concerned in the same circumstances, in particular with respect to residence, are or may be subjected.	
3	The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities. This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.	
4	Except where the provisions of paragraph 1 of Article 9, paragraph 6 of Article 11, or paragraph 4 of Article 12, apply, interest, royalties and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State. Similarly, any debts of an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable capital of such enterprise, be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned State.	Except where the provisions of paragraph 1 of Article 9, paragraph 6 of Article 11, paragraph 6 of Article 12, paragraph 7 of Article 12A or paragraph 11 of Article 12B apply, interest, royalties, fees for technical services, payments underlying income from automated digital services, and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State. Similarly, any debts of an enterprise of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable capital of such enterprise, be deductible under the same conditions as if they had been contracted to a resident of the first-mentioned State
5	Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of the first-mentioned State are or may be subjected.	
6	The provisions of this Article shall, notwithstanding the provisions of Article 2, apply to taxes of every kind and description.	
	Article 25 "Mutual Agreement Procedure"	
1 to 5	1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case to the competent authority of either Contracting State. The case must be presented within three years from the first notification of the	**Alternative A** 1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case to the competent authority of the Contracting

Para	OECD Model Tax Convention	UN Model Convention
	action resulting in taxation not in accordance with the provisions of the Convention. 2. The competent authority shall endeavour, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with the Convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States. 3. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention. 4. The competent authorities of the Contracting States may communicate with each other directly, including through a joint commission consisting of themselves or their representatives, for the purpose of reaching an agreement in the sense of the preceding paragraphs. 5. Where, a. under paragraph 1, a person has presented a case to the competent authority of a Contracting State on the basis that the actions of one or both of the Contracting States have resulted for that person in taxation not in accordance with the provisions of this Convention, and b. the competent authorities are unable to reach an agreement to resolve that case pursuant to paragraph 2 within two years from the date when all the information required by the competent authorities in order to address the case has been provided to both competent authorities, any unresolved issues arising from the case shall be submitted to arbitration if the person so requests in writing. These unresolved issues shall not, however, be submitted to arbitration	State of which he is a resident or, if his case comes under paragraph 1 of Article 24, to that of the Contracting State of which he is a national. The case must be presented within three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Convention. 2. The competent authority shall endeavour, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with this Convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States. 3. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention. 4. The competent authorities of the Contracting States may communicate with each other directly, including through a joint commission consisting of themselves or their representatives, for the purpose of reaching an agreement in the sense of the preceding paragraphs. The competent authorities, through consultations, may develop appropriate bilateral procedures, conditions, methods and techniques for the implementation of the mutual agreement procedure provided for in this Article. **Alternative B** 1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case to the competent authority of the Contracting

Para	OECD Model Tax Convention	UN Model Convention
	if a decision on these issues has already been rendered by a court or administrative tribunal of either State. Unless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision, that decision shall be binding on both Contracting States and shall be implemented notwithstanding any time limits in the domestic laws of these States. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this paragraph.	State of which he is a resident or, if his case comes under paragraph 1 of Article 24, to that of the Contracting State of which he is a national. The case must be presented within three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Convention. 2. The competent authority shall endeavour, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with this Convention. Any agreement reached shall be implemented notwithstanding any time limits in the domestic law of the Contracting States. 3. The competent authorities of the Contracting States shall endeavour to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention. 4. The competent authorities of the Contracting States may communicate with each other directly, including through a joint commission consisting of themselves or their representatives, for the purpose of reaching an agreement in the sense of the preceding paragraphs. The competent authorities, through consultations, may develop appropriate bilateral procedures, conditions, methods and techniques for the implementation of the mutual agreement procedure provided for in this Article. 5. Where, a. under paragraph 1, a person has presented a case to the competent authority of a Contracting State on the basis that the actions of one or both of the Contracting States have resulted for that person in taxation not in accordance with the provisions of this Convention, and

Para	OECD Model Tax Convention	UN Model Convention
		b. the competent authorities are unable to reach an agreement to resolve that case pursuant to paragraph 2 within three years from the presentation of the case to the competent authority of the other Contracting State, any unresolved issues arising from the case shall be submitted to arbitration if either competent authority so requests. The person who has presented the case shall be notified of the request. These unresolved issues shall not, however, be submitted to arbitration if a decision on these issues has already been rendered by a court or administrative tribunal of either State. The arbitration decision shall be binding on both States and shall be implemented notwithstanding any time limits in the domestic laws of these States unless both competent authorities agree on a different solution within six months after the decision has been communicated to them or unless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this paragraph.
Article 26 "Exchange of Information"		
1	The competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of this Convention or to the administration or enforcement of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention. The exchange of information is not restricted by Articles 1 and 2.	The competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of this Convention or to the administration or enforcement of the domestic laws of the Contracting States concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention. In particular, information shall be exchanged that would be helpful to a Contracting State in preventing avoidance or evasion of such taxes. The exchange of information is not restricted by Articles 1 and 2.

Para	OECD Model Tax Convention	UN Model Convention
2	Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, the determination of appeals in relation to the taxes referred to in paragraph 1, or the oversight of the above. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions. Notwithstanding the foregoing, information received by a Contracting State may be used for other purposes when such information may be used for such other purposes under the laws of both States and the competent authority of the supplying State authorises such use.	Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and it shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes referred to in paragraph 1, or the oversight of the above. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions. Notwithstanding the foregoing, information received by a Contracting State may be used for other purposes when such information may be used for such other purposes under the laws of both States and the competent authority of the supplying State authorizes such use
3	In no case shall the provisions of paragraphs 1 and 2 be construed so as to impose on a Contracting State the obligation: a. To carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State; b. To supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State; c. To supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information, the disclosure of which would be contrary to public policy (ordre public).	
4	If information is requested by a Contracting State in accordance with this Article, the other Contracting State shall use its information gathering measures to obtain the requested information, even though that other State may not need such information for its own tax purposes. The obligation contained in the preceding sentence is subject to the limitations of paragraph 3 but in no case shall such limitations be construed to permit a Contracting State to decline to supply information solely because it has no domestic interest in such information	
5	In no case shall the provisions of paragraph 3 be construed to permit a Contracting State to decline to supply information solely because the information is held by a bank, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person.	
6	--	The competent authorities shall, through consultation, develop appropriate methods and techniques concerning the matters in respect of which exchanges of information under paragraph 1 shall be made

Para	OECD Model Tax Convention	UN Model Convention
	Article 27 "Assistance in the Collection of Taxes"	
1	The Contracting States shall lend assistance to each other in the collection of revenue claims. This assistance is not restricted by Articles 1 and 2. The competent authorities of the Contracting States may by mutual agreement settle the mode of application of this Article.	
2	The term "revenue claim" as used in this Article means an amount owed in respect of taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to this Convention or any other instrument to which the Contracting States are parties, as well as interest, administrative penalties and costs of collection or conservancy related to such amount	
3	When a revenue claim of a Contracting State is enforceable under the laws of that State and is owed by a person who, at that time, cannot, under the laws of that State, prevent its collection, that revenue claim shall, at the request of the competent authority of that State, be accepted for purposes of collection by the competent authority of the other Contracting State. That revenue claim shall be collected by that other State in accordance with the provisions of its laws applicable to the enforcement and collection of its own taxes as if the revenue claim were a revenue claim of that other State.	
4	When a revenue claim of a Contracting State is a claim in respect of which that State may, under its law, take measures of conservancy with a view to ensure its collection, that revenue claim shall, at the request of the competent authority of that State, be accepted for purposes of taking measures of conservancy by the competent authority of the other Contracting State. That other State shall take measures of conservancy in respect of that revenue claim in accordance with the provisions of its laws as if the revenue claim were a revenue claim of that other State even if, at the time when such measures are applied, the revenue claim is not enforceable in the first-mentioned State or is owed by a person who has a right to prevent its collection.	
5	Notwithstanding the provisions of paragraphs 3 and 4, a revenue claim accepted by a Contracting State for purposes of paragraph 3 or 4 shall not, in that State, be subject to the time limits or accorded any priority applicable to a revenue claim under the laws of that State by reason of its nature as such. In addition, a revenue claim accepted by a Contracting State for the purposes of paragraph 3 or 4 shall not, in that State, have any priority applicable to that revenue claim under the laws of the other Contracting State.	
6	Proceedings with respect to the existence, validity or the amount of a revenue claim of a Contracting State shall not be brought before the courts or administrative bodies of the other Contracting State.	
7	Where, at any time after a request has been made by a Contracting State under paragraph 3 or 4 and before the other Contracting State has collected and remitted the relevant revenue claim to the first-mentioned State, the relevant revenue claim ceases to be a. in the case of a request under paragraph 3, a revenue claim of the first-mentioned State that is enforceable under the laws of that State and is owed by a person who, at that time, cannot, under the laws of that State, prevent its collection, or b. in the case of a request under paragraph 4, a revenue claim of the first-mentioned State in respect of which that State may, under its laws, take measures of conservancy with a view to ensure its collection the competent authority of the first-mentioned State shall promptly notify the competent authority of the other State of that fact and, at the option of the other State, the first-mentioned State shall either suspend or withdraw its request.	

Para	OECD Model Tax Convention	UN Model Convention
8	In no case shall the provisions of this Article be construed so as to impose on a Contracting State the obligation: a. to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State; b. to carry out measures which would be contrary to public policy (ordre public); c. to provide assistance if the other Contracting State has not pursued all reasonable measures of collection or conservancy, as the case may be, available under its laws or administrative practice; d. to provide assistance in those cases where the administrative burden for that State is clearly disproportionate to the benefit to be derived by the other Contracting State.	
Article 28 "Members of Diplomatic Missions and Consular Posts"		
	Nothing in this Convention shall affect the fiscal privileges of members of diplomatic missions or consular posts under the general rules of international law or under the provisions of special agreements.	
Article 29 "Entitlement to Benefits"		
	Provision that, subject to paragraphs 3 to 5, restricts treaty benefits to a resident of a Contracting State who is a "qualified person" as defined in paragraph 2	Except as otherwise provided in this Article, a resident of a Contracting State shall not be entitled to a benefit that would otherwise be accorded by this Convention (other than a benefit under paragraph 3 of Article 4, paragraph 2 of Article 9 or Article 25) unless such resident is a "qualified person", as defined in paragraph 2, at the time that the benefit would be accorded.
Article 30 "Territorial Extension"		
	1. This Convention may be extended, either in its entirety or with any necessary modifications [to any part of the territory of (State A) or of (State B) which is specifically excluded from the application of the Convention or], to any State or territory for whose international relations (State A)	

Para	OECD Model Tax Convention	UN Model Convention
	or (State B) is responsible, which imposes taxes substantially similar in character to those to which the Convention applies. Any such extension shall take effect from such date and subject to such modifications and conditions, including conditions as to termination, as may be specified and agreed between the Contracting States in notes to be exchanged through diplomatic channels or in any other manner in accordance with their constitutional procedures. 2. Unless otherwise agreed by both Contracting States, the termination of the Convention by one of them under Article 32 shall also terminate, in the manner provided for in that Article, the application of the Convention [to any part of the territory of (State A) or of (State B) or] to any State or territory to which it has been extended under this Article.	--
	Article 31 (OECD Model) / Article 30 (UN Model) "Entry into Force"	
	1. This Convention shall be ratified and the instruments of ratification shall be exchanged at _____ as soon as possible. 2. The Convention shall enter into force upon the exchange of instruments of ratification and its provisions shall have effect: (a) (In State A): ..... (b) (In State B):	
	Article 32 (OECD Model) / Article 31 (UN Model) "Termination"	
	This Convention shall remain in force until terminated by a Contracting State. Either Contracting State may terminate the Convention, through diplomatic channels, by giving notice of termination at least six months before the end of any calendar year after the year ..... In such event, the Convention shall cease to have effect: a) (in State A): ..... b) (in State B):	

Solved Case 1:

Mr. Amin, a resident individual in India (age 42) furnishes you the following particulars of income for the previous year 2023–24:

Particulars	₹
Income from business in India (computed)	11,00,000
Dividend received from Company incorporated in Country X (gross)	2,00,000
Royalty income from writing text book for schools in Country Y (gross)	6,00,000
Expenditure incurred for authoring text book	50,000

Particulars	₹
Business loss in Country Y (gross)	2,50,000
Health insurance premium paid for his father (age 67) a resident in India (His father is not dependent on Mr. Amin)	30,000

The business loss in Country Y is eligible for set off against other income as per the Income-tax law of that country.

There is no DTAA between India and Country "X" and Country "Y" given above. The rate of tax in Country "X" and Country "Y" may be taken as 10% and 25% respectively (without any threshold exemption limit).

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be his tax liability, assuming he has opted for old regime) before any relief u/s 90 or 91?
2. What is his average rate of tax?
3. State the eligible amount of relief u/s 90 or 91

Solution:

Computation of Total Income of Mr. Amin for A.Y. 2024–25

Particulars	₹	₹	₹
Profits and gains of Business or profession			
Income from business in India			11,00,000
Loss from business in Country "Y"		2,50,000	
Less: Set off against royalty income		2,50,000	-
Income from other Sources			
Dividend from companies in Country "X"		2,00,000	
Royalty income from Country "Y"	6,00,000		
Less: Expenditure thereon	50,000		
	5,50,000		
Loss from business in Country "Y"	2,50,000	3,00,000	5,00,000
Gross Total Income			16,00,000
Less: Deduction under Chapter VI-A			
Section 80D Health insurance premium for father, senior citizen is deductible even though he is not dependent on the assessee.		30,000	
Section 80QQB: As the assessee has authored text-book for schools in Country "Y hence it is not eligible for deduction.		-	30,000
Total Income			**15,70,000**
Tax on above			2,83,500
Add: Cess			11,340
Tax and cess			2,94,840
Less: Relief u/s 91 [See Working]			76,339
Tax after relief			**2,18,500**

Working:

Average rate of tax in India ₹ 2,94,840 x 100 / ₹ 15,70,000	18.78%	
Average rate of tax in country X	10%	
Doubly taxed income of country X	2,00,000	
Relief u/s 91 would be 10% or average rate @ 18.78%, whichever is lower [10% on ₹ 2 lakhs]		₹ 20,000
Doubly taxed income of country Y (after set-off of business loss)	3,00,000	
Rate of tax country Y	25%	
Relief u/s 91 would be @ 18.78% or 25% whichever is lower [18.78% on ₹ 3 lakhs]		₹ 56,339
Relief under section 91		**₹ 76,339**

Exercise

A. Theoretical Questions

Multiple Choice Questions

1. In respect of DTAA, generally, India follows:
   a. UN Model
   b. UK Model
   c. OECD Model
   d. US Model
2. Sec. 91 deals with
   a. Bilateral Relief
   b. Unilateral Relief
   c. Both (a) and (b)
   d. None of the above

[Answer - 1 - a; 2 - b]

Short Essay Type Questions

1. State the provisions of sec. 91.
2. Write a brief note on Model tax conventions.

B. Numerical Questions

Comprehensive Numerical Problems

Anupam Gulati, a resident in India, is a famous badminton player, who plays in several tournaments. For the year ended 31-03-2024, he has derived income from playing in tournaments outside India and also share income from a firm, from nations with which no DTAA exists.

The summarized results of the income earned during the year are as under:

	₹
Income from tournaments in India	32,50,000
Income from tournaments outside India (as converted into INR)	16,00,000
Share of loss from a partnership firm abroad (Set off permitted in that nation)	2,00,000
Residential house property purchased at Colombo (including registration and stamp duty for ₹ 1,80,000)	4,00,00,000

On the foreign income, he has paid tax of ₹ 3,50,000. Compute relief u/s 90 or 91, assuming that he has opted for old regime?

[Ans: ₹ 3,50,000]

Unsolved Case

Suresh (age 61) an individual resident in India furnishes you particulars of income for the previous year 2023-24. He earned income in country M and India has not entered into double taxation avoidance agreement with that country.

Particulars	₹
Income from house property in country M	2,50,000
Business income in India	8,00,000
Royalty income country M (see note below)	₹ 4,00,000
Business income in country M	₹ 2,00,000
Dividend from country M	₹ 1,00,000
Income from house property in India	₹ 5,00,000
Donation to Prime Minister's National Relief Fund	₹ 50,000
Incurred medical expenses for his mother aged 85	₹ 50,000
Rate of tax in country M (no basic exemption limit)	20%

Note : He disputed royalty income in country M but paid the tax on that income in June, 2023 after the appeal was decided by the appellate authority. The royalty income is charged to tax at concessional rate of 15% in country M.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be his total income, if he has opted for old regime
   a. ₹ 21,50,000
   b. ₹ 20,50,000
   c. ₹ 22,50,000
   d. None of the above
2. Does he eligible for any relief & rebate
   a. Yes, relief u/s 91
   b. Yes, relief u/s 91 and rebate u/s 87A
   c. No
   d. None of the above
3. What will be his tax liability as per old regime?
   a. ₹ 3,03,245
   b. ₹ 4,75,800
   c. ₹ 3,55,800
   d. None of the above

References

https://www.incometaxindia.gov.in/
https://www.incometax.gov.in/
https://www.indiabudget.gov.in/

Transfer Pricing 13

This Module includes:

13.1 Transfer Pricing including Specified Domestic Transactions

13.2 Determination of Arm's Length Price

13.3 Advance Pricing Agreement- Concept and Application

13.4 Safe Harbour Rules, Thin Capitalisation and Secondary Adjustment

Transfer Pricing

SLOB Mapped against the Module:

1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.

Module Learning Objectives:

After studying this module, the students will be able to -

- Appreciate the meaning of various terms like international transaction, specified domestic transactions, etc.
- Appreciate the provision of income tax in respect of international transactions
- Appreciate the method of computing arm's length price
- Apply such method in computing arm's length price
- Understand the provision of advance pricing agreement, thin capitalisation, etc.

Introduction

13

"Globalisation and new electronic technologies can permit a proliferation of tax regimes designed to attract geographically mobile activities. Governments must take measures, in particular intensifying their international cooperation, to avoid the world-wide reduction in welfare caused by tax-induced distortions in capital and financial flows and to protect their tax bases.

International taxation is the study or determination of tax on a person or business subject to the tax laws of different countries or the international aspects of an individual country's tax laws. Governments usually limit the scope of their income taxation in some manner territorially or provide for offsets to taxation relating to extraterritorial income. The manner of limitation generally takes the form of a territorial, residency, or exclusionary system. Some governments have attempted to mitigate the differing limitations of each of these three broad systems by enacting a hybrid system with characteristics of two or more. Systems of taxation vary widely, and there are no broad general rules. These variations create the potential for double taxation (where the same income is taxed by different countries) and no taxation (where income is not taxed by any country). Income tax systems may impose tax on local income only or on worldwide income. Generally, where worldwide income is taxed, reductions of tax or foreign credits are provided for taxes paid to other jurisdictions. Limits are almost universally imposed on such credits. With any system of taxation, it is possible to shift or recharacterize income in a manner that reduces taxation. Jurisdictions often impose rules relating to shifting of income among commonly controlled parties, often referred to as transfer pricing rules. Residency based systems are subject to taxpayer attempts to defer recognition of income through use of related parties. A few jurisdictions impose rules limiting such deferral ("anti-deferral" regimes). Deferral is also specifically authorized by some governments for particular social purposes or other grounds. Agreements among governments (treaties) often attempt to determine who should be entitled to tax what. Most tax treaties provide for at least a skeleton mechanism for resolution of disputes between the parties. Tax laws in India are becoming more and more complex. Globalisation of economies, signing and review of free trade agreements, increase in the number of cross border transactions, mergers, acquisitions, tax treaties, transfer pricing etc. have added to these complexities.

Tax Heaven

Many fiscally sovereign territories and countries use tax and non-tax incentives to attract activities in the financial and other services sectors. These territories and countries offer the foreign investor an environment with a no or only nominal taxation which is usually coupled with a reduction in regulatory or administrative constraints. The activity is usually not subject to information exchange because, for example, of strict bank secrecy provisions. These jurisdictions are known as tax havens. In other words, any country which modifies its tax laws to attract foreign capital could be considered a tax haven. The central feature of a haven is that its laws and other measures can be used to evade or avoid the tax laws or regulations of other jurisdictions. A tax haven is a state or a country or territory where income tax are levied at a low rate or no tax at all is levied. Individuals and/or corporate entities can find it attractive to establish shell subsidiaries or move themselves to areas where reduced or nil tax is charged. This creates a situation of tax competition among governments though tax heaven countries may not always be

profitable. Some tax heavens have become failure like Beirut, Tangiers, Liberia, etc. Different jurisdictions tend to be havens for different types of taxes, and for different categories of people and/or companies.

Geoffrey Colin Powell (former economic adviser to Jersey) has defined it as under:

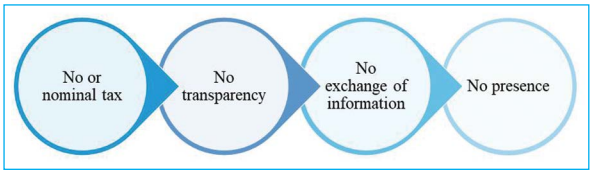
"What ... identifies an area as a tax haven is the existence of a composite tax structure established deliberately to take advantage of, and exploit, a worldwide demand for opportunities to engage in tax avoidance."

Some important destinations of tax heavens are:

In USA	Delaware, Nevada, Wyoming
In Europe	Andorra, Canary, Netherlands, Cyprus
In Asia	Mauritius, Singapore, Dubai
In Africa	Capetown, Nairobi

Key Factors

Four key factors are used to determine whether a jurisdiction is a tax haven:



- **Imposes no or only nominal taxes:** Tax havens impose nil or only nominal taxes (generally or in special circumstances) and offer themselves, or are perceived to offer themselves, as a place to be used by non-residents to escape high taxes in their country of residence.
- **Lack of transparency:** Transparency ensures that there is an open and consistent application of tax laws among similarly situated taxpayers and that information needed by tax authorities to determine a taxpayer's correct tax liability is available (e.g., accounting records and underlying documentation). A lack of transparency in the operation of the legislative, legal or administrative provisions is another factor used to identify tax havens. The OECD is concerned that laws should be applied openly and consistently, and that information needed by foreign tax authorities to determine a taxpayer's situation is available. Lack of transparency in one country can make it difficult, if not impossible, for other tax authorities to apply their laws effectively. 'Secret rulings', negotiated tax rates, or other practices that fail to apply the law openly and consistently are examples of a lack of transparency. Limited regulatory supervision or a government's lack of legal access to financial records are contributing factors.
- **Lack of effective exchange of tax information with foreign tax authorities:** Whether there are laws or administrative practices that prevent the effective exchange of information for tax purposes with other governments on taxpayers benefiting from the no or nominal taxation. Tax havens typically have laws or administrative practices under which businesses and individuals can benefit from strict rules and other protections against scrutiny by foreign tax authorities. This prevents the transmittance of information about taxpayers who are benefiting from the low tax jurisdiction.
- **No requirement for a substantive local presence of the entity:** The absence of a requirement that the activity be substantial is important because it suggests that a jurisdiction may be attempting to attract investment and transactions that are purely tax driven. It may also indicate that a country does not provide a legal or commercial environment or offer any economic advantages that would attract substantive business activities in the absence of the tax minimising opportunities it provides. The no substantial activities criterion was included in the 1998 Report as a criterion for identifying tax havens because the lack of such activities suggests that a

jurisdiction may be attempting to attract investment and transactions that are purely tax driven. In 2001, the OECD's Committee on Fiscal Affairs agreed that this criterion would not be used to determine whether a tax haven was co-operative or unco-operative.

With regard to exchange of information in tax matters, the OECD encourages countries to adopt information exchange on an "upon request" basis. Exchange of information upon request describes a situation where a competent authority of one country asks the competent authority of another country for specific information in connection with a specific tax inquiry, generally under the authority of a bilateral exchange arrangement between the two countries. An essential element of exchange of information is the implementation of appropriate safeguards to ensure adequate protection of taxpayers' rights and the confidentiality of their tax affairs.

Methodology

The methods followed in doing business through tax heavens, broadly, are as under:

Personal residency

Wealthy individuals from high-tax jurisdictions have sought to relocate themselves in low-tax jurisdictions. In most countries in the world, residence is the primary basis of taxation. In some cases the low-tax jurisdictions levy no, or only very low, income tax, capital gain tax and inheritance tax. Individuals who are unable to return to a higher-tax country in which they used to reside for more than a few days a year are sometimes referred to as tax exiles.

Asset holding

Asset holding involves utilizing a trust or a company, or a trust owning a company. The company or trust will be formed in one tax haven, and will usually be administered and resident in another. The function is to hold assets, which may consist of a portfolio of investments under management, trading companies or groups, physical assets such as real estate or valuable chattels. The essence of such arrangements is that by changing the ownership of the assets into an entity which is not resident in the high-tax jurisdiction, they cease to be taxable in that jurisdiction. Often the mechanism is employed to avoid inheritance tax.

Trading and other business activity

Many businesses which do not require a specific geographical location or extensive labour are set up in tax havens, to minimize tax exposure. Perhaps the best illustration of this is the number of reinsurance companies which have migrated to Bermuda over the years. Other examples include internet based services and group finance companies. In the 1970s and 1980s corporate groups were known to form offshore entities for the purposes of "reinvoicing". These reinvoicing companies simply made a margin without performing any economic function, but as the margin arose in a tax free jurisdiction, it allowed the group to "skim" profits from the high-tax jurisdiction. Most sophisticated tax codes now prevent transfer pricing schemes of this nature.

Financial intermediaries

Much of the economic activity in tax havens today consists of professional financial services such as mutual funds, banking, life insurance and pensions. Generally, the funds are deposited with the intermediary in the low-tax jurisdiction, and the intermediary then on-lends or invests the money (often back into a high-tax jurisdiction). Although such systems do not normally avoid tax in the principal customer's jurisdiction, it enables financial service providers to provide multi-jurisdictional products without adding an additional layer of taxation. This has proved particularly successful in the area of offshore funds.

Counteracting harmful tax practices

OECD has issued a report on Harmful Tax Competition and has made 19 specific recommendations, some of them are as follows:

a. Adopt Controlled Foreign Corporations (CFC) or equivalent rules

b. Consider foreign information reporting rules

c. Enter into Tax Information Exchange Agreement (TIEA)

d. Application of provision of withholding tax[1] while making payment to offshore recipients

e. Curbing 'treaty shopping nations' of existing treaties with tax heaven

f. Mutual assistance of tax authorities in the recovery of cross boarder tax claims

g. More international co-operation by establishing Forum to avoid Harmful Tax Practices

h. Other measures

- Adopt foreign investment fund or equivalent rules
- Considering restrictions on participation exemption and other systems of exempting foreign income in the context of harmful tax competition
- Formulation and adoption of transfer pricing rules
- Providing access to banking information for tax purposes
- Considering co-ordinated enforcement regimes (joint audits; co-ordinated training programmes, etc.)
- Guidelines to develop and actively promote Principles of Good Tax Administration

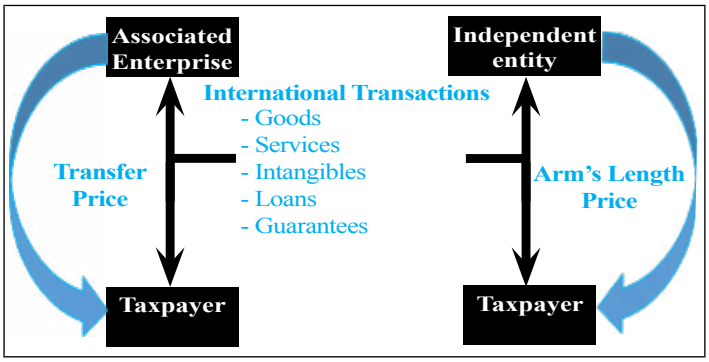
[1] Tax deducted at source

Transfer Pricing including Specified Domestic Transactions

13.1

The increasing participation of multinational groups in economic activities in the country has given rise to new and complex issues emerging from transactions entered into between two or more enterprises belonging to the same multinational group. The profits derived by such enterprises carrying on business in India can be controlled by the multinational group, by manipulating the prices charged and paid in such intra-group transactions, thereby, leading to erosion of tax revenues. In other words, the course of business between a resident person and an associated non-resident or not ordinarily resident person, is so arranged that the resident makes either no profit or less than the ordinary profit in that business. Such an arrangement would deprive that Indian revenue of the tax which would otherwise be payable by the resident.

With a view to provide a statutory framework which can lead to computation of reasonable, fair and equitable profits and tax in India, in case of such multinational enterprise, new set of special provisions relating to avoidance of tax have been introduced under chapter X in the Income tax Act. These provisions relate to computation of income from international transaction having regard to arm's length price, meaning of associated enterprises, meaning of international transaction, determination of arm's length price, keeping and maintaining of information and documents by persons entering into international transaction, furnishing of a report from an accountant by persons entering into such transactions.



Computation of income from international transaction or specified domestic transaction having regard to arm's length price [Sec. 92]

The provisions are as under:

Provisions	Example	Treatment	Impact on income
Any income arising from an international transaction shall be computed having regard to the arm's length price.	X Ltd., resident, sold goods or services to its associated enterprises, XY Plc. (a foreign company), for □ 5 lacs whereas the arm's length price of such goods or services is □ 9 lacs	While computing income of X Ltd., □ 9 lacs shall be considered as sale value	Income of X Ltd. will be increased by □ 4 lacs.

Provisions	Example	Treatment	Impact on income
The allowance for any expense or interest arising from an international transaction or specified domestic transaction[2] shall also be determined having regard to the arm's length price.	R Ltd. takes a loan of ₹20 lacs from an associated enterprise in Ireland @ 20% p.a. whereas the arm's length rate of interest is 12% p.a.	Interest @ 12% p.a. shall be allowed as deduction to R Ltd.	Income of R Ltd. will be increased by □ 1,60,000/-
Where in an international transaction or specified domestic transaction, • two or more associated enterprises • enter into a mutual agreement or arrangement for the apportionment of, or any contribution to, any cost incurred • in connection with a benefit, service or facility provided to any such enterprises, the cost apportioned to (contributed by), any such enterprise shall be determined having regard to the arm's length price of such benefit, service or facility.	An enterprise in Germany makes research on a new product and incurred □ 50 lacs. Out of this, □ 40 lacs has been allocated to its Indian associated enterprises dealing in the same product.	While computing income of Indian enterprise, it will be required to be examined whether the Indian enterprise is deriving proportionate benefit to the research expenditure allocated	If no such benefit is available to the Indian enterprise, total income of such enterprises is suitably increased by disallowing proportionate allocated cost.
The provisions (in any of aforesaid situation) shall not apply in a case where the computation of income or the determination of the allowance for any expense or interest or the determination of any cost or expense allocated or contributed has the effect of reducing the income chargeable to tax or increasing the loss, as the case may be, computed on the basis of entries made in the books of account in respect of the previous year in which the international transaction or specified domestic transaction was entered into.	X Ltd., resident, sold goods or services to its associated enterprises, XY Plc. (a foreign company), for □ 5 lacs whereas the arm's length price of such goods or services is □ 3 lacs	The provision of transfer pricing is not applicable	No Impact

Arm's length price [Sec. 92F(ii)]

Arm's length price means

(i) a price which is applied or proposed to be applied in a transaction

(ii) between persons other than associated enterprises (i.e., unrelated person, resident or non-resident),

(iii) in uncontrolled conditions.

Taxpoint: There may be more than one arm's length price.

2 Any allowance for an expenditure or interest or allocation of any cost or expense or any income in relation to the specified domestic transaction shall be computed having regard to the arm's length price.

Process

The process to arrive at the appropriate arm's length price typically involves the following processes or steps:

(a) Comparability analysis

The concept of establishing comparability is central to the application of the arm's length principle. An analysis under the arm's length principle involves information on associated enterprises involved in the controlled transactions, the transactions at issue between the associated enterprises, the functions performed and the information derived from independent enterprises engaged in comparable transactions (i.e., uncontrolled transactions). The objective of comparability analysis is always to seek the highest practicable degree of comparability, recognising that there will be unique transactions and cases where any applied method cannot be relied on. It is clear that the closest approximation of the arm's length price will be dependent on the availability and reliability of comparables. There are many factors determining the comparability of transactions for transfer pricing analysis:

(i) Characteristics of the property or services

Property, tangible or intangible, as well as services, may have different characteristics which may lead to a difference in their values in the open market. Therefore, these differences must be accounted for and considered in any comparability analysis of controlled and uncontrolled transactions. Characteristics that may be important to consider are:

- In case of tangible property, the physical features, quality, reliability and availability of volume and supply;
- In the case of services, the nature and extent of such services; and
- In case of intangible property, the type and form of property, duration and degree of protection and anticipated benefits from use of property.

