SUGGESTED ANSWERS

PAPER – 7 : DIRECT TAX LAWS AND INTERNATIONAL TAXATION

COMMON FOR NEW AND OLD SYLLABUS

Solution to Question 1(a)

(i) No, the transaction of demerger would not attract any income-tax liability in the hands of SS(P) or RV(P) Ltd.

As per section 47(vib), any transfer in a demerger, of a capital asset, by the demerged company to the resulting company would not be regarded as "transfer" for levy of capital gains tax if the resulting company is an Indian company.

Hence, capital gains tax liability would not be attracted in the hands of SS(P) Ltd., the demerged company, in this case, since RV(P) Ltd. is an Indian company

(ii) There would be no capital gains liability in the hands of Mr. N.K. on receipt of shares of RV (P) Ltd., since as per section 47(vid), any issue of shares by the resulting company in a scheme of demerger to the shareholders of the demerged company will not be regarded as "transfer" for levy of capital gains tax, if the issue is made in consideration of demerger of the undertaking.

(iii) Yes, capital gains would arise in the hands of Mr. N.K. on sale of shares of RV (P) Ltd.

Sale consideration ` 8,00,000

Less: Indexed cost of acquisition of shares of RV (P) Ltd.

Cost of acquisition of shares of RV(P) Ltd. as per section 49(2C):

Cost of acquisition of shares of SS(P) Ltd. × Net book value of assets transferred in a demerger / Net worth of the demerged company immediately before demerger

`6,00,000 × 10 crore / 40 crore = `1,50,000

Indexed cost of acquisition of shares of RV(P) Ltd

`1,50,000 × 272 = `3,74,312
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Long term capital gain [since period of holding of shares in demerged company is also to be considered]	`4,25,688

(iv) No, sale of shares by Mr. N.K. would not affect the tax benefits availed by SS(P) Ltd. or RV (P) Ltd.

One of the conditions to be satisfied is that the shareholders holding not less than three-fourths in value of the shares in the demerged company become shareholders of the resulting company by virtue of the de-merger. It is presumed that the condition is satisfied in this case.

There is no stipulation that they continue to remain shareholders for any period of time thereafter.

(v) Since the resultant capital gain on sale of shares of RV(P) Ltd. is a long-term capital gain (on account of the period of holding of shares in demerged company being considered by virtue of section 2(42A)(g)), Mr. N.K. can avail exemption –

(1) Under section 54EC by investing the long-term capital gains in bonds of National Highways Authority of India (NHAI) or Rural Electrification Corporation Ltd. (RECL) or notified bonds within a period of 6 months from the date of transfer; or

(2) Under section 54EE, by investing the long-term capital gain units of specified fund, within a period of 6 months from the date of transfer.

(3) Under section 54F by investing the entire net consideration in purchase (within one year before and two years after the date of transfer) or construction (within three years after the date of transfer) of one residential house in India. If part of the net consideration is invested, only proportionate exemption would be available.

Solution to Question 1(b)

Computation of taxable income of Mr. Singh for A.Y.2018-19

Income from house property

Gross Annual Value [Higher of Expected Rent & Actual Rent]		3,00,000
Expected Rent (lower of Fair Rent and Standard Rent)	2,50,000	
Actual Rent	3,00,000	
Less:		
Municipal taxes paid by Mr. Singh during the year (including arrears) [` 35,000 + `1,50,000]		1,85,000
Net Annual Value (NAV)		1 , 15,000

Less: Deductions under section 24		
(a) 30% of NAV 34,500		
(b) Interest on loan borrowed for major repairs	1,50,000	1,84,500
		(69,500)
Arrears of rent taxable under section 25A	30,000	
Less:		
Deduction@30%	9,000	21,000
		(48,500)

Capital Gains

Full value of consideration	30,00,000

As per section 50C, the full value of consideration would be the higher of –

Actual Consideration	25,00,000
Stamp Duty Value [3,90,000/13%]	30,00,000

Less – Indexed Cost of Acquisition [`1,25,000 × 272 / 117]

As per section 49(1), cost of acquisition of the residential house gifted by Mr. Singh's father to Mr. Singh would be the cost for which Mr. Singh's father acquired the asset 2,90,598

27,09,402

Less:

Exemption under section 54 (8,00,000 + 7,00,000)	15,00,000

Purchase of residential house within the stipulated time (within one year before or two years after the date of sale)

[Where the flats are situated side by side and the builder had effected the necessary modification to make it as one house, the assessee would be entitled to exemption under section 54 in respect of investment in both the flats, despite the fact that they were purchased by separate sale deeds]

[CIT v. Ananda Basappa (2009) 331 ITR 211 (Kar.)]

Exemption under section 54EC	*10,00,000*

Investment in bonds of NHAI within six months from the date of transfer. Where the payment for bonds has been made within the six month period, exemption under section 54EC would be available even if the allotment of bonds was made after the expiry of the six months [Hindustan Unilever Ltd. v.

DCIT (2010) 325 ITR 102 (Bom.)]

