Mock Test Paper - Series I: November, 2025

Date of Paper: 24th November, 2025

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FINAL COURSE: GROUP – II

PAPER – 7: DIRECT TAX LAWS & INTERNATIONAL TAXATION

SOLUTIONS

Division A – Multiple Choice Questions

MCQ No.	Most Appropriate Answer	MCQ No.	Most Appropriate Answer
1.	(a)	9.	(d)
2.	(c)	10.	(d)
3.	(b)	11.	(b)
4.	(c)	12.	(d)
5.	(a)	13.	(b)
6.	(c)	14.	(c)
7.	(a)	15.	(b)
8.	(c)		

1. Computation of Total Income of Bhagwati Private Ltd. as per section 115BAA for the A.Y.2025-26

	Particulars	Amount (₹)	
I	**Income from house property**		
	[Rental income from commercial property]		
	Gross Annual Value[1]/Net Annual Value	5,30,000	
	Less: Deduction under section 24(a)		
	30% of Net Annual Value	1,59,000	
			3,71,000
II	**Profits and gains of business and profession**		
	Net profit as per profit and loss account	1,07,00,000	

[1] *Rent received has been taken as the Gross Annual Value (GAV) in the absence of information relating to Municipal Value, Fair Rent and Standard rent.*

	Add: **Items debited but to be considered separately or to be disallowed**				
	B(ii) Donation paid to Swachh Bharat Kosh	85,000			
	[Not an expenditure incurred wholly and exclusively for the manufacturing business. Hence, not allowable under section 37]				
	B(iii) Contribution towards pension scheme of employees	50,000			
	[Contribution towards pension scheme, referred to in section 80CCD, of employees is allowed only to the extent of 14% of salary of the employee in the P.Y. i.e., ₹ 1,40,000 being 14% of ₹ 10,00,000. Therefore, the excess contribution of ₹ 50,000 [i.e., ₹ 1,90,000 – ₹ 1,40,000] is disallowed u/s 36(1)(iva).				
	B(iv) Bonus to employees	4,48,000			
	[Since the payment is made after the due date of filing return of income, disallowance under section 43B is attracted]				
	B(v) Provision for income-tax (including interest of ₹ 70,000 thereon)	4,20,000			
	[Not allowable as deduction. Disallowance under section 40(a)(ii) is attracted]				
	B(vi) Contribution to a University approved and notified u/s 35(1)(ii)	1,00,000			
	No deduction is allowed u/s 115BAA in respect of contribution to a University approved and notified u/s 35(1)(ii)				

	B(vii) Interest on loan borrowed for investing in shares of AMA Inc. [Allowability or otherwise of interest expenditure on earning dividend has to be considered separately under the head "Income from Other Sources"]	1,50,000	12,53,000		
			1,19,53,000		
	Add: Cash Payment for purchase of raw material deemed as income		45,000		
	AI(4) [Since the provision for outstanding bill for purchase of raw material has been allowed as deduction during the P.Y. 2023-24, cash payment in excess of ₹ 10,000 against such bill in the P.Y. 2024-25 would be deemed as income of P.Y. 2024-25 as per section 40A(3A)]				
			1,19,98,000		
	Less: Expenditure to be allowed				
	B(i) & AI(1) Depreciation [Difference between the normal depreciation of ₹ 16.75 lakhs as per Income-tax Act, 1961 *[See Note below]* and depreciation charged to the statement of profit and loss of ₹ 11.86 lakhs]. ***Note –*** [2]*Printers and scanners form an integral part of the computer system and they cannot be used without the computer. Thus, they are part of the computer system, they would be eligible for depreciation at the higher rate of 40% applicable to computers including computer*	4,89,000			

[2] *CIT v. BSES Yamuna Powers Ltd (2013) 358 ITR 47 (Delhi)*

	software. However, EPABX is not a computer and is, hence, not entitled to higher depreciation @40%[3] *Accordingly, depreciation of ₹ 1,25,000 on EPABX computed @ 25% (40% - 15%) is to be reduced from the depreciation given as per the Income-tax Act, 1961 of ₹ 18 lakhs. Thus, depreciation as per Income-tax Act, 1961 allowed as deduction would be ₹ 16.75 lakhs.*				
	AI(2)Additional depreciation on new plant and machinery [Not allowable as deduction under section 115BAA]	Nil			
	AI(3) Audit Fees relating to P.Y.2023-24	30,000	5,19,000		
	[₹ 30,000, being 30% of audit fees of ₹ 1,00,000 provided for in the books of account of F.Y.2023-24 would have been disallowed due to non-deduction of tax at source. Since tax has been deducted in October, 2024 and paid on 12.12.2024, the amount of ₹ 30,000 is deductible while computing business income of P.Y.2024-25].				
			1,14,79,000		
	Less: Items credited to statement of profit and loss, but not includible in business income				
	A(i) Rent received from vacant land [Chargeable to tax under the head "Income from other sources"]	2,55,000			