(ii) Functional analysis (Functions, Assets and Risks)

- In dealings between two independent enterprises, the compensation usually reflects the functions that each enterprise performs, taking into account assets used and risks assumed. Therefore, in determining whether controlled and uncontrolled transactions are comparable, a proper study of all specific characteristics of an international transaction or functional activity needs to be undertaken, including comparison of the functions performed, assets used and risks assumed by the parties. Such a comparison is based on a "functional analysis".
- A functional analysis seeks to identify and compare the economically significant activities and responsibilities undertaken by the independent and associated enterprises. An economically significant activity is considered to be any activity which materially affects the price charged in a transaction and the profits earned from that transaction.
- Functional analysis is thus a key element in a transfer pricing exercise. It is a starting point and lays down the foundation of the arm's length analysis. The purpose of functional analysis is to describe and analyse the operations of an enterprise and its associated enterprises.
- Functional analysis typically involves identification of '**f**unctions performed', '**a**ssets employed' and '**r**isks assumed' (therefore named a "FAR analysis") with respect to the international transactions of an enterprise. Functions that may need to be accounted for in determining the comparability of two transactions can include:
  - Research and development

- Product design and engineering;
- Manufacturing, production and process engineering;
- Product fabrication, extraction and assembly;
- Marketing and distribution functions, including inventory management and advertising activities;
- Transportation and warehousing; and
- Managerial, legal, accounting and finance, credit and collection, training and personnel management services.
- Outsourcing nature of work
- Business process management

- Risks that need to be considered while determining the degree of comparability between controlled and uncontrolled transactions include:
  - Financial risks including method of funding, funding of losses, foreign exchange risk
  - Product risk including design & development of product, after sales service, product liability risk, intellectual property risk, risks associated with R&D, obsolescence / upgrading of product
  - Market risks including fluctuations in prices and demand, business cycle risks, development of market including advertisement and product promotion
  - Credit and collection risks;
  - Entrepreneurial risk including risk of loss associated with capital investment
  - General business risks related to ownership of plant, property and equipment.
- Furthermore, it is not only necessary to identify the risks but to identify who *bears* such risks. The allocation of risk is usually based on contractual terms between the parties; however these may not always reflect the reality of a transaction or a relationship, and an allocation of risk between controlled taxpayers after the outcome of such risk is known or reasonably knowable lacks economic substance.
- Consider an example where company S, situated in country A, is the wholly owned subsidiary of company P, situated in country B but a foreign manufacturer. The subsidiary company S acts as the distributor of goods manufactured by the parent company P and both parties execute an agreement that any product liability costs will be borne by the parent company P. However, in practice when product liability claims are raised, subsidiary company S always pays the resulting damages. In such a case the tax authorities will generally disregard the contractual arrangement and treat the risk as having been in reality assumed by subsidiary company S.

(iii) Contractual Terms

- The conduct of the contracting parties is a result of the terms of the contract between them and the contractual relationship thus warrants careful analysis when arriving at the transfer price. Other than a written contract, the terms of the transactions may be figured out from correspondence and communication between the parties involved. In case the terms of the arrangement between the two parties are not explicitly defined, then the terms have to be deduced from their economic relationship and conduct.
- One important point to note in this regard is that associated enterprises may not hold each other to the terms of the contract as they have common overarching interests, unlike independent enterprises,

who are expected to hold each other to the terms of the contract. Thus, it is important to figure out whether the contractual terms between the associated enterprises are a "sham" (something that appears genuine, but when looked closer lacks reality, and is not valid under many legal systems) and/or have not been followed in reality.

- Also, explicit contractual terms of a transaction involving members of a MNE may provide evidence as to the form in which the responsibilities, risks and benefits have been assigned among those members. For example, the contractual terms might include the form of consideration charged or paid, sales and purchase volumes, the warranties provided, the rights to revisions and modifications, delivery terms, credit and payment terms etc. This material may also indicate the substance of a transaction, but will usually not be determinative on that point.
- It must be noted that contractual differences can influence *prices* as well as *margins* of transactions. The party concerned should document contractual differences and evaluate them in the context of the transfer pricing methods discussed in detail in a later chapter of this Manual, in order to judge whether comparability criteria are met and whether any adjustments need to be made to account for such differences.

(iv) Market Conditions

Market prices for the transfer of the same or similar property may vary across different markets owing to cost differentials prevalent in the respective markets**.** Markets can be different for numerous reasons; it is not possible to itemise exhaustively all the market conditions which may influence transfer pricing analysis but some of the key market conditions which influence such an analysis are as follows:

Geographical location – In general, uncontrolled comparables ordinarily should be derived from the geographic market in which the controlled taxpayer operates, because there may be significant relevant differences in economic conditions between different markets. If information from the same market is not available, an uncontrolled comparable derived from a different geographical market may be considered if it can be determined that (i) there are no differences between the market relevant to the transaction or (ii) adjustments can be made to account for the relevant differences between the two markets.

Another aspect of having different geographic markets is the concept of "*location savings*" which may come into play during transfer pricing analysis. Location savings are the cost savings that a MNE realises as a result of relocation of operations from a high cost jurisdiction to a low cost jurisdiction. Typically, cost savings include costs of labour, raw materials and tax advantages offered by the new location. However, there might be disadvantages in relocating also; the "dis-savings" on account of relocation might be high costs for transportation, quality control, etc. The savings attributable to location into a low-cost jurisdiction (offset by any "dis-savings") are referred to collectively as the "location savings". The important point, where there are such location savings, is not just the amount of the savings, but also the issues of to whom these savings belong (i.e. the captive service provider or the principal). In this respect, the allocation of location savings depends especially on the relative bargaining positions of the parties. Relative bargaining power of buyer, seller and end user is dependent on issues such as the beneficial ownership of intangible property and the relative competitive position.

The computation of location savings might seem simple in theory; however its actual computation may pose many difficulties. Moving to an offshore location might be accompanied by changes in technologies, productions volumes or production processes. In such a circumstance, the additional profit derived cannot be treated as only due to location savings as the profitability is due both to low costs and introduction of new technology. A simple comparison before and after in such a scenario would give a distorted picture of location savings.

If the tax authorities were to administer transfer pricing principles to "shift" profits without any consideration of market forces prevalent in the respective countries, then such reconfiguration of economic profile, and consequently the financial statements in the host country, would be against the principles of transfer pricing and may result in unrelieved double taxation if the tax authority in another country does not agree to reduce the profits of an associated enterprise in its country.

Government rules and regulations – Generally, government interventions in the form of price controls, interest rate controls, exchange controls, subsidies for certain sectors, anti□ dumping duties etc, should be treated as conditions of the market in the particular country and in the ordinary course they should be taken into account in arriving at an appropriate transfer price in that market. The question becomes whether, in light of these conditions, the transactions by controlled parties are consistent with "uncontrolled" transactions between independent enterprises.

An example of where government rules affect the market are the Export Oriented Units (EOU's) which may be subject to beneficial provisions under the taxation laws of the country; ideally companies which enjoy similar privileges should be used as the comparables, and if that is not possible, adjustments may need to be made as part of the comparability analysis.

Level of Market – For example, the price at the wholesale level (sale to other sellers) and retail levels (sale to consumers) would generally differ, and there may be many levels of wholesalers before a product reaches the consumer.

Other market conditions – Some other market conditions which influence the transfer price include costs of production (including costs of land, labour and capital), availability of substitutes (both goods and services), level of demand/supply, transport costs, size of the market, the extent of competition.

(v) Business Strategies

- Business strategies relating to new product launches, innovations, market penetration or expansion of market share may require selling products cheaper as part of such a strategy and thus earning lower profit in the anticipation of increased profits in the coming years, once the product has become more established in the market. Such strategies must be taken into account when determining the comparability of controlled and uncontrolled transactions. E.g., "start-up" companies are prone to incurring losses during their early life and it would not generally be appropriate to include such start-ups when the tested party (i.e. the party in the controlled transaction to whom the transfer pricing method is applied) is a company with a track record over many years.
- The evaluation of the claim that a business strategy was being followed which decreased profits in the short-term but provided for higher long-term profits is one that has to be considered by the tax authorities carefully after weighing several factors. One factor being - who bears the cost of the market penetration strategy? Another factor to consider is whether the nature of relationship reflects the taxpayer bearing the cost of the business strategy –for example, a sales agent with little responsibility or risk typically cannot be said to bear costs for a market penetration strategy. Another factor is whether the business strategy itself is prima- facie plausible or needs further investigation; an endless "market penetration strategy" that has yielded no profits in many years might under examination have no such real basis in practice.

(b) Transaction analysis

The arm's length price must be established with regard to transactions actually undertaken; the tax authorities should not substitute other transactions in the place of those that have actually happened and should not disregard those transactions actually undertaken unless there are special circumstances - such as that the real

economic substance of the transaction differs from its form or the transaction arrangements are not structured in the commercially rational manner that would be expected between independent enterprises. In general, restructuring of transactions should not be undertaken lightly as it may lead to double taxation due to divergent views by the nation states on how the transactions are structured. Whether authorities are able to do so will ultimately depend on their ability to do so under applicable local law, and even where it is possible, a good understanding of business conditions and realities is necessary for a fair "reconstruction". These issues are relevant not only to the administration of transfer pricing, but also to developing the underlying legislation at the beginning of a country's transfer pricing "journey" to allow effective administration (and to assist, and reduce the costs of, compliance by taxpayers) during the course of that journey.

(c) Evaluation of separate and combined transactions

- An important aspect of transfer pricing analysis is whether this analysis is required to be carried out with respect to individual international transactions or a group of international transactions having close economic nexus. In most cases, it has been observed that application of the arm's length principle on a transaction-by-transaction basis becomes cumbersome for all involved, and thus recourse is often had to the "aggregation" principle.
- For example with transactions dealing with intangible property such as the licensing of "know-how" (practical technical knowledge of how to do something, such as of an industrial process, that is not widely-held) to associate enterprises it may prove difficult to separate out the transactions involved. Similarly long-term service supply contracts and pricing of closely linked products are difficult to separate out transaction-wise.
- Another important aspect of combined transactions is the increasing presence of composite contracts and "package deals" in an MNE group; a composite contract and/or package deal may contain a number of elements including royalties, leases, sale and licenses all packaged into one deal. The tax authorities would generally consider the deal in its totality and arrive at the appropriate transfer price; in such a case comparables need to be similar (deals between independent enterprises). In certain cases, the tax authorities might find it appropriate for various reasons to allocate the price to the elements of the package or composite contract. It must be noted that any application of the arm's length principle, whether on a transaction by transaction basis or on aggregation basis, needs to be evaluated on a case to case basis, applying the relevant methodologies to the facts as they exist in that particular case.

(d) Use of an arm's length range

- The arm's length principle as applied in practice usually results in an arm's length range (that is, a range of acceptable/comparable prices) rather than a single transfer price for a controlled transaction. The range of transfer prices exists because the transfer pricing methods attempt to reflect prices and conditions between independent parties. However at times it is difficult to make highly precise adjustments due to differences between controlled transactions and uncontrolled transactions. If only one transfer pricing method is applied, the method may indicate a single acceptable price range. If more than one transfer pricing method is being used, each method may indicate different ranges. If the range of prices that are common to the methods is used, the range is more likely to be reliable in fairly reflecting business conditions.
- If the transfer prices used by a taxpayer are within the arm's length range, adjustments should not be required. If the transfer prices used by a taxpayer are outside the range of prices determined by a tax authority, the taxpayer should be given an opportunity to explain the differences.
- If a taxpayer is able to explain the difference and provides its own transfer pricing documentation used in setting its transfer prices which supports this, a tax authority will usually decide not to make adjustment. On the other hand, if the taxpayer is unable to justify its transfer prices an adjustment may be required.

(e) Use of multiple year data

- When economic and financial data is being tested, previous years' data may truly represent the results achieved by both the controlled and uncontrolled taxpayers. The use of multiple year data allows the data to be better harmonised, as it tends to average the results over a period of time. Multiple year data can also uncover relevant abnormal economic factors affecting the results, such as strikes or other adverse conditions. Such an approach also tries to test the data thrown up in typical business cycles and thus eliminates the risk of testing data of only a particularly bad or good year.
- Furthermore, in certain industries which are more cyclical in nature the multiple year data may give a better standard of comparison than use of single year data; the automotive industry can be one example of such a cyclical industry. That is not to say, however, that use of multiple year data prevents authorities from challenging artificial attempts to take advantage of such an approach by, for example, wrongly pricing in the last year of the data in the hope that such pricing will be "absorbed" into the wider data set. Some countries consider that they are legally required to consider data on a year-by year basis; that will be a matter for domestic law, but if the choice exists when setting up a transfer pricing regime, it would generally be preferable to have a multi-year approach to deal with legitimate variations in business conditions across years.
- While using multi-year data for comparability analysis, it is in any case necessary to adjust for factors such as the occurrence of significant events in the preceding years and the role of inflation in changing prices of commodities and services.
- Overall, multiple year data provides information about the relevant business and product life cycles of the comparables; differences in business or product life cycles may have an effect on the conditions which determine comparability. Data from previous years can show whether an independent enterprise engaged in comparable transactions was affected by similar economic conditions so as to be used as a comparable or not.

(f) Losses

- In an MNE group, one of the enterprises might be suffering a loss, even a recurring one, but the overall group may be extremely profitable. The fact that there is an enterprise making losses that is doing business with profitable members of its MNE group may warrant scrutiny by the tax authorities concerned. Such a situation perhaps indicates that the loss-making enterprise is not receiving adequate compensation from the MNE group of which it is a part in relation to the benefits derived from its activities.
- However there are many facets of these losses that have to be studied such as the nature of the loss (spread across group, history of loss-making within entity and group etc), the reasons for the loss (economic downtime, business cycle, start-up business, poor management, excessive risk etc), and the period of loss (short-term, long-term) as all these factors play a significant role in determining how the loss should be treated with respect to transfer pricing.

(g) Intentional set-offs

- A deliberate or intentional set-off occurs when an associated enterprise has provided a benefit to another associated enterprise within the MNE group and is compensated in return by that other enterprise with some other benefits. These enterprises may claim that the benefit that each has received should be set-off against the benefit each provided and only the net gain or loss if any on the transactions needs to be considered for tax assessment.

- Set-offs can be quite complex; they might involve a series of transactions and not just a simple "one transaction, two party" set-off. Ideally the parties disclose all set-offs accurately and have enough documentation to substantiate their set-off claims so that after taking account of set-offs, the conditions governing the transactions are consistent with the arm's length principle.
- The tax authorities may evaluate the transactions separately to determine which of the transactions satisfy the arm's length principle. However, the tax authorities may also choose to evaluate the set-off transactions together, in which case comparables have to be carefully selected; set-offs in international transactions and in domestic transactions may not be easily comparable, such as due to the differences in the tax treatment of the set-offs under the taxation systems of different countries.

(h) Use of custom valuations

- The General Agreement on Trades and Tariff (GATT, Article VII), now part of the World Trade Organization (WTO) set of agreements, has laid down the general principles for an international system of custom valuation. Customs valuation is the procedure applied to determine the customs value of imported goods. Member countries of WTO typically harmonise their internal legislation dealing with the customs valuation with the WTO Agreement on Customs Valuation.
- In appropriate circumstances, the documented custom valuation may be used for justifying the transfer prices of imported goods in international transactions between associated enterprises. The arm's length principle is applied by many customs administrations as a principle of comparison between the value attributable to goods imported by associated enterprises and the value of similar goods imported by independent enterprises. However when there is no customs duty imposed and goods are valued only for statistical purposes, and for items which have no rate of duty, this approach would not be useful. Even when utilising the custom valuation for imports in a transfer pricing context, certain additional upward or downward adjustments may be required to derive the arm's length price for the purpose of taxation.
- Internationally, there is a great deal of focus on the interplay of transfer pricing methods on the one hand and custom valuation methods on the other hand. Debates have centred on the feasibility and desirability of the convergence of the systems surrounding the two sets of value determination. The issue is considered in more detail in a later chapter.

(i) Use of transfer pricing methods

- It is important to note at the outset that there is no one transfer pricing method which is generally applicable to every possible situation. The bottom line is that comparables play a critical role in arriving at arm's length prices; it is also abundantly clear that computing an arm's length price using transfer pricing analysis is a complex task; it requires a lot of effort and goodwill from both the taxpayer and the tax authorities in terms of documentation, groundwork, analysis and research.

Enterprise [Sec. 92F(iii)]

Enterprise means a person (including a permanent establishment[1] of such person) who is, or has been, or is proposed to be, engaged:

- in any activity, relating to the production, storage, supply, distribution, acquisition or control of:
  - (a) articles or goods; or
  - (b) know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature; or

(c) any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights; or

- in the provision of services of any kind; or
- in carrying out any work in pursuance of a contract; or
- in investment, or providing loan; or
- in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate,

whether such activity or business is carried on, directly or through one or more of its units or divisions or subsidiaries; or

whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or places.

[1.] Permanent establishment includes a fixed place of business through which the business of the enterprise is wholly or partly carried on [Sec. 92F(iiia)]

Meaning of international transaction [Sec. 92B]

- International transaction means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of

  (i) purchase, sale or lease of tangible or intangible property, or

  (ii) provision of services, or

  (iii) lending or borrowing money, or

  (iv) any other transaction having a bearing on the profits, income, losses or assets of such enterprises; &

  shall include a mutual agreement or arrangement between two or more associated enterprises

  a. for the allocation or apportionment of, or

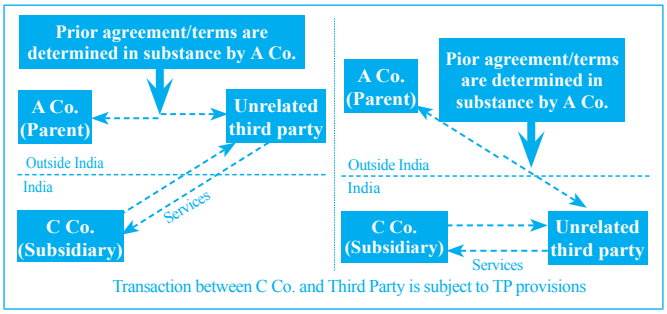
  b. any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises [Sec. 92B(1)]

- A transaction entered into by an enterprise with a person other than an associated enterprise shall, be deemed to be an international transaction entered into between two associated enterprises,

  (i) if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise; or

  (ii) the terms of the relevant transaction are determined in substance between such other person and the associated enterprise

  where the enterprise or the associated enterprise or both of them are non-residents irrespective of whether such other person is a non-resident or not [Sec. 92B(2)]



E.g. C Co., an Indian company, and A Co., a foreign company, are associated enterprise. Z Plc., a foreign company, (not an associated enterprise of C Co.) and A Co. enters into an agreement for determining the terms of transactions between C Co. and Z Plc. The transaction as may be entered between C Co. and Z Plc., which is governed by such an agreement existing between A Co. and Z Plc. shall be deemed to be a transaction between two associated enterprises.

Taxpoint

- Non-resident means a person who is not a 'resident' including a person who is not ordinarily resident [Sec. 2(30)]
- Transaction includes an arrangement, understanding or action in concert,—

  (A) whether or not such arrangement, understanding or action is formal or in writing; or

  (B) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceeding. [Sec. 92F(v)]
- For a transaction to be an international transaction, it should satisfy the following two conditions cumulatively:

  a) It must be a transaction between two associated enterprises; and

  b) At least one of the two enterprises must be a non-resident.

Deemed International Transaction

International transaction shall include:

a. the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

b. the purchase, sale, transfer, lease or use of intangible property[3], including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer

3 Intangible property shall include:

a. marketing related intangible assets, such as, trademarks, trade names, brand names, logos;

b. technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;

c. artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;

d. data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;

e. engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schema-tics, blueprints, proprietary documentation;

f. customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

g. contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;

h. human capital related intangible assets, such as, trained and organised work force, employment agreements, union contracts;

i. location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

j. goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;

k. methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;

l. any other similar item that derives its value from its intellectual content rather than its physical attributes.

list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

c. capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

d. provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

e. a transaction of business restructuring or reorganisation, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

Meaning of Specified Domestic Transactions [Sec. 92BA]

"Specified Domestic Transaction" in case of an assessee means any of the following transactions, not being an international transaction, namely:

i. any transaction referred to in sec. 80A;

ii. any transfer of goods or services referred to in sec. 80-IA(8);

iii. any business transacted between the assessee and other person as referred to in sec. 80-IA(10);

iv. any transaction, referred to in any other section under Chapter VI-A or sec. 10AA, to which provisions of sec. 80-IA(8) or (10) are applicable; or

v. any business transacted between the persons referred to in sec. 115BAB(4);

vi. any business transacted between the assessee and other person[4] as referred to in sec. 115BAE(4);

vii. any other transaction as may be prescribed,

and where the aggregate of such transactions entered into by the assessee in the previous year exceeds a sum of □ 20 crore.

Example 1:

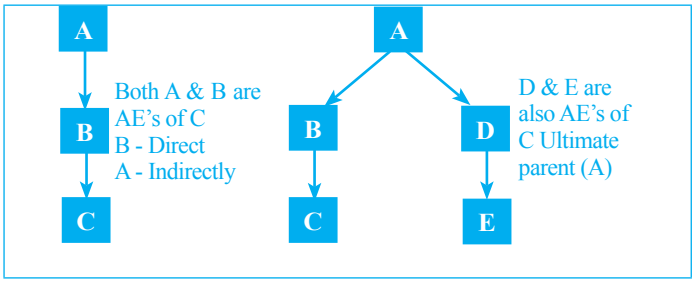
Sultan Ltd. took services of one of its group company, an associated enterprise enjoying tax holiday. The transaction is a specified domestic transaction. Sultan Ltd. paid □ 28,40,00,000 for the said service to the group company. The arms length price of such service is □ 17,00,00,000. The arms length price, i.e., the fair value of the service is □ 17,00,00,000 but by paying higher charges, Sultan Ltd. claimed a higher deduction and reduced its profit by □ 11,40,00,000. In this case the provisions of sec. 92 will be applicable and the income of Sultan Ltd. will be recomputed by taking into account the arms length price of the specified domestic transaction.

In other words, the taxable income of Sultan Ltd. will have to be computed by allowing deduction of only □ 17,00,00,000 on account of service charges instead of the actually paid amount of □ 28,40,00,000.

If in the above example, the transaction is not a specified domestic transaction, then the provisions of sec. 92 will not apply.

4 certain new manufacturing co-operative societies

Meaning of associated enterprise [Sec. 92A]



Associated enterprise, in relation to another enterprise, means an enterprise:

(a) which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or

(b) in respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Deemed associated enterprise [Sec. 92A(2)]

For the above purpose, two enterprises shall be deemed to be associated enterprises if, at any time during the previous year fulfill any of the following conditions (if one of following conditions are not satisfied, then mere participation in management or control or capital of the other enterprise, etc. shall not make them associate):

(a) one enterprise holds (directly or indirectly) shares carrying not less than 26% of the voting power (i.e., equity shares in case of company) in the other enterprise; or

(b) any person or enterprise holds (directly or indirectly) shares carrying not less than 26% of the voting power in each of such enterprises; or

(c) the manufacture or processing of goods or articles or business carried out by one enterprise is wholly (not partially) dependent on the use of know-how, patents, copyrights, trade-marks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights; or

(d) 90% or more of the raw materials and consumables required for the manufacture or processing of goods or articles carried out by one enterprise, are supplied by the other enterprise or by persons specified by the other enterprise, and the prices and other conditions relating to the supply are influenced by such other enterprise; or

(e) the goods or articles manufactured or processed by one enterprise, are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by such other enterprise; or

(f) where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual; or

(g) where one enterprise is controlled by a Hindu undivided family, the other enterprise is controlled by a member of such Hindu undivided family, or by a relative of a member of such Hindu undivided family, or jointly by such member and his relative; or

(h) where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds not less than 10% interest in such firm, association of persons or body of individuals; or

(i) a loan advanced by one enterprise to the other enterprise constitutes not less than 51% of the book value of the total assets of the other enterprise; or

Taxpoint: Revaluation of asset shall not be ignored.

(j) one enterprise guarantees not less than 10% of the total borrowings of the other enterprise; or

(k) more than ½ of the board of directors or members of the governing board, **or** one (not ½ of total number of executive director) or more executive directors or executive members of the governing board of one enterprise, are **appointed** by the other enterprise; or

Taxpoint: Mere power to appoint director is not sufficient, such power must be exercised.

(l) more than ½ of the directors or members of the governing board, or one or more of the executive directors or members of the governing board, of each of the two enterprises are **appointed** by the same person or persons; or

(m) there exists between the two enterprises, any relationship of mutual interest, as may be prescribed.

HOLDING	MANAGEMENT	ACTIVITIES	CONTROL
• >= 26% **Direct / Indirect holding** by enterprise (or) • By **SAME PERSON** in each enterprise • **LOAN** >= 51% of total assets • **GUARANTEES** >= 10% of debt • > 10% **INTEREST** in Firm/AOP/BOI	• Appointment > 50% of **DIRECTORS**/ one or more Executive Director by an enterprise (or) • Appointment by same person in each enterprise	• 100% **DEPENDENCE** on use of Intangibles for manufacture/ processing/business • Direct/Indirect Supply of >= 90% **RAW MATERIALS** under influenced prices and conditions • Sale under **INFLUENCED** prices and conditions	• One enterprise controlled **BY AN INDIVIDUAL** and the other by himself or his relative or jointly • One enterprise controlled **BY HUF** and the other by - a member of HUF his relative or Jointly by member and relative

Determination of Arm's Length Price

13.2

Computation of arm's length price [Sec. 92C]

- The arm's length price in relation to an international transaction or specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely:

  Transaction Based Methods

  a. comparable uncontrolled price method;

  b. resale price method;

  c. cost plus method;

  Profit Based Methods

  d. profit split method;

  e. transactional net margin method;

  f. such other method as may be prescribed by the Board.

  See Rule 10B & Rule 10AB as given in Annexure 1.

- The most appropriate method shall be applied, for determination of arm's length price, in the manner as may be prescribed.

  More than one arm's length price: Where more than one price is determined by the most appropriate method, the arm's length price shall be computed in such manner as may be prescribed.

- **Computation by the Assessing Officer:** As per sec. 92C(3), where during the course of any proceeding for the assessment of income, the Assessing Officer is, on the basis of material or information or document in his possession, of the opinion that:

  (a) the price charged or paid in an international transaction or specified domestic transaction has not been determined in accordance with above provision; or

  (b) any information and document relating to an international transaction or specified domestic transaction have not been kept and maintained by the assessee in accordance with the provisions contained in sec. 92D(1) and the rules made in this behalf; or

  (c) the information or data used in computation of the arm's length price is not reliable or correct; or

  (d) the assessee has failed to furnish, within the specified time, any information or document which he was required to furnish by a notice issued u/s 92D(3),

the Assessing Officer may proceed to determine the arm's length price (in accordance with above provisions) in relation to the said international transaction or specified domestic transaction, on the basis of such material or information or document available with him.

However, an opportunity shall be given by the Assessing Officer by serving a notice calling upon the assessee to show cause, on a date and time to be specified in the notice, why the arm's length price should not be so determined on the basis of material or information or document in the possession of the Assessing Officer.

- Where an arm's length price is determined by the Assessing Officer, the Assessing Officer may compute the total income of the assessee having regard to the arm's length price so determined u/s 92C(4). However:
  - No deduction u/s 10AA or under Chapter VIA shall be allowed in respect of the amount of income by which the total income of the assessee is enhanced after computation of income by the assessing officer.
  - Where the total income of an associated enterprise is computed by assessing officer on determination of the arm's length price paid to another associated enterprise from which tax has been deducted or was deductible, the income of the other associated enterprise shall not be recomputed by reason of such determination of arm's length price in the case of the first mentioned enterprise.

Due to application of transfer pricing provisions, there should be no loss to the revenue.

Reference to Transfer Pricing Officer (TPO) [Sec. 92CA]

- Where any person, being the assessee, has entered into an international transaction or specified domestic transaction in any previous year, and the Assessing Officer considers it necessary or expedient so to do, he may, with the previous approval of the Commissioner, refer the computation of the arm's length price in relation to the said international transaction or specified domestic transaction u/s 92C to the Transfer Pricing Officer.
- Where a reference is made, the Transfer Pricing Officer shall serve a notice on the assessee requiring him to produce or cause to be produced on a date to be specified therein, any evidence on which the assessee may rely in support of the computation made by him of the arm's length price in relation to such international transaction or specified domestic transaction.
- On the date specified in the notice or as soon thereafter as may be, after hearing such evidence as the assessee may produce, including any information or documents referred to in sec. 92D and after considering such evidence as the Transfer Pricing Officer may require on any specified points and after taking into account all relevant materials which he has gathered, the Transfer Pricing Officer shall, by order in writing, determine the arm's length price in relation to the international transaction or specified domestic transaction [in accordance with sec. 92C(3)] and send a copy of his order to the Assessing Officer and to the assessee.
- Where a reference was made, an order may be made at any time before 60 days prior to the date on which the period of limitation referred to in sec. 153 for making the order of assessment or reassessment or recomputation or fresh assessment, as the case may be, expires.
- In case assessment proceedings stayed in any circumstances referred to in Explanation (1) [clause (ii) or (x)] to sec. 153 and the period of limitation available to the Transfer Pricing Officer for making an order is less than 60 days, such remaining period shall be extended to 60 days and the aforesaid period of limitation shall be deemed to have been extended accordingly.
- On receipt of the order, the Assessing Officer shall proceed to compute the total income of the assessee u/s 92C(4) in conformity with the arm's length price as so determined by the Transfer Pricing Officer

- With a view to rectifying any mistake apparent from the record, the Transfer Pricing Officer may amend any order passed by him and the provisions of section 154 shall, so far as may be, apply accordingly.
- Where any amendment is made by the Transfer Pricing Officer, he shall send a copy of his order to the Assessing Officer who shall thereafter proceed to amend the order of assessment in conformity with such order of the Transfer Pricing Officer.
- Where any other international transaction, comes to the notice of the Transfer Pricing Officer during the course of the proceedings before him, the provisions of this Chapter shall apply as if such other international transaction is an international transaction referred to him.
- Where in respect of an international transaction, the assessee has not furnished the report u/s 92E and such transaction comes to the notice of the Transfer Pricing Officer during the course of the proceeding before him, the provisions of this Chapter shall apply as if such transaction is an international transaction referred to him.
- The Transfer Pricing Officer may, for the purposes of determining the arm's length price under this section, exercise all or any of the powers specified in sec. 131(1) or 133(6) or 133A.
- The Central Government may make a scheme, for the purposes of determination of the arm's length price, so as to impart greater efficiency, transparency and accountability by—

  a. eliminating the interface between the Transfer Pricing Officer and the assessee or any other person to the extent technologically feasible;

  b. optimising utilisation of the resources through economies of scale and functional specialisation;

  c. introducing a team-based determination of arm's length price with dynamic jurisdiction.

  The Central Government may, for the purpose of giving effect to the scheme, direct (within 31-03-2024) that any of the provisions of this Act shall not apply or shall apply with such exceptions, modifications and adaptations as may be specified.
- Transfer Pricing Officer means a Joint Commissioner or Deputy Commissioner or Assistant Commissioner authorised by the Board to perform all or any of the functions of an Assessing Officer specified in sections 92C and 92D in respect of any person or class of persons.

Advance Pricing Agreement – Concept and Application

13.3

Advance Pricing Agreement [Sec. 92CC]

- APA is a contract
- Usually for multiple years
- Between a taxpayer and at least one tax authority
- Mainly to prospectively resolve real or potential transfer pricing issues
- Involving transactions between related parties

Advance Pricing Agreement is an agreement between a taxpayer and a taxing authority on an appropriate transfer pricing methodology for a set of transactions over a fixed period of time in future. The APAs offer better assurance on transfer pricing methods and are conducive in providing certainty and unanimity of approach. A framework for advance pricing agreement are as under:

- The Board, with the approval of the Central Government, may enter into an advance pricing agreement with any person, determining the—
  a. arm's length price or specifying the manner in which the arm's length price is to be determined, in relation to an international transaction to be entered into by that person;
  b. income referred to in sec. 9(1)(i), or specifying the manner in which said income is to be determined, as is reasonably attributable to the operations carried out in India by or on behalf of that person, being a non-resident.
- The manner of determination of arm's length price, may include the methods referred to in sec. 92C or any other method, with such adjustments or variations, as may be necessary or expedient so to do.
- The arm's length price of any international transaction, in respect of which the advance pricing agreement has been entered into, shall be determined in accordance with the advance pricing agreement so entered.
- The agreement shall be valid for such period not exceeding 5 consecutive previous years as may be specified in the agreement.
- The advance pricing agreement entered into shall be binding:
  a. on the person in whose case, and in respect of the transaction in relation to which, the agreement has been entered into; and
  b. on the Commissioner, and the income-tax authorities subordinate to him, in respect of the said person and the said transaction.
- The agreement shall not be binding if there is a change in law or facts having bearing on the agreement so entered.
- The Board may, with the approval of the Central Government, by an order, declare an agreement to be void ab initio, if it finds that the agreement has been obtained by the person by fraud or misrepresentation of facts.