Long term capital gain	2,09,402
Total Income	*1,60,902*

Solution to question 1(c)

Computation of total income of Siddarth Ltd. for A.Y.2018-19

Particulars	`	`
Profits and gains of business or profession		
Unit X (See Note 4)	63,81,000	
Less: Deduction under section 10AA (See Working below)	35,45,000	
	28,36,000	
Unit Y (See Note 4)	36,54,000	
Total Income	*64,90,000*	

Deduction under section 10AA in respect of Unit X (See Notes 1, 2 & 3)

$$= \text{Profit of SEZ Unit} \times \frac{\text{Export turnover of SEZ Unit}}{\text{Total turnover of SEZ Unit}}$$

$$= \text{`}63,81,000 \times \frac{1 \text{ crore}}{1.8 \text{ crore}}$$

= `35,45,000

Notes:

(1) Deduction under section 10AA is available in respect of units established in Special Economic Zones which begin to manufacture or produce articles or things or provide any services during the previous year relevant to A.Y.2006-07 or thereafter. Under section 10AA(1), 100% of the profits and gains derived from export of such articles or things or from services is allowable as deduction for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be. Therefore, in this case, the profits from Unit X, located in a SEZ, will be eligible for deduction of 100% of the profits and gains derived from export, since P.Y.2017-18 is the second year of its operations. It is assumed that Unit X has fulfilled all the specified conditions for claim of deduction. Unit Y is, however, not eligible for deduction under section 10AA in respect of the exports made by it since it is located in a Free Trade Zone.

(2) Export turnover, for the purpose of section 10AA, means the consideration received in respect of export by the unit in SEZ. Therefore, in this case, the amount of ` 20,00,000 which has become irrecoverable due to bankruptcy of one of the foreign buyers in Unit X will not be included in its export turnover.

Therefore, export turnover of Unit X (in SEZ) = ` 1,20,00,000 – ` 20,00,000 = ` 1,00,00,000.

(3) Profits and gains from on site development of computer software outside India shall be deemed to be the profits and gains derived from export of computer software outside India. Since the same has already been included in the figure of export sales, no further adjustment is required.

(4) Computation of unit-wise profits of the business

Particulars	*Unit X*	*Unit Y*	*Total*
Profit earned [after claim of bad debts under section 36(1)(vii) in Unit X] 63,00,000 36,00,000 99,00,000	63,00,000 5,40,000	36,00,000 3,60,000	99,00,000 9,00,000
Add: Depreciation calculated on SLM basis and charged in the proportion of sales (3:2)	68,40,000	39,60,000	1,08,00,000
Less: Depreciation calculated @15% on WDV basis and charged in the proportion of sales (3:2) (See Note 5)	4,59,000	3,06,000	7,65,000
Profits of the business	***63,81,000***	***36,54,000***	***1,00,35,000***

(5) Depreciation as per the Income-tax Rules, 1962 for the A.Y.2018-19 has to be calculated as follows –

Particulars	*Amount in* `
Actual cost of plant and machinery (9,00,000 / 15%)	60,00,000
Less: Depreciation @15% for P.Y.2016-17 (being the first year of operations). It is logical to assume that the assets were put to use for more than 180 days during the year.	_9,00,000
Written down value as on 1.4.2017	51,00,000
Depreciation@15% on WDV for *P.Y.2017-18 (` 51,00,000 × 15%)*	*7,65,000*

Solution to Question No.2

Computation of Total Income of XYZ Ltd. for the A.Y.2018-19

Profits and Gains from Business and Profession	
Profit as per Statement of profit and loss account	7,00,00,000
Add: Items debited but to be considered separately or to be disallowed	
(a) Depreciation as per Companies Act, 2013 disallowed	50,00,000
(b) Employees' contribution to EPF *[See Note 1 below]*	2,00,000

[Since employees' contribution to EPF has not been deposited on or before the due date under the PF Act, the same is not allowable as deduction as per section 36(1)(va). Since the same has been debited to profit and loss account, it has to be added back for computing business income].

(c) Employers contribution to EPF

[As per section 43B, employers' contribution to EPF is allowable as deduction since the same has been deposited on or before the 'due date' of filing of return under section 139(1). Since the same has been debited to profit and loss account, no further adjustment is necessary] NIL

(d) Industrial power tariff concession received from State Government NIL

[Any assistance in the form of, inter alia, concession received from the Central or State Government would be treated as income as per section 2(24)(xviii). Since the same has been credited to profit and loss account, no adjustment is required.

(e) Provision for wages payable to workers Nil

[The provision is based on fair estimate of wages and reasonable certainty of revision, the provision is allowable as deduction, since ICDS X requires 'reasonable certainty for recognition of a provision, which is present in this case. As the provision has been debited to profit and loss account, no adjustment is required while computing business income]

(f) Provision for doubtful debts [10% of ` 200 lakhs] 20,00,000

[Provision for doubtful debts is allowable as deduction under section 36(1)(viia) only in case of banks, public financial institutions, state financial corporations, state industrial investment corporations and non-banking financial corporations. Such

provision is not allowable as deduction in the case of a manufacturing company. Since the same has been debited to profit and loss account, it has to be added back for computing business income]

(g) Bad debts written off NIL

[Bad debts write off in the book of account is allowable as deduction under section 36(1)(vii). Since the same has already been debited to profit and loss account, no further adjustment is required]

(h) Discount given by Sundry Creditors for supply of raw materials NIL

[Discount of 75% given by Sundry Creditors for supply of raw materials is taxable under section 41(1). Since the same has already been credited to profit and loss account, no further adjustment is required]

(i) Provision for gratuity 2,00,00,000

[Provision of ` 500 lakhs for gratuity based on actuarial valuation is not allowable as deduction as per section 40A(7). However, actual gratuity of ` 300 lakhs paid is allowable as deduction. Hence, the difference has to be added back]