[3] *Federal Bank Ltd. v. ACIT (2011) 332 ITR 319 (Kerala)*

	A(ii) Rent received from commercial property owned by the company [Chargeable to tax under the head "Income from house property"]	5,30,000		
	A(iii) Interest received on income tax refund [Chargeable to tax under the head "Income from other sources"]	48,000		
	A(iv) Profit on sale of plot [Chargeable to tax under the head "Capital Gains"]	8,00,000		
	A(v) Dividend from AMA Inc. company	6,00,000	22,33,000	
	[Dividend received from foreign company is taxable under the head "Income from Other Sources"]			
			92,46,000	
	Profits and gains from the business of manufacturing			92,46,000
III	**Capital Gains**			
	Capital gain on sale of plot			
	Sale consideration		58,00,000	
	Less: Cost of Acquisition [since land is transferred on or after 23.7.2024, indexation benefit will not be to a person other than an individual or a HUF, resident in India]		50,00,000	
	Long-term capital gain			8,00,000
IV	**Income from Other Sources**			
	Rent received from vacant land		2,55,000	
	Interest received on income-tax refund		48,000	
	Dividend from AMA Inc., a foreign company	6,00,000		
	Less: Interest expenditure of ₹ 1,50,000 allowed deduction upto 20% of dividend	1,20,000	4,80,000	
				7,83,000

	Gross Total Income		**1,12,00,000**
	Less: Deductions under Chapter VI-A		
	Deduction under section 80G		
	Not allowable u/s 115BAA	-	
	Deduction under section 80M	4,80,000	
	Deduction in respect of inter-corporate dividend to the extent of ₹ 5,20,000, being dividend distributed by it one month prior to the due date specified u/s 139(1) or ₹ 4,80,000 dividend received to the extent includible in the gross total income, whichever is lower		4,80,000
	Total Income		**1,07,20,000**

2. (a) Computation of "Book Profit" for levy of MAT under section 115JB for A.Y. 2025-26

Particulars	₹	₹
Net Profit as per Statement of Profit and Loss		26,00,000
Add: Net profit to be increased by the following amounts as per *Explanation 1* to section 115JB(2):		
- **Provision for the loss of subsidiary**	2,00,000	
- **Provision for doubtful debts,** being the amount set aside as provision for diminution in the value of any asset	2,25,000	
- **Provision for income-tax** [As per *Explanation 2* to section 115JB, income-tax shall include, inter alia, any interest charged under the Act, therefore, whole of the amount of provision for income-tax including ₹ 55,000 towards interest payable has to be added back]	2,50,000	
- **Depreciation**	5,20,000	11,95,000
		37,95,000

Less: Net profit to be decreased by the following amounts as per *Explanation 1* to section 115JB:		
- **Share in income of an AOP as a member** [In a case, where AOP has paid tax on its total income at maximum marginal rate, no income-tax is payable by the company, being a member of AOP, in accordance with the provisions of section 86. Therefore, share in income of an AOP on which no income-tax is payable in accordance with the provisions of section 86, would be reduced while computing book profit, since the same has been credited to profit and loss account]	2,50,000	
- **Income from units in UTI** [Income from units in UTI not to be reduced while computing the book profits, since the same is taxable in the hands of unitholders]	-	
- **Depreciation** other than depreciation on revaluation of assets (₹ 5,20,000 – ₹ 3,00,000)	2,20,000	
- **Unabsorbed depreciation or brought forward business loss**, whichever is less, as per the books of account. Lower of unabsorbed depreciation ₹ 5,00,000 and brought forward business loss ₹ 9,00,000 as per books of accounts has to be reduced while computing the book profit]	5,00,000	9,70,000
Book Profit		**28,25,000**

Computation of MAT liability under section 115JB

Particulars	₹
15% of book profit	4,23,750
Add: Health & education cess@4%	16,950
Minimum Alternate Tax liability	**4,40,700**

Notes:

(1) It is only the specific items mentioned under *Explanation 1* to section 115JB, which can be adjusted from the net profit as per the Statement of Profit and Loss prepared as per the Companies Act for computing book profit for levy of MAT. Since the following items are not specified thereunder, the same cannot be adjusted for computing book profit:

- Interest to financial institution (unpaid before filing of return) and
- Penalty for infraction of law

(2) Provision for gratuity based on actuarial valuation is an ascertained liability *[CIT v. Echjay Forgings (P) Ltd. (2001) 251 ITR 15 (Bom.)]*. Hence, the same should not be added back to compute book profit.

(3) As per proviso to section 115JB(6), the profits from unit established in special economic zone cannot be excluded while computing the book profit, and hence, such income would be liable for MAT.