- Upon declaring the agreement void ab initio,:
  a. all the provisions of the Act shall apply to the person as if such agreement had never been entered into; and
  b. for the purpose of computing any period of limitation under this Act, the period beginning with the date of such agreement and ending on the date of such order shall be excluded.

  However, where immediately after the exclusion of the aforesaid period, the period of limitation, referred to in any provision of this Act, is less than 60 days, such remaining period shall be extended to 60 days and the aforesaid period of limitation shall be deemed to be extended accordingly.
- The agreement may, subject to such conditions, procedure and manner as may be prescribed, provide for determining
  a. the arm's length price or specify the manner in which arm's length price shall be determined in relation to the international transaction entered into by the person
  b. income referred to in sec. 9(1)(i), or specifying the manner in which the said income is to be determined, as is reasonably attributable to the operations carried out in India by or on behalf of that person, being a non-resident

  during any period not exceeding four previous years preceding the first of the previous years referred to in sec. 92CC(4), and the arm's length price of such international transaction or the income of such person shall be determined in accordance with the said agreement
- Where an application is made by a person for entering into an agreement, the proceeding shall be deemed to be pending in the case of the person for the purposes of the Act.
- The Board may prescribe a scheme specifying therein the manner, form, procedure and any other matter generally in respect of the advance pricing agreement. Following scheme has been framed by the Board in respect of Advance Pricing Agreement

Meaning of expressions used in matters in respect of advance pricing agreement [Rule 10F]

a) "agreement" means an advance pricing agreement entered into between the Board and the applicant, with the approval of the Central Government, as referred to in sec. 92CC(1);

b) "application" means an application for advance pricing agreement made under rule 10-I;

c) "applicant" means a person who has made an application;

d) "bilateral agreement" means an agreement between the Board and the applicant, subsequent to, and based on, any agreement referred to in rule 44GA between the competent authority in India with the competent authority in the other country regarding the most appropriate transfer pricing method or the arms' length price;

e) "competent authority in India" means an officer authorised by the Central Government for the purpose of discharging the functions as such for matters in respect of any agreement entered into under section 90 or 90A of the Act;

f) "covered transaction" means the international transaction or transactions for which agreement has been entered into;

g) "critical assumptions" means the factors and assumptions that are so critical and significant that neither party entering into an agreement will continue to be bound by the agreement, if any of the factors or assumptions is changed;

h) "most appropriate transfer pricing method" means any of the transfer pricing method, referred to in sec. 92C(1) of the Act, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or function performed by such persons or such other relevant factors prescribed by the Board under rules 10B and 10C;

i) "multilateral agreement" means an agreement between the Board and the applicant, subsequent to, and based on, any agreement referred to in rule 44GA between the competent authority in India with the competent authorities in the other countries regarding the most appropriate transfer pricing method or the arms' length price;

j) "rollback year" means any previous year, falling within the period not exceeding four previous years, preceding the first of the previous years referred to in sec. 92CC(4);

k) "tax treaty" means an agreement under section 90, or section 90A of the Act for the avoidance of double taxation;

l) "team" means advance pricing agreement team consisting of income-tax authorities as constituted by the Board and including such number of experts in economics, statistics, law or any other field as may be nominated by the Director General of Income-tax (International Taxation);

Unilateral APA	Bilateral APA	Multilateral APA
• APA entered into between a taxpayer and the tax administration of the country where it is subject to taxation	• APA entered into between the taxpayers, the tax administration of the host country and the foreign tax administration	• APA entered between the taxpayers, the tax administration of the host country and more than one foreign tax administrations

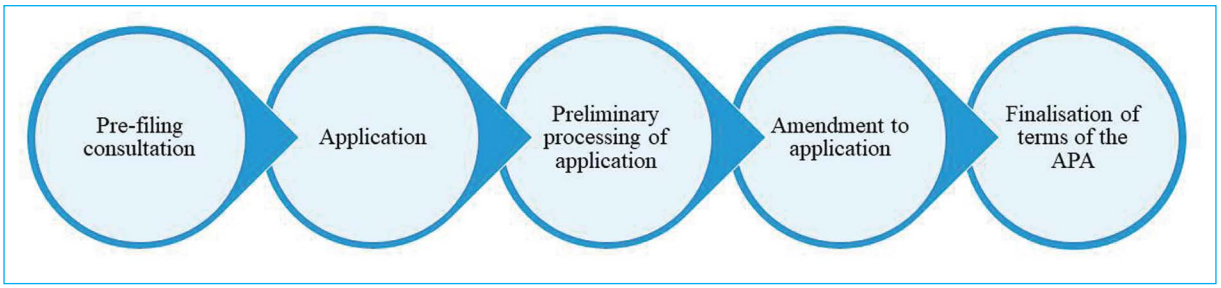
Persons eligible to apply [Rule 10G]

Any person who –

(i) has undertaken an international transaction; or

(ii) is contemplating to undertake an international transaction,

shall be eligible to enter into an agreement under these rules.



Process of APA

Pre-filing Consultation [Rule 10H]

1. Any person proposing to enter into an agreement under these rules may, by an application in writing, make a request for a pre-filing consultation.
2. The request for pre-filing consultation shall be made in Form No. 3CEC to the Director General of Income Tax (International Taxation).
3. On receipt of the request in Form No. 3CEC, the team shall hold pre-filing consultation with the person referred to in rule 10G.

4. The competent authority in India or his representative shall be associated in pre-filing consultation involving bilateral or multilateral agreement.
5. The pre-filing consultation shall, among other things,-
   (i) determine the scope of the agreement;
   (ii) identify transfer pricing issues;
   (iii) determine the suitability of international transaction for the agreement;
   (iv) discuss broad terms of the agreement.
6. The pre-filing consultation shall–
   (i) not bind the Board or the person to enter into an agreement or initiate the agreement process;
   (ii) not be deemed to mean that the person has applied for entering into an agreement.

Application for advance pricing agreement [Rule 10-I]

1. Any person, referred to in rule 10G may, if desires to enter into an agreement furnish an application in Form No. 3CED alongwith the requisite fee.
2. The application shall be furnished to Director General of Income Tax (International Taxation) in case of unilateral agreement and to the competent authority in India in case of bilateral or multilateral agreement.
3. Application in Form No. 3CED may be filed by the person referred to in rule 10G at any time–
   i. before the first day of the previous year relevant to the first assessment year for which the application is made, in respect of transactions which are of a continuing nature from dealings that are already occurring; or
   ii. before undertaking the transaction in respect of remaining transactions.
4. Every application in Form No. 3CED shall be accompanied by the proof of payment of specified fees.
5. The fees payable shall be in accordance with following table based on the amount of international transaction entered into or proposed to be undertaken in respect of which the agreement is proposed:

Amount of international transaction entered into or proposed to be undertaken in respect of which agreement is proposed during the proposed period of agreement.	Fee □
Amount not exceeding □ 100 crores	10 lacs
Amount not exceeding □ 200 crores	15 lacs
Amount exceeding □ 200 crores	20 lacs

Withdrawal of application for agreement [Rule 10J]

1. The applicant may withdraw the application for agreement at any time before the finalisation of the terms of the agreement.
2. The application for withdrawal shall be in Form No. 3CEE.
3. The fee paid shall not be refunded on withdrawal of application by the applicant.

Preliminary processing of application [Rule 10K]

1. Every application filed in Form No. 3CED shall be complete in all respects and accompanied by requisite documents.
2. If any defect is noticed in the application in Form No. 3CED or if any relevant document is not attached thereto or the application is not in accordance with understanding reached in any pre-filing consultation referred to in rule 10H, the Director General of Income-tax (International Taxation) (for unilateral agreement) and competent authority in India (for bilateral or multilateral agreement) shall serve a deficiency letter on the applicant before the expiry of 1 month from the date of receipt of the application.
3. The applicant shall remove the deficiency or modify the application within a period of 15 days from the date of service of the deficiency letter or within such further period which, on an application made in this behalf, may be extended, so however, that the total period of removal of deficiency or modification does not exceed 30 days.
4. The Director General of Income Tax (International Taxation) or the competent authority in India, as the case may be, on being satisfied, may pass an order providing that application shall not be allowed to be proceeded with if the application is defective and defect is not removed by applicant in accordance with aforesaid rule.
5. No such order shall be passed without providing an opportunity of being heard to the applicant and if an application is not allowed to be proceeded with, the fee paid by the applicant shall be refunded.

Procedure [Rule 10L]

1. If the application referred to in rule 10K has been allowed to be proceeded with, the team or the competent authority in India or his representative shall process the same in consultation and discussion with the applicant in accordance with provisions of this rule.
2. For this purpose, it shall be competent for the team or the competent authority in India or its representative to:
   i. hold meetings with the applicant on such time and date as it deem fit;
   ii. call for additional document or information or material from the applicant;
   iii. visit the applicant's business premises; or
   iv. make such inquiries as it deems fit in the circumstances of the case.
3. The applicant may, if he considers it necessary, provide further document and information for consideration of the team or the competent authority in India or his representative.
4. For bilateral or multilateral agreement, the competent authority shall forward the application to Director General of Income-tax (International Taxation) who shall assign it to one of the teams.
5. The team, to whom the application has been assigned, shall carry out the enquiry and prepare a draft report which shall be forwarded by the Director General of Income-tax (International Taxation) to the competent authority in India.
6. If the applicant makes a request for bilateral or multilateral agreement in its application, the competent authority in India shall in addition to the procedure provided in this rule invoke the procedure provided in rule 44GA.
7. The Director General of Income-tax (International Taxation) (for unilateral agreement) or the competent authority in India (for bilateral or multilateral agreement) and the applicant shall prepare a proposed mutually agreed draft agreement enumerating the result of the process including the effect of the arrangement referred to in rule 44GA(5) which has been accepted by the applicant in accordance with rule 44GA(8).

8. The agreement shall be entered into by the Board with the applicant after its approval by the Central Government.
9. Once an agreement has been entered into the Director General of Income-tax (International Taxation) or the competent authority in India, as the case may be, shall cause a copy of the agreement to be sent to the Commissioner of Income-tax having jurisdiction over the assessee.

Terms of the agreement [Rule 10M]

1. An agreement may among other things, include –
   i. the international transactions covered by the agreement;
   ii. the agreed transfer pricing methodology, if any;
   iii. determination of arm□s length price, if any;
   iv. definition of any relevant term to be used in items (ii) or (iii);
   v. critical assumptions;
   vi. rollback provision referred to in rule 10MA;
   vii. the conditions if any other than provided in the Act or these rules.
2. The agreement shall not be binding on the Board or the assessee if there is a change in any of critical assumptions or failure to meet conditions subject to which the agreement has been entered into.
3. The binding effect of agreement shall cease only if any party has given due notice of the concerned other party or parties.
4. In case there is a change in any of the critical assumptions or failure to meet the conditions subject to which the agreement has been entered into, the agreement can be revised or cancelled, as the case may be.
5. The assessee which has entered into an agreement shall give a notice in writing of such change in any of the critical assumptions or failure to meet conditions to the Director General of Income Tax (International Taxation) as soon as it is practicable to do so.
6. The Board shall give a notice in writing of such change in critical assumptions or failure to meet conditions to the assessee, as soon as it comes to the knowledge of the Board.
7. The revision or the cancellation of the agreement shall be in accordance with rules 10Q and 10R respectively.

Roll Back of the Agreement [Rule 10MA]

Sec. 92CC of the Act provides for Advance Pricing Agreement (APA). It empowers the Central Board of Direct Taxes, with the approval of the Central Government, to enter into an APA with any person for determining the Arm's Length Price (ALP) or specifying the manner in which ALP is to be determined in relation to an international transaction which is to be entered into by the person. The agreement entered into is valid for a period, not exceeding 5 previous years, as may be mentioned in the agreement. Once the agreement is entered into, the ALP of the international transaction, which is subject matter of the APA, would be determined in accordance with such an APA.

In many countries the APA scheme provides for "roll back" mechanism for dealing with ALP issues relating to transactions entered into during the period prior to APA. The "roll back" provisions refers to the applicability of the methodology of determination of ALP, or the ALP, to be applied to the international transactions which had already been entered into in a period prior to the period covered under an APA. However, the "roll back" relief is provided on case to case basis subject to certain conditions. Providing of such a mechanism in Indian legislation

would also lead to reduction in large scale litigation which is currently pending or may arise in future in respect of the transfer pricing matters.

1. Subject to the provisions of this rule, the agreement may provide for determining the arm's length price or specify the manner in which arm's length price shall be determined in relation to the international transaction entered into by the person during the rollback year (hereinafter referred to as "rollback provision").

2. The agreement shall contain rollback provision in respect of an international transaction subject to the following:

   i. the international transaction is same as the international transaction to which the agreement (other than the rollback provision) applies;

   ii. the return of income for the relevant rollback year has been or is furnished by the applicant before the due date specified u/s 139;

   iii. the report in respect of the international transaction had been furnished in accordance with sec. 92E;

   iv. the applicability of rollback provision, in respect of an international transaction, has been requested by the applicant for all the rollback years in which the said international transaction has been undertaken by the applicant; and

   v. the applicant has made an application seeking rollback in Form 3CEDA in accordance with sub-rule (5);

3. Rollback provision shall not be provided in respect of an international transaction for a rollback year, if:

   i. the determination of arm's length price of the said international transaction for the said year has been subject matter of an appeal before the Appellate Tribunal and the Appellate Tribunal has passed an order disposing of such appeal at any time before signing of the agreement; or

   ii. the application of rollback provision has the effect of reducing the total income or increasing the loss, as the case may be, of the applicant as declared in the return of income of the said year.

4. Where the rollback provision specifies the manner in which arm's length price shall be determined in relation to an international transaction undertaken in any rollback year then such manner shall be the same as the manner which has been agreed to be provided for determination of arm's length price of the same international transaction to be undertaken in any previous year to which the agreement applies, not being a rollback year.

5. The applicant may, if he desires to enter into an agreement with rollback provision, furnish along with the application, the request for the same in Form No. 3CEDA with proof of payment of an additional fee of □ 5 lakh.

Amendments to Application [Rule 10N]

1. An applicant may request in writing for an amendment to an application at any stage, before the finalisation of the terms of the agreement.

2. The Director General of Income Tax (International Taxation) (for unilateral agreement) or the competent authority in India (for bilateral or multilateral agreement) may, allow the amendment to the application, if such an amendment does not have effect of altering the nature of the application as originally filed.

3. The amendment shall be given effect only if it is accompanied by the additional fee, if any, necessitated by such amendment in accordance with fee as provided in rule 10-I.

Furnishing of Annual Compliance Report [Rule 10-O]

1. The assessee shall furnish an annual compliance report to Director General of Income Tax (international Taxation) for each year covered in the agreement.
2. The annual compliance report shall be in Form 3CEF.
3. The annual compliance report shall be furnished in quadruplicate, for each of the years covered in the agreement, within 30 days of the due date of filing the income tax return for that year, or within 90 days of entering into an agreement, whichever is later.
4. The Director General of Income Tax (International Taxation) shall send one copy of annual compliance report to the competent authority in India, one copy to the Commissioner of Income Tax who has the jurisdiction over the income-tax assessment of the assessee and one copy to the Transfer Pricing Officer having the jurisdiction over the assessee.

Compliance Audit of the agreement [Rule 10P]

1. The Transfer Pricing Officer having the jurisdiction over the assessee shall carry out the compliance audit of the agreement for each of the year covered in the agreement.
2. The Transfer Pricing Officer may require:
   i. the assessee to substantiate compliance with the terms of the agreement, including satisfaction of the critical assumptions, correctness of the supporting data or information and consistency of the application of the transfer pricing method;
   ii. the assessee to submit any information, or document, to establish that the terms of the agreement has been complied with.
3. The Transfer Pricing Officer shall submit the compliance audit report, for each year covered in the agreement, to the Director General of Income Tax (International Taxation) in case of unilateral agreement and to the competent authority in India, in case of bilateral or multilateral agreement, mentioning therein his findings as regards compliance by the assessee with terms of the agreement.
4. The Director General of Income Tax (International Taxation) shall forward the report to the Board in a case where there is finding of failure on part of assessee to comply with terms of agreement and cancellation of the agreement is required.
5. The compliance audit report shall be furnished by the Transfer Pricing Officer within 6 months from the end of the month in which the Annual Compliance Report referred to in rule 10-O is received by the Transfer Pricing Officer.
6. The regular audit of the covered transactions shall not be undertaken by the Transfer Pricing Officer if an agreement has been entered into under rule 10L except where the agreement has been cancelled under rule 10R.

Revision of an agreement [Rule 10Q]

1. An agreement, subsequent to it having been entered into, may be revised by the Board, if.-
   i. there is a change in critical assumptions or failure to meet a condition subject to which the agreement has been entered into;
   ii. there is a change in law that modifies any matter covered by the agreement but is not of the nature which renders the agreement to be non binding ; or

iii. there is a request from competent authority in the other country requesting revision of agreement, in case of bilateral or multilateral agreement.

2. An agreement may be revised by the Board either suo-moto or on request of the assessee or the competent authority in India or the Director General of Income Tax (International Taxation).
3. Except when the agreement is proposed to be revised on the request of the assessee, the agreement shall not be revised unless an opportunity of being heard has been provided to the assessee and the assessee is in agreement with the proposed revision.
4. In case the assessee is not in agreement with the proposed revision the agreement may be cancelled in accordance with rule-10R.
5. In case the Board is not in agreement with the request of the assessee for revision of the agreement, the Board shall reject the request in writing giving reason for such rejection.
6. For the purpose of arriving at the agreement for the proposed revision, the procedure provided in rule 10 L may be followed so far as they apply.
7. The revised agreement shall include the date till which the original agreement is to apply and the date from which the revised agreement is to apply.

Cancellation of an agreement [Rule 10R]

1. An agreement shall be cancelled by the Board for any of the following reasons:
   i. the compliance audit referred to in rule 10P has resulted in the finding of failure on the part of the assessee to comply with the terms of the agreement;
   ii. the assessee has failed to file the annual compliance report in time;
   iii. the annual compliance report furnished by the assessee contains material errors; or
   iv. the agreement is to be cancelled under rule 10Q(4) or rule 10RA(7).
2. The Board shall give an opportunity of being heard to the assessee, before proceeding to cancel an application.
3. The competent authority in India shall communicate with the competent authority in the other country or countries and provide reason for the proposed cancellation of the agreement in case of bilateral or multilateral agreement.
4. The order of cancellation of the agreement shall be in writing and shall provide reasons for cancellation and for non acceptance of assessee□s submission, if any.
5. The order of cancellation shall also specify the effective date of cancellation of the agreement, where applicable.
6. The order under the Act, declaring the agreement as void ab initio, on account of fraud or misrepresentation of facts, shall be in writing and shall provide reason for such declaration and for non acceptance of assessee□s submission, if any.
7. The order of cancellation shall be intimated to the Assessing Officer and the Transfer Pricing Officer, having jurisdiction over the assessee.

Procedure for giving effect to rollback provision of an Agreement [Rule 10RA]

1. The effect to the rollback provisions of an agreement shall be given in accordance with this rule.
2. The applicant shall furnish modified return of income referred to in sec. 92CD in respect of a rollback year to which the agreement applies along with the proof of payment of any additional tax arising as a consequence of and computed in accordance with the rollback provision.

3. The modified return referred above shall be furnished along with the modified return to be furnished in respect of first of the previous years for which the agreement has been requested for in the application.

4. If any appeal filed by the applicant is pending before the Commissioner (Appeals), Appellate Tribunal or the High Court for a rollback year, on the issue which is the subject matter of the rollback provision for that year, the said appeal to the extent of the subject covered under the agreement shall be withdrawn by the applicant before furnishing the modified return for the said year.

5. If any appeal filed by the Assessing Officer or the Principal Commissioner or Commissioner is pending before the Appellate Tribunal or the High Court for a rollback year, on the issue which is subject matter of the rollback provision for that year, the said appeal to the extent of the subject covered under the agreement shall be withdrawn by the Assessing Officer or the Principal Commissioner or the Commissioner, as the case may be, within 3 months of filing of modified return by the applicant.

6. The applicant, the Assessing Officer or the Principal Commissioner or the Commissioner, shall inform the Dispute Resolution Panel or the Commissioner (Appeals) or the Appellate Tribunal or the High Court, as the case may be, the fact of an agreement containing rollback provision having been entered into along with a copy of the same as soon as it is practicable to do so.

7. In case effect cannot be given to the rollback provision of an agreement in accordance with this rule, for any rollback year to which it applies, on account of failure on the part of applicant, the agreement shall be cancelled.

Renewing an agreement [Rule 10S]

Request for renewal of an agreement may be made as a new application for agreement, using the same procedure as outlined in these rules except pre filing consultation as referred to in rule 10H.

Miscellaneous [Rule 10T]

1. Mere filing of a application for an agreement under these rules shall not prevent the operation of Chapter X of the Act for determination of arms length price under that Chapter till the agreement is entered into.

2. The negotiation between the competent authority in India and the competent authority in the other country or countries, in case of bilateral or multilateral agreement, shall be carried out in accordance with the provisions of the tax treaty between India and the other country or countries.

Procedure to deal with requests for bilateral or multilateral advance pricing agreements [Rule 44GA]

1. Where a person has made request for a bilateral or multilateral advance pricing agreement in an application filed in Form No. 3CED in accordance with rule 10-I, the request shall be dealt with subject to provisions of this rule.

2. The process for bilateral or multilateral advance pricing agreement shall not be initiated unless the associated enterprise situated outside India has initiated process of advance pricing agreement with the competent authority in the other country.

3. The competent authority in India shall, on intimation of request of the applicant for a bilateral or multilateral agreement, consult and ascertain willingness of the competent authority in other country or countries, as the case may be, for initiation of negotiation for this purpose.

4. In case of willingness of the competent authority in other country or countries, as the case may be, the competent authority in India shall enter into negotiation in this behalf and endeavour to reach a set of terms which are acceptable to the competent authority in India and the competent authority in the other country or countries, as the case may be.

5. In case of an agreement after consultation, the competent authority in India shall formalise a mutual agreement procedure arrangement with the competent authority in other country or countries, as the case may be, and intimate the same to the applicant.
6. In case of failure to reach agreement on such terms as are mutually acceptable to parties mentioned in sub-rule (4), the applicant shall be informed of the failure to reach an agreement with the competent authority in other country or countries.
7. The applicant shall not be entitled to be part of discussion between competent authority in India and the competent authority in the other country or countries, as the case may be; however the applicant can communicate or meet the competent authority in India for the purpose of entering into an advance pricing agreement.
8. The applicant shall convey acceptance or otherwise of the agreement within thirty days of it being communicated.
9. The applicant, in case the agreement is not acceptable may at its option continue with process of entering into an advance pricing agreement without benefit of mutual agreement process or withdraw application in accordance with rule 10J

Effect to Advance Pricing Agreement [Sec. 92CD]

- Where any person has entered into an agreement and prior to the date of entering into the agreement, any return of income has been furnished u/s 139 for any assessment year relevant to a previous year to which such agreement applies, such person shall furnish, within a period of 3 months from the end of the month in which the said agreement was entered into, a modified return in accordance with and limited to the agreement.
- Save as otherwise provided in this section, all other provisions of this Act shall apply accordingly as if the modified return is a return furnished u/s 139.
- If the assessment or reassessment proceedings for an assessment year relevant to a previous year to which the agreement applies have been completed before the expiry of period allowed for furnishing of modified return, the Assessing Officer shall, in a case where modified return is filed, pass an order modifying the total income of the relevant assessment year determined in such assessment or reassessment, as the case may be having regard to and in accordance with the agreement.
- Where the assessment or reassessment proceedings for an assessment year relevant to the previous year to which the agreement applies are pending on the date of filing of modified return, the Assessing Officer shall proceed to complete the assessment or reassessment proceedings in accordance with the agreement taking into consideration the modified return so furnished.
- The order shall be passed within a period of 1 year from the end of the financial year in which the modified return is furnished.
- The period of limitation as provided in sec. 153, 153B or 144C for completion of pending assessment or reassessment proceedings shall be extended by a period of 12 months.
- The assessment or reassessment proceedings for an assessment year shall be deemed to have been completed where:

  (a) an assessment or reassessment order has been passed; or

  (b) no notice has been issued u/s 143(2) till the expiry of the limitation period provided under that sub-section.

Maintenance, keeping of information and document by persons entering into an international transaction or specified domestic transaction [Sec. 92D]

- Every person,—
  a. who has entered into an international transaction or specified domestic transaction shall keep and maintain such information and document in respect thereof as may be prescribed;
  b. being a constituent entity[4] of an international group, shall keep and maintain such information and document in respect of an international group as may be prescribed.
- The Board may prescribe the period for which the information and document shall be kept and maintained[5] under the said sub-section.
- The Assessing Officer or the Commissioner (Appeals) may, in the course of any proceeding under this Act, require any person referred to in (a) to furnish any information or document referred therein, within a period of 10 days from the date of receipt of a notice issued in this regard. However, such period may, on an application made by such person, extend the period of ten days by a further period not exceeding 30 days.
- The person referred to in (b) shall furnish the information and document referred therein to the authority prescribed u/s 286(1), in such manner, on or before such date, as may be prescribed.
- If constituent entity fails to furnish the information and documents, penalty of □ 5,00,000 shall be levied on that person u/s 271AA. In other case, a sum equal to 2% of the value of each international transaction or specified domestic transaction entered into by such person shall be levied as penalty

Report from an accountant to be furnished by persons entering into international transaction or specified domestic transaction [Sec. 92E]

Every person who has entered into an international transaction or specified domestic transaction during a previous year shall obtain a report from an accountant and furnish such report on or before the specified date (i.e., 31st Oct, being one month prior the due date of filing of return of income) in the prescribed form [Form 3CEB] duly signed and verified in the prescribed manner by such accountant and setting forth such particulars as may be prescribed.

Special measures in respect of transactions with persons located in notified jurisdictional area [Sec. 94A]

- The Central Government may, having regard to the lack of effective exchange of information with any country or territory outside India, specify by notification in the Official Gazette such country or territory as a notified jurisdictional area in relation to transactions entered into by any assessee.
- If an assessee enters into a transaction where one of the parties to the transaction is a person located in a notified jurisdictional area, then—
  i. all the parties to the transaction shall be deemed to be associated enterprises within the meaning of sec. 92A;
  ii. any transaction in the nature of purchase, sale or lease of tangible or intangible property or provision of service or lending or borrowing money or any other transaction having a bearing on the profits,

4 "constituent entity" and "international group" shall have the meaning assigned to it in sec. 286(9).
5 8 years from the end of the relevant assessment year

income, losses or assets of the assessee including a mutual agreement or arrangement for allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided by or to the assessee shall be deemed to be an international transaction within the meaning of sec. 92B,

and the provisions of sec. 92, 92A, 92B, 92C [except the second proviso to sec. 92C(2)], 92CA, 92CB, 92D, 92E and 92F shall apply accordingly.

- Person located in a notified jurisdictional area shall include:
  a. a person who is resident of the notified jurisdictional area;
  b. a person, not being an individual, which is established in the notified jurisdictional area; or
  c. a permanent establishment of a person not falling above, in the notified jurisdictional area;
- No deduction,—
  i. in respect of any payment made to any financial institution located in a notified jurisdictional area shall be allowed under this Act, unless the assessee furnishes an authorisation in the prescribed form authorising the Board or any other income-tax authority acting on its behalf to seek relevant information from the said financial institution on behalf of such assessee; and
  ii. in respect of any other expenditure or allowance (including depreciation) arising from the transaction with a person located in a notified jurisdictional area shall be allowed under any other provision of this Act, unless the assessee maintains such other documents and furnishes such information as may be prescribed [under rule 10FC], in this behalf.
- Where, in any previous year, the assessee has received or credited any sum from any person located in a notified jurisdictional area and the assessee does not offer any explanation about the source of the said sum in the hands of such person or in the hands of the beneficial owner (if such person is not the beneficial owner of the said sum) or the explanation offered by the assessee, in the opinion of the Assessing Officer, is not satisfactory, then, such sum shall be deemed to be the income of the assessee for that previous year.
- Where any person located in a notified jurisdictional area is entitled to receive any sum or income or amount on which tax is deductible under Chapter XVII-B, the tax shall be deducted at the highest of the following rates:
  a. 30%
  b. at the rate or rates in force;
  c. at the rate specified in the relevant provisions of this Act;

Penalty

Failure to keep and maintain information and document in respect of international transaction or specified domestic transaction [Sec. 271AA]

If any person in respect of an international transaction or specified domestic transaction:

i. fails to keep and maintain any such information and document as required by sec. 92D;

ii. fails to report such transaction which he is required to do so; or

iii. maintains or furnishes an incorrect information or document,

the Assessing Officer or Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to 2% of the value of each international transaction or specified domestic transaction entered into by such person.

Penalty for failure to furnish report under section 92E [Sec. 271BA]

If any person fails to furnish a report from an accountant as required by sec. 92E, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of □ 1,00,000.

Penalty for failure to furnish information or document under section 92D [Sec. 271G]

If any person who has entered into an international transaction or specified domestic transaction fails to furnish any such information or document as required by sec. 92D(3), the Transfer Pricing Officer or Assessing Officer or the Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to 2% of the value of the international transaction or specified domestic transaction for each such failure.

However, where assessee shows reasonable cause, then no penalty u/s 271AA or 271BA or 271G shall be levied [Sec. 273B]

Safe Harbour Rules, Thin Capitalisation and Secondary Adjustment

13.4

Power of Board to make safe harbour rules [Sec. 92CB]

The determination of—

a. income referred to in sec. 9(1)(i); or

b. arm's length price u/s 92C or 92CA,

- shall be subject to safe harbour rules.

Taxpoint

- The Board may make rules for safe harbour[6].
- "Safe harbour" means circumstances in which the income-tax authorities shall accept the transfer price or income, deemed to accrue or arise u/s 9(1)(i), as the case may be, declared by the assessee.

Limitation on interest deduction in certain cases [Sec. 94B]

Thin Capitalization

A company is typically financed or capitalized through a mixture of debt and equity. The way a company is capitalized often has a significant impact on the amount of profit it reports for tax purposes as the tax legislations of countries typically allow a deduction for interest paid or payable in arriving at the profit for tax purposes while the dividend paid on equity contribution is not deductible. Therefore, the higher the level of debt in a company, and thus the amount of interest it pays, the lower will be its taxable profit. For this reason, debt is often a more tax efficient method of finance than equity. Multinational groups are often able to structure their financing arrangements to maximize these benefits. For this reason, country's tax administrations often introduce rules that place a limit on the amount of interest that can be deducted in computing a company's profit for tax purposes. Such rules are designed to counter cross-border shifting of profit through excessive interest payments, and thus aim to protect a country's tax base.

Under the initiative of the G-20 countries, the Organization for Economic Co-operation and Development (OECD) in its Base Erosion and Profit Shifting (BEPS) project had taken up the issue of base erosion and profit shifting by way of excess interest deductions by the MNEs in Action plan 4. The OECD has recommended several measures in its final report to address this issue.

In view of the above, sec. 94B was inserted in line with the recommendations of OECD BEPS Action Plan 4, to provide that interest expenses claimed by an entity to its associated enterprises shall be restricted to 30% of its earnings before interest, taxes, depreciation and amortization (EBITDA) or interest paid or payable to associated enterprise, whichever is less.

6 Rule 10TA to Rule 10THD

The provisions are enumerated here-in-below:

Applicable to

Indian company, or a permanent establishment of a foreign company in India, being the borrower

- Permanent establishment includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.

Conditions

a) The borrower has debt issued by a non-resident, being an associated enterprise of such borrower.

   - Debt means any loan, financial instrument, finance lease, financial derivative, or any arrangement that gives rise to interest, discounts or other finance charges that are deductible in the computation of income chargeable under the head "Profits and gains of business or profession";

b) He incurs any expenditure by way of interest or of similar nature exceeding ₹ 1 crore;

c) Such expenditure is deductible in computing income chargeable under the head "Profits and gains of business or profession"

Effect

If all the aforesaid conditions are satisfied then, excess interest shall not be deductible in computation of income under the said head.