(j) Commission paid to recovery agent for realization of a debt. NIL

[Commission of ` 1 lakh paid to a recovery agent for realisation of a debt is an allowable expense under section 37 as per DCIT v. Super Tannery (India) Ltd. (2005) 274 ITR 338 (All). Since the same has been debited to profit and loss account, no further adjustment is required]

(k) Purchase of paper at a price higher than the fair market value 10,00,000

[As per section 40A(2), the difference between the purchase price (` 30,000 per ton) and the fair market value (` 28,000 per ton) multiplied by the quantity purchased (500 tons) has to be added back since the purchase is from a related party, a firm in which majority of the directors are partners, at a price higher than the fair market value]

(l) Sales tax not refunded to customers out of sales tax refund 1,00,000

[The amount of sales tax refunded to the company by the Government is a revenue receipt chargeable to tax under section 41 (1). Deduction can be claimed of amount refunded to customers [CIT v. Thirumalaiswamy Naidu & Sons (1998) 230 ITR 534 (SC)]. Hence, the net amount of ` 1,00,000
(i.e., ` 3,00,000 minus ` 2,00,000) would be chargeable to tax]

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9,83,00,000

Less: Items credited but to be considered separately/ permissible expenditure and allowances

(m) Depreciation as per Income-tax Act, 1961 80,00,000

(n) Over-valuation of stock [` 55 lakhs × 10/110] 5,00,000

[The amount by which stock is over-valued has to be reduced for computing business income. ` 50 lakhs, being the difference between closing and opening stock, has to be adjusted to remove the effect of over-valuation]

(o) Additional Depreciation*[See Note 2 below]* ***10,00,000***

[Additional depreciation@20% is allowable on ` 50 lakhs, being actual cost of new plant & machinery acquired on 10.06.2017, as the same was put to use for more than 180 days in the P.Y.2017-18.]

(p) Payment to a sub-contractor where tax deducted last year was remitted after the due date of filing of return *[See Note 3 below]* ***3,00,000***

[30% of ` 10 lakhs, being payment to a sub-contractor, would have been disallowed under section 40(a)(ia) while computing the business income of A.Y.2017-18, since tax deducted was remitted after the due date of filing of return. However, the same is allowable in A.Y.2018-19, since the remittance has been made on 31.12.2017]

Total Income ***8,85,00,000***

Computation of tax liability of XYZ Ltd. for A.Y.2018-19

Tax @30% on the above total income (since the turnover exceeded ` 50 crore in the P.Y. 2015-16) 2,65,50,000

Add: Surcharge@7% 18,58,500

(since total income exceeds ` 1 crore but less than ` 10 crore)

2,46,91,500

Add: Education cess@2% 4,93,830

Secondary and higher education cess@1% 2,46,915

Total tax liability 2,54,32,245

Total tax liability (rounded off) ***2,54,32,250***

Notes:

(1) Employees contribution to PF deposited after the due date mentioned under the PF Act is not allowable as deduction as per section 36(1)(va). The same has also been affirmed by the Gujarat High Court in CIT v. Gujarat State Road Transport Corporation (2014) 366 ITR 170. Hence, in the above solution, employees' contribution to PF has been disallowed while computing business income.

The CBDT has, vide Circular No. 22/2015, dated 17.12.2015, clarified that the employer contribution to provident fund remitted on or before due date of filing of return under section 139(1), is allowable as deduction while computing Business Income. Further, it has also clarified that the circular does not apply to claim of deduction relating to employee's contribution welfare funds which are governed by section 36(1)(va) of the Act.

Alternate View - An alternate view has, however, been expressed in CIT v. Kiccha Sugar Co. Ltd. (2013) 356 ITR 351 (Uttarakhand), CIT v. AIMIL Ltd (2010) 321 ITR 508 (Del) and CIT v. Nipso Polyfabriks Ltd (2013) 350 ITR 327 (HP) that employees contribution to PF, deducted from the salaries of the employees of the assessee, shall be allowed as deduction from the income of the employer-assessee, if the same is deposited by the employer-assessee with the provident fund authority on or before the due date of filing of return for the relevant previous year. If this view is considered, then no disallowance would be attracted in this case, since the employees' contribution has been remitted before the due date of filing of return of income.

(2) ` 50 lakhs, being the addition to plant and machinery on 10.6.2017 qualifies for additional depreciation@20% under section 32(1)(iia). Since only the normal depreciation as per Income-tax Rules, 1962, has been debited to profit and loss account, additional depreciation of ` 10 lakhs (being 20% of ` 50 lakhs) has to be deducted while computing business income.

(3) Since the tax deducted during the P.Y.2016-17 was remitted only on 31 . 12.2017, i.e., after the due date of filing of return for A.Y.2017-18, ` 3,00,000, being 30% of ` 10 lakh would have been disallowed while computing the business income of that year. Since the tax deducted has been remitted on 31 . 12.2017, ` 3,00,000 would be allowed as deduction while computing the business income of the A.Y.2018-19.

Solution to question 3(a)

Mr. A is eligible for deduction under section 80JJAA since he is subject to tax audit under section 44AB for A.Y.2018-19, as his total turnover from business exceeds ` 1 crore and he has employed "additional employees" during the P.Y.2017-18.