(b) Since Mr. Arvind is an individual resident in India for the P.Y.2024-25, his global income would be subject to tax in India. Therefore, income earned by him in Country X and Country Y would be taxable in India. He would, however, be entitled to deduction under section 91, since India does not have a DTAA with Country X and Country Y, and all conditions under section 91 are satisfied.

Computation of total income of Mr. Arvind for A.Y. 2025-26 under default tax regime

Particulars	₹	₹
Income under the head "Salaries"		
Pension from State Government	4,10,000	
Less: Standard deduction u/s 16(ia)	75,000	
		3,35,000

Income from House Property		
Rental income from property in Country Y[4]	3,40,000	
Less: Municipal taxes	25,000	
	3,15,000	
Less: Deduction u/s 24(a)@30%	94,500	
		2,20,500
Profits and Gains of Business or Profession		
Speculative income in India	1,25,000	
Less: Set-off of business loss from proprietary business in Country Y under section 70	1,20,000	
		5,000
Short-term capital gains on sale of plot in India		2,40,000
Income from Other Sources		
Agricultural income from Country X [not exempt u/s 10(1), since it is earned from land situated outside India]	1,00,000	
Dividend from a company in Country X	70,000	
		1,70,000
Gross Total Income		9,70,500
***Less:* Deduction under Chapter VI-A [No deduction allowable as per section 115BAC]**	-	-
Total Income		**9,70,500**

Computation of net tax liability of Mr. Arvind for A.Y.2025-26

Particulars		₹
Tax payable on ₹ 9,70,500		
Upto ₹ 3,00,000	Nil	
₹ 3,00,000 to ₹ 7,00,000 @ 5%	20,000	
₹ 7,00,000 to ₹ 9,70,500 @10%	27,050	47,050
Add: Health and education cess@4%		1,882
		48,932
Less: Rebate under section 91 **(See Working Note below)**		10,067

[4] *In the absence of any information relating to fair rent, municipal value and standard rent, rental income is assumed to be the gross annual value.*

Tax Payable		**38,865**
Tax Payable (rounded off)		**38,870**
Calculation of Rebate under section 91:	₹	
Average rate of tax in India [i.e., ₹ 48,932/ ₹ 9,70,500 x 100] = 5.042%		
Doubly taxed income pertaining to Country X		
Agricultural income	1,00,000	
Dividend from a company in Country X [Not includible, since exempt in Country X]	-	
	1,00,000	
Rebate under section 91 on ₹ 1,00,000 @5.042% [being the lower of average Indian tax rate (5.042%) and Country X tax rate (10%)]		5,042
Doubly taxed income pertaining to Country Y		
Income from house property ***less*** business loss set-off against income chargeable to tax in India (₹ 2,20,500 – ₹ 1,20,000)	1,00,500	
Rebate under section 91 on ₹ 1,00,500 @5% [being the lower of average Indian tax rate (5.042%) and Country Y tax rate (5%)]		5,025
Total rebate under section 91 (Country X + Country Y)		**10,067**

3. (a) (i) As per *Explanation* 4(iii) to Section 11(1), only 85% of the amount paid to Harmony Educational Trust (other than for corpus) is considered as an application of income. Accordingly, ₹ 68 lakh will be treated as an application of income for charitable purposes.

(ii) As per *Explanation 2* to Section 11(1), any contribution made by one trust to another trust or institution (even if registered under Section 12AB or Section 10(23C)(iv)/(v)/(vi)/(via)) with a direction that such amount shall form part of corpus is **not** considered as an application of income for charitable purposes. Therefore, the ₹ 80 lakhs given for corpus will **not** be treated as an application of income for Lotus Welfare Foundation.

As per section 11(1)(d), an amount received by a fund/ trust/ institution etc. would not be included in the total income, if such amount is received with a specific direction that it shall form part of the corpus and the said corpus contribution is invested in any of the modes specified under section 11(5).

(b) As per section 13(2), if any part of the income or the property of the trust or institution is or continues to be lent to any "specified person" referred to in section 13(3) for any period during the previous year without either adequate security or adequate interest or both, such income or property is to be deemed to have been used or applied for the benefit of a person referred to in section 13(3).

In the present case, Mr. Karan has made a substantial contribution of ₹ 70,000 which exceeds the limit of ₹ 50,000 to SDP Foundation, he would fall within the category of persons specified under section 13(3).

SDP Foundation trust gave loan of ₹ 5 lakhs out of the income of the trust without any security to Mr. Karan though rate of interest i.e., 12% is higher than the market rate of 11.50%, such income/loan amount of ₹ 5 lakhs is deemed to have been used or applied for the benefit of Mr. Karan, being a person specified u/s 13(3). By virtue of section 13(1)(c), the provisions of section 11 or 12 would not apply to such income to exclude from the total income of the P.Y. 2024-25.