- Excess interest means lower of the following:

  a) An amount of total interest paid or payable in excess of 30% of earnings before interest, taxes, depreciation and amortisation (EBITDA) of the borrower in the previous year; or

  b) Interest paid or payable to associated enterprises for that previous year

Taxpoint

- **Guarantee:** Where the debt is issued by a lender which is not associated but an associated enterprise either provides an implicit or explicit guarantee to such lender or deposits a corresponding and matching amount of funds with the lender, such debt shall be deemed to have been issued by an associated enterprise.
- **Exception:**

  The provision of sec. 94B is not applicable:

  a) to an Indian company or a permanent establishment of a foreign company which is engaged in the business of banking or insurance or notified non-banking financial companies (NBFC)

  b) to interest paid in respect of a debt issued by a lender which is a permanent establishment in India of a non-resident, being a person engaged in the business of banking

- Carry forward: Where for any assessment year, the interest expenditure is not wholly deducted against income under the head "Profits and gains of business or profession", so much of the interest expenditure as has not been so deducted, shall be carried forward to the following assessment year(s), and it shall be allowed as a deduction against the profits and gains, if any, of any business or profession carried on by it and assessable for that assessment year to the extent of maximum allowable interest expenditure.
- Maximum carried forward: No interest expenditure shall be carried forward for more than 8 assessment years immediately succeeding the assessment year for which the excess interest expenditure was first computed.

Example 2:

Computation of interest expenses disallowed u/s 94B:

₹ in crore

Particulars	Case 1	Case 2	Case 3
EBIDTA of the Indian Borrower	100	100	100
30% of the above **[A]**	30	30	30
Interest payable to associated enterprise **[B]**	35	Nil	15
Interest payable to non-associated enterprise **[C]**	Nil	35	20
Total Interest expense incurred **[D = B + C]**	35	35	35
Total interest expenses incurred in excess of 30% of EBITDA **[E = D – A]**	5	5	5
Interest payable to associated enterprise **[B]**	35	Nil	15
Excess interest [lower of (E) and (B)] being disallowed u/s 94B	**5**	**Nil**	**5**

Secondary adjustment in certain cases [Sec. 92CE]

"Secondary adjustment" means an adjustment in the books of account of the assessee and its associated enterprise to reflect that the actual allocation of profits between the assessee and its associated enterprise are consistent with the transfer price determined as a result of primary adjustment, thereby removing the imbalance between cash account and actual profit of the assessee.

The provisions are enumerated here-in-below:

- Where a primary adjustment to transfer price,:
  - i. has been made suo motu by the assessee in his return of income;
  - ii. made by the Assessing Officer has been accepted by the assessee;
  - iii. is determined by an advance pricing agreement entered into by the assessee u/s 92CC on or after 01-04-2017;
  - iv. is made as per the safe harbour rules framed u/s 92CB; or
  - v. is arising as a result of resolution of an assessment by way of the mutual agreement procedure under an agreement entered into u/s 90 or 90A for avoidance of double taxation,
  - the assessee shall make a secondary adjustment.
- Exception: Nothing contained in this section shall apply, if:
  - i. the amount of primary adjustment made in any previous year does not exceed ₹ 1 crore; or
  - ii. the primary adjustment is made in respect of an assessment year commencing on or before 01-04-2016.
- Where, as a result of primary adjustment to the transfer price, there is an increase in the total income or reduction in the loss, as the case may be, of the assessee, the excess money (or part thereof) which is available with its associated enterprise, if not repatriated to India within the time as may be prescribed, shall be deemed to be an advance made by the assessee to such associated enterprise and the interest on such advance, shall be computed in such manner as may be prescribed [Sec. 92CE(2)]
  - ➢ Excess money means the difference between the arm's length price determined in primary adjustment and the price at which the international transaction has actually been undertaken;

- Primary adjustment to a transfer price, means the determination of transfer price in accordance with the arm's length principle resulting in an increase in the total income or reduction in the loss, as the case may be, of the assessee;
- Excess money (or part thereof) may be repatriated from any of the associated enterprises of the assessee which is not a resident in India.

Example 3:

An Indian company sells certain products to its Associated Enterprise for INR 100 crores, whereas the Arm's Length Price (ALP) of such transaction is INR 150 crores. The TPO confirms an upward adjustment (Primary adjustment) of INR 50 crores, the difference between the Selling price INR 100 crores and the ALP INR 150 crores, which is taxed in the hands of Indian company.

Subsequently, for the purpose of Secondary adjustment, it would be deemed that the AE owes INR 50 crores to Indian company (the difference between ALP and actual transfer price), which will be deemed to be a Loan or an Advance by Indian company to its AE. As a consequence, an interest would be imputed on such Loan or Advance and an Adjustment (Secondary adjustment) would be carried out in the hands of the Indian company.

Optional Scheme

- Where the excess money (or part thereof) has not been repatriated within the prescribed time, the assessee may, at his option, pay additional income-tax @ 18% (plus surcharge @ 12% + cess) on such excess money.
- The tax so paid by the assessee shall be treated as the final payment of tax in respect of such money not repatriated and no further credit therefor shall be claimed by the assessee or by any other person in respect of the amount of tax so paid.
- No deduction shall be allowed to the assessee in respect of the amount on which tax has been paid.
- Where the additional income-tax is paid by the assessee, he shall not be required to make secondary adjustment and compute interest from the date of payment of such tax

Computation of interest income pursuant to secondary adjustments [Rule 10CB]

1. For the purposes of sec. 92CE(2), the time limit for repatriation of excess money or part thereof shall be on or before 90 days,—
   i. from the due date of filing of return u/s 139(1) where primary adjustments to transfer price has been made suo-moto by the assessee in his return of income;
   ii. from the date of the order of Assessing Officer or the appellate authority, as the case may be, if the primary adjustments to transfer price as determined in the aforesaid order has been accepted by the assessee;
   iii. in a case where primary adjustment to transfer price is determined by an advance pricing agreement entered into by the assessee u/s 92CC in respect of a previous year,-
      a. from the date of filing of return u/s 139(1) if the advance pricing agreement has been entered into on or before the due date of filing of return for the relevant previous year;
      b. from the end of the month in which the advance pricing agreement has been entered into if the said agreement has been entered into after the due date of filing of return for the relevant previous year
   iv. from the due date of filing of return u/s 139(1) in the case of option exercised by the assessee as per the safe harbour rules u/s 92CB; or

v. from the date of giving effect by the Assessing Officer under rule 44H to the resolution arrived at under mutual agreement procedure, where the primary adjustment to transfer price is determined by such resolution under a Double Taxation Avoidance Agreement entered into u/s 90 or 90A.

2. The imputed per annum interest income on excess money or part thereof which is not repatriated within the time limit as per sec. 92CE(1) shall be computed,—

   i. at the 1 year marginal cost of fund lending rate of State Bank of India as on 1st of April of the relevant previous year plus 325 basis points in the cases where the international transaction is denominated in Indian rupee; or

   ii. at 6 months London Interbank Offered Rate as on 30th September of the relevant previous year plus 300 basis points in the cases where the international transaction is denominated in foreign currency.

3. The aforesaid interest shall be chargeable on excess money or part thereof which is not repatriated—

   a. in cases referred to in sub-rule (1)(i), (iii)(a) and (iv), from the due date of filing of return u/s 139(1);

   b. in cases referred to in sub-rule (1)(ii), from the date of the order of Assessing Officer or the appellate authority, as the case may be;

   c. in cases referred to in sub-rule (1)(iii)(b), from the end of the month in which the advance pricing agreement has been entered into by the assessee u/s 92CC;

   d. in cases referred to in sub-rule (1)(v), from the date of giving effect by the Assessing Officer under rule 44H to the resolution arrived at under mutual agreement procedure.

Taxpoint

- "International transaction" shall have the same meaning as assigned to it in sec. 92B;
- The rate of exchange for the calculation of the value in rupees of the international transaction denominated in foreign currency shall be the telegraphic transfer buying rate of such currency on the last day of the previous year in which such international transaction was undertaken and the "telegraphic transfer buying rate" shall have the same meaning as assigned in the Explanation to rule 26 [i.e., "telegraphic transfer buying rate", in relation to a foreign currency, means the rate or rates of exchange adopted by the State Bank of India, for buying such currency, having regard to the guidelines specified from time to time by the Reserve Bank of India for buying such currency, where such currency is made available to that bank through a telegraphic transfer.

Annexure 1

Determination of income in the case of non-residents [Rule 10]

In any case in which the Assessing Officer is of opinion that the actual amount of the income accruing or arising to any non-resident person whether directly or indirectly, through or from any business connection in India or through or from any property in India or through or from any asset or source of income in India or through or from any money lent at interest and brought into India in cash or in kind cannot be definitely ascertained, the amount of such income for the purposes of assessment to income-tax may be calculated:

i. at such percentage of the turnover so accruing or arising as the Assessing Officer may consider to be reasonable, or

ii. on any amount which bears the same proportion to the total profits and gains of the business of such person (such profits and gains being computed in accordance with the provisions of the Act), as the receipts so accruing or arising bear to the total receipts of the business, or

iii. in such other manner as the Assessing Officer may deem suitable.

Determination of arm's length price under section 92C [Rule 10B]

- For the purposes of sec. 92C(2), the arm's length price in relation to an international transaction or a specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, in the following manner:

a. comparable uncontrolled price (CUP) method, by which,—

i. the price charged or paid for property transferred or services provided in a comparable uncontrolled transaction, or a number of such transactions, is identified;

- Uncontrolled transaction means a transaction between enterprises other than associated enterprises, whether resident or non-resident – Rule 10A
- Transaction includes a number of closely linked transactions

ii. such price is adjusted to account for differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions, which could materially affect the price in the open market;

iii. the adjusted price arrived at under (ii) is taken to be an arm's length price in respect of the property transferred or services provided in the international transaction or the specified domestic transaction

- Property includes goods, articles or things, and intangible property;
- Services include financial services

Taxpoint:

- Typical transactions in respect of which the comparable uncontrolled price method may be adopted are:

a. Transfer of goods;

b. Provision of services;

c. Intangibles;

d. Interest on loans.

- CUP can be either of the following:

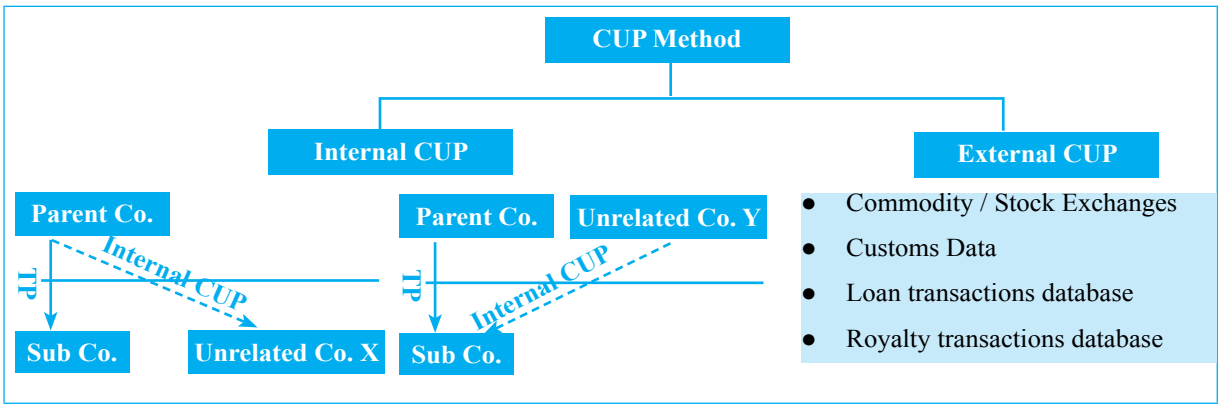
1. **Internal CUP:** this would be available if the taxpayer (or one of its group entities) enters into a comparable transaction with an unrelated party where the goods or services under consideration are same or similar.

Situations where Internal CUP may be applicable:

a. The tax payer or any other member of the group sells similar goods in similar quantities and under similar terms to an independent enterprise in a similar market.

b. The tax payer or another member of the group buys similar goods in similar quantities and under similar terms from an independent enterprise in a similar market (an internal comparable).

2. **External CUP**: this would be applicable if a transaction between two independent enterprises involves comparable goods or services under comparable conditions.
   a. An independent enterprise **sells** the particular product in similar quantities and under similar terms to another independent enterprise in a similar market;
   b. An independent enterprise **buys** similar goods in similar quantities and under similar terms from another independent enterprise in a similar market.



- Compare the prices charged for property or services
- Price under 'controlled transaction' is compared with 'uncontrolled transaction'
- It requires close similarity in products, property or services that are involved
- Where the prices of the product fluctuate regularly, timing of the transaction also relevant

Example 4:

AE1 Ltd., is an Indian company. The shareholding pattern of AE1 Ltd., is as follows:

Shareholder's name	Status	% holding
AE2 Ltd.	Foreign Company	30
AE3 Ltd.	Indian Company	30
Financial Institutions	Indian Company	10
Public		30

AE1 Ltd., is a manufacturer of compact disc (CD) writers and its customers, inter alia, include AE2 Ltd, and M Ltd.

AE1 Ltd., during the year has supplied 10,000 nos. of the product to AE2 Ltd. at a price of ₹ 2,000 per unit and 200 nos. of the same product to AE3 Ltd., at a price of ₹ 2,750 per unit. AE1 Ltd., has sold 100 units of the same product to M Ltd. at ₹ 3,000 per unit.

Analysis of the international transaction with comparable uncontrolled transaction

	International transaction (with AE2 Ltd.)	Comparable uncontrolled transaction (with M Ltd.)	
Price	FOB	CIF	Freight and insurance ₹ 550
Quantity discount	Yes	No	One CD of ₹ 10 each for every CD writer plus ₹ 20 per CD writer

Credit	One month	Cash and carry	Cost of credit 1.25% per month
Warranty	No warranty	Six months warranty	Cost of warranty is ₹ 250 per unit

Factors to be considered while determining ALP:

a. In the CUP method, one has to start from the price charged in the case of the comparable uncontrolled transaction.

b. In this illustration one has to start with the price charged by AE1 Ltd., to M Ltd.

c. The price charged to AE3 Ltd., cannot be considered as AE3 Ltd., is itself an associated enterprise of AE1 Ltd.

d. The price charged to M Ltd., will have to be increased by the value of credit which is at the rate at 1.25% p.m. (i.e. 15% p.a.). If the similar credit were offered to M Ltd., the price charged to M Ltd. would have been higher, after factoring this cost.

e. The price charged to M Ltd., will have to be reduced by the following;

   i. ₹ 550 representing the freight and insurance –This is for the reason that if the price to M Ltd., had been on FOB basis, it would have been less by ₹ 550.

   ii. ₹ 250 per unit representing the estimated cost of warranty execution for a period of 6 months on the basis of a technical analysis and past experience - This is for the reason that if the warranty was not given, the price to M Ltd. would have been lower, without factoring this cost.

   iii. ₹ 10 representing the cost of each CD – This is for the reason that if similar gift had been offered to M Ltd., the effective price to M Ltd., would have been less.

   iv. ₹ 20 representing a quantity discount - This is for the reason that if similar discount had been offered to M Ltd., the effective price to M Ltd., would have been less.

The following points are to be noticed:

i. All adjustments in the course of applying this method are to be made to the price charged in the uncontrolled transaction. The presence or absence of any specific features in the uncontrolled transaction as compared to the international transaction is to be adjusted for. These Methods of Computation of Arm's Length Price features are to be evaluated in monetory terms. This is a subjective process based on objective facts.

ii. Only differences that would materially affect the price in the open market are required to be adjusted. Two points may be noted. Firstly, materiality would have to be judged in the light of various circumstances. If there are numerous adjustments, which are individually not material but collectively material, the necessary adjustments are required to be made. Secondly, the term 'open market', though not defined, would mean a transaction between a knowledgeable and a willing purchaser and a knowledgeable and willing seller where neither of them is influenced or compelled to act in a particular manner.

   a. resale price method, by which,—

      i. the price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise, is identified;

      ii. such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;

iii. the price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;

iv. the price so arrived at is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;

v. the adjusted price arrived at under (iv) is taken to be an arm's length price in respect of the purchase of the property or obtaining of the services by the enterprise from the associated enterprise.

Taxpoint

- The steps involved in the application of this method are:

i. identify the international transaction of purchase of property or services;

ii. identify the price at which such property or services are resold or provided to an unrelated party (resale price);

iii. identify the normal gross profit margin in a comparable uncontrolled transaction whether internal or external. The normal gross profit margin is that margin which an enterprise would earn from purchase of the similar product from an unrelated party and the resale of the same to another unrelated party.

iv. deduct the normal gross profit from the resale price.

v. deduct expenses incurred in connection with the purchase of goods;

vi. adjust the resultant amount for the differences between the uncontrolled transaction and the international transaction. These differences could be functional and other differences including differences in accounting practices. Further these differences should be such as would materially affect the amount of gross profit margin in the open market;

vii. the price arrived at is the arm's length price of the international transaction;

- RPM is a method based on the price at which a product that has been purchased from a related party is resold to an unrelated enterprise.
- The resale price is reduced by the resale price margin/ gross profit margin.
- This is further reduced by the expenses incurred in connection with the purchase of product or obtaining of services.
- When goods are purchased from AE or Unrelated party and same are sold to AE, this method cannot be applied, since it can be applied only in a situation where goods are purchased from AE and same are sold to Unrelated party.

⊙ The application of the resale price method can be understood with the following example:

AE1 Ltd., is an Indian company. The shareholding pattern of AE1 Ltd., is as follows;

Shareholder's name	Status	% holding
AE2 Ltd.	Foreign Company	30
AE3 Ltd.	Indian Company	30
Financial Institutions	Indian Company	10
Public		30

AE1 Ltd., trades in compact disc (CD) writers. AE1 Ltd., procures CD writers both locally and in the international market. Its imports consist of CD writers purchased from AE2 Ltd. as well as other manufacturers (Non AEs).

AE1 Ltd., during the year purchased 100 CD writers from AE2 Ltd. at ₹ 2,900 per unit. These are resold to A Ltd., at a price of ₹ 3,000 per unit.

AE1 Ltd., has also purchased similar products from an unrelated supplier, viz. K Ltd., and has resold the same to M Ltd., who is also an unrelated party and has earned a gross profit of 15% on sales.

Analysis of the sales transactions

	Sales to A Ltd.	Sales to M Ltd.	
Price	Ex shop	FOR Destination with cost of freight and insurance estimated at 2% of GP	Impact of Freight and insurance on GP is 2% as the sale price increases but corresponding expenses are not debited to trading account but to profit and loss account
Quantity discount	Yes - the cost of the same is estimated at 1% of GP	No	Impact of quantity discount on GP is 1%
Free gifts	No	One CD pack for every CD writer with no change in sale price	As cost of gift is not debited to trading account but to P & L Account, there is no impact on GP
Warranty	No	6 months warranty (without change in sale price) - cost of warranty is estimated at ₹ 250 per unit	As cost of warranty is not debited to trading account but to P&L Account, there is no impact on GP

Analysis of the purchase transactions

	Purchase from AE2 Ltd. (International transaction)	Purchase from K Ltd.	
Customs duty	₹ 25 per unit	₹ 25 per unit	No impact
Freight inwards	₹ 10 per unit	Nil	Cost of purchase from K Ltd., is lower
Quantity discount	₹ 15 per unit	Nil	Cost of purchase from K Ltd., is higher

Warranty	Nil	6 months warranty purchase price remaining unchanged	No impact

Factors to be considered while determining ALP:

a. In the above example, the international transaction is the purchase transaction entered into by AE1 Ltd., with AE2 Ltd. which should be determined on the basis of arm's length price;

Purchase from AE2 Ltd. ⟶ [AE1] ⟶ Sales to A Ltd.

b. The comparable uncontrolled transaction is the purchase transaction entered into by AE1 Ltd., with K Ltd.

Purchase from K Ltd. ⟶ [AE1 Ltd] ⟶ Sales to M Ltd.

c. The starting point for arriving at the ALP of such purchase transaction is the resale price charged to A Ltd. viz. ₹ 3,000 [Rule 10B(1)(b)(i)].

d. From the said resale price, the normal gross profit margin which AE1 Ltd., would earn in a comparable uncontrolled transaction should be reduced. In this example, the actual gross profit margin earned by AE1 Ltd., in respect of its purchase from K Ltd, and its resale to M Ltd, is 15%.

e. The following adjustments are made to arrive at the normal GP;

Actual gross profit margin with M Ltd.		15%
Less:		
1. Difference between Ex-shop and FOR prices	2%	
2. Difference due to quantity discount	1%	3%
Normal gross profit margin with M Ltd.		**12%**

Note: While arriving at normal gross profits from the actual gross profits, only the differences in the sale transactions of AE1 Ltd., with A Ltd., and M Ltd., have been taken. The differences in the purchase transactions of AE1 Ltd., with AE2 Ltd. and K Ltd., affecting the gross profits are taken separately as provided in sub rule (iv).

f. The resale price of ₹ 3,000 to M Ltd., is reduced by the normal gross profit margin of 12%. The resultant cost of sales is ₹ 2,640 (i.e. 3,000 - 360) [Rule 10B(1)(b)(ii)].

g. The cost of sales so arrived at is reduced by the expenses incurred inconnection with the purchase (international transaction) i.e. freight of ₹ 10 and customs duty of ₹ 25. The resultant amount is ₹ 2,605 (i.e. 2640 – 25 - 10) [Rule 10B(1)(b)(iii)].

h. The above amount is further adjusted to take into account functionaland accounting differences between the international transaction and the comparable uncontrolled transaction with AE2 Ltd the purchase transaction with K Ltd., which will affect the amount of gross profit margin as explained below.

i. The aforesaid amount of ₹ 2605 should be increased by ₹ 10 being the freight incurred by AE1 Ltd., in the case of purchase from AE2 Ltd., but not incurred in case of purchase from K Ltd., This is for the reason that if a similar freight had been paid in respect of transaction with K Ltd, the gross profit margin from K Ltd., would have been lower and the resultant price would have been higher.

j. A decrease by ₹ 15 representing the quantity discount allowed by AE2 Ltd., is to be made. This is for the

reason that if a similar discount had been allowed in respect of transaction with K Ltd, the gross profit margin from K Ltd., would have been higher and the resultant price would have been lower.

Determination of arm's length price under resale price method

1. Associated enterprises : AE1 Ltd. and AE2 Ltd.
2. Other enterprises : K Ltd. and M Ltd.
3. International transaction : AE1 Ltd. and AE2 Ltd.
4. Bought from AE2 Ltd. and resold to : A Ltd.
5. CUT is purchase from K Ltd. and sales to M Ltd.

Details	₹ / unit
Price paid to AE2 Ltd.(FOB)	2,900
Quantity	100
Purchases cost (actual) (A)	**2,90,000**
Actual GP Margin on sales to M Ltd.(%)	15
Normal GP Margin on sales to M Ltd.(%)	12
Price charged to A Ltd.	3,000
Less: Normal GP margin	360
Balance	2640
Less: Expenses connected with purchase (freight & customs duty paid)	35
Price before adjustment	2,605
Add:	
Freight incurred in case of purchase from AE2 Ltd.	10
Sub total	10
Less:	
Quantity discount allowed by AE2 Ltd.	15
Sub total	15
Arm's length price	**2,600**
Adjusted purchase cost (B)	**2,60, 000**
Income increases by (A-B)	**30,000**

The following points are to be noticed:

i. The resale price method is to be adopted only when goods purchased from an associated enterprise are resold to unrelated parties.

ii. As provided in Rule 10B(1)(b)(iii), the expenses incurred in connection with the purchase from AE are to be reduced from cost of sales. In resale price method, the arm's length purchase price is arrived at reducing the normal gross profit margin from the resale price as the first step. If the computation is stopped at this step itself, the derived purchase amount would be inclusive of the such expenses. It is therefore necessary to reduce such expenses in arriving at the arm's length purchase price.

iii. Adjustments have to be made also for accounting practices apart from functional and other differences. Differences in accounting practices may be because:

a. sales and purchases have been accounted for inclusive of taxes or exclusive of taxes;

(b) method of pricing the goods namely, FOB or CIF;

(c) fluctuations in foreign exchange.

iv. In actual practice, the resale in any financial year may be also out of opening stock. Similarly, the goods purchased during the said year may remain in closing stock. Under the resale price method, the arm's length price of purchases from AE during the financial year should be determined. The process of determination under Rule 10B(1)(b) culminates in the cost of sales rather than value of purchase during the year. This 'cost of sales' should be converted into 'value of purchase'. For this purpose, the closing stock of goods purchased from AE should be added and the opening stock of purchases from AE should be deducted.

c. cost plus method, by which,—

i. the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise, are determined;

ii. the amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, is determined;

iii. the normal gross profit mark-up referred to in (ii) is adjusted to take into account the functional and other differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market;

iv. the costs referred to in (i) are increased by the adjusted profit mark-up arrived at under (iii);

v. the sum so arrived at is taken to be an arm's length price in relation to the supply of the property or provision of services by the enterprise;

Taxpoint

- Typical transactions where the cost plus method may be adopted are:

(a) provision of services;

(b) joint facility arrangements;

(c) transfer of semi finished goods;

(d) long term buying and selling arrangements.

- The steps involved in the application of this method are:

i. Determine the direct and indirect cost of production in respect of property transferred or service provided to an associated enterprise.

ii. Identify one or more comparable uncontrolled transactions for same or similar property or service.

iii. Determine normal gross profit mark-up on costs in the comparable uncontrolled transaction. Such costs should be computed according to the same accounting norms. In other words, the components of costs of comparable uncontrolled transaction should be the same as those of international transaction.

iv. Adjust the gross profit mark-up to account for functional and other differences between the international transaction and the comparable uncontrolled transaction. Such adjustments should also be made for enterprise level differences.

v. The direct and indirect cost of production in the international transaction is increased by such adjusted gross profit mark-up.

vi. The resultant figure is the arm's length price.

- CPM determines ALP by adding Gross Profit Margin (mark-up) earned in comparable transaction(s) / by comparable companies to the cost incurred by Tested Party under controlled transaction
- CPM is useful when tested party is supplying made-to-order goods (e.g. engineering goods) to its related party
- While RPM focuses on the control of profit margin at the distribution level, CPM focusses on the control of profit mark-up at the manufacturing level.

➢ The application of the cost plus method can be understood with the following example:

AE1 Ltd., is an Indian company. The shareholding pattern of AE1 Ltd., is as follows:

Shareholder's name	Status	% holding
AE2 Ltd.	Foreign Company	30
AE3 Ltd.	Indian Company	30
Financial Institutions	Indian Company	10
Public		30

AE1 Ltd., develops software for various customers, who include AE2 Ltd. and M Ltd.

AE1 Ltd., during the year billed AE2 Ltd. ₹ 2,00,000. The total cost (direct and indirect) for executing this work was ₹ 1,75,000.

AE1 Ltd., provided similar services to M Ltd., and earned a gross profit (GP) of 50% on costs.

Analysis of transactions

	Transactions with AE2 Ltd.	Transactions with M Ltd.
Technology support	Yes	No - value of technology support incurred by AE1 Ltd., is ₹ 17,500
Discount	Yes – Discount offered is ₹ 8,750	No
Business risks and marketing	Yes – Value of the same is estimated at ₹ 13,125	No
Credit	Yes – Cost of credit is estimated at ₹ 2,625	No

Factors to be considered while determining ALP:

a. In the CPM, one has to start with the gross profit mark up which the enterprise earned in a comparable uncontrolled transaction. In this example, the comparable uncontrolled transaction is between AE1 Ltd., and M Ltd.

b. Such gross profit (GP) mark up needs to be decreased by the following:

- As AE1 Ltd., did not receive the technology support from M Ltd., it has priced its services higher resulting in its earning a higher GP with M Ltd.. The value of technology support of ₹ 17,500 received from AE2 Ltd. is 10% of cost. Therefore, the GP with M Ltd., has to be reduced by 10%.
- AE1 Ltd. did not provide discount to M Ltd., as volume of business from M Ltd., was not as high as that from AE2 Ltd. Had AE1 Ltd., offered similar discount to M Ltd., the GP with M Ltd., would have been lower. The discount of ₹ 8,750 offered to AE2 Ltd. is 5% of cost. Therefore, the GP with M Ltd., has to be decreased by 5%.
- AE1 Ltd., has incurred ₹ 15,000 towards marketing functions in respect of its transactions with M Ltd., which is 7.5% of its cost. However, in its transactions with AE2 Ltd. the said functions are assumed by AE2 Ltd. Had AE1 Ltd., not incurred similar expenses with M Ltd., it would have settled for a lower GP. Therefore, the GP with M Ltd., has to be reduced by 7.5%.
- The cost of credit of ₹ 2,625 provided by AE1 Ltd., to AE2 Ltd. is 1.5% of its cost. However, in its transactions with M Ltd., such credit is not provided. Had AE1 Ltd., provided similar credit to M Ltd., it would have increased its price resulting in a higher GP. Therefore, the GP with M Ltd., has to be increased by 1.5%.

c. The resultant gross profit mark up is the arm's length gross profit mark up.

d. The costs of AE1 Ltd., in its transactions with AE2 Ltd. should be increased by the arm's length gross profit mark up to arrive at the arm's length income.

Determination of arm's length price under costs plus method

1. Associated enterprise : AE1 Ltd. and AE2.
2. Other enterprise : AE1 Ltd. and M Ltd
3. International transaction : AE1 Ltd and AE2 Ltd
4. Comparable uncontrolled transaction : AE1 Ltd. and M Ltd

Determination of arm's length gross profit mark up

Details	
Gross profit mark up in case of M Ltd.	50.00%
Less:	
1. Technology support from AE2 Ltd.	10.00%
2. Quantity discount to AE2 Ltd not to M Ltd.	5.00%
3. Marketing functions performed by AE1 Ltd., in respect of M Ltd.	7.50%
Sub total	22.50%
Add:	
1. Cost of credit to AE2. Ltd.	1.50%
Sub total	1.50%
Arm's length gross profit mark up	**29.00%**

Determination of arm's length price

Details	
Direct and indirect costs incurred by AE1 Ltd. in respect of transactions with AE2 Ltd.	1,75,000
Arm's length gross profit mark up	29.00%

Arm's length income (A)	**2,25,750**
Actual price charged to AE2 Ltd. (B)	**2,00,000**
Income increases by (A-B)	**25,750**

The following points are to be noticed:

i. In this method, the direct and indirect costs of production are to be determined. The terms 'direct' or 'indirect' costs are however not defined. A reference may therefore be made to the industry practice as well as the pronouncements of the ICAI

ii. In determining the direct and indirect cost, the following factors have to be borne in mind:

(a) if the plant has been under utilised the costs may have to be suitably adjusted;

(b) absorption costing method is normally to be preferred.

iii. This method is to be adopted only in cases of supply of property or services to an associated enterprise. This method is not to be applied when the enterprise is in receipt of property or services from an associated enterprise.

e. profit split method, which may be applicable mainly in international transactions or specified domestic transactions involving transfer of unique intangibles or in multiple international transactions or specified domestic transactions which are so interrelated that they cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction, by which:

i. the combined net profit of the associated enterprises arising from the international transaction or the specified domestic transaction in which they are engaged, is determined;

ii. the relative contribution made by each of the associated enterprises to the earning of such combined net profit, is then evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances;

iii. the combined net profit is then split amongst the enterprises in proportion to their relative contributions, as evaluated under (ii);

iv. the profit thus apportioned to the assessee is taken into account to arrive at an arm's length price in relation to the international transaction or the specified domestic transaction.

➢ The combined net profit referred to in (i) may, in the first instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction or specified domestic transaction in which it is engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution in the manner specified under (ii) and (iii), and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise on the basis of its relative contribution shall be taken to be the net profit arising to that enterprise from the international transaction or the specified domestic transaction.

Taxpoint

➢ Typical transactions where the profit-split method may be used are transactions involving:

a. integrated services provided by more than one enterprise for e.g., in case of financial service sector, where the activities performed by Indian company and foreign AEs in relation of a merger and acquisition

transaction are so interrelated that it may not possible to segregate them;

b. transfer of unique intangibles, for e.g. two associated enterprises contribute their respective intangibles to develop a new product or process and earn income from such product or process.

- There are two approaches to this method, namely, total profits split and residual profit split.