I If Mr. A is engaged in the business of manufacture of computers

Additional employee cost = ` 24,000 × 12 × 75 *[See Working Note below]*

2,16,00,000

Deduction under section 80JJAA = 30% of ` 2,16,00,000 = ` 64,80,000.

Working Note:

Number of additional employees

Total number of employees employed during the year	350
Less: Casual employees employed on 1.8.2017 who do not participate in recognized provident fund	50

Regular employees employed on 1 . 5.2017, since their total monthly emoluments exceed ` 25,000	125
Regular employees employed on 1.9.2017 since they have been employed for less than 240 days in the P.Y.2017-18.	100
Number of "additional employees"	***75***

Note - Since casual employees do not participate in recognized provident fund, they do not qualify as additional employees. Further, 125 regular employees employed on 1.5.2017 also do not qualify as additional employees since their monthly emoluments exceed ` 25,000. Also, 100 regular employees employed on 1.9.2017 do not qualify as additional employees for the P.Y.2017-18, since they are employed for less than 240 days in that year.

Therefore, only 75 employees employed on 1.4.2017 qualify as additional employees, and the total emoluments paid or payable to them during the P.Y.2017-18 is deemed to be the additional employee cost.

II If Mr. A is engaged in the business of manufacture of apparel

If Mr. A is engaged in the business of manufacture of apparel, then, he would be entitled to deduction under section 80JJAA in respect of employee cost of regular employees employed on 1.9.2017, since they have been employed for more than 150 days in the previous year 2017-18.

Additional employee cost = ` 2,16,00,000 + ` 24,000 × 7 × 100 = ` 3,84,00,000

Deduction under section 80JJAA = 30% of ` 3,84,00,000 = ` 1 , 15,20,000

Solution to question 3(b)

The time limit for service of notice under section 143(2) is six months from the end of the financial year in which the return of income was furnished by the assessee. The return of income for assessment year 2017-18 was filed by the assessee on 6th June, 2017. Therefore, the notice under section 143(2) has to be served by 30th September, 2018. However, the notice was served on the assessee only on 3rd October, 2018. Hence, the notice issued under section 143(2) is time-barred.

However, as per section 292BB, where an assessee had appeared in any proceedings or co-operated in any enquiry relating to an assessment or reassessment, it shall be deemed that any notice required to be served upon him, has been duly served upon him in time in accordance with the provisions of the Act and such assessee shall be precluded from raising any objection in any proceeding or enquiry 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.

The above provision shall not be applicable where the assessee has raised such objection before the completion of such assessment or reassessment. Therefore, in the instant case, if the assessee, Tai Limited, had raised an objection to the proceeding, on the ground of non-service of the notice under section 143(2) upon it on time, then, the validity of the assessment order can be challenged. In absence of such objection, the assessment order cannot be challenged.

Solution to question 3(c)

(1) X Inc. is a specified foreign company in relation to A Ltd. Therefore, the condition of A Ltd. holding shares carrying not less than 26% of the voting power in X Inc is satisfied. Hence, X Inc. and A Ltd. are deemed to be associated enterprises. Therefore, provision of systems support services by A Ltd., an Indian company, to X Inc., a foreign company, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

Systems support services falls within the definition of "software development services", and hence, is an eligible international transaction. Since A Ltd. is providing software development services to a non-resident associated enterprise and has exercised a valid option for safe harbour rules, it is an eligible assessee.

Since the value of international transactions entered does not exceed ` 100 crore, A Ltd. should have declared an operating profit margin of not less than 17% in relation to operating expense, to be covered within the safe harbour rules. However, since A Ltd. has declared an operating profit margin of only 16% (ie, 12÷ 75×100), the same is not in accordance with the circumstance mentioned in Rule 10TD. Hence, it is not binding on the income-tax authorities to accept the transfer price declared by A Ltd.

(2) Y Inc., a foreign company, is a subsidiary of B Ltd., an Indian company. Hence, Y Inc. and B Ltd. are associated enterprises. Therefore, provision of data processing services by B Ltd., an Indian company, to Y Inc., a foreign company, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

Solution to question No.4(a)

Section 192 casts liability on the employer to deduct tax at source from the salary paid to its employees. In this case, the employer has paid leave travel concession / facility to its employees and the said concession / facility would be eligible for exemption subject to the conditions laid down in section 10(5) read with Rule 2B of the Income-tax Rules, 1962.

Section 192(2D) casts responsibility on the person responsible for paying any income chargeable under the head 'Salaries' to obtain from the assessee, the evidence or proof or particulars of prescribed claims under the provisions of the Act in the prescribed form and manner for the purposes of –

(1) estimating income of the assesses; or

(2) computing tax deductible under section 192(1).

Rule 26C of the Income-tax Rules, 1962 mandates a salaried assessee claiming, inter alia, leave travel concession or assistance to furnish evidence of expenditure incurred in relation thereto to the person responsible for making such for payment under section 192(1), for the purpose of estimating his income for computing the tax deductible under section 192.

Solution to Question 4(b)

The income received by Mr. Ankur from a filmmaker for allowing them to shoot a film in the agricultural land owned by him is not in the nature of agricultural income because it was neither received by him against the sale of agricultural produce obtained nor for carrying out the normal agricultural operations on the land. The amount paid was only for the purpose of shooting of a film on such land.

To claim exemption in respect of agricultural income under section 10(1), the conditions contained in section 2(1A)(a) to (c) have to be first complied with/fulfilled by the assessee. The Madras High Court in the case of B. Nagi Reddi v. CIT (2002) 258 ITR 719, following the judgment of Apex Court in the case of CIT v Raja Benoy Kumar Sahas Roy (1957) 32 ITR 466, has held, on identical facts, that the income derived for allowing a shooting of film in the agricultural land cannot be treated as agricultural income, as it has no nexus with the land, except that it was carried out on agricultural land.

Solution to Question No.4(c)

The issue under consideration is whether loan or advance given to a shareholder by the company, in return of an advantage or benefit conferred on the company by the shareholder, can be deemed as dividend under section 2(22)(e) of the Income-tax Act, 1961 in the hands of the shareholder

The facts of the case are similar to the facts in Pradip Kumar Malhotra v. CIT (2011) 338 ITR 538, wherein the above issue came up before the Calcutta High Court.

The High Court observed that the phrase "by way of advance or loan" appearing in section 2(22)(e) must be construed to mean those advances or loans which a shareholder enjoys simply on account of being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than 10% of the voting power.

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

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

In this case, advance of ` 10 lakhs was given by VKS Manufacturing (P) Ltd. to Mr. Santhanam holding 25% of voting power in lieu of non-release of his personal property from mortgage thereby enabling the company to retain the benefit of loan obtained from bank. Therefore, applying the rationale of the Calcutta High Court ruling in Pradip Kumar Malhotra's case, such advance cannot be brought within the purview of section 2(22)(e), since it was not in the nature of gratuitous advance but was given to protect the interest of the company.

The proposition of the Assessing Officer to tax the amount of ` 10 lakhs by invoking the provisions of section 2(22)(e) in this case is, therefore, ***not correct.***

Solution to Question No.4(d)

Section 2(15) defines "charitable purpose" to include relief of the poor, education, yoga, medical relief, preservation of environment (including places or objects of artistic or historic interest and the advancement of any other object of general public utility. However, the "advancement of any other object of general public utility" shall not be a charitable purpose, if the institution is carrying on any activity in the nature of trade, commerce or business, or 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 derived from such activity.

Therefore, preservation of wildlife is included in the definition of "charitable purpose" under section 2(15). Further, an institution having the preservation of wildlife as its main object would not be subject to the restrictions which are applicable to the "advancement of any other object of general public utility". Such institution would continue to retain its "charitable" status, even if it derives income from an activity in the nature of trade.

However, if an institution having its main object as "advancement of any other object of general public utility", derives income from an activity in the nature of trade during a financial year, it would lose its "charitable" status for that year, even if it applies such income for its main objects.

It may be noted that if the receipts from such activity does not exceed 20% of the total receipts in that year, then, the institution would not lose its "charitable" status, even its main object is "advancement of any other object of general public utility", if such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility.

Solution to question 4(e)

Section 119(2)(b) empowers the CBDT to authorise any income tax authority to admit an application or claim for any exemption, deduction, refund or any other relief under the Act after the expiry of the period specified under the Act, to avoid genuine hardship in any case or class of cases. The claim for carry forward of loss in case of late filing of a return is relatable to a claim arising under the category of "any other relief available under the Act". Therefore, the CBDT has the power to condone delay in filing of such loss return due to genuine reasons.

The facts of the case are similar to the case of Lodhi Property Company Ltd. v. Under Secretary, (ITA-II), Department of Revenue (2010) 323 ITR 0441, where the Delhi High Court held that the Board has the power to condone the delay in case of a return which was filed late and where a claim for carry forward of losses was made. The delay was only one day and the assessee had shown justifiable reason for the delay of one day in filing the return of income. If the delay is not condoned, it would cause genuine hardship to the assessee. Therefore, the Court held that the delay of one day in filing of the return had to be condoned.

Solution to question no.5(a)

The Explanation below section 9(2) clarifies that income by way of, inter alia, fees for technical services from services utilized in India would be deemed to accrue or arise in India under section 9(1)(vii) in case of a non-resident and be included in his total income, whether or not such services were rendered in India.

In this case, the technical services rendered by the foreign company, JJ Ltd., were for setting up a fertilizer plant in Orissa. Therefore, the services were utilized in India. Consequently, as per section 9(2), the fee of ` 2.5 Crore for technical services rendered by JJ Ltd. (both off-shore and on-shore services) to KK Ltd. is deemed to accrue or arise in India and includible in the total income of JJ Ltd.

Solution to question no.5(b)

In the given case, Mr. Vasudevan gifted a sum of 6 lakhs to his brother's wife on 14.06.2017 and simultaneously, his brother gifted a sum of 5 lakhs to Mr. Vasudevan's wife on 12.07.2017. The gifted amounts were invested as fixed deposits in banks by Mrs. Vasudevan and his brother's wife. These transfers are in the nature of cross transfers. Accordingly, the income from the assets transferred would be assessed in the hands of the deemed transferor because the transfers are so intimately connected to form part of a single transaction and each transfer constitutes consideration for the other by being mutual or otherwise.

If two transactions are inter-connected and are part of the same transaction in such a way that it can be said that the circuitous method was adopted as a device to evade tax, the implication of clubbing provisions would be attracted. It was so held by the Apex Court in CIT vs. Keshavji Morarji (1967) 66 ITR 142.

Accordingly, the interest income arising to Mrs. Vasudevan in the form of interest on fixed deposits would be included in the total income of Mr. Vasudevan and interest income arising in the hands of his brother's wife would be taxable in the hands of Mr. Vasudevan's brother as per section 64(1), to the extent of amount of cross transfers i.e., 5 lakhs.