Total profits split: The steps involved are as follows:

i. Determine the combined net profit of the associated enterprises arising from the international transactions in which they are engaged. Such profits represent the profits earned from third parties due to the combined efforts of the associated enterprises. It may be noted that the 'combined net profit' referred to in the rule is not the aggregate of entire profits earned by the associated enterprises. Example: AE1 may earn profits from certain transactions wherein there is no contribution by AE2 and vice versa. Such profits do not enter into the determination of combined net profit. Only those profits that are earned as a result of joint efforts of AE1 and AE2 should be taken as combined net profit.

ii. Evaluate relative contribution made by each entity involved in the transaction on the basis of:

   a. functions performed;

   b. assets employed;

   c. risks assumed;

   d. the reliable external market data indicating how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances. It may be noted that reference to 'external market data' indicates comparable uncontrolled transactions. The use of word 'external' does not preclude use of internal CUT. In the process of choosing CUTs, the function performed, assets used and risks taken (FAR) of the uncontrolled transactions would have been compared with the FAR of the international transactions. When the FAR of the international transaction and CUT are similar, the relative contribution adopted in the CUT should be applied to the international transaction. Any significant differences between the two should be suitably adjusted.

iii. Thereafter, split the combined net profit in proportion to the relative contribution determined as above.

iv. The profit so apportioned is taken to arrive at the arm's length price in relation to the international transaction. The profits so apportioned to the AE when added to the costs incurred by it in relation to international transaction would result in arm's length price.

Residual profit split approach

- In this approach, firstly, a basic return is determined for each of the enterprises and profits of each such enterprise is ascertained. This amount is reduced from the combined net profits. Residual profits are allocated on the basis of relative contribution.

- Steps involved in this approach are as follows:

i. Determine the combined net profit of the associated enterprises arising from the international transactions in which they are engaged.

ii. At the first stage, depending on functions performed, assets employed and risks assumed, determine the basic return appropriate to the respective activities. Allocate the combined net profit on the basis of above. This step results in a partial allocation of the combined net profit to each enterprise. For this purpose, the allocation is undertaken with reference to margins of comparable uncontrolled entities.

iii. the balance of the combined net profit is allocated on the basis of the evaluation of the relative contribution.

iv. the total net profit from such two-tier allocation is taken to arrive at the arm's length price. The profits so apportioned to the AE when added to the costs incurred by it in relation to international transaction would result in arm's length price.

- PSM is used when transactions are inter-related and is not possible to evaluate separately.
- PSM first identifies the profit to be split for the AE. The profit so determined is split between the AE on the basis of the functions performed
- Division of profit maybe done on Contribution analysis basis or Residual analysis basis.
- Under Contribution analysis, the assessee must use comparable uncontrolled transactions as well as factors such as risks undertaken and assets employed, to determine the division of profit
- Under Residual analysis during division of profit, step 1 involves division of profits to each party upto the extent of just covering the costs incurred in producing the good. Step 2 involves further proportionate distribution of residual profits in accordance with each party's contribution, after carrying out step 1.

➢ The application of the profit split-method can be understood with the following example:

AE1 Ltd., is an Indian company. The shareholding pattern of AE1 Ltd., is as follows;

Shareholder's name	Status	% holding
AE2 Ltd.	Foreign Company	30
AE3 Ltd.	Foreign Company	30
Financial Institutions	Indian Company	10
Public		30

AE1 Ltd., is an investment advisory company, which in association with AE2 Ltd. assists its clients with foreign acquisitions.

AE3 Ltd., which is based in U.S.A., has worldwide presence. AE1 Ltd. is approached by M for identifying potential target companies for acquisitions in the USA. In order to serve M, AE1 Ltd. and AE3 Ltd., have each contributed integrally to identification of potential target and assisting M with the acquisition process. For the above, AE1 Ltd., received consideration of US$ 50,000. The financials are as follows;

	AE1 Ltd.	AE3 Ltd.
Revenue	30,000	20,000
Cost	20,000	8,000
Profit	10,000	12,000

Factors to be considered:

a. The normal basic return is ordinarily calculated as a percentage of the costs incurred or gross revenues or capital employed. In this example, it is assumed as a percentage of the cost.

b. Based on the FAR analysis, the basic return for AE1 Ltd., and AE3 Ltd., are determined to be 15% and 10% respectively. Accordingly, the normal basic return for AE1 Ltd. in India for the aforesaid operation is US$ 3000. The similar returns for AE3 Ltd., US$ 800. The total basic return, thus, is US $ 3,800.

c. On the basis of functions performed, risks assumed and assets employed, the relative contribution may be taken at 70%, 30% for AE1 Ltd. and AE3 Ltd., respectively.

Determination of arm's length price under profit split method:

First Approach: Total Profit Split Method

1. Associated enterprises : AE1 Ltd. and AE3 Ltd.
2. Ultimate delivery of product is : By AE3 Ltd. to M Ltd.
3. International transaction : AE1 Ltd. and AE3 Ltd.

Details	US$
Price charged by AE3 Ltd from M Ltd	50,000
AE3 Ltd share of revenue	20,000
AE1 Ltd share of revenue	30,000
Combined total profits	22,000
Evaluation of relative contribution	
AE1 Ltd : India return – 70%	15,400
AE3 Ltd : US return – 30%	6,600
Total	**22,000**
Total return for AE1 Ltd	15,400
Total cost of AE1 Ltd	20,000
Income of AE1 Ltd on arm's length price (A)	**35,400**
Actual revenue (B)	**30,000**
Increased income (A-B)	5,400

Note: In this example, the basic return is not required to be taken into account.

Second Approach: Residual profit split method

Details	US$
Price charged by AE3 Ltd from M Ltd	50,000
AE3 Ltd share of revenue	20,000
AE1 Ltd share of revenue	30,000
Combined total profits	22,000
1. Basic return	
AE1 Ltd : India return	3,000
AE3 Ltd : US return	800
Total	**3,800**
2. Residual net profit	18,200
AE1 Ltd: India return – 70%	12,740
AE3 Ltd: US return – 30%	5,460
Total	**18,200**

Details	US$
Total return for AE1 Ltd (12740 + 3000)	15,740
Total cost of AE1 Ltd.	20,000
Income of AE1 Ltd. on arm's length price (A)	35,740
Actual revenue (B)	30,000
Increased income (A-B)	**5,740**

The following points are to be noticed:

a. It is the profit from a transaction with the associated enterprise that needs to be ascertained. If there are other transactions, which contribute to the profits, then the profits from transactions with associated enterprise may have to be arrived at on some approximation.

b. The rule itself provides an alternative method to arrive at the arm's length price being the two-tier profit split-method;

c. If in either of the alternatives, a range of figures is available, the arithmetical mean of such figures may be adopted as the arm's length price. It may however not be possible to adopt the arithmetical mean of the two alternatives.

d. Under the two-tier split-method, the basic rate of return may have to be adopted having regard to the profits compared to the net worth of the enterprise. Such rate of return may not be uniform for all the associated enterprises involved in the transaction.

e. This is the only method for which the Rule itself has prescribed the types of transaction to which it may be applicable.

f. Even though the computation proceeds with the profits from a transaction, the purpose is only to arrive at the arm's length price of a transaction. It is only by substituting the arm's length price for the price in the international transaction that an adjustment may be made to the income returned.

e. transactional net margin method, by which,—

i. the net profit margin realised by the enterprise from an international transaction or a specified domestic transaction] entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

ii. the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;

iii. the net profit margin referred to in (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction or the specified domestic transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;

iv. the net profit margin realised by the enterprise and referred to in (i) is established to be the same as the net profit margin referred to in (iii);

v. the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to the international transaction or the specified domestic transaction;

Taxpoint

- Typical transactions where the transactional net margin method may be adopted are:

  (a) provision of services;

  (b) distribution of finished products where resale price method cannot be applied;

  (c) transfer of semi finished goods where cost plus method cannot be applied;

  (d) transactions involving intangibles where profit split method cannot be applied.

- The steps involved in the application of this method are:

  i. Identify the net profit margin realised by the enterprise from an international transaction. Where the assessee also has transactions, segments or businesses where the international transactions with associated enterprises are not relevant, then the net profit margin to be considered for the purposes of this TNMM method should be such net profit margin as is derived only from the transactions, segments or businesses related to the international transaction. The net profit margin may be computed in relation to costs incurred or sales effected or assets employed or any other relevant base.

     For example,

     - In case where the assessee acts as a distributor and the transaction pertains to import, the revenue may be used as base.
     - In case the transaction involves export of services/goods, costs may be taken as base.

  ii. Identify the net profit margin from a comparable uncontrolled transaction or a number of such transactions having regard to the same base; In practice, net profit margin is ascertained at segment level where segment data are available. The unallocated expenses are allocated on a reasonable basis and the segmental net profit is determined. Where segment data are not available, net profit is normally determined at enterprise level. Where internal CUT is available transaction level net profit may be determined.

  iii. In case internal CUT is not available, external CUT is taken. In such case, as discussed above, net profit margin should be taken at enterprise level (segmental or enterprise as a whole) of comparable companies. A search should be carried out to identify comparable companies on the basis of information and data available with the assessee. Where such information and data are not available, search may be carried out with reference to database in public domain.

  iv. The net profit margin so identified is adjusted to take into account the transaction level and enterprise level differences if any. The Methods of Computation of Arm's Length Price differences should be those that could materially affect the net profit margin in the open market;

  iv. The adjusted net profit margin is taken into account to arrive at the arm's length price in relation to the international transaction.

- The application of the transactional net margin method may be understood with the following example:

  AE1 Ltd., is an Indian company

  AE1 Ltd., manufactures compact disc (CD) writers and sells the same to AE2 Ltd., which is an associated enterprise of AE1 Ltd.

  As AE1 Ltd., does not have similar transaction with a non AE, no internal CUT is available. As AE1 Ltd., does

not have information and data to identify a comparable company, it has used the databases in public domain for carrying out the search. The result of the search may be summarised as follows:

		No. of companies
Search on the basis of following keywords:		
(a) Computer		800
(b) Computer hardware		250
(c) Computer peripherals		66
	Sub total	1116
Elimination process :		
Companies with different activities		800
Companies with duplication when multiple database are used		75
Companies with no financials		90
Companies having significant operations like sales or purchases with related party		100
Companies reporting no operations		50
	Sub total	1115
Company/companies selected – Z Ltd.		1

Note: The search criteria and filters adopted above should be taken as illustrative only.

The comparison between AE1 Ltd., and Z Ltd., is carried out as follows:

Financials	AE1 Ltd. (₹ in crores)	Z Ltd. (₹ in crores)
Sales	130	200
Other income	5	10
Total Income	135	210
Operating expenses	85	120
Interest	5	7
Depreciation	10	12
Loss on sale of undertaking	5	0
Expenses relating to non operating income	1	3
Total expenditure	106	142
Net profits	**24**	**58**
Operating margin		
Sales	130	200
Gross revenue	130	200
Operating expenses	85	120
Interest	5	7
Depreciation	10	12
Total operating cost	100	139
Operating profit	**30.00**	**61.00**

Financials	AE1 Ltd. (₹ in crores)	Z Ltd. (₹ in crores)
Operating margin (before interest and depreciation)	52.94	66.67
Operating margin (after depreciation but before interest)	36.84	51.52

- Rule 10B(e)(iii) requires that transaction level and enterprise level differences should be adjusted if such differences materially affect the amount of net profit margin.

  In this example, following enterprise level differences could be visualised;

a. **Working capital –** There may be differences in stock holding, debtors and creditors. Appropriate adjustment to eliminate the impact of above difference may be made by taking the prevailing interest rate. For this purpose, useful reference may be made to the guidelines issued by Internal Revenue Service of USA. However, in this example, it is assumed that the difference in the working capital is not significant requiring any adjustment.

b. **Cost of capital –** There may be difference in the manner of funding such as equity, preference, debenture, inter corporate loans etc. In order that such difference does not impact the net profit, the operating margin on operating cost before interest is taken as profit level indicator.

c. **Assets employed –** There may be difference in assets employed and the method of providing depreciation. In order that such difference does not impact the net profit, the operating margin on operating cost before depreciation is taken as profit level indicator.

d. **Assured or risk bearing business –** There may be a difference in the customer/ revenue model of the assessee vis-à-vis the comparables. For example, the comparables identified may be entrepreneurs bearing the market risks of business volume, customer continuity, etc and the assessee's international transaction is in the nature of captive service provider or contract manufacturer with assured volumes and/or assured compensation and/ or assured business period, etc. Such differences may be eliminated by making appropriate adjustment for low-risk or risk free business.

   In the above table, the transaction level differences cannot be noticed. However, some transaction level differences may exist and the same may be adjusted if requisite information is available. Some of the common transaction level differences may be as follows;

   i. Free gifts

   ii. Extended warranty (in addition to the normal one-year)

   iii. Marketing risks

   iv. Pricing - Ex-Shop or FOR-destination.

   v. Quantity discount

Computation of arm's length price under the transactional net margin method

1. Associated enterprise : AE1 Ltd. and AE2 Ltd.
2. International transaction : AE1 Ltd. and AE2 Ltd.
3. Comparable uncontrolled company : Z Ltd.

	%
Net profit margin of Z Ltd. - i.e. operating margin on cost before interest and after depreciation	51.52

	%
Adjustments for transaction level differences	0.00
Arm's length net profit margin	51.52
	(₹ in crores)
Operating costs before interest and after depreciation	95.00
Arm's length sale revenue	143.94
Actual sales	130.00
Income increases by	**13.94**

The following points are to be noticed:

a. Different bases of determining the net profit margin [i.e. profit level indicators (PLI)] are recognised. The same basis of arriving at the net profit margin is to be adopted year after year, unless circumstances justify an alternate base;

b. Whichever base is selected in determining the net profit margin in an international transaction, the same basis is to be adopted for arriving at the net profit margin in the comparable uncontrolled transaction;

c. It is recommended that operating profit margin may be used instead of net profit margin. Operating profit margin would eliminate the nonoperating items (the items of revenue and costs which do not result from routine business operations such as profit on sale of assets, dividend etc.). Further, the operating profit margins should be computed on the basis of financial statements of the assessee and the comparable company.

d. The accounting treatment of expenses and depreciation is also a critical factor in computing the arm's length price. Unlike the preceding methods, the rule does not explicitly provide for adjustment on account of differing accounting practices. Nevertheless, such differing practices should also be factored in;

e. It is not uncommon to find purchase transaction being an international transaction where TNMM is used. TNMM requires the determination of the net profit margin from an international transaction and purchase transaction as such does not result in net profit. However, as purchase is inextricably linked to earning net profit, TNMM may be used for establishing arm's length purchase value. In such case, comparable operating margin should be appropriately used to work back the arm's length purchase cost. This may be illustrated as follows:

Illustration 1:

1. Actual Profit and loss account of the assessee

	₹ in lakhs		₹ in lakhs
Opening stock-AE purchases	100	Sales of AE purchases	800
Opening stock-Non AE purchases	150	Sales of Non AE purchases	1200
Purchases from AE	500	Closing stock-AE purchases	120
Purchases from Non AE	1000	Closing stock-Non AE purchases	160
Gross profit	530		
	2280		2280
Expenses	200	Gross profit	530
Net profit	330		
	530		530

2. Comparable operating margin (PLI being operating profit on sale): 35%

3. Profit and loss account - recast to compute arm's length price of purchase

	(₹ in lakhs)		(₹ in lakhs)
Opening stock-AE purchases	100	Sales of AE purchases	800
Purchases from AE (balancing figure)	460	Closing stock-AE purchases	120
Gross profit (brought back)	360		
	920		920
Expenses-allocated (in the ratio of sales)	80	Gross profit (worked back)	360
Net profits	280		
(applying TNMM margin on AE sales)			
	360		360

4. Arm's length value of purchase is ₹ 460 as against actual value of ₹ 500. Therefore, income increases by ₹40.

Illustration 2 :

1. Profit and loss account of the assessee – Actual

	₹ in lakhs		₹ in lakhs
Opening stock of raw material (AE purchases)	100	Sale of finished goods	2500
Opening stock of raw material (Non-AE purchases)	150	Closing stock of raw material (AE purchases)	120
Purchases of raw material from AE	500	Closing stock of raw material (Non-AE purchases)	160
Purchases of raw material from Non-AE	1000	Closing stock of finished goods	500
Manufacturing costs	400		
Admin, selling and finance expenses	200		
Net profit	930		
	3280		3280

2. Comparable operating margin (PLI being operating profit on sale): 45%

3. Profit and loss account - recast:

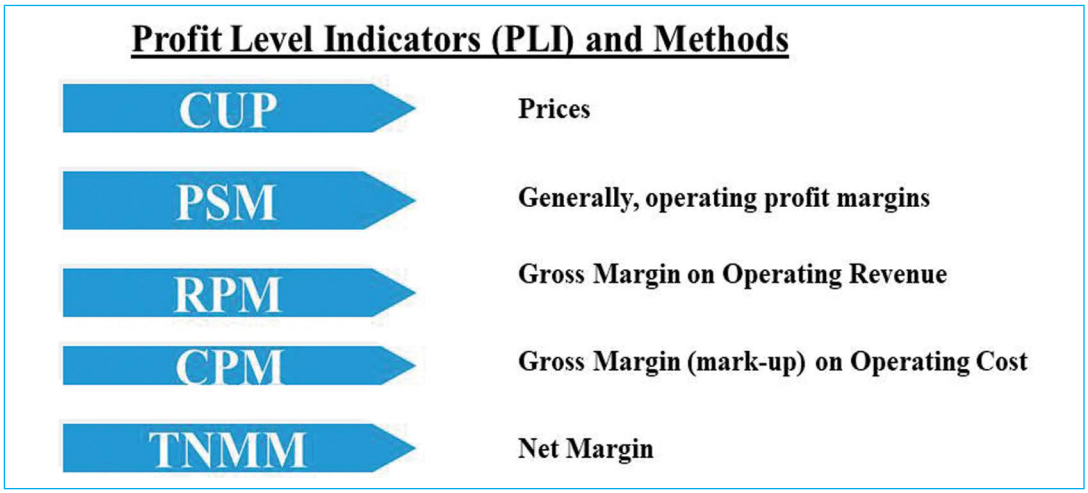
	₹ in lakhs		₹ in lakhs
Opening stock of raw material	150	Sale of finished goods	2500
(Non-AE purchases)			
Cost of purchase from AE (net of stock)	405	Closing stock of raw material	160
(balancing figure)		(Non-AE purchases)	
Purchases of raw material from Non AE	1000	Closing stock of finished goods	500
Manufacturing costs	400		
Admin, selling and finance expenses	200		

	₹ in lakhs		₹ in lakhs
Net profit	1125		
(arrived on basis of TNMM margin)			
	3280		3280
Arm's length Purchase value:			
Cost of purchase from AE (net of stock)			405
Add : Closing stock of Raw Material			120
Add : Closing stock of Raw Material in finished goods (see Note 1 below)			20
Less : Opening stock			100
Arm's length Purchase value			445
Actual purchase			500
Excess price paid			**55**

Notes:

1. In the above illustration, the raw material cost (of purchases from AE) built into closing stock of finished goods is assumed to be ₹ 20.

2. It is assumed that there is no opening stock of finished goods.



f. any other method as provided in rule 10AB.

Taxpoint

The application of the sixth method may be understood with the following examples:

Illustration 3:

AE1 Ltd. is an Indian Company.

AE1 Ltd. owns certain registered patents which it has developed by undertaking research and development.

It is a subsidiary of AE2 Ltd., a foreign company.

AE1 Ltd. has sold its registered patents to AE2 Ltd., for ₹ 50 crores. The price has been determined based on a valuation report obtained from an independent valuer.

The sale of patents is a unique transaction and AE1 Ltd or AE2 Ltd. has not entered into similar transactions with third parties and hence no internal or external CUP is available.

AE1 Ltd. may select the Other Method as the most appropriate method and use the independent valuation report for comparability purposes.

Illustration 4:

An Indian Company (I Co) buys back its equity shares issued to its foreign associated enterprise (AE Co). I Co obtains a valuation report from an external firm identifying the fair market value of these shares. I Co purchases the shares at the value determined in the valuation report. This value denotes a price that would have been charged if a third party would have bought the same shares. Hence, I Co could use Rule 10AB and rely upon the valuation report to demonstrate this transaction to be arm's length.

Illustration 5:

Another example where this method could be used is in cases of cost allocation arrangements where a taxpayer benefits from certain services provided by a central entity of the group and has to pay a portion of the total cost incurred by the service provider. These costs are generally allocated on the basis of allocation keys like headcount, time spent, revenues etc. and a third party outside the group may not have the capability to provide identical services. Hence, in the absence of comparable prices or transactions, Rule 10AB may be applied and the cost allocation arrangement could be justified appropriately.

- For the purposes of aforesaid rule, the comparability of an international transaction or a specified domestic transaction with an uncontrolled transaction shall be judged with reference to the following:

  a. the specific characteristics of the property transferred or services provided in either transaction;

  b. the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;

  c. the contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions;

  d. conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, the laws and Government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail.

- An uncontrolled transaction shall be comparable to an international transaction or a specified domestic transaction if—

  i. none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market; or

  ii. reasonably accurate adjustments can be made to eliminate the material effects of such differences.

- The data to be used in analysing the comparability of an uncontrolled transaction with an international transaction or a specified domestic transaction shall be the data relating to the financial year (hereafter in this rule and in rule 10CA referred to as the 'current year') in which the international transaction or the specified domestic transaction has been entered into.
- In a case where the most appropriate method for determination of the arm's length price of an international transaction or a specified domestic transaction, entered into on or after 01-04-2014, is the method specified in sec. 92C(1)(b), (c) or (e), then, the data to be used for analysing the comparability of an uncontrolled transaction with an international transaction or a specified domestic transaction shall be:

  i. the data relating to the current year; or

  ii. the data relating to the financial year immediately preceding the current, if the data relating to the current year is not available at the time of furnishing the return of income by the assessee, for the assessment year relevant to the current year.

  Where the data relating to the current year is subsequently available at the time of determination of arm's length price of an international transaction or a specified domestic transaction during the course of any assessment proceeding for the assessment year relevant to the current year, then, such data shall be used for such determination irrespective of the fact that the data was not available at the time of furnishing the return of income of the relevant assessment year.

Other method of determination of arm's length price [Rule 10AB]

For the purposes of sec. 92C(1)(f), the other method for determination of the arm's length price in relation to an international transaction or a specified domestic transaction shall be any method which takes into account the price which has been charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts.

Most appropriate method [Rule 10C]

The most appropriate method shall be the method which is best suited to the facts and circumstances of each particular international transaction or specified domestic transaction, and which provides the most reliable measure of an arm's length price in relation to the international transaction or specified domestic transaction. In selecting the most appropriate method, the following factors shall be taken into account:

(a) the nature and class of the international transaction or specified domestic transaction;

(b) the class or classes of associated enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises;

(c) the availability, coverage and reliability of data necessary for application of the method;

(d) the degree of comparability existing between the international transaction or specified domestic transaction and the uncontrolled transaction and between the enterprises entering into such transactions;

(e) the extent to which reliable and accurate adjustments can be made to account for differences, if any, between the international transaction or specified domestic transaction and the comparable uncontrolled transaction or between the enterprises entering into such transactions;

(f) the nature, extent and reliability of assumptions required to be made in application of a method.

Comparison of Methods of computing Arm's Length Price

Methods	Product Comparability	Functional Comparability	Approach	Remarks
CUP	Very High	Medium	Prices are benchmarked	Very difficult to apply as very high degree of comparability required
RPM	High	Medium	GPM (on sales) benchmarked	Difficult to apply as high degree of comparability required
CPM	High	High	GPM (on costs) benchmarked	Difficult to apply as high degree of comparability required
PSM	Medium	Very High	Profit Margins	Complex Method, sparingly used
TNMM	Medium	Very High	Net Profit Margins	Most commonly used Method

Some Important Ratios

Cost Cover Ratio

The cost coverage ratio measures the ability of a company to cover its operating expenses through operating revenue. Given the limitation of financial information publicly available, the operating expenses of a selected comparable company are the sum of its operating revenue less EBIT.

Return on Assets Ratio

The return on assets ratio measures the amount of EBIT per rupee of asset invested. This is a profitability ratio measuring each company's operational efficiency, that is, how efficiently the assets have been deployed by the company.

Berry Ratio

Berry ratio is the ratio of gross profit to operating expenses. It measures the return on operating expenses. As the functions performed by the tax-payers are often reflected in the operating expenses, this ratio determines the relationship of the income earned in relation to the functions performed. This ratio helps in overcoming the difficulties in applying the RPM, which does not explain the creation of gross profit. This ratio is used in conducting an arm's length analysis of service-oriented industry such as limited risk distributor, advertising, marketing and engineering services. The Berry ratio may be used to test whether service providers have earned enough mark-up on their operating expenses. In essence, the Berry ratio implicity assumes that there is a relationship between the level of operating expenses and the level of gross profits earned by routine distributors and service providers.

Annexure 2

Information and documents to be kept and maintained under section 92D [Rule 10D]

1. Every person who has entered into an international transaction or a specified domestic transaction shall keep and maintain the following information and documents:

   a. a description of the ownership structure of the assessee enterprise with details of shares or other ownership interest held therein by other enterprises;

   b. a profile of the multinational group of which the assessee enterprise is a part along with the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom

international transactions or specified domestic transactions, as the case may be, have been entered into by the assessee, and ownership linkages among them;

c. a broad description of the business of the assessee and the industry in which the assessee operates, and of the business of the associated enterprises with whom the assessee has transacted;

d. the nature and terms (including prices) of international transactions or specified domestic transactions entered into with each associated enterprise, details of property transferred or services provided and the quantum and the value of each such transaction or class of such transaction;

e. a description of the functions performed, risks assumed and assets employed or to be employed by the assessee and by the associated enterprises involved in the international transaction or specified domestic transactions;

f. a record of the economic and market analyses, forecasts, budgets or any other financial estimates prepared by the assessee for the business as a whole and for each division or product separately, which may have a bearing on the international transactions or specified domestic transactions entered into by the assessee;

g. a record of uncontrolled transactions taken into account for analysing their comparability with the international transactions or specified domestic transactions entered into, including a record of the nature, terms and conditions relating to any uncontrolled transaction with third parties which may be of relevance to the pricing of the international transactions or specified domestic transactions, as the case may be;

h. a record of the analysis performed to evaluate comparability of uncontrolled transactions with the relevant international transaction or specified domestic transactions;

i. a description of the methods considered for determining the arm's length price in relation to each international transaction or specified domestic transactions or class of transaction, the method selected as the most appropriate method along with explanations as to why such method was so selected, and how such method was applied in each case;

j. a record of the actual working carried out for determining the arm's length price, including details of the comparable data and financial information used in applying the most appropriate method, and adjustments, if any, which were made to account for differences between the international transaction or specified domestic transactions and the comparable uncontrolled transactions, or between the enterprises entering into such transactions;

k. the assumptions, policies and price negotiations, if any, which have critically affected the determination of the arm's length price;

l. details of the adjustments, if any, made to transfer prices to align them with arm's length prices determined under these rules and consequent adjustment made to the total income for tax purposes;

m. any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the arm's length price.

2. Threshold limit in case of international transaction: Nothing contained in sub-rule (1), in so far as it relates to an international transaction, shall apply in a case where the aggregate value, as recorded in the books of account, of international transactions entered into by the assessee does not exceed ₹ 1 crore

However, the assessee shall be required to substantiate, on the basis of material available with him, that income arising from international transactions entered into by him has been computed in accordance with sec. 92.

3. Eligible assessee, on which safe harbour rule applies in respect of specified domestic transaction: Nothing contained in sub-rule (1), in so far as it relates to an eligible specified domestic transaction referred to in rule

10THB, shall apply in a case of an eligible assessee mentioned in rule 10THA and:

a. the eligible assessee, referred to in rule 10THA(i) [i.e., Government company engaged in the business of generation, supply, transmission or distribution of electricity], shall keep and maintain the following information and documents:

   i. a description of the ownership structure of the assessee enterprise with details of shares or other ownership interest held therein by other enterprises;

   ii. a broad description of the business of the assessee and the industry in which the assessee operates, and of the business of the associated enterprises with whom the assessee has transacted;

   iii. the nature and terms (including prices) of specified domestic transactions entered into with each associated enterprise and the quantum and value of each such transaction or class of such transaction;

   iv. a record of proceedings, if any, before the regulatory commission and orders of such commission relating to the specified domestic transaction;

   v. a record of the actual working carried out for determining the transfer price of the specified domestic transaction;

   vi. the assumptions, policies and price negotiations, if any, which have critically affected the determination of the transfer price; and

   vii. any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the transfer price;

b. the eligible assessee, referred to in rule 10THA(ii) [i.e., co-operative society engaged in the business of procuring and marketing milk and milk products], shall keep and maintain the following information and documents:

   i. a description of the ownership structure of the assessee co-operative society with details of shares or other ownership interest held therein by the members;

   ii. description of members including their addresses and period of membership;

   iii. the nature and terms (including prices) of specified domestic transactions entered into with each member and the quantum and value of each such transaction or class of such transaction;

   iv. a record of the actual working carried out for determining the transfer price of the specified domestic transaction;

   v. the assumptions, policies and price negotiations, if any, which have critically affected the determination of the transfer price;

   vi. the documentation regarding price being routinely declared in transparent manner and being available in public domain; and

   vii. any other information, data or document which may be relevant for determination of the transfer price.

4. The information specified in aforesaid rules shall be supported by authentic documents, which may include the following:

   a. official publications, reports, studies and data bases from the Government of the country of residence of the associated enterprise, or of any other country;

b. reports of market research studies carried out and technical publications brought out by institutions of national or international repute;

c. price publications including stock exchange and commodity market quotations;

d. published accounts and financial statements relating to the business affairs of the associated enterprises;

e. agreements and contracts entered into with associated enterprises or with unrelated enterprises in respect of transactions similar to the international transactions [56e][or the specified domestic transactions, as the case may be];

f. letters and other correspondence documenting any terms negotiated between the assessee and the associated enterprise;

g. documents normally issued in connection with various transactions under the accounting practices followed.

Taxpoint

- The information and documents specified under aforesaid rules, should, as far as possible, be contemporaneous and should exist latest by the specified date [i.e., due date u/s 139(1)].
- Where an international transaction or specified domestic transaction continues to have effect over more than one previous years, fresh documentation need not be maintained separately in respect of each previous year, unless there is any significant change in the nature or terms of the international transaction or specified domestic transaction, in the assumptions made, or in any other factor which could influence the transfer price, and in the case of such significant change, fresh documentation shall be maintained bringing out the impact of the change on the pricing of the international transaction or specified domestic transaction.
- Aforesaid information and documents shall be kept and maintained for a period of **8 years** from the end of the relevant assessment year.

Illustration 6:

Brain Inc. London has 35% equity in Salem Ltd. The company Salem Ltd. is engaged in development of software and maintenance of customers across the globe, which includes Brain Inc.

During the year 2023-24, Salem Ltd. spent 2000 men hours for developing and maintaining a software for Brain Inc. and billed at ₹ 1,000 per hour. The cost incurred for executing maintenance work to Brain Inc. for Salem Ltd. amount to ₹ 15,00,000. Similar such work was done for unrelated party Try Ltd. in which the profit was at 50%.

Brain Inc. gives technical support to Salem Ltd. which can be valued at 8% of gross profit. There is no such functional relationship with try Ltd.

Salem Ltd. gives credit period of 90 days the cost of which is 3% of the normal billing rate which is not given to other parties.

Compute ALP under cost plus method in the hands of Salem Ltd. and the impact of the same on the total income.

Solution:

A. Computation of Arms Length Gross Profit Mark-up

Particulars	%
Normal Gross Profit Mark up	50.00
Less: Adjustment for differences	
Technical support from Brain Inc [8% of Normal GP = 8% of 50%]	(4.00)
	46.00
Add: Cost of Credit to Brain Inc 3% of Normal Bill [3% ×GP 50%]	1.50
Arm's Length Gross Profit mark-up	47.50

B. Computation of Increase in Total Income of Brain Inc

Particulars	Amount
Cost of services	15,00,000
Arm's length Billed Value [Cost / [(100 – Arm's Length mark up)] [₹ 15,00,000 / (100% - 47.50%)]	28,57,143
Less: Billed amount [2,000 hours x ₹ 1,000 per hour]	20,00,000
Therefore, Increase in Total Income	**8,57,143**

Illustration 7:

A Co. Ltd. of Chennai and Sky Inc. of Singapore are associate enterprises. A Co. Ltd. imported 1000 television sets at ₹ 16,000 per set without any warranty period. A Co. Ltd. also imports similar TV sets from unrelated party Sign Inc. of Japan. It is imported at ₹ 15,000 per set with warranty time of 2 years. The cost of warranty in respect of goods imported from Sky Inc. for a period of 2 years would cost ₹ 2,000.

Compute arm's length price and the amount of increase in total income of A Co. Ltd. as per CUP method.