This is because both Mr. Vasudevan and his brother are the indirect transferors of the income to their respective spouses with an intention to reduce their burden of taxation.

However, the interest income earned by his spouse on fixed deposit of ` 5 lakhs alone would be included in the hands of Mr. Vasudevan's brother and not the interest income on the entire fixed deposit of ` 6 lakhs, since the cross transfer is only to the extent of ` 5 lakhs.

Solution to question 5(c)

Under section 132(1), the income-tax authorities listed therein are empowered to authorise other income-tax authorities to conduct search and seizure operations. The authorities empowered to issue authorization include such Additional Director, Additional Commissioner, Joint Director and Joint Commissioner as are empowered by the CBDT to do so.

However, a Joint Commissioner can issue warrant of authorization only if he has been specifically empowered to do so by the CBDT. Therefore, only if the Joint Commissioner has not been specifically empowered by the CBDT to do so, the contention of the assessee would hold good.

Solution to question 5(d)

M/s. XYZ is deemed to have under-reported its income since:

(1) its income assessed under 143(3) exceeds its income determined in a return processed under section 143(1)(a); and

(2) the income reassessed under section 147 exceeds the income assessed under section 143(3).

Therefore, penalty is leviable under section 270A for under-reporting of income.

Computation of penalty leviable under section 270A

Assessment under section 143(3)

Under-reported income:

Total income assessed under section 143(3)	75,00,000
(-) Total income determined u/s 143(1)(a)	60,00,000
	15,00,000

Tax payable on under-reported

Income: Tax on under-reported income of ` 15 lakhs plus tax on total income of ` 60 lakhs determined u/s 143(1)(a) [30% of ` ***75 lakh + EC & SHEC@3%]*** 23,17,500

Less: Tax on total income determined u/s 143(1)(a) [30% of ` ***60 lakh + EC & SHEC@3%]*** 18,54,000

4,63,500

Reassessment under section 147

Under-reported income:

Total income reassessed under section 147 95,00,000

(-) Total income assessed under section 143(3) 75,00,000

20,00,000

Tax payable on under-reported income:

Tax on under-reported income of ` 20 lakhs plus tax on total income of ` 75 lakhs assessed u/s 143(3) [30% of `95 lakh + EC & SHEC@3%] 29.35,500

Less: Tax on total income assessed u/s 143(3) [30% of ` 75 lakh + EC & SHEC@3%] 23,17,500

6,18,000

Penalty leviable@50% of tax payable 3,09,000

Note – The following assumptions have been made -

(1) None of the additions or disallowances made in assessment or reassessment qualifies under section 270A(6); and

(2) The under-reported income is not on account of misreporting.

Solution to question 6(a)

(i) The statement given is not correct. As per the provisions of section 255, in the event of difference in opinion between the members of the Bench of the Income-tax Appellate Tribunal, the matter shall be decided on the basis of the opinion of the majority of the members. In case the members are equally divided, they shall state the point or points of difference and the case shall be referred by the President of the Tribunal for hearing on such points by one or more of the other members of the Tribunal. Such point or points shall be decided according to the opinion of majority of the members of the Tribunal who heard the case, including those who had first heard it.

(ii) The statement given is not correct. The Supreme Court, in CIT v. Meghalaya Steels Ltd. (2015) 377 ITR 112, observed that the power of review would inhere on High Courts, being courts of record under article 215 of the Constitution of India. There is nothing in article 226 of the Constitution to preclude a High Court from exercising the power of review which inheres in every court of plenary jurisdiction to prevent miscarriage of justice or to correct grave and palpable errors committed by it. The Supreme Court further observed that section 260A(7) does not purport in any manner to curtail or restrict the application of the provisions of the Code of Civil Procedure. Section 260A(7) only states that all the provisions that would apply qua appeals in the Code of Civil Procedure would apply to appeals under section 260A. The Supreme Court opined that this does not in any manner suggest either that the other provisions of the Code of Civil Procedure are necessarily excluded or that the High Court's inherent jurisdiction is in any manner affected.

Solution to question 6(b)

(1)

Explanation 3 to section 147 permits the Assessing Officer to assess or reassess the income in respect of any issue (which has escaped assessment) which comes to his notice subsequently in the course of proceedings under section 147, even though the reason for such issue does not form part of the reasons recorded under section 148(2).

Therefore, in the instant case, the Assessing Officer has the power to disallow expenses under section 14A in addition to disallowing excess depreciation for which notice under section 148 was issued even though the reason for issue relating to disallowance under section 14A was not recorded under section 148(2).

Hence, there is no deficiency in the order passed by the Assessing Officer.

(2)

The issue under consideration is whether the Settlement Commission can pass an order making addition to the income on the basis of difference in gross profit rate adopted, which was neither an issue in the application nor in the report of the Commissioner of Income-tax.

Section 245D(4) provides that the Settlement Commission, after examination of records and the report of the Commissioner and after examining such further evidence as may be placed before it or obtained by it, may, in accordance with the provisions of the Act, pass such order as it thinks fit.

Further, section 245D(5) provides that the materials brought on record before the Settlement Commission shall be considered by the Members of the concerned Bench before passing any order under section 245D(4).

"Consideration" means independent examination of the evidence and material brought on record before the Settlement Commission by the members and application of mind thereto with a view to independently assess the materials and evidence, whether adduced by the applicant or by the Commissioner, and come to a conclusion by themselves.