Solution:

A. Computation of Arms Length Price

Particulars	Amount
Cost of TV Set acquired from Sign Inc	15,000
Less: Cost of Warranty	2,000
Arm's Length Gross Profit mark-up	13,000

B. Computation of Increase in Total Income

Particulars	Amount
Cost of TV Set acquired from Sky Inc [₹ 16,000 * 1,000]	1,60,00,000
Less: Arm's length Value [₹ 13,000 * 1,000]	1,30,00,000
Therefore, Increase in Total Income	**30,00,000**

Illustration 8:

J Inc. of Korea and CD Ltd, an Indian Company are associated enterprises. CD Ltd manufactures Cell Phones and sells them to J.K.& F Inc., a Company based in Nepal. During the year CD Ltd. supplied 2,50,000 Cellular Phones to J Inc. Korea at a price of ₹ 3,000 per unit and 35,000 units to JK & F Inc. at a price of ₹ 5,800 per unit. The transactions of CD Ltd with JK & F Inc. are comparable subject to the following considerations:

Sales to J Inc. are on FOB basis, sales to JK & F Inc. are CIF basis. The freight and insurance paid by J Inc. for each unit @ ₹ 700. Sales to JK & F Inc. are under a free warranty for Two Years whereas sales to J Inc. are without any such warranty. The estimated cost of executing such warranty is ₹ 500. Since J Inc.'s order was huge in volume, quantity discount of ₹ 200 per unit was offered to it.

Compute the Arm's Length Price and the subsequent amount of increase in the Total Income of CD Ltd, if any.

Solution:

Computation of Arm's Length Price of Products sold to J Inc. Korea by CD Ltd

Particulars	₹	₹
Price per Unit in a Comparable Uncontrolled Transaction		5,800
Less: Adjustment for Differences -		
(a) Freight and Insurance Charges	700	
(b) Estimated Warranty Costs	500	
(c) Discount for Voluminous Purchase	200	(1,400)
Arms's Length Price for Cellular Phone sold to J Inc. Korea		**4,400**

Computation of Increase in Total Income of CD Ltd

Particulars	₹
Arm's Length Price per Unit	4,400
Less: Price at which actually sold to J Inc. Korea	(3,000)
Increase in Price per Unit	1,400
No. of Units sold to J Inc. Korea	2,50,000
Increase in Total Income of CD Ltd (2,50,000 x ₹ 1,400)	₹ 35 Crores

Illustration 9: Comparable sales of same product

DSM, a manufacturer, sells the same product to both controlled and uncontrolled distributor. The circumstances surrounding the controlled and uncontrolled transactions are substantially the same, except that the controlled sales price is a delivered price to the buyer and the uncontrolled sales are made F.O.B. DSM's factory. Differences in the contractual terms of transportation and insurance generally have a definite and reasonably ascertainable effect on price, and adjustments are made to the results of the uncontrolled transaction to account for such differences. In this case the transactions are comparable and internal CUP can be applied by comparing the prices of both, the controlled and uncontrolled transactions, albeit after subtracting the costs of transportation and insurance of the controlled transaction.

Illustration 10: Effect of geographic differences

FM, a foreign specialty radio manufacturer, also exports its radios to a controlled U.S. distributor, AM, which serves the United States. FM also exports its radios to uncontrolled distributors to serve in South America. The product in the controlled and uncontrolled transactions is the same, and all other circumstances surrounding the

controlled and uncontrolled transactions are substantially the same, other than the geographic differences. The geographic differences e.g. differences in purchasing power, levels of economic development, etc, in two different geographies, are likely to have a material effect on price, for which accurate adjustments cannot be made and hence the transactions are not comparable. Thus, CUP method cannot be applied.

Illustration 11: External Commercial Borrowing

Pharma Ltd, an Indian company has borrowed funds from its parent company at LIBOR plus 150 basis points. The LIBOR prevalent at the time of borrowing is 4% for US$, thus its cost of borrowings is 5.50%. The borrowings allowed under the External Commercial Borrowings guidelines issued under FEMA, for example, say is LIBOR plus 250 basis points, then it can be said that Pharma's borrowing at 5.50% is less than 6.50% and thus at arm's length. In this connection, one may rely on Rule 10B (2) (d) which specifies that the comparability of an international transaction with an uncontrolled transaction shall be judged with reference to the laws and government orders in force.

Illustration 12:

Megabyte Inc. of France and R Ltd. of India are associated enterprises. R Ltd. imports 3,000 compressors for Air Conditioners from Megabyte Inc. at ₹ 7,500 per unit and these are sold to Pleasure Cooling Solutions Ltd at a price of ₹ 11,000 per unit. R Ltd. had also imported similar products from Cold Inc. Poland and sold outside at a Gross Profit of 20% on Sales. Megabyte Inc. offered a quantity discount of ₹ 1,500 per unit. Cold Inc. could offer only ₹ 500 per unit as Quantity Discount. The freight and customs duty paid for imports from Cold Inc. Poland had cost R Ltd. ₹ 1,200 per piece. In respect of purchase from Terabyte Inc., R Ltd. had to pay ₹ 200 only as freight charges. Determine the Arm's Length Price and the amount of increase in Total Income of R Ltd.

Solution:

Computation of Arm's Length Price

Particulars	Amount
Resale Price of Goods Purchased from Megabyte Inc.	11,000
Less: Adjustment for Differences –	
a) Normal Gross Profit Margin at 20% of Sale Price [20% x ₹ 11,000]	2,200
b) Incremental Quantity Discount by Megabyte Inc. [₹ 1,500 – ₹ 500]	1,000
c) Difference in Purchase related expenses [₹ 1,200 – ₹ 200]	1,000
Arms Length Price	**6,800**

Computation of Increase in Total Income of R Ltd

Particulars	Amount
Price at which actually bought from Megabyte Inc. of France	7,500
Less: Arms Length Price per unit under Resale Price Method	6,800
Decrease in Purchase Price per unit	**700**
No. of units purchased from Megabyte Inc.	3,000 units
Increase in Total Income (3,000 units x ₹ 700)	₹ 21,00,000

Illustration 13:

NBR Medical Equipments Inc. (NBR) of Canada has received an order from a leading UK based Hospital for development of a hi-tech medical equipment which will integrate the best of software and latest medical examination tool to meet varied requirements. The order was for 3,00,000 Euros. To execute the order, NBR joined hands with its subsidiary Precision Components Inc. (PCI) of USA and Bioinformatics India Ltd (BIL), an Indian Company. PCI holds 30% of BIL. NBR paid to PCI and BIL Euro 90,000 and Euro 1,00,000 respectively and kept the balance for itself. In the entire transaction, a profit of Euro 1,00,000 is earned. Bioinformatics India Ltd incurred a Total Cost of Euro 80,000 in execution of its work in the above contract. The relative contribution of NBR, PCI and BIL may be taken at 30%, 30% and 40% respectively. Compute the Arm's Length Price and the incremental Total Income of Bioinformatics India Ltd, if any due to adopting Arms Length Price determined here under.

A	Share of each of the Associates in the Value of the Order	**3,00,000**
	Share of BIL [Given]	1,00,000
	Share of PCI [Given]	90,000
	Share of NBR [Amount Retained = 3,00,000 – 1,00,000 - 90,000]	1,10,000
B	**Share of each of the Associates in the Profit of the Order**	
	Combined Total Profits	**1,00,000**
	Share of BIL [Contribution of 40% x Total Profit € 1,00,000]	40,000
	Share of PCI [Contribution of 30% x Total Profit € 1,00,000]	30,000
	Share of NBR [Contribution of 30% x Total Profit € 1,00,000]	30,000
C	**Computation of Incremental Total Income of BIL**	
	Total Cost to BIL Ltd	80,000
	Add: Share in the Profit to BIL (from B above)	40,000
	Revenue of BIL on the basis of Arm's Length Price	1,20,000
	Less: Revenue Actually received by BIL	1,00,000
	Increase in Total Income of BIL	20,000

Illustration 14:

lndco, an Indian company, has developed and manufactures a robot to be used for multiple industrial applications. The robot is considered to be an innovative technological advance. Chco, a Chinese subsidiary of Indco, has developed and manufactures a software programme which incorporates the new programme in the robot and makes it more effective. The success of the robot is attributable to both companies for the design of the robot and the software programme.

Indco manufactures and supplies Chco with the robot for installing of the new software programme for assembly and manufacture of the robot. Chco manufactures the robot and sells to an arm's length distributor.

In light of the innovative nature of the robot and software, the group was unable to find comparables with similar intangible assets. Because they were unable to establish a reliable degree of comparability, the group was unable to apply the traditional transaction methods or the TNMM.

However, reliable data are available on robot and software manufacturers without innovative intangible property, and they earn a return of 10% on their manufacturing costs.

The total profits attributable to manufacture of robots are calculated as follows:

Particulars	Amount	Amount
Sales to the arm's length distributor		1,000
Less:		
Indco's manufacturing costs	200	
Chco's manufacturing costs	300	
Total manufacturing costs for the group		500
Gross Margin		500
Less:		
Indco's development costs	100	
Chco's development costs	50	
Indco's operating costs	50	
Chco's operating costs	100	300
Net profit		200
Indco's return to manufacturing (200 x 10%)	20	
Chco's return to manufacturing (300 x 10%)	30	50
Residual profit attributable to development		**150**

The split of the residual profit has been considered on the basis of the development cost considering the significance of technology in the manufacturing process.

Based on proportionate development costs

Particulars	Amount
Indco's share of residual profit [100/)100+50)] x 150	100
Chco's share of residual profit [50/(100+50)] x 150	50

Indco's transfer price is calculated as follows:

Particulars	Amount
Manufacturing costs	200
Development costs	100
Operating costs	50
Routine 10% return on manufacturing costs	20
Share of residual profit	100
Transfer price	**470**

Illustration 15:

Fox Solutions Inc. a US Company, sells Laser Printer Cartridge Drums to its Indian Subsidiary Quality Printing Ltd at S 20 per drum. Doc Solutions Inc. has other takers in India for its Cartridge Drums, for whom the price is $ 30 per drum. During the year, Fox Solutions had supplied 12,000 Cartridge Drums to Quality Printing Ltd.

Determine the Arm's Length Price and taxable income of Quality Printing Ltd if its income after considering the above is ₹ 45,00,000. Compliance with TDS provisions may be assumed and Rate per USD is ₹ 45. Also determine income of Doc Solutions Inc.

Solution:

Computation of Total Income of Quality Printing Ltd.

Particulars	Amount	Amount
Total Income before adjusting for differences due to Arm's Length Price	1,08,00,000	
Add: Difference on Account of adopting Arm's Length Price [12,000 x $20 x ₹ 45]	1,62,00,000	
Less: Amount under Arm's Length Price [12,000 x $ 30 x ₹ 45]	(54,00,000)	45,00,000
Incremental Cost on adopting ALP u/s 92(3), Taxable Income cannot be reduced on applying ALP. Therefore, difference on account of ALP is ignored.		
Total Income of Quality Printing Ltd.		**45,00,000**

Computation of Total Income of Fox Solutions Inc.

The provisions relating to taxing income of Fox Solutions Inc., on applying Arm's Length Price for transactions entered into by a Foreign Company is given in Circular 23 dated 23.7.1969, which is as follows:

i Transactions Not Taxable in India: Transactions will not be subject tax in India if transactions are on principal-to-principal basis and are entered into at ALP, and the subsidiary also carries on business on its own.

ii Transactions Taxable in India if the Indian Subsidiary does not carry on any business on its own. The following are the other considerations in this regard:

   a. Adopting ALP does not affect the computation of taxable income of Fox Solutions Inc. if tax has been deducted at source or if tax is deductible.

   b. Where ALP is adopted for taxing income of the Parent Company, income of the recipient Company (i.e. Quality Printing Ltd) will not be recomputed.

Illustration 16:

Khazana Ltd is an Indian Company engaged in the business of developing and manufacturing Industrial components. Its Canadian Subsidiary Techpro Inc. supplies technical information and offers technical support to Khazana for manufacturing goods, for a consideration of Euro 1,00,000 per year. Income of Khazana Ltd is ₹ 90 Lakhs. Determine the Taxable Income of Khazana Ltd if Techpro charges Euro 1,30,000 per year to other entities in India. What will be the answer if Techpro charges Euro 60,000 per year to other entities. (Rate per Euro may be taken at ₹ 50.)

Solution:

Computation of Total Income of Khazana Ltd

Particulars	Amount	Amount
When price charged for Comparable Uncontrolled Transaction	€ 1,00,000	€ 50,000
Price actually paid by Khazana Ltd [€1,00,000 x ₹ 50]	50,00,000	50,00,000
Less: Price charged in Rupees (under ALP)		
[€1,30,000 x ₹ 50]	65,00,000	
[€60,000 x ₹ 50]		30,00,000
Incremental Profit on adopting ALP (A)	(15,00,000)	20,00,000

Particulars	Amount	Amount
Total Income before adjusting for differences due to Arm's Length Price	90,00,000	90,00,000
Add: Difference on account of adopting Arms Length Price [if (A) is positive]	NIL	20,00,000
Total Income of Khazana Ltd.	**90,00,000**	**1,10,00,000**

Note: u/s 92(3), Taxable Income cannot be reduced on applying ALP. Therefore, difference on account of ALP which reduces the Taxable Income is ignored.

Illustration 17:

Videsh Ltd., a US company has a subsidiary, Hind Ltd. in India. Videsh Ltd. sells mobile phones to Hind Ltd. for resale in India. Videsh Ltd. also sells mobile phones to Bharat Ltd. another mobile phone reseller. It sold 48,000 mobile phones to Hind Ltd. at ₹ 12,000 per unit. The price fixed for Bharat Ltd. is ₹ 11,000 per unit. The warranty in case of sale of mobile phones by Hind Ltd. is handled by itself, whereas, for sale of mobile phones by Bhart Ltd., Videsh Ltd. is responsible for warranty for 6 months. Both Videsh Ltd. and Hind Ltd. extended warranty at a standard rate of ₹ 500 per annum.

On the above facts, how is the assessment of Hind Ltd. going to be affected?

Solution:

Computation of Arms Length Price

Particulars	Amount
Cost of Mobile Phone sold to Bharat Ltd.	11,000
Less**:** Cost of Warranty	250
Arm's Length Price	10,750

Computation of Increase in Total Income

Particulars	Amount (₹) (in lacs)
Cost of mobile phone acquired from Videsh Ltd. [₹ 12,000 * 48,000]	5,760
Less: Arm's length Value [₹ 10,750 x 48,000]	5,160
Therefore, Increase in Total Income	600

Illustration 18:

ABC India Limited ('the Company') is engaged in the business of import and sales of computers, laptops & printers. The company is a 100% subsidiary ABC Inc., USA. The company purchases laptops from ABC Inc., USA at negotiated rates and sells to independent customers in India under its own terms and conditions.

The company also trades in computers and printers which it procures from independent vendors in USA and sell to its own customers in India under its own terms and condition.

Below is the profit and loss account of the company.

Particulars	₹	Particulars	₹

Particulars	₹	Particulars	₹
Opening stock		Sales	
- Computers	500	- Computers	8,000
- Printers	200	- Printers	2,000
- Laptops	800	- Laptops	11,000
Purchases (Imports)		Closing Stock	
- Computers	5,000	- Computers	800
- Printers	1,300	- Printers	250
- Laptops	6,000	- Laptops	1,200
Gross profit c/f	9,450		
	23,250		**23,250**
		Gross profit c/f	9,450
Salary	2,000		
Rent	1,000		
Fright Outward	250		
Travel and Conveyance	300		
PBITD	5,900		
	9,450		**9,450**

Other relevant information:

1. Credit period of 2 months is allowed for customers of computers and printers and hence 2% extra margin towards interest cost is factored in sale price.
2. Purchase of materials accounted at landed costs. It is estimated that around 20% of the purchase cost reported in P&L is towards customs duty and clearing charges.
3. Delivery of computers and printers made at company's cost. For laptop, the customers collect the goods for company premises.
4. For laptop purchases, the company has incurred ocean freight (around ₹300) whereas for computer and printers the terms of import are CIF, Chennai.

Question and Solution

1. Identify the Associated Enterprise in the scenario?

Ans: ABC Inc., USA by virtue of ownership criteria.

2. Identify the International transaction?

Ans: Purchase of the laptop during the year of ₹4,800 (₹6,000 less 20%)

3. Which is the comparable uncontrolled transaction here?

Ans: Sale of computers and printers (since they are similar product to laptops), procured from, as well as sold to independent parties.

4. What is the normal gross profit margin on the comparable transactions?

Ans:

	₹
Gross profit as per trading account [8,000 + 2,000 + 800 + 250 – 500 – 200 – 5,000 – 1,300]	4,050
Less: Interest elements factored in sale price [2% of [8,000 + 2,000]	200
Less: Fright outward costs	250
Normal gross profit	3,600
Normal gross profit percentage [3,600 / 10,000 x 100]	36%

At this stage, the difference in the terms of sales transactions of computers and printers vis-a-vis the sale transactions of laptops are considered. The difference in terms of purchase will be adjusted in subsequent stage.

5. What is the price of laptop being purchased from the AE, is resold to unrelated enterprise?

Ans: ₹11,000

6. What is the resultant cost of sales after deducting 'Normal Gross Profit Margin'

Ans: ₹7,040 (i.e. ₹11,000 less 36% Normal Gross Profit Margin)

7. What are the expenses incurred in connection with purchase?

Ans: ₹1,200 (since it is mentioned that around 20% of the purchase cost reported in P&L is toward freight, customs duty and clearance charges)

8. What are the functional difference, including accounting practices, between the international transaction and the comparable uncontrolled transaction, which could materially affect the amount of gross profit margin?

Ans: ₹300 on account of ocean freight

9. What is the cost of sale after adjustment made as per 7 & 8 above?

Ans: ₹5,540 (i.e. ₹7,040 less ₹1,200 less ₹300)

10. How is the arm's length purchase price determined?

Ans:

Price as arrived at 9 above		₹5,540
Add: Amount in closing stock (80% of ₹1200)	₹ 960	
		₹6,500
Less: Amount in opening stock (80% of ₹800)		₹640
Arm's length price of purchase		₹5,860

11. Is the purchase price at arm's length?

Ans: Yes. Since the purchase price is ₹4,800 is less than arm's length price determined at ₹5,860.

Illustration 19:

Compute arm's length price from following information

Particulars	Related Party	Unrelated Party
Price paid (inclusive of taxes)	INR 25,000	INR 23,500
Delivery terms	CIF	FOB
Quantity	100 pcs	110 pcs
Availability of Input Tax Credit	No	Yes
Quantity	100 pcs	110 pcs
Freight cost	-	INR 1,200
Insurance cost	-	INR 700
Input Tax Credit	-	INR 2,000

Solution:

Computation of ALP

Particulars	Amount
Price paid to unrelated party (inclusive of taxes)	INR 23,500
Adjustments of differences -	
Delivery terms – Freight cost	INR 1,200
Delivery terms – Insurance cost	INR 700
Quantity	-
Input tax credit available	(INR 2000)
Arm's Length Price	INR 23,400

Illustration 20:

Compute arm's length price from following information

Particulars	Related Party	Unrelated Party
Price paid (inclusive of taxes)	INR 25,000	INR 23,500
Delivery terms	CIF	FOB
Quantity	100 pcs	110 pcs
Availability of Input Tax Credit	No	Yes
Quantity	100 pcs	110 pcs
Freight cost	-	INR 1,200
Insurance cost	-	INR 700
Input Tax Credit	-	INR 2,000
Credit period	90 days	Upon dispatch
Interest rate on working capital	12% p.a.	-

Solution:

Computation of ALP

Particulars	Amount
Price paid (inclusive of taxes)	INR 23,500
Adjustments of differences	
Delivery terms – Freight cost	INR 1,200
Delivery terms – Insurance cost	INR 700
Input Tax Credit available	(INR 2000)
Credit period (Interest on INR 23,500 for 3 months @ 12% p.a.)	INR 705
Arm's length price	INR 24,105

Illustration 21:

Compute ALP through following information:

- A Ltd. is a distributor of IT products.
- A Ltd. purchases these products from its related party, P Ltd.
- A Ltd. also trades in laptops manufactured by X Ltd.
- P Ltd as well as X Ltd would supply the warranty replacements free of cost to A Ltd.
- Other details are as under:

Particulars	P Ltd (AE)	X Ltd
Purchase price of A Ltd.	INR 15,000	INR 22,000
Sale price of A Ltd	INR 18,000	INR 26,000
Other expenses incurred by A Ltd	INR 500	INR 700

Solution:

Computation of gross profit margin on unrelated transaction

Particulars	Amount (INR)
Sale price of laptop in India	26,000
Expenses incurred by A Ltd	700
Net Sale proceeds of laptop in India [A]	25,300
Purchase price [B]	22,000
Gross profit [A - B]	3,300
GP on sale (%)	12.69%

Computation of arm's length price

Particulars	Amount
Sales price of desktop in India	18,000
Less: Expenses incurred by A ltd	500

Particulars	Amount
Less: Arm's length resale margin @ 12.69 % of sale	2,284
Arm's length purchase price	**15,216**
Purchase price paid to AE	**15,000**

Thus, no adjustment is required.

Illustration 22:

A sold a machine to B (associated enterprise) and in turn B sold the same machinery to C (an independent party) at sale margin of 30% for ₹ 4,00,000 but B has incurred ₹ 4,000 in sending the machine to C. From the above data, determine arm's length price.

Solution:

Computation of Arm's Length Price

Particulars	Details	Amount
Sales price to B		4, 00,000
Less: Gross Margin	4,00,000 × 30%	1, 20,000
Balance		2, 80,000
Less: Expenses incurred by B		4,000
Arm's length price		2,76,000

Emerging Transfer Pricing challenges in India

Transfer Pricing Regulations in India

The Indian TP regulations are based on arm's length principle. The regulations came into effect from 1 April, 2001. The regulations provide that any income arising from an international transaction between associated enterprises shall be computed having regard to the arm's length price (ALP). The concept of associated enterprises has been defined in detail in the regulations. The regulations do not provide any hierarchy of the Arm's Length Methods and support concept of "most appropriate method" which provide the most reliable measure of an arm's length result under a particular set of facts and circumstances. The regulation prescribes mandatory annual filing requirements as well as maintenance of contemporaneous documentation by the taxpayer in case international transactions between associated enterprises cross a threshold and contains stringent penalty implications in case of non-compliance. The primary onus of proving arm's length price of the transaction lies with the taxpayer. Indian transfer pricing administration prefer Indian comparables in most of the cases and also accept foreign comparables in cases where foreign associated enterprises is less or least complex entity and requisite information are available about tested party and comparables. In order to provide uniformity in application of transfer pricing law there is a specialized Directorate of transfer pricing to administer transfer pricing rule under supervision of Director General of Income tax (International Taxation). Transfer Pricing officers (TPO) are vested with powers of inspection, discovery, enforcing attendance, examining a person under oath, on-the-spot enquiry/verification and compelling the production of books of account and other relevant documents during the course of a transfer pricing audit. A dispute resolution panel (in short DRP) is available to taxpayer to resolve disputes relating to transfer pricing before disputes of final order by Assessing Officer, (which incorporates the order of TPO).

Key Current and Emerging TP Audit Issues in India

Indian transfer pricing administration over the past 10 years has witnessed several challenges in administration of transfer pricing law. Following are some of the emerging transfer pricing issues and difficulties in implementation of arm's length principle:

1. Challenges in the comparability analysis

India believes that comparability analysis is key to determine arm's length price of international transaction. However, increased market volatility and increased complexity in international transaction have thrown open serious challenges to comparability analysis and determination of arm's length price. Some of these challenges and responses of Indian transfer pricing administration in dealing with these challenges are as under:

a. Use of contemporaneous data: Commodity price volatility, debt, recession and worries have brought volatility to world market. The volatility impede a stable business environment and result in fluctuation in margins of MNEs and their subsidiaries. In this context, use of contemporaneous comparables provides a more accurate arm's length price in a particular year.

b. Application of data rules: The Indian transfer pricing regulation stipulates that data to be used in analyzing the comparability of uncontrolled transaction with an international transaction should be the data relating to the financial year in which international transactions have been entered into. However, the rule also provides exception and permits use of data for the preceding two years if and only if, it is proved that such data reveals a fact which could have an influence on the determination of arm's length price. Therefore, the exception comes into the play only when a proof that earlier year data could have an influence on determination of arm's length price is brought on the record.

c. Rationale: The mandatory requirement under the law to use contemporaneous document has a solid economic sense in the way that contemporaneous transaction reflect similar economic condition. Therefore, use of current year data is more relevant and appropriate for ensuring a higher degree of comparability of uncontrolled transaction for arriving at arm's length price in respect of international transaction. In India, contemporaneous data which may be available to the taxpayer and tax administration at the time of filing of the tax return or conducting ex post facto analysis of transfer pricing studies cannot be held as use of hindsight.

2. Issue relating to risks

a. A comparison of functions performed, assets employed and risks assumed is basic to any comparability analysis. India believes that the risk of a MNE is a by-product of performance of functions and ownership, exploitation or use of assets employed over a period of time. Accordingly, risk is not an independent element but is similar in nature to functions and assets. In this context, India believes that it is unfair to give undue importance to risk in determination of arm's length price in comparison to functions performed and assets employed.

b. Identification of risk and the party who bears such risks are important steps in comparability analysis. India believes that the conduct of the parties is key to determine whether the actual allocation of risk conforms to contractual risk allocation. Allocation of risk depends upon ability of parties to transaction to exercise control over risk. Core functions, key responsibilities, key decision making and level of individual responsibility for the key decisions are important factors to identity party which has control over the risks.

c. In India, MNEs are making claims before the transfer pricing auditor that related parties engaged in contract R&D or other contract services in India are risk free entities. Accordingly, these related parties are entitled to only routine (low) cost plus remuneration. MNEs also contend that the risks of R&D activities or services are being controlled by them and Indian entities being risk free entities are entitled to (low) cost plus remuneration.

d. The Indian transfer pricing administration does not agree with the notion that risk can be controlled remotely by the parent company and that the Indian subsidiaries or related party engaged in core functions, such as carrying out research and development activities or providing services are risk free entities. India believes that core function of R&D or services are located in India which in turn require important strategic decisions by management and employees of Indian subsidiaries or related party to design, direction of R&D activities or providing services and monitoring of R&D activities etc. Accordingly, the Indian subsidiary exercises control over the operational and other risks. In these circumstances, the ability of the parent company to exercise control over the risk - remotely and from a place where core functions of R&D and services are not located - is very limited. In these circumstances, allocation of risk to the parent MNE is not only questionable but is devoid of logical conclusion.

e. India believes that the subsidiary carries out core functions and by taking strategic operational decisions controls a substantial part of risk. India believes that the parent company should be entitled to appropriate returns for provision of funds and overall direction to R&D activity or services. The Indian subsidiary should also similarly be entitled to returns on their core function including strategic decisions and control on risk related to operation of R&D activities. In this context, Indian tax administration is of the view that allocation of routine cost plus return in these cases will not reflect a true arm's length price of the transaction.

3. Arm's length range

Application of most appropriate method may set up comparable data which may result in computation of more than one arm's length price. Where there may be more than one arm's length price, mean of such prices is considered. Indian transfer pricing regulations provide that in such a case the arithmetic mean of the prices should be adopted as arm's length price. If the variation between the arithmetic mean of uncontrolled prices and price of international transaction does not exceed 3% or notified percentage of such transfer pricing, then transfer price will be considered to be at arm's length. In case transfer price crosses the tolerance limit, the adjustment is made from the central point determined on the basis of arithmetic mean. Indian transfer pricing regulation do not mandate use of inter quartile range.

4. Comparability adjustment

a. Like many other countries, Indian transfer pricing regulations provide for "reasonably accurate comparability adjustments". The onus to prove "reasonably accurate comparability adjustment" is on the taxpayer. The experience of Indian transfer pricing administration indicates that it is possible to address the issue of accounting difference and difference in capacity utilization and intensities of working capital by making comparability adjustments. However, Indian transfer pricing administration finds it extremely difficult to make risk adjustments in absence of any reliable and robust and internationally agreed methodology to provide risk adjustment. In some cases taxpayers have used Capital Asset Pricing Method (CAPM). However, the methodology was found flawed for the reasons outlined in the following paragraphs

b. The CAPM model assumes that most assets rate of return within a portfolio are normally distributed (meaning rates of return do not deviate too much from the mean). However, historically speaking, equities have been prone to large deviations from the mean much more frequently than it is generally assumed under the CAPM model. So, if an asset is actually prone to large swings in either direction from its mean, then it stands to reason that its risk aspect may not be correctly captured by the CAPM calculation.

c. Capital asset pricing model is not able to capture all variations in equity returns in same industry segment. Past empirical studies have demonstrated that some stocks, although they had lower beta and implied lower risk vs. return ratio, still managed to pull off higher returns than the CAPM model would have assumed initially.

d. On a more practical level, one of the shortfalls of CAPM is that the model assumes all investors have the same ideas of what constitutes risk and required rates of return, as well as the fact that the model excludes the impact of taxes and transaction costs which, in reality, have adverse impact on the expected rate of return.

e. The CAPM assumes the application of the market portfolio, which is supposed to consist of all risky assets in all markets. The CAPM also assumes that investors have no individual preference as to which risky assets they wish to invest in and in which markets. Yet, investors have been known to depart from assets 'risk vs. return profiles often and particularly at times when markets were not normally distributed.

f. The CAPM accepts the concepts of the market portfolio, which theorizes inclusion of literally all asset classes, including real estate, art intellectual property etc. However, in reality such a market portfolio is impossible to construct which is why it is often equated with various composites. However, limiting the market portfolio in such a manner could and it indeed has created fallacies within the CAPM model, thus rendering it at the very least empirically inconsistent.

g. An important flaw relating to the computation of risk adjustment by the taxpayer is use of the "Beta" concept. It is important to remember that computation of beta is based on a presumption that high-beta shares usually give the highest returns. Over a long period of time, however, high beta shares are the worst performers during market declines (bear market) which are more common phenomena in Indian stock exchange. While someone might receive high returns from high beta shares, there is no guarantee that the CAPM return is realized. It is worthwhile to mention here that the computation of beta in this case is based on seven year average price of comparables and tested party shares; the methodology of taking an average of such a long period is highly questionable in existing volatile world market conditions.

h. The Indian tax administration has also experienced difficulties in getting reliable data for computation of comparability adjustments like capacity and working capital adjustments, where methodology to provide comparability adjustment is more or less internationally agreed.

5. Location Savings

a. It is view of the Indian transfer pricing administration that the concept of "location savings" - which refer to cost savings in a low cost jurisdiction like India – should be one of the major aspects to be considered while carrying out comparability analysis during transfer pricing audits. Location savings has a much broader meaning; it goes beyond the issue of relocating a business from a 'high cost' location to a 'low cost' location and relates to any cost advantage. MNEs continuously search options to lower their costs in order to increase profits. India provides operational advantages to the MNEs such as labour or skill employee cost, raw material cost, transaction costs, rent, training cost, infrastructure cost, tax incentive etc. It has also been noticed that India also provides following Location Specific Advantages (LSAs) to MNE in addition to location savings:

- Highly specialized skilled manpower and knowledge
- Access and proximity to growing local/regional market
- Large customer base with increased spending capacity
- Superior information network
- Superior distribution network
- Incentives
- Market premium

b. The incremental profit from LSAs is known as "location rents". The main issue in transfer pricing is the quantification and allocation of location savings and location rents among the associated enterprises. Under arm's length pricing, allocation of location savings and rents between associated enterprises should be made by reference to what independent parties would have agreed in comparable circumstances. The Indian transfer pricing administration believes it is possible to use the profit split method to determine arm's length allocation of location savings and rents in cases where comparable uncontrolled transactions are not available. In these circumstances, it is considered that the functional analysis of the parties to the transaction (functions performed, assets owned and risks assumed), **and** the bargaining power of the parties (which at arm's length would be determined by the competitiveness of the market - availability of substitutes, cost structure etc) should both be considered appropriate factors.

b. Comparability analysis and benchmarking by taking local comparables will determine the price of a transaction with a related party in a low cost jurisdiction. However, it will not take into account the benefit of location savings which can be computed by taking into account cost difference between cost of low cost country and high cost country from where the business activity was relocated. In view of this, the price determined on the basis of local comparables is not consistent with arm's length price because any arm's length transaction between two unrelated parties would not be possible without benefiting both parties to the transaction.

b. Hypothetically, if an unrelated third party had to compensate another party to the transaction in a low cost jurisdiction that was equal to the cost savings and location rents attributable to the location, there would be no incentive for the unrelated third party to relocate business to a low cost jurisdiction. Thus, arm's length compensation for cost savings and location rents should be such that both parties would benefit from participating in the transaction. In other words, it should be not less than zero and not greater than the value of cost savings and locations rents; it should also reflect an appropriate split of the cost savings and location rents between the parties.