This view has been upheld in case of Supreme Agro Foods P Ltd. v. Income-tax Settlement Commission (2013) 353 ITR 385 (P&H)

The Settlement Commission, therefore, has to consider the material brought on record before it and "consideration" means independent examination of the evidence and material on record.

In this case, since the material was available before the Settlement Commission and such material has been taken into consideration for returning a finding which is relevant for determining the undisclosed income of the applicant, the addition made on the basis of difference in gross profit rate adopted is justified.

Therefore, the order of the Settlement Commission is valid.

(3)

The Supreme Court has, in Goetze (India) Ltd. v. CIT (2006) 284 ITR 323, ruled that the assessing authority has no power to entertain a claim for deduction made after filing of the return of income otherwise than by way of a revised return. In the instant case, Ram has claimed the deduction under section 80C, which he omitted to claim in the original return of income, through a letter addressed to the Assessing Officer and not by filing a revised return under section 139(5). In view of the decision of the Supreme Court cited above, the Assessing Officer was justified in completing the assessment without allowing the deduction under section 80C.

Solution to question 6(C)

(1)

As per the definition under section 194C, "work" shall not include manufacturing or supplying a product according to the requirement or specification of a customer by using raw material purchased from a person, other than such customer. This is regardless of the quantum of expenditure incurred towards printing or processing comprised in the bill amount.

The problem clearly states that Raj Kumar & Co. has to manufacture the jute bags using raw materials purchased from outsiders and that the assessee Bharathi Cements Ltd has not sold any material to them. Therefore, in this case, it is a contract of sale. Hence, the provisions of section 94C are not attracted and no liability to deduct tax at source would arise.

(2)

This issue has been clarified by the CBDT Circular No.8/2009 dated 24.11.2009. As per provisions of section 194J(1), any person, who is responsible for paying to a resident any sum by way of fees for professional services, shall, at the time of credit of such sum to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to 10% of such sum as TDS.

Further, as per clause (a) of Explanation to section 194J "professional services" includes services rendered by a person in the course of carrying on medical profession.

The services rendered by hospitals to various patients are primarily medical services and, therefore, ***the provisions of section 194J are applicable on payments made by TPAs to hospitals*** etc. Further, for invoking provisions of section 194J, there is no stipulation that the professional services have to be necessarily rendered to the person who makes payment to hospital. Therefore, TPAs who are making payment on behalf of insurance companies to hospitals for settlement of medical/ insurance claims etc. under various schemes including Cashless Schemes are liable to deduct tax at source under section 194J on all such payments to hospitals etc.

In view of the above, all such transactions between TPAs and hospitals would fall within the ambit of provisions of section 194J.

(3)

(i) Where the payer is an individual or HUF whose turnover exceeds the monetary limits specified in clause (a) of section 44AB, he has to deduct tax at source. Since the turnover of Mr. Anand was ` 202 lakhs for the A.Y.2017-18, he is liable to deduct tax at source under section 194-I in respect of rental payments during the financial year 2017-18.

Accordingly, Mr. Anand is liable to deduct tax at source under section 194-I on the rental payments made. Section 194-I provides that rent includes any payment, by whatever name called, for the use of land or building together with furniture, fittings etc. Therefore, in the given case, apart from monthly rent of ` 10,000 p.m., service charge of ` 6,000 p.m. for use of furniture and fixtures would also attract TDS under section 194-I. Since the aggregate rental payments to Mr. R during the financial year 2016-17 exceeds ` 1,80,000, Mr. Anand is liable to deduct tax at source @10% under section 194-I from rent paid to Mr. R.

(ii) The definition of "work" under Explanation to section 194-C includes catering services and therefore, TDS provisions under section 194C are attracted in respect of payments to a caterer. As the payment exceeds ` 30,000, the nationalised bank is required to deduct tax at source at 2% on the payments made to catering organisation under 194-C. If the catering organization is an individual or HUF, then the tax deduction shall be @1%.

Solution to question 7

(a)

Computation of tax liability of Nandita for the A.Y. 2018-19 Particulars `	`
Indian Income	5,10,000
Foreign Income	1 , 10,000
Gross Total Income	***6,20,000***
Less: Deduction under section 80C	
Deposit in PPF	1,50,000
Under section 80CCC	

Contribution to approved Pension Fund of LIC			32,000
Under section 80CCE			1,82,000
The aggregate deduction under section 80C, 80CCC and 80CCD(1) has to be restricted to ` 1,50,000			1,50,000
Under section 80D			
Contribution to Central Government Health Scheme ` 28,000 is also allowable as deduction under section 80D. Since she is a resident senior citizen, the deduction is allowable to a maximum of ` 30,000 *(See Note 1)*			28,000
Medical insurance premium of ` 26,000 paid for father aged 84 years. Since the father is a non-resident in India, he will not be entitled for the higher deduction of ` 30,000 eligible for a senior citizen, who is resident in India. Hence, the deduction will be restricted to maximum of ` 25,000.		25,000	2,03,000
Total Income		***4,17,000***	
Tax on Total Income			
Income-tax (See Note below)		5,850	
Add : Education cess @2%		117	
Add: SHEC @1%		58	
		6,025	
Average rate of tax in India (i.e. ` 6,025/ ` 4,17,000 × 100)	***1.445%***		
Average rate of tax in foreign country (i.e. ` 11,000/ ` 1,10,000 ×100)	***10%***		
Rebate under section 91 on ` 1,10,000 @ 1.445% (lower of average Indian-tax rate or average foreign tax rate)	***1,589***		

Tax payable in India (` 6,025 – ` 1,589) *4,436*

(b)

The amount of capital gains arising to R has to be computed applying the provisions of sub-section (7) of section 94, which provides that "where:

(a) any person buys or acquires any securities or unit within a period of three months prior to the record date; and

(b) such person sells or transfers -

(i) such securities within a period of three months after such date; or

(ii) such unit within a period of nine months after such date; and

(c) the dividend or income on such securities or unit received or receivable by such person is exempted, then the loss, if any, arising to him on account of such purchase and sale of securities or unit, to the extent such loss does not exceed the amount of dividend or income received or receivable on such securities or unit, shall be ignored for the purpose of computing his income chargeable to tax".

For this purpose, "record date" means such date as may be fixed by a company for the purpose of entitlement of the holder of the securities to receive dividend; "securities" includes stocks and shares.

Computation of capital gains of Mr. R for the assessment year 2018-19

Long term capital gain on sale of building		75,000
Less: Short term capital loss on sale of shares		
700 shares		7,000
300 shares	7,500	14,500
Taxable Long term capital gain		60,500

Computation of capital gain on sale of shares of A Ltd. by Mr. R

Date of purchase of shares		30.5.2017
Record date		10.8.2017
Date of sale of shares	30.9.2017	20.12.2017
Number of shares sold	700	300
Sale price per share	`35	`25
Sale consideration	`24,500	`7,500
Less:		
Cost of acquisition	`35,000	`15,000
	`10,500	***`7,500***
Less:		
Dividend income as per section 94(7)[700× `10×50%] [See Note below]	`3,500	
Short term capital loss on sale of shares	***`7000***	***`7500***

Note:

(1) 700 shares are sold within 3 months after the record date. Hence, as per section 94(7), the related dividend income should be deducted from the loss.

(2) 300 shares having been sold after 3 months of record date, section 94(7) is not attracted. Therefore, the dividend income of ` 1,500 [300×`10×50%] should not be deducted. Such dividend is exempt under section 10(34).

(3) Short-term capital loss can be set-off against long-term capital gains as per the provisions of section 74(1)(a). Therefore, short-term capital loss on sale of shares can be set-off against long-term capital gains on sale of building.

(c)

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

"Specified Service" means

(1) online advertisement;

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

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

However, equalisation levy shall not be levied-

- where the non-resident providing the specified services has a permanent establishment in India

- the aggregate amount of consideration for specified service received or receivable during the previous year does not exceed ` 1 lakh.

- where the payment for specified service is not for the purposes of carrying out business or profession

(i) Where PQR Inc. has no permanent establishment in India

In the present case, ABC Ltd. is required to deduct equalisation levy of ` 30,000 i.e., @6% of ` 5 lakhs, being the amount paid towards online advertisement services provided by PQR Inc., a non-resident having no permanent establishment in India. Non-deduction of equalisation levy would attract disallowance under section 40(a)(ib) of 100% of the amount paid while computing business income.

(ii) Where PQR Inc. has permanent establishment in India

Equalisation levy would not be attracted where the non-resident service provider (PQR Inc., in this case) has a permanent establishment in India. Therefore, the ABC Ltd. is not required to deduct equalisation levy on ` 5 lakhs, being the amount paid towards online advertisement services to PQR Inc, in this case.

However, tax has to be deducted by ABC Ltd. at the rates in force under section 195 in respect of such payment to PQR Inc. Non-deduction of tax at source under section 195 would attract disallowance under section 40(a)(i) of 100% of the amount paid while computing business income.

(d)

Every jurisdiction, in its domestic tax law, prescribes the mechanism to determine residential status of a person. If a person is considered to be resident of both the Contracting States, relief should be sought from Article 4 of the Tax Treaty. A series of tie-breaker rules are provided in Paragraph 2 Article 4 of Model Convention to determine single state of residence for an individual.

The tie-breaker rule would be applied in the following manner:

(i) The first test is based on where the individual has a permanent home. Permanent home would mean a dwelling place available to him at all times continuously and not occasionally and includes place taken on rent for a prolonged period of time. Any place taken for a short duration of stay or for temporary purpose, may be for reasons such as short business travel, or a short holiday etc. is not regarded as a permanent home.

(ii) If that test is inconclusive for the reason that the individual has permanent home available to him in both Contracting States, he will be considered a resident of the Contracting State where his personal and economic relations are closer, in other words, the place where lies his centre of vital interests. Thus, preference is given to family and social relations, occupation, place of business, place of administration of his properties, political, cultural and other activities of the individual.

(iii) Paragraph (ii) establishes a secondary criterion for two quite distinct and different situations:

* The case where the individual has a permanent home available to him in both Contracting States and it is not possible to determine in which one he has his centre of vital interests;
- The case where the individual has a permanent home available to him in neither Contracting State.

In the aforesaid scenarios, preference is given to the Contracting State where the individual has an ***habitual abode7***.

(iv) If the individual has habitual abode in both Contracting States or in neither of them, he shall be treated as a resident of the Contracting State of which he is a ***national.***

(v) If the individual is a national of both or neither of the Contracting States, the matter is left to be ***considered by the competent authorities*** of the respective Contracting States.