6. Intangibles

a. Transfer pricing of intangibles is well known as a difficult area of taxation practice. However, the pace of growth of the intangible economy has opened new challenges to the arm's length principle. The transactions involving intangible assets are difficult to evaluate because of the following reasons:

- Intangibles are seldom traded in the external market and it is very difficult to find comparables' in the public domain.
- Intangibles are often transferred bundled along with tangible assets. They are difficult to be detected.

b. A number of difficulties arise while dealing with intangibles. Some of the key issues revolve around determination of arm's length price of rate of royalties, allocation of cost of development of market and brand in a new country, remuneration for development of marketing, Research and Development intangibles and their use, transfer pricing of co-branding etc. Some of the Indian experiences in this regard are discussed below.

- With regard to payment of royalties, MNEs often enter into agreements allowing use of brands, trademarks, know how, design, technology etc. by their subsidiaries or related parties in India. Such payments can be in a lump sum, periodical payments or a combination of both types of payments. It is an internationally agreed position that intellectual property which is owned by one entity and used by another entity generally requires royalty payment. However, the important issue in this regard is determination of the rate of royalty. The main challenge in determination of arm's length price of royalty rate is to find comparables in the public domain with sufficient information required for comparability analysis. The Indian experience suggests that it is impossible to find comparable arm's length prices in most cases. The use of profit split method as an alternative is generally not a feasible option due to lack of requisite information.

- The Indian tax administration has noticed serious difficulties in determining the rate of royalty charged for use of brand and trademark in certain cases. In some cases the user had borne significant costs on promotion of the brand/trademark, and to promote and develop customer loyalty for brand/trademark in a new market. In these cases, royalty rate charged by the MNE will depend upon the cost borne by the subsidiary or related party to promote the brand and trademark and to develop customer loyalty for brand and product. In many cases no royalty may be charged under uncontrolled environment and the subsidiary would require arm's length compensation for economic ownership of marketing intangible developed by it and for enhancing the value of brand and trademark owned by parent MNEs in the new emerging market like India.
- In many cases, Indian subsidiaries which use technical know-how of their parent company have incurred significant expenditure to customize such know-how and to enhance its value by their R&D efforts. Costs on activities, such as R&D activities which have contributed in enhancing the value of know-how owned by parent company is generally considered by Indian transfer pricing officer while determining arm's length price of royalty for use of technical know-how.
- The Indian transfer pricing administration has also noted significant transfer pricing issues in cases of co-branding of new foreign brand of parent MNE (which is unknown to new market like India) with popular Indian brand name. Since the Indian subsidiary has developed valuable Indian brand in the domestic market over a period of time, incurring huge expenditure on advertisement, marketing and sales promotion, it should be entitled for arm's length remuneration for contributing to the value of foreign little known brand through market recognition by co-branding it with a popular Indian brand.

7. R&D activities

a. Several global MNEs have established subsidiaries in India for research and development activities on contract basis to take advantage of the large pool of skilled manpower which are available at a lower cost. These Indian subsidiaries are generally compensated on the basis of routine and low cost plus mark up. The parent MNE of these R&D centres justify low cost plus markup on the ground that they control all the risk and their subsidiaries or related parties are risk free or limited risk bearing entities. The claim of parent MNEs that they control the risk and are entitled for major part of profit from R&D activities is based on following contentions:

- Parent MNE designs and monitors all the research programmes of the subsidiary.
- Parent MNE provides fund needed for R&D activities.
- Parent MNE controls the annual budget of the subsidiary for R&D activities.
- Parent MNE controls and takes all the strategic decisions with regards to core functions of R&D activities of the subsidiary.
- Parent MNE bears the risk of unsuccessful R&D activities.

b. The Indian transfer pricing administration always undertakes a detailed enquiry in cases of contract R&D centres. Such an enquiry seeks to ascertain correctness of the functional profile of subsidiary and parent MNE on the basis of transfer pricing report filed by the taxpayers, as well as information available in the public domain and commercial databases. After conducting detailed enquiries, the Indian tax administration often reaches the following conclusions:

- Most parent MNEs were not able to file relevant documents to justify their claim of controlling risk of core functions of R&D activities and asset (including intangible assets) which are located in the country of subsidiary or related party.

- Contrary to the above, it was found that day to day strategic decisions and monitoring of R&D activities were carried out by personnel of subsidiary who were engaged in actual R&D activities and bore relevant operational risks.
- The management of Indian subsidiary also took decision of allocation of budget to different streams of R&D activities and Indian management also monitored day to day performance of R&D activities.
- It was true that in most of the cases funds for R&D activities were transferred from the MNE parent and they bore the risk of such fund. However, in addition to "capital" other important assets like technically skilled manpower, know how for R&D activities etc were developed and owned by the Indian subsidiary. Accordingly, control of risk of the asset lies both with the MNE parent and Indian subsidiary but the Indian subsidiary controls more risks as compared to the MNE parent.

c. On the basis of above functional analysis, the Indian transfer pricing administration decided in most of the cases that Indian subsidiaries were not risk free entities but bore significant risk. Accordingly Indian subsidiaries were entitled to an appropriate return for their function including the strategic decision, monitoring, use of their assets and control over the risk. In view of these facts, routine cost plus compensation model was not held at arm's length price.

d. Most of these R&D centres in India were actually found to be engaged in creation of unique intangibles, legal ownership of which was transferred to their parent MNEs under agreement. Such transfer took place without any appropriate compensation and patents for these intangibles were registered in the name of parent MNE. In these cases the Indian transfer pricing administration allocated additional arm's length compensation for transfer of such intangibles in addition to arm's length compensation for R&D activities.

8. Marketing Intangibles

a. Transfer pricing aspect of marketing intangibles has been a focus area for the Indian transfer pricing administration. The issue is particularly relevant to India due to its unique market specific characteristics such as location advantages, market accessibility, large customer base, market premium, spending power of Indian customers etc. The Indian market has witnessed substantial marketing activities by the subsidiary/ related party of the MNE groups in recent past, that have resulted in creation of local marketing intangibles. For Indian transfer pricing administration first important step is to identify marketing intangibles. The marketing intangibles are generally identified on the basis of the efforts of Indian subsidiary/related party on:

- Enhancing the value of foreign trade mark/brand unknown to Indian market by incurring huge advertisement, marketing and sale promotion expenditure.
- Creation of brand and product loyalty in the minds of customers.
- Creation of efficient supply chain.
- Establishing distributor network in the country.
- After sale services support network in the country.
- Conducting customer and market researches.
- Establishing customer list etc.

b. Since Indian subsidiaries/related parties (which are claimed as no risk and limited risk bearing distributors by parent MNE in order to justify low cost plus return) have incurred and borne huge expenditure on development of marketing intangibles. These entities generally incur huge losses or disclose very nominal profit as evident from their return of income. Determination of ALP in cases of marketing intangibles generally involves following steps:

- Functional analysis of profile of the Indian and parent MNE to ascertain whether the Indian taxpayer is a risk free, limited risk bearing or risk bearing entity?
- Identification of nature, types and stages of development of marketing intangibles. The Indian entity may be engaged in different stages of development of marketing intangibles. For example if an MNEs is new entrant in Indian market, the related party in India will incur substantial expenditure:
  - to create awareness about trade mark, brand and product or services of MNE group in India.
  - customer loyalty for brand and products/services for dealer network.
  - after sale services network.
  - market and customer research for creation of customer list.

c. After some years of operation, the cost on developing and sustaining marketing intangible may be reduced.
   - Identification of expenditure on launch of new products in India and to ascertain who had borne such expenditure.
   - to ascertain who had borne the cost of development of marketing intangibles.
   - examination of remuneration model to Indian related party.

d. The Indian tax administration computes the ALP in the cases involving marketing intangibles following the concept of bright line i.e., no risk or limited risk distributor will bear the cost of only routine expenditure on advertisement, marketing and sale promotion. However, the tax administration faces following challenges in determination of the ALP:
   - Whether parent MNE should reimburse the cost incurred by the Indian related party on development of marketing intangibles with or without mark-up.
   - Lack of uniform accounting codes creates a significant challenge in identification of advertisement, marketing and sales promotion (AMP) expenditure in comparable companies and tested party.
   - The developer of marketing intangibles who has economic ownership in the intangibles is entitled to additional returns. However, the difficult question is what should be the arm's length price of such returns.

e. The important issue in the determination of ALP in these cases is to examine who benefits from the extraordinary AMP expenditure. Taxpayers generally claim that such extraordinary expenditure helps the business of the Indian entity also in addition to parent MNE. However, the tax authorities in India have found that Indian distributors are claimed to be no risk or low risk bearing entities and are getting fixed and routine return on cost plus basis. They do not get a share in the excess profit relatable to local marketing intangibles. Accordingly, extra-ordinary AMP expenditure does not enhance the profitability of Indian subsidiary or related party. This conclusion of the tax authorities is further supported by the fact that these so called risk-free or limited risk distributors have disclosed huge losses even when they are entitled for fixed return on cost plus basis and should not have incurred losses.

f. In this context, the Transfer Pricing administration have taken a view that such Indian entities which incur excessive AMP expenses, bear risks and perform functions beyond what an independent distributor with similar profile would incur or perform for the benefit of its own distribution activities should be compensated for return on intangibles. Such compensation would be in the form of reimbursement of the excess AMP expenditure along with mark-up. Alternatively, the Indian entity should be allowed to share profit related to marketing intangibles. If no reimbursement is made in these type of cases along with

mark-up, or the related party does not get an arm's length return for development of marketing intangibles in the form of its entitlement to share profits, the Indian tax administration makes adjustment on account of reimbursement of excess AMP expenditure along with a mark-up for the functions undertaken by the subsidiary/related party.

9. Intragroup Services

a. Globalization and the drive to achieve efficiencies within MNE groups have encouraged sharing of resources to provides support between one or more location by way of shared services. Since these intra group services are the main component of "tax efficient supply chain management" within an MNE group, the Indian transfer pricing authorities attach high priority to this aspect of transfer pricing. The tax administration has noticed that some of the services are relatively straight forward in nature like marketing, advertisement, trading, management consulting etc. However, other services may be more complex and can often be provided on stand-alone basis or to be provided as part of the package and is linked one way or another to supply of goods or intangible assets. An example can be agency sale technical support which obligates the licensor to assist the licensee in setting up of manufacturing facilities, including training of staff. The Indian transfer pricing administration generally considers following questions in order to identify intra group services requiring arm's length remuneration:

- Whether Indian subsidiaries have received any related party services i.e., intra group services? Nature and detail of services including quantum of services received by the related party.
- Whether services have been provided in order to meet specific need of recipient of the services? What are the economic and commercial benefits derived by the recipient of intra group services?
- Whether in comparable circumstances an independent enterprise would be willing to pay the price for such services?
- Whether an independent third party would be willing and able to provide such services?

b. The answers to above questions enable the Indian tax administration to determine if the Indian subsidiary has received or provided intra group services which requires arms' length remuneration. Determination of the arm's length price of intra-group services normally involve following steps:

- Identification of the cost incurred by the group entity in providing intra group services to the related party.
- Understanding the basis for allocation of cost to various related parties i.e., nature of allocation keys.
- Whether intra group services will require reimbursement of expenditure along with markup.
- Identification of arm's length price of markup for rendering of services.

c. Identification of the services which require an arm's length remuneration is one of the main challenges before the Indian transfer pricing administration. India believes that shareholder services, duplicate services and incidental benefit from group services do not give rise to intra group services requiring arm's length remuneration. However, such conclusion would need a great deal of analysis. The biggest challenge in determination of the arm's length price is allocation of cost by using allocation keys. The nature of allocation keys generally varies with the nature of services. However, it is difficult to reach agreement between the tax administration and taxpayer on the nature of allocation of keys.

d. The next challenge before the transfer pricing administration is a most commonly asked question whether or not it is necessary for services provider to make a profit. Typical example of this would include treatment of pass through cost. Another important question is how to determine a percentage of mark up and to fix

the benchmark of markup are tedious processes. The fixing up of the cost base to compute the markup is another complex issue and it is a difficult decision to include or not to include various types of overhead.

e. A brief review of cases where adjustments have been made by Indian transfer pricing administration has revealed that most of MNE parents do not allow any profit markup on the services rendered by Indian subsidiaries to them. However, in some exceptional cases a low markup of 5% to 10% is allowed on some services with a restricted cost base. On the other hand, where Indian subsidiaries or related parties receive intra group services, parent MNEs generally charge mark up on all the services provided to such entities, including duplicate services, shareholding services and services which provide only incidental benefits to the Indian entities. The rate of markup charged on such intra-group services is also mostly on the higher side. The Indian transfer pricing administration has also noticed that in several cases, the claim of rendering services was found to be incorrect or the services were found not to be intra-group services which required arm's length remuneration.

f. In view of the above facts, transfer pricing of intra-group services is a high risk area for the Indian transfer pricing administration.

10. Financial Transactions

a. Intercompany loans and guarantees are becoming common international transactions between related parties due to management of cross border funding within group entities of a MNE group. Transfer pricing of inter-company loans and guarantees are increasingly being considered some of the most complex transfer pricing issues in India. The Indian transfer pricing administration has followed a quite sophisticated methodology for pricing inter-company loans which revolves around:

- comparison of terms and conditions of loan agreement.
- determination of credit rating of lender and borrower.
- Identification of comparables third party loan agreement.
- suitable adjustments to enhance comparability.

b. The Indian transfer pricing administration has come across cases of outbound loan transactions where the Indian parent has advanced to its associated entities (AE) in a foreign jurisdiction either interest free loans or loans at LIBOR/EURIBOR rates. The main issue before the transfer pricing administration is benchmarking of these loan transactions to arrive at the ALP of the rates of interest applicable on these loans. The Indian transfer pricing administration has determined that since the loans are advanced from India and Indian currency has been subsequently converted into the currency of the geographic location of the AE, the Prime Lending Rate (PLR) of the Indian banks should be applied as the external CUP and not the LIBOR or EURIBOR rate.

c. A further issue in financial transactions is credit guarantee fees. With the increase in outbound investments, the Indian transfer pricing administration has come across cases of corporate guarantees extended by Indian parents to its associated entities (AEs) abroad, where the Indian parent as guarantor agrees to pay the entire amount due on a loan instrument on default by the borrower. The guarantee helps an AE of the Indian MNE to secure a loan from the bank. The Indian transfer pricing administration generally determines the ALP of such guarantee under the comparable uncontrolled price method. In most cases, interest rates quotes and guarantee rate quotes available from banking companies are taken as the benchmark rate to arrive at the ALP. The Indian tax administration also uses the interest rate prevalent in the rupee bond markets in India for bonds of different credit ratings. The difference in the credit ratings between the parent in India and the foreign subsidiary is taken into account and the rate of interest specific to a credit rating of Indian bond is also considered for determination of the arm's length price of such guarantees.

d. However, the Indian transfer pricing administration is facing a challenge due to non-availability of specialized database and transfer price of complex cases of inter-company loans in cases of mergers and acquisitions which involve complex inter-company loan instruments as well as implicit element of guarantee from parent company in securing debt.

Solved Case

Terabyte Inc. of France and R Ltd. of India are associated enterprises. R Ltd. imports 6,000 compressors for Air Conditioners from Terabyte Inc. at ₹ 6,700 per unit and these are sold to Refresh Cooling Solutions Ltd at a price of ₹ 10,000 per unit. R Ltd. had also imported similar products from Gold Inc. Poland and sold outside at a Gross Profit of 20% on Sales. Terabyte Inc. offered a quantity discount of ₹ 1,000 per unit. Gold Inc. could offer only ₹ 500 per unit as Quantity Discount. The freight and customs duty paid for imports from Gold Inc. Poland had cost R Ltd. ₹ 1,200 per piece. In respect of purchase from Terabyte Inc., R Ltd. had to pay ₹ 200 only as freight charges.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. What will be considered as arm's length price per unit?

2. State the amount of addition required to be made in the computation of R Ltd.?

Solution:

Computation of Arm's Length Price

Particulars	Amount (₹)
Resale Price of Goods Purchased from Terabyte Inc.	10,000
Less: Adjustment for Differences –	
a) Normal Gross Profit Margin at 20% of Sale Price [20% x ₹ 10,000]	2,000
b) Incremental Quantity Discount by Terabyte Inc. [₹ 1,000 – ₹ 500]	500
c) Difference in Purchase related expenses [₹ 1,200 – ₹ 200]	1,000
Arms Length Price	**6,500**

Computation of Increase in Total Income of R Ltd

Particulars	Amount
Price at which actually bought from Terabyte Inc. of France	6,700
Less: Arms Length Price per unit under Resale Price Method	6,500
Decrease in Purchase Price per unit	**200**
No. of units purchased from Terabyte Inc.	3,000 units
Increase in Total Income (6,000 units x ₹ 200)	₹ 12,00,000

Exercise

A. Theoretical Questions

Multiple Choice Questions

1. The provisions of sec. 92 will apply only if the aggregate value of specified domestic transactions entered into by the taxpayer during the year exceeds a sum of ₹ _____.
   a. 100 crore
   b. 5 crore
   c. 10 crore
   d. 20 crore

2. As per section _____ when any specified domestic transaction is carried out between associated enterprises, the said transaction should be carried out at arm's length price.
   a. 90
   b. 91
   c. 92
   d. 90A

3. Section _____ deals with methods of computation of arm's length price.
   a. 94
   b. 93
   c. 92C
   d. 91

4. Arm's length price is to be determined by applying _____
   a. Resale Price Method
   b. Fair Market Value Method
   c. Stamp Duty Value Method
   d. Indexed Cost of Acquisition Method

5. Advance Pricing Agreement shall be valid for such period not exceeding _____ consecutive previous years as may be specified in the agreement.
   a. 5
   b. 3
   c. 10
   d. 2

6. As per sec. 94B, interest expenses claimed by an entity to its associated enterprises shall be restricted to _____ of its earnings before interest, taxes, depreciation and amortization (EBITDA) or interest paid or payable to associated enterprise, whichever is less.
   a. 30%
   b. 25%
   c. 20%
   d. 50%

7. If any person fails to keep and maintain any such information and document as required by sec. 92D in respect of an international transaction or specified domestic transaction, the Assessing Officer or Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to _____
   a. ₹ 5,00,000
   b. 2% of the value of each international transaction or specified domestic transaction entered into by such person
   c. ₹ 1,00,000
   d. 1% of the value of each international transaction or specified domestic transaction entered into by such person

8. Uncontrolled transaction means a transaction between _____, whether resident or non-resident
   a. enterprises other than associated enterprises
   b. associated enterprises
   c. any enterprises
   d. none of the above

9. Information and documents required to maintained u/s 92D shall be kept and maintained for a period of _____ from the end of the relevant assessment year.
   a. 8 years
   b. 5 years
   c. 10 years
   d. 16 years

10. When an assessee fails to furnish any information relating to a specified domestic transaction, the quantum of penalty as a percentage of value of the transaction would be —
   a. 2%
   b. 1%
   c. 5%
   d. 3%

[Answer : 1-d; 2-c; 3-c; 4-a; 5-a; 6-a; 7-b; 8-a; 9-a; 10-a]

Short Essay Type Questions

1. What do you mean by advance pricing agreement?
2. What is thin capitalisation?
3. State the provisions relating to secondary adjustments.

B. Numerical Questions

Comprehensive Numerical Problems

On the basis of following information, you are requested to compute disallowance u/s 94B

Particulars	Case I	Case II	Case III
	₹ in lakhs		
Net Profit after deduction of the following items:	1,000	1,000	1,000
Interest to SBI	70	50	200
Interest to associated enterprise	200	110	320
Interest to unrelated parties	500	190	300
Depreciation	90	80	110
Provision for taxation	340	170	70
Proposed dividend	300	150	100

[Ans: Nil]

Unsolved Case

1. Bharat Cellphones Ltd. (BCL) of Mumbai and Japan Mobiles Ltd. (JML) of Tokyo are associated enterprises. BCL imported 10,000 mobile handsets from JML for ₹ 15,000 per handset which are sold to unrelated parties in India for ₹ 20,000 per handset. BCL also imported similar mobile sets from Europe Ltd. (EL) of London which was sold with a gross profit margin of 25% on cost. JML offered quantity discount @ ₹ 2,000 per unit and whereas EL offered discount @ ₹ 800 per unit as quantity discount. The freight and customs duty paid for imports from EL had cost BCL ₹ 1,500 per unit. In respect of purchases from EL, the expenditure towards freight and customs duty was ₹ 500 per unit.

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. Which method shall be considered as most appropriate method for computation of arm's length transaction?

   a. Resale Price Method

   b. Cost Plus Method

   c. Comparable Uncontrolled Price Method

   d. None of the above

2. What will be the arm's length price per mobile handset?

   a. ₹ 13,800

   b. ₹ 14,600

   c. ₹ 15,000

   d. None of the above

3. State the amount of increment required to be made in the total income on account of transfer pricing.
   a. ₹ 120 lakhs
   b. ₹ 40 lakhs
   c. Nil
   d. None of the above

2. S Limited, an Indian Company supplied billets to its holding company, G Limited, Germany during the previous year 2020-21. S Limited also supplied the same product to another German-based company, Z Limited, an unrelated entity. The transactions with G Limited are priced at Euro 500 per MT (FOB), whereas the transactions with Z Limited are priced at Euro 900 per MT (CIF). Insurance and Freight amounts to Euro 300 per MT.

During the year, 10,000 MT were supplied to G Limited.

Assume an exchange rate of 1 Euro = 90 INR

On the basis of aforesaid information, you are requested to choose correct options for the following:

1. Which will be considered as the most appropriate method for computing arm's length price in this case?
   a. Comparable Uncontrolled Price
   b. Resale Price Method
   c. Cost Plus Method
   d. None of the above

2. What will be the arm's length price for the transaction with G Limited?
   a. Euro 600
   b. Euro 500
   c. Euro 650
   d. None of the above

3. What will be the effect of the change in the ALP on the profits of S Limited?
   a. Total income will be increased by ₹ 9 crore
   b. Total income will be increased by ₹ 1 crore
   c. Total income will be increased by ₹ 3 crore
   d. None of the above

4. If export profits of the Indian company are covered by exemption u/s 10AA (seventh year), will there be any increase in the quantum of exemption u/s 10AA?

   a. Nil

   b. Exemption will be increased by ₹ 9 crore

   c. Total income will be increased by ₹ 3 crore

   d. Total income will be increased by ₹ 1 crore

3. X Ltd., a resident Indian Company, on 01-04-2023 has borrowed ₹ 100 crores from M/s. A Inc, a Company incorporated in US, at an interest rate of 9% p.a. The said loan is repayable over a period of 10 years. Further, loan is guaranteed by M/s B Inc incorporated in US. M/s. K Inc, a non-resident, holds shares carrying 30% of voting power both in M/s X Ltd. and M/s B. Inc. M/s K Inc has also deposited ₹ 100 crores with M/s A Inc.

Other information

Net profit of M/s. X Ltd. was ₹ 10 crores after debiting the above interest, depreciation of ₹ 5 crores and income-tax of ₹ 3.40 crores.

Based on the above information, please answer the following:

1. State the amount of addition required to be made u/s 94B

   a. Nil, as provision of sec. 94B is not applicable

   b. ₹ 78 lakhs

   c. ₹ 18 lakhs

   d. None of the above

2. What will be the taxable income of the assessee?

   a. ₹ 1,418 lakhs

   b. ₹ 1,358 lakhs

   c. ₹ 1,078 lakhs

   d. None of the above

4. U Ltd., a US company has a subsidiary, B Ltd., in India. U Ltd. sells computer monitors to B Ltd. for resale in India. U Ltd. also sells computer monitors to K Ltd., another computer reseller. It sells 50,000 computer monitors to B Ltd. at ₹ 11,000 per unit. The price fixed for K Ltd. is ₹ 10,000 per unit. The warranty in the case of sale of monitors by B Ltd. is handled by B Ltd. However, for sale of monitors by K Ltd., U Ltd. is responsible for the warranty for 3 months. Both U Ltd. and B Ltd. offer extended warranty at a standard rate of ₹ 1,000 per annum. On these facts, answer the following:

1. What will be the arm's length price per computer monitor?

   a. ₹ 9,750

b. ₹ 11,000

c. ₹ 10,000

d. None of the above

2. State the amount of increment required to be made in the total income on account of transfer pricing.

a. ₹ 625 lakhs

b. ₹ 500 lakhs

c. Nil

d. None of the above

5. I Ltd. is an Indian Company in which Z Inc., a US company, has 28% shareholding and voting power. Following transactions were effected between these two companies during the financial year 2023-24:

a. I Ltd. sold 1,00,000 pieces of T-shirts at $ 2 per T-Shirt to Z Inc. The identical T-Shirts were sold to unrelated party namely Kennedy Inc., at $ 3 per T-Shirt.

b. I Ltd. borrowed $ 2,00,000 from a foreign lender based on the guarantee of Z Inc. For this, I Ltd. paid $ 10,000 as guarantee fee to Z Inc. To an unrelated party for the same amount of loan, Z Inc. collected $ 7000 as guarantee fee.

c. I Ltd. paid $15,000 to Z Inc. for getting various potential customers details to improve its business. Z Inc. provided the same service to unrelated parties for $ 10,000.

Assume the rate of exchange as 1 $ = ₹ 82

I Ltd. is located in a Special Economic (SEZ) and its income before transfer pricing adjustments for the year ended 31st March, 2024 was ₹ 1,200 lakhs.

On the basis of above information, answer the following:

1. State the amount of increment required to be made in the total income of I Ltd. on account of transfer pricing.

a. ₹ 88,56,000

b. ₹ 82,00,000

c. Nil

d. None of the above

2. State the amount of incremental deduction u/s 10AA available to I Ltd. on account of addition made due to transfer pricing provisions

a. ₹ 88,56,000

b. ₹ 82,00,000

c. Nil

d. None of the above

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

GAAR 14

This Module includes:

14.1 Applicability of General Anti-Avoidance Rule [Sec. 95]

14.2 Impermissible Avoidance Arrangement [Sec. 96]

GAAR

SLOB Mapped against the Module:

1. To develop understanding about various provisions of direct taxation laws and rules including international taxation laws, and inherent issues that are subject to interpretation with reference to case laws, etc.
2. To attain abilities to apply the acquired understanding for solving complex taxation problems and taking tax efficient business decision and execution thereof.

Module Learning Objectives:

After studying this module, the students will be able to -

- Understand the provision of income tax in respect of General Anti Avoidance Rules (GAAR)
- Appreciate the applicability of such rules
- Understand the impact of applicability.

Introduction

14

Chapter X-A: GENERAL ANTI-AVOIDANCE RULE (GAAR)

The question of substance over form has consistently arisen in the implementation of taxation laws. In the Indian context, judicial decisions have varied. While some courts in certain circumstances had held that legal form of transactions can be dispensed with and the real substance of transaction can be considered while applying the taxation laws, others have held that the form is to be given sanctity. The existence of anti-avoidance principles are based on various judicial pronouncements. There are some specific anti-avoidance provisions but general anti-avoidance has been dealt only through judicial decisions in specific cases.

In an environment of moderate rates of tax, it is necessary that the correct tax base be subject to tax in the face of aggressive tax planning and use of opaque low tax jurisdictions for residence as well as for sourcing capital. Most countries have codified the "substance over form" doctrine in the form of General Anti Avoidance Rule (GAAR).

In the above background and keeping in view the aggressive tax planning with the use of sophisticated structures, there is a need for statutory provisions so as to codify the doctrine of "substance over form" where the real intention of the parties and effect of transactions and purpose of an arrangement is taken into account for determining the tax consequences, irrespective of the legal structure that has been superimposed to camouflage the real intent and purpose. Internationally several countries have introduced, and are administering statutory General Anti Avoidance Provisions. It is, therefore, important that Indian taxation law also incorporate a statutory General Anti Avoidance Provisions to deal with aggressive tax planning. The basic criticism of statutory GAAR which is raised worldwide is that it provides a wide discretion and authority to the tax administration which at times is prone to be misused. This vital aspect, therefore, needs to be kept in mind while formulating any GAAR regime.

In addition to GAAR there also exists SAAR- Specific Anti-Avoidance Rules which specifically aim at certain arrangements of tax avoidance. SAAR have many points to its favour, since its specific there is no scope of confusion, it doesn't provide taxation authorities any discretion and from the point of view of tax payer it provides certainty regarding the nature of his arrangement. Provisions of SAAR are there in Chapter X of the Income Tax Act 1961 and some of the provisions pertaining to SAAR are in various other chapters of Income Tax Act.

It is accordingly provided in the Finance Act, 2013 to provide General Anti Avoidance Rule in the Income Tax Act to deal with aggressive tax planning w.e.f. 01-04-2018.

Applicability of General Anti-Avoidance Rule [Sec. 95]

14.1

An arrangement entered into by an assessee may be declared to be an impermissible avoidance arrangement and the consequence in relation to tax arising therefrom may be determined subject to the provisions of this Chapter.

The provisions of this Chapter may be applied to any step in, or a part of, the arrangement as they are applicable to the arrangement.

Taxpoint

1. "Arrangement" means any step in, or a part or whole of, any transaction, operation, scheme, agreement or understanding, whether enforceable or not, and includes the alienation of any property in such transaction, operation, scheme, agreement or understanding;
2. "Step" includes a measure or an action, particularly one of a series taken in order to deal with or achieve a particular thing or object in the arrangement;

Non-Application of General Anti Avoidance Rule [Rule 10U]

1. The provisions of Chapter X-A (i.e., GAAR Provisions) shall not apply to:
   a. an arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of ₹ 3 crore;
   b. a Foreign Institutional Investor:
      i. who is an assessee under the Act;
      ii. who has not taken benefit of an agreement referred to in sec. 90 or 90A; and
      iii. who has invested in listed securities, or unlisted securities, with the prior permission of the competent authority, in accordance with the Securities and Exchange Board of India (Foreign Institutional Investor) Regulations, 1995 and such other regulations as may be applicable, in relation to such investments;
   c. a person, being a non-resident, in relation to investment made by him by way of offshore derivative instruments or otherwise, directly or indirectly, in a Foreign Institutional Investor.
   d. any income accruing or arising to, or deemed to accrue or arise to, or received or deemed to be received by, any person from transfer of investments made before 01-4-2017 by such person.
      - The provisions shall apply to any arrangement, irrespective of the date on which it has been entered into, in respect of the tax benefit obtained from the arrangement on or after 01-04-2017.

Taxpoint: "Tax benefit" includes,—

a. a reduction or avoidance or deferral of tax or other amount payable under this Act; or

b. an increase in a refund of tax or other amount under this Act; or

c. a reduction or avoidance or deferral of tax or other amount that would be payable under this Act, as a result of a tax treaty; or

d. an increase in a refund of tax or other amount under this Act as a result of a tax treaty; or

e. a reduction in total income; or

f. an increase in loss,

in the relevant previous year or any other previous year;

Impermissible Avoidance Arrangement [Sec. 96]

14.2

1. An impermissible avoidance arrangement means an arrangement, the main purpose of which is to obtain a tax benefit, and it—

   (a) creates rights, or obligations, which are not ordinarily created between persons dealing at arm's length;

   (b) results, directly or indirectly, in the misuse, or abuse, of the provisions of this Act;

   (c) lacks commercial substance or is deemed to lack commercial substance u/s 97, in whole or in part; or

   (d) is entered into, or carried out, by means, or in a manner, which are not ordinarily employed for bona fide purposes.

2. An arrangement shall be presumed, unless it is proved to the contrary by the assessee, to have been entered into, or carried out, for the main purpose of obtaining a tax benefit, if the main purpose of a step in, or a part of, the arrangement is to obtain a tax benefit, notwithstanding the fact that the main purpose of the whole arrangement is not to obtain a tax benefit.

   Taxpoint: "Tax treaty" means an agreement referred to in sec. 90(1) or 90A(1).

Arrangement to lack commercial substance [Sec. 97]

1. An arrangement shall be deemed to lack commercial substance, if—

   a. the substance or effect of the arrangement as a whole, is inconsistent with, or differs significantly from, the form of its individual steps or a part; or

   b. it involves or includes—

      i. round trip financing;

      ii. an accommodating party;

      iii. elements that have effect of offsetting or cancelling each other; or

      iv. a transaction which is conducted through one or more persons and disguises the value, location, source, ownership or control of funds which is the subject matter of such transaction; or

   c. it involves the location of an asset or of a transaction or of the place of residence of any party which is without any substantial commercial purpose other than obtaining a tax benefit (but for the provisions of this Chapter) for a party; or

   d. it does not have a significant effect upon the business risks or net cash flows of any party to the arrangement apart from any effect attributable to the tax benefit that would be obtained (but for the provisions of this Chapter).

2. For the aforesaid purposes, round trip financing includes any arrangement in which, through a series of transactions—

   a. funds are transferred among the parties to the arrangement; and

   b. such transactions do not have any substantial commercial purpose other than obtaining the tax benefit (but for the provisions of this Chapter),

   without having any regard to —

   A. whether or not the funds involved in the round trip financing can be traced to any funds transferred to, or received by, any party in connection with the arrangement;

   B. the time, or sequence, in which the funds involved in the round trip financing are transferred or received; or

   C. the means by, or manner in, or mode through, which funds involved in the round trip financing are transferred or received.

3. A party to an arrangement shall be an accommodating party, if the main purpose of the direct or indirect participation of that party in the arrangement, in whole or in part, is to obtain, directly or indirectly, a tax benefit (but for the provisions of this Chapter) for the assessee whether or not the party is a connected person in relation to any party to the arrangement.

4. The following may be relevant but shall not be sufficient for determining whether an arrangement lacks commercial substance or not, namely:—

   i. the period or time for which the arrangement (including operations therein) exists;

   ii. the fact of payment of taxes, directly or indirectly, under the arrangement;

   iii. the fact that an exit route (including transfer of any activity or business or operations) is provided by the arrangement.

Taxpoint

1. "Asset" includes property, or right, of any kind;

2. "Fund" includes—

   (a) any cash;

   (b) cash equivalents; and

   (c) any right, or obligation, to receive or pay, the cash or cash equivalent;

3. "Party" includes a person or a permanent establishment which participates or takes part in an arrangement;

4. "Connected person" means any person who is connected directly or indirectly to another person and includes,—

   a. any relative of the person, if such person is an individual;

   b. any director of the company or any relative of such director, if the person is a company;

   c. any partner or member of a firm or association of persons or body of individuals or any relative of such partner or member, if the person is a firm or association of persons or body of individuals;

   d. any member of the Hindu undivided family or any relative of such member, if the person is a Hindu undivided family;

e. any individual who has a substantial interest in the business of the person or any relative of such individual;

f. a company, firm or an association of persons or a body of individuals, whether incorporated or not, or a Hindu undivided family having a substantial interest in the business of the person or any director, partner, or member of the company, firm or association of persons or body of individuals or family, or any relative of such director, partner or member;

g. a company, firm or association of persons or body of individuals, whether incorporated or not, or a Hindu undivided family, whose director, partner, or member has a substantial interest in the business of the person, or family or any relative of such director, partner or member;

h. any other person who carries on a business, if—

i. the person being an individual, or any relative of such person, has a substantial interest in the business of that other person; or

ii. the person being a company, firm, association of persons, body of individuals, whether incorporated or not, or a Hindu undivided family, or any director, partner or member of such company, firm or association of persons or body of individuals or family, or any relative of such director, partner or member, has a substantial interest in the business of that other person;

5. Relative shall have the meaning assigned to it in the Explanation to sec. 56(2)(vi).

6. A person shall be deemed to have a substantial interest in the business, if,—

a. in a case where the business is carried on by a company, such person is, at any time during the financial year, the beneficial owner of equity shares carrying twenty per cent or more, of the voting power; or

b. in any other case, such person is, at any time during the financial year, beneficially entitled to twenty per cent or more, of the profits of such business;

Consequences of impermissible avoidance arrangement [Sec. 98]

1. If an arrangement is declared to be an impermissible avoidance arrangement, then, the consequences, in relation to tax, of the arrangement, including denial of tax benefit or a benefit under a tax treaty, shall be determined, in such manner as is deemed appropriate, in the circumstances of the case, including by way of but not limited to the following:

a. disregarding, combining or recharacterising any step in, or a part or whole of, the impermissible avoidance arrangement;

b. treating the impermissible avoidance arrangement as if it had not been entered into or carried out;

c. disregarding any accommodating party or treating any accommodating party and any other party as one and the same person;

d. deeming persons who are connected persons in relation to each other to be one and the same person for the purposes of determining tax treatment of any amount;

e. reallocating amongst the parties to the arrangement—

i. any accrual, or receipt, of a capital nature or revenue nature; or

ii. any expenditure, deduction, relief or rebate;

f. treating—

i. the place of residence of any party to the arrangement; or

ii. the situs of an asset or of a transaction,

at a place other than the place of residence, location of the asset or location of the transaction as provided under the arrangement; or

g. considering or looking through any arrangement by disregarding any corporate structure.

2. For this purposes:

i. any equity may be treated as debt or vice versa;

ii. any accrual, or receipt, of a capital nature may be treated as of revenue nature or vice versa; or

iii. any expenditure, deduction, relief or rebate may be recharacterised.

Taxpoint: "Benefit" includes a payment of any kind whether in tangible or intangible form;

Treatment of connected person and accommodating party [Sec. 99]

For the purposes of this Chapter, in determining whether a tax benefit exists,—

i. the parties who are connected persons in relation to each other may be treated as one and the same person;

ii. any accommodating party may be disregarded;

iii. the accommodating party and any other party may be treated as one and the same person;

iv. the arrangement may be considered or looked through by disregarding any corporate structure.

Application of this Chapter [Sec. 100]

The provisions of this Chapter shall apply in addition to, or in lieu of, any other basis for determination of tax liability.

Framing of guidelines [Sec. 101]

The provisions of this Chapter shall be applied in accordance with such guidelines and subject to such conditions, as may be prescribed. The following scheme has been framed:

Determination of consequences of impermissible avoidance arrangement [Rule 10UA]

For the purposes of sec. 98(1), where a part of an arrangement is declared to be an impermissible avoidance arrangement, the consequences in relation to tax shall be determined with reference to such part only.

Notice, Forms for reference under section 144BA [Rule 10UB]

1. For the purposes of sec. 144BA(1), the Assessing Officer shall, before making a reference to the Commissioner, issue a notice in writing to the assessee seeking objections, if any, to the applicability of provisions of Chapter X-A in his case.

2. The notice shall contain the following:

i. details of the arrangement to which the provisions of Chapter X-A are proposed to be applied;

ii. the tax benefit arising under the arrangement;

iii. the basis and reason for considering that the main purpose of the identified arrangement is to obtain tax benefit;

iv. the basis and the reasons why the arrangement satisfies the condition provided in sec. 96; and

v. the list of documents and evidence relied upon in respect of (iii) and (iv) above.

3. The reference by the Assessing Officer to the Commissioner u/s 144BA(1) shall be in Form No. 3CEG.

4. Where the Commissioner is satisfied that the provisions of Chapter X-A are not required to be invoked with reference to an arrangement after considering:

   i. the reference received from the Assessing Officer u/s 144BA(1); or

   ii. the reply of the assessee in response to the notice issued u/s 144BA(2),

   - he shall issue directions to the Assessing Officer in Form No. 3CEH.

5. Before a reference is made by the Commissioner to the Approving Panel u/s 144BA(4), he shall record his satisfaction regarding the applicability of the provisions of Chapter X-A in Form No. 3CEI and enclose the same with the reference.

Time limits [Rule 10UC]

For the purposes of sec. 144BA:

i. no directions u/s 144BA(3) shall be issued by the Commissioner after the expiry of 1 month from the end of the month in which the date of compliance of the notice issued u/s 144BA(2) falls;

ii. no reference shall be made by the Commissioner to the Approving Panel u/s 144BA(4) after the expiry of 2 months from the end of the month in which the final submission of the assessee in response to the notice issued u/s 144BA(2) is received;

iii. the Commissioner shall issue directions to the Assessing Officer in Form No.3CEH:

   a. in the case referred to in rule 10UB(4)(i), within a period of 1 month from the end of month in which the reference is received by him; and

   b. in the case referred to in rule 10UB(4)(ii), within a period of 2 months from the end of month in which the final submission of the assessee in response to the notice issued u/s 144BA(2) is received by him.

Example 1[1]:

Facts

M/s India Chem Ltd. is a company incorporated in India. It sets up a unit in a Special Economic Zone (SEZ) in F.Y. 2017-18 for manufacturing of chemicals. It claims 100% deduction of profits earned from that unit in F.Y. 2018-19 and subsequent years. Is GAAR applicable in such a case?

Interpretation:

There is an arrangement of setting up of a unit in SEZ which results into a tax benefit. However, this is a case of tax mitigation where the tax payer is taking advantage of a fiscal incentive offered to him by submitting to the conditions and economic consequences of the provisions in the legislation e.g., setting up the business unit in SEZ area. Hence, the Revenue would not invoke GAAR as regards this arrangement.

1 Indco = Indian Company; Subco = Subsidiary company; NTJ = No tax jurisdiction; LTJ = Low tax jurisdiction

Example 1A:

Facts:

In the above example 1, let us presume M/s India Chem Ltd. has another unit for manufacturing chemicals in a non-SEZ area. It then diverts its production from such manufacturing unit and shows the same as manufactured in the tax exempt SEZ unit, while doing only process of packaging there. Is GAAR applicable in such a case?

Interpretation:

This is a case of misrepresentation of facts by showing production of non-SEZ unit as production of SEZ unit. Hence, this is an arrangement of tax evasion and not tax avoidance. Tax evasion, being unlawful, can be dealt with directly by establishing correct facts. GAAR provisions will not be invoked in such a case.

Example 1B:

Facts:

In the above example 1A, let us presume that M/s India Chem Ltd. does not show production of non-SEZ unit as a production of SEZ unit but transfers the product of non-SEZ unit at a price lower than the fair market value and does only some insignificant activity in SEZ unit. Thus, it is able to show higher profits in SEZ unit than in non-SEZ unit, and consequently claims higher deduction in computation of income. Can GAAR be invoked to deny the tax benefit?

Interpretation:

As there is no misrepresentation of facts or false submissions, it is not a case of tax evasion. The company has tried to take advantage of tax provisions by diverting profits from non-SEZ unit to SEZ unit. This is not the intention of the SEZ legislation. However, such tax avoidance is specifically dealt with through transfer pricing regulations that deny tax benefits. Hence, the Revenue would not invoke GAAR in such a case.

Example 1C:

Facts:

In the above example 1B, let us presume, that both units in SEZ area (say A) and non-SEZ area (say B) work independently. M/s India Chem Ltd. started taking new export orders from existing as well as new clients for unit A and gradually, the export from unit B declined. There has not been any shifting of equipment from unit B to unit A. The company offered lower profits from unit B in computation of income. Can GAAR be invoked on the ground that there has been shifting or reconstruction of business from unit B to unit A for the main purpose of obtaining tax benefit?

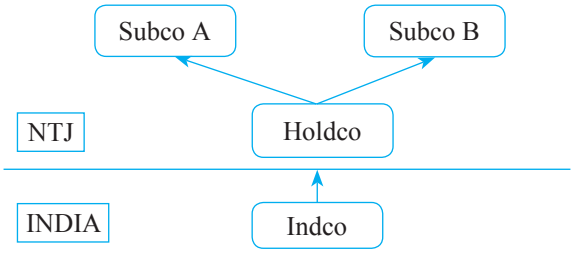
Interpretation:

The issue of tax avoidance through shifting / reconstruction of existing business from one unit to another has been specifically dealt with in the relevant section of deduction of the Act. Hence, the Revenue would not invoke GAAR in such a case.

Example 2:

Facts:

An Indian company (Indco) has set up a holding company (Holdco) in a no tax jurisdiction outside India (say NTJ) which has set up further subsidiary companies (Subco A and Subco B) which pay dividends to Holdco. Such dividends are not repatriated to Indco. Can GAAR be invoked to look through Holdco to tax dividends in the hands of Indco?



Interpretation:

Declaration / repatriation of dividend is a business choice of a company. India does not have anti-deferral provisions in the form of Controlled Foreign Company (CFC) rules in the I.T. Act. Accordingly, GAAR would not be invoked in such a case.

Example 2A:

Facts:

In the above example 2, dividend is accumulated in Holdco for a number of years and subsequently, Holdco is merged into Indco through a cross–border merger. Can GAAR be invoked on the ground that the merger route has been adopted to avoid payment of tax on dividend in India?

Interpretation:

It is true that if Holdco declares dividends to Indco before merger, then, such dividend would have been taxable in India. But the timing or sequencing of an activity is a business choice available to the taxpayer. Moreover, sec. 47 of the Act specifically exempts capital gains on cross border merger of a foreign company into an Indian company. Hence, GAAR cannot be invoked when taxpayer makes a choice about timing or sequencing of an activity to deny a tax benefit granted by the statute.

Example 3:

Facts:

The merger of a loss-making company into a profit making one results in losses setting off profits, a lower net profit and lower tax liability for the merged company. Would the losses be disallowed under GAAR?

Interpretation:

As regards setting off of losses, the provisions relating to merger and amalgamation already contain specific anti-avoidance safeguards. Therefore, GAAR would not be invoked when SAAR is applicable.

Example 4:

Facts:

A choice is made by a company by acquiring an asset on lease over outright purchase. The company claims deduction for lease rentals in case of acquisition through lease rather than depreciation as in the case of purchase of the asset. Would the lease rent payment, being higher than the depreciation, be disallowed as expense under GAAR?

Interpretation:

GAAR provisions, would not, prima facie, apply to a decision of leasing (as against purchase of an asset). However, if it is a case of circular leasing, i.e. the taxpayer leases out an asset and through various sub-leases, takes it back on lease, thus creating a tax benefit without any change in economic substance, Revenue would examine the matter for invoking GAAR provisions.

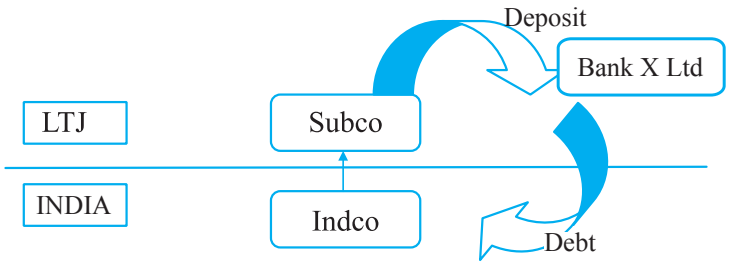
Example 5:

Facts:

1. X Ltd. is a banking institution in LTJ (low tax jurisdiction);
2. There is a closely held company Subco in LTJ which is a wholly owned subsidiary of another closely held Indian company Indco;
3. Subco has reserves and, if it provides a loan to Indco, it may be treated as deemed dividend u/s 2(22)(e) of the Act.
4. Subco makes a term deposit with X Bank Ltd. and X Bank Ltd. bank based on this security provides a back to back loan to Indco.

Say, India-LTJ tax treaty provides that interest payment to a LTJ banking company is not taxable in India.

Can this be examined under GAAR?



Interpretation:

This is an arrangement whose main purpose is to bring money out of reserves in Subco to India without payment of due taxes. The tax benefit is saving of taxes on income to be received from Subco by way of dividend or deemed dividend. The arrangement disguises the source of funds by routing it through X Bank Ltd. X Bank Ltd. may also be treated as an accommodating party. Hence the arrangement shall be deemed to lack commercial substance.

Consequently, in the case of Indco, the loan amount would be treated as dividend income received from Subco to the extent reserves are available in Subco; and no expense by way of interest would be allowed.

In the case of X Bank Ltd, exemption from tax on interest under the DTAA may not be allowed as X Ltd is not a beneficial owner of the interest, provided the DTAA has anti-avoidance rule of beneficial ownership. If such anti-avoidance rule is absent in DTAA, then GAAR may be invoked to deny treaty benefit as arrangement will be perceived as an attempt to hide the source of funds of Subco.

Example 6:

Facts:

Indco incorporates a Subco in a NTJ with equity of US$100. Subco has no reserves; it gives a loan of US$100 to Indco at the rate of 10% p.a. which is utilized for business purposes. Indco claims deduction of interest payable to Subco from the profit of business. There is no other activity in Subco. Can GAAR be invoked in such a case?

Interpretation:

The main purpose of the arrangement is to obtain interest deduction in the hands of Indco and thereby tax benefit. There is no commercial substance in establishing Subco since without it there is no effect on the business risk of Indco or any change in the cash flow (apart from the tax benefit). Moreover, it is a case of round tripping which

means a case of deemed lack of commercial substance. Hence, it would be treated as an impermissible avoidance arrangement.

Consequently, in the case of Indco, interest payment would be disallowed by disregarding Subco. No corresponding relief would be allowed in the case of Subco by way of refund of taxes withheld, if any.

Example 7

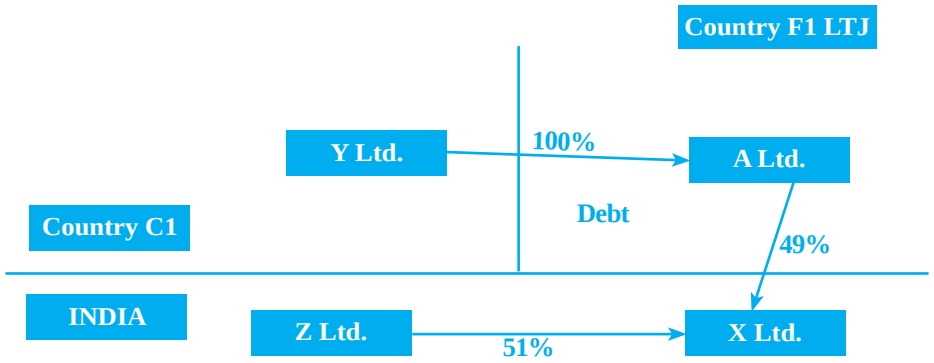
Facts:

A large corporate group has created a service company to manage all its non core activities. The service company then charges each company for the services rendered on a cost plus basis. Can the mark up in the cost of services be questioned using GAAR.

Interpretation:

There are specific anti avoidance provisions through transfer pricing regulations as regards transactions among related parties. GAAR will not be invoked in this case.

Example 8:



Facts:

1. Y Ltd. is a company incorporated in country C1. It is a non-resident in India.
2. Z Ltd. is a company resident in India.
3. A Ltd. is a company incorporated in country F1 and it is a 100% subsidiary of Y Ltd.
4. A Ltd. and Z Ltd. form a joint venture company X Ltd. in India after the date of commencement of GAAR provisions. There is no other activity in A Ltd.
5. The India-F1 tax treaty provides for non-taxation of capital gains in the source country and country F1 charges no capital gains tax in its domestic law.
6. A Ltd. is also designated as a ―permitted transferee of Y Ltd. ―Permitted transferee means that though shares are held by A Ltd, all rights of voting, management, right to sell etc., are vested in Y Ltd.
7. As per the joint venture agreement, 49% of X Ltd‘s equity is allotted to A Ltd. and 51% is allotted to Z Ltd..
8. Thereafter, the shares of X Ltd. held by A Ltd. are sold to C Ltd., a company connected to the Z Ltd. group.

As per the tax treaty with country F1, capital gains arising to A Ltd. are not taxable in India. Can GAAR be invoked to deny the treaty benefit?

Interpretation

The arrangement of routing investment through country F1 results into a tax benefit. Since there is no business purpose in incorporating company A Ltd. in country F1 which is a LTJ, it can be said that the main purpose of the arrangement is to obtain a tax benefit. The alternate course available in this case is direct investment in X Ltd. joint venture by Y Ltd. The tax benefit would be the difference in tax liabilities between the two available courses.

The next question is, does the arrangement have any tainted element? It is evident that there is no commercial substance in incorporating A Ltd. as it does not have any effect on the business risk of Y Ltd. or cash flow of Y Ltd. As the twin conditions of main purpose being tax benefit and existence of a tainted element are satisfied, GAAR may be invoked.

Additionally, as all rights of shareholders of X Ltd. are being exercised by Y Ltd instead of A Ltd, it again shows that A Ltd lacks commercial substance.

Hence, unless it is a case where Circular 789 relating Tax Residence Certificate in the case of Mauritius, or Limitation of Benefits clause in India-Singapore treaty is applicable, GAAR can be invoked.

Example 9:

Facts:

A Ltd. is incorporated in country F1 as a wholly owned subsidiary of company Y Ltd. which is not a resident of F1 or of India. The India-F1 tax treaty provides for non-taxation of capital gains in India (the source country) and country F1 charges no capital gains tax in its domestic law. Some shares of X Ltd., an Indian company, are acquired by A Ltd in the year after date of coming into force of GAAR provisions. The entire funding for investment by A Ltd. in X Ltd. was done by Y Ltd. These shares are subsequently disposed of by A Ltd after 5 years. This results in capital gains which A Ltd. claims as not being taxable in India by virtue of the India-F1 tax treaty. A Ltd. has not made any other transaction during this period. Can GAAR be invoked?

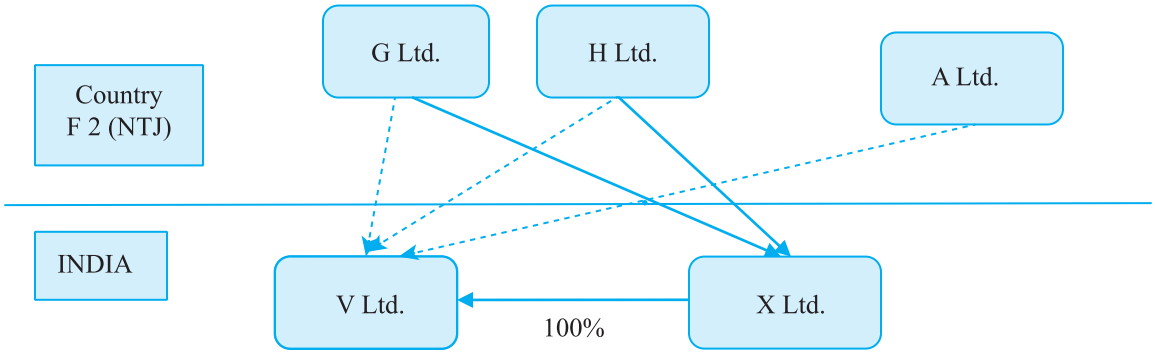
Interpretation:

This is an arrangement which has been created with the main purpose of avoiding capital gains tax in India by routing investments through a favourable jurisdiction. There is neither a commercial purpose nor commercial substance in terms of business risks or cash flow to Y Ltd in setting up A Ltd. It should be immaterial here whether A Ltd has office, employee etc in country F1. Both the purpose test and tainted element tests are satisfied for the purpose of invoking GAAR. Unless it is a case where Circular 789 relating Tax Residence Certificate in the case of Mauritius, or Limitation of Benefits clause in India-Singapore treaty is applicable, the Revenue may invoke GAAR and consequently deny treaty benefit.

Example 10:

Facts:

The shares of V Ltd., an asset owning Indian company, was held by another Indian company X Ltd. X Ltd. was in turn held by two companies G Ltd. and H Ltd., incorporated in country F2, a NTJ. The India-F2 tax treaty provides for non-taxation of capital gains in the source country and country F2 charges no capital gains tax in its domestic law. X Ltd. was liquidated by consent and without any Court Decree. This resulted in transfer of the asset/shares from X Ltd., to G Ltd. and H Ltd. Subsequently, companies G Ltd and H Ltd sold the shares of V Ltd to A Ltd. which was incorporated in F2. The companies G Ltd and H Ltd claimed benefit of tax treaty and the resultant gains from the transaction are claimed to be not taxable. Can GAAR be invoked to deny treaty benefit?



Interpretation:

The alternative courses available to taxpayer to achieve the same result (with or without the tax benefit) are:

i. **Option 1:** (as mentioned in facts): X Ltd. liquidated, G Ltd. and H Ltd. become shareholders of V Ltd.; A Ltd. acquires shares from G Ltd. and H Ltd.; and becomes shareholder of V Ltd.

ii. **Option 2:** A Ltd. acquires shares of X Ltd. from G Ltd. and H Ltd.; X Ltd. is liquidated; and A Ltd. becomes shareholder of V Ltd.

iii. **Option 3:** X Ltd. sells its entire shareholding in V Ltd. to A Ltd. and subsequently, X Ltd is liquidated.

In Options 1 & 2, there is no tax liability in India except the deemed dividend taxation to the extent reserves are available in X Ltd. This is because of the treaty between India and country F1. In option 3, tax liability arises to X Ltd., an Indian company, on sale of shares of V Ltd. Subsequently, when X Ltd. is liquidated, tax liability arises on account of deemed dividend to the extent reserves are available in X Ltd.

The taxpayer exercises the most tax efficient manner in disposal of its assets through proper sequencing of transactions. The Revenue cannot invoke GAAR as regards this arrangement.

Clarifications on implementation of GAAR [Circular 07/2017 dated 27/01/2017]

1. **Will GAAR be invoked if SAAR (Specific Anti-Avoidance Rules) applies?**

Ans. It is internationally accepted that specific anti avoidance provisions may not address all situations of abuse and there is need for general anti-abuse provisions in the domestic legislation. The provisions of GAAR and SAAR can coexist and are applicable, as may be necessary, in the facts and circumstances of the case.

2. **Will GAAR be applied to deny treaty eligibility in a case where there is compliance with Limitation of Benefits (LOB) test of the treaty?**

Ans. Adoption of anti-abuse rules in tax treaties may not be sufficient to address all tax avoidance strategies and the same are required to be tackled through domestic anti-avoidance rules. If a case of avoidance is sufficiently addressed by LOB in the treaty, there shall not be an occasion to invoke GAAR.

3. **Will GAAR interplay with the right of the taxpayer to select or choose method of implementing a transaction?**

Ans. GAAR will not interplay with the right of the taxpayer to select or choose method of implementing a transaction.

4. **Will GAAR provisions apply where the jurisdiction of the FPI is finalised based on non-tax commercial considerations and such FPI has issued P-notes referencing Indian securities? Further, will GAAR be invoked with a view to denying treaty eligibility to a Special Purpose Vehicle (SPV), either on the ground that it is located in a tax friendly jurisdiction or on the ground that it does not have its own premises or skilled professional on its own roll as employees.**

Ans. For GAAR application, the issue, as may be arising regarding the choice of entity, location etc., has to be resolved on the basis of the main purpose and other conditions provided u/s 96 of the Act. GAAR shall not be invoked merely on the ground that the entity is located in a tax efficient jurisdiction. If the jurisdiction of FPI is finalized based on non-tax commercial considerations and the main purpose of the arrangement is not to obtain tax benefit, GAAR will not apply.

5. **Will GAAR provisions apply to (i) any securities issued by way of bonus issuances so long as the original securities are acquired prior to 01 April, 2017 (ii) shares issued post 31 March, 2017, on conversion of Compulsorily Convertible Debentures, Compulsorily Convertible Preference Shares (CCPS), Foreign Currency Convertible Bonds (FCCBs), Global Depository Receipts (GDRs), acquired prior to 01 April, 2017; (iii) shares which are issued consequent to split up or consolidation of such grandfathered shareholding?**

Ans. Grandfathering under Rule 10U(1)(d) will be available to investments made before 1st April 2017 in respect of instruments compulsorily convertible from one form to another, at terms finalized at the time of issue of such instruments. Shares brought into existence by way of split or consolidation of holdings, or by bonus issuances in respect of shares acquired prior to 1st April 2017 in the hands of the same investor would also be eligible for grandfathering under Rule 10U(1)(d) of the Income Tax Rules.

6. **The expression "investments" can cover investment in all forms of instrument — whether in an Indian Company or in a foreign company, so long as the disposal thereof may give rise to income chargeable to tax. Grandfathering should extend to all forms of investments including lease contracts (say, air craft leases) and loan arrangements, etc.**

Ans. Grandfathering is available in respect of income from transfer of investments made before 1st April, 2017. As per Accounting Standards, 'investments' are assets held by an enterprise for earning income by way of dividends, interest, rentals and for capital appreciation. Lease contracts and loan arrangements are, by themselves, not 'investments' and hence grandfathering is not available.

7. **Will GAAR apply if arrangement held as permissible by Authority for Advance Ruling?**

Ans. No. The AAR ruling is binding on the PCIT / CIT and the Income Tax Authorities subordinate to him in respect of the applicant.

8. **Will GAAR be invoked if arrangement is sanctioned by an authority such as the Court, National Company Law Tribunal or is in accordance with judicial precedents etc.?**

Ans. Where the Court has explicitly and adequately considered the tax implication while sanctioning an arrangement, GAAR will not apply to such arrangement.

9. **Will a Fund claiming tax treaty benefits in one year and opting to be governed by the provisions of the Act in another year attract GAAR provisions? An example would be where a Fund claims treaty benefits in respect of gains from derivatives in one year and in another year sets-off losses from derivatives transactions against gains from shares under the Act.**

Ans. GAAR provisions are applicable to impermissible avoidance arrangements as under section 96. In so far as the admissibility of claim under treaty or domestic law in different years is concerned, it is not a matter to be decided through GAAR provisions.

10. How will it be ensured that GAAR will be invoked in rare cases to deal with highly aggressive and artificially pre-ordained schemes and based on cogent evidence and not on the basis of interpretation difference?

Ans. The proposal to declare an arrangement as an impermissible avoidance arrangement under GAAR will be vetted first by the Principal Commissioner / Commissioner and at the second stage by an Approving Panel, headed by judge of a High Court. Thus, adequate safeguards are in place to ensure that GAAR is invoked only in deserving cases.

11. **Can GAAR lead to assessment of notional income or disallowance of real expenditure? Will GAAR provisions expand the scope of charging provisions or scope of taxable base and/or disallow the expenditure which is actually incurred and which otherwise is admissible having regard to diverse provisions of the Act?**

Ans. If the arrangement is covered under section 96, then the arrangement will be disregarded by application of GAAR and necessary consequences will follow.

12. **A definite timeline may be provided such as 5 to 10 years of existence of the arrangement where GAAR provisions will not apply in terms of the provisions in this regard in section 97(4) of the IT Act.**

Ans. Period of time for which an arrangement exists is only a relevant factor and not a sufficient factor under section 97(4) to determine whether an arrangement lacks commercial substance.

13. **It may be ensured that in practice, the consequences of a transaction being treated as an 'impermissible avoidance arrangement' are determined in a uniform, fair and rational basis. Compensating adjustments u/s 98 of the Act should be done in a consistent and fair manner. It should be clarified that if a particular consequence is applied in the hands of one of the participants, there would be corresponding adjustment in the hands of another participant.**

Ans. Adequate procedural safeguards are in place to ensure that GAAR is invoked in a uniform, fair and rational manner. In the event of a particular consequence being applied in the hands of one of the participants as a result of GAAR, corresponding adjustment in the hands of another participant will not be made. GAAR is an anti-avoidance provision with deterrent consequences and corresponding tax adjustments across different taxpayers could militate against deterrence.

14. **Tax benefit of INR 3 crores as defined in section 102(10) may be calculated in respect of each arrangement and each taxpayer and for each relevant assessment year separately. For evaluating the main purpose to be obtaining of tax benefit, the review should extend to tax consequences across territories. The tax impact of INR 3 crores should be considered after taking into account impact to all the parties to the arrangement i.e. on a net basis and not on a gross basis (i.e. impact in the hands of one or few parties selectively).**

Ans. The application of the tax laws is jurisdiction specific and hence what can be seen and examined is the 'Tax Benefit' enjoyed in Indian jurisdiction due to the 'arrangement or part of the arrangement'. Further, such benefit is assessment year specific. Further, GAAR is with respect to an arrangement or part. of the arrangement and therefore limit of ₹ 3 crores cannot be read in respect of a single taxpayer only.

15. **Will a contrary view be taken in subsequent years if arrangement held to be permissible in an earlier year?**

Ans. If the PCIT/Approving Panel has held the arrangement to be permissible in one year and facts and circumstances remain the same, as per the principle of consistency, GAAR will not be invoked for that arrangement in a subsequent year.

16. **No penalty proceedings should be initiated pursuant to additions made under GAAR at least for the initial 5 years.**

Ans. Levy of penalty depends on facts and circumstances of the case and is not automatic. No blanket exemption for a period of five years from penalty provisions is available under law. The assessee, may at his option, apply for benefit u/s 273A if he satisfies conditions prescribed therein.

Exercise

A. Theoretical Questions

Multiple Choice Questions

1. General Anti Avoidance Rule (GAAR) is applicable from
   a. 01-04-2018
   b. 01-04-2017
   c. 01-07-2017
   d. 01-07-2018

2. GAAR provisions shall not apply to
   a. an arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of ₹ 3 crore
   b. an arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of ₹ 5 crore
   c. an arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of ₹ 1 crore
   d. None of the above

[Answer : 1-a; 2-a]

Short Essay Type Questions

1. State the cases when provisions relating to GAAR are not applicable
2. Define impermissible avoidance arrangement.

References

https://www.incometaxindia.gov.in/

https://www.incometax.gov.in/

https://www.indiabudget.gov.in/

NOTES

NOTES