Consequently, the income of ₹ 5 lakhs would be considered as specified income u/s 115BBI and be taxable @30%.

Further, in terms of section 271AAE, penalty of ₹ 5 lakhs would also be leviable, calculated at 100% of income provided as a benefit, where the violation is noticed for the first time during any previous year.

(c) Computation of total income and tax liability of Winter Technologies Inc., a non-resident German company, for the A.Y. 2025-26:

Particulars	₹
Profits and gains from business or profession	
Business Income from a unit established at Mumbai	8,00,000
Income from other sources	
➢ Dividend income from BlueWave Ltd. an Indian company	12,50,000
➢ Fees for technical services [would be equivalent to the amount of debentures of ₹ 20,00,000 received from an Indian company, issued in consideration of providing technical knowhow]	20,00,000
➢ Interest on Debentures [₹ 20,00,000 x 8% x 6/12]	80,000
➢ Dividend on Global Depository Receipts (GDRs) of Greenfields Ltd. an Indian company, issued under a scheme of Central Government against the initial issue of Greenfields Ltd. and purchased in foreign currency by Winter Technologies Inc	5,50,000

➢ Royalty income received from RedTech Ltd. an Indian company in pursuance of an agreement approved by Central Government	10,00,000
Gross Total Income/ Total income	56,80,000
Computation of tax liability	
Dividend income of ₹ 12,50,000, taxable @20% u/s 115A	2,50,000
Dividend on GDRs of ₹ 5,50,000, taxable @10% u/s 115AC	55,000
Royalty income of ₹ 10,00,000, taxable @20% u/s 115A, since it is in pursuance of an agreement approved by the Central Government	2,00,000
FTS of ₹ 20,00,000, taxable @35%, since it is not in pursuance of an agreement approved by the Central Government	7,00,000
Interest on debentures of ₹ 80,000, taxable @35%, since debt is incurred in Indian currency, it is not eligible for concessional rate of 20% u/s 115A	28,000
Business income of ₹8,00,000 [taxable @35%]	2,80,000
	15,13,000
Add: Health and education cess@4%	60,520
Tax liability	**15,73,520**

4. **(a)** **(i)** M/s Crystal Wash Pvt. Ltd is required to deduct tax at source on commission paid to Mr. Mohan Kumar under section 194H @5% till 30.9.2024 and @2% from 1.10.2024, being sum exceeding ₹ 15,000.

Reimbursement of expenses of ₹ 1.6 lakhs for booking air tickets for Mr. Mohan Kumar and his family and laptop of ₹ 80,000 for achieving sale target is benefit or perquisite arising to Mr. Mohan Kumar from his business or the exercise of his profession, being sum exceeding ₹ 20,000. Accordingly,
M/s Crystal Wash Pvt. Ltd is required to deduct tax at source under section 194R @10%.

Tax to be deducted under section 194H = 5% on ₹ 1,55,000 + 2% on ₹ 1,80,000 = ₹ 11,350

Tax to be deducted under section 194R = 10% on ₹ 1,60,000 (Air tickets) + + ₹ 80,000 (laptop) = ₹ 24,000

(ii) Section 192 provides that tax is required to be deducted on the payment made as salaries. Tax is to be deducted on the estimated income at the

rates specified under section 115BAC(1A) or at the average of income tax computed on the basis of the rates in force for the financial year in which payment is made in case the employee submitted a declaration of opt out of the default regime under section 115BAC.

The employee may declare details of his other incomes (including loss under the head "Income from house property" but not any other loss) to his employer. In this case, since Mr. Suhas has submitted a declaration of opt out of section 115BAC and also notified his employer TP Ltd. of loss from self-occupied house property, the employer has to take the same into consideration for deduction of tax at source.

Therefore, TP Ltd. is required to deduct tax at source on the salary of ₹ 85,000 per month paid to Mr. Suhas, in the following manner:

Particulars	Amount (₹)
Income under the head salaries (₹ 85,000 x 12)	10,20,000
Less: Standard deduction under section 16(ia)	50,000
	9,70,000
Income under the head "house property"	(1,95,000)
Gross total income	**7,75,000**
Less: Deduction under Chapter VI-A	Nil
Total Income	**7,75,000**
Tax on ₹ 7,75,000	67,500
Add: Health and Education cess@4%	2,700
Tax to be deducted at source	**70,200**

(b) Any income arising from an international transaction, between two or more "associated enterprises", shall be computed having regard to arm's length price as per the provisions of Chapter X of the Act. Section 92A defines an "associated enterprise" and sub-section (2) of this section speaks of the situations when the two enterprises shall be deemed to be associated enterprises.

Transaction with Sakura Industries Ltd.

Sakura Industries Ltd. is a wholly owned subsidiary of PCIL and is a non-resident company. Hence, it is an associated enterprise. Royalty falls within the meaning of international transaction, since it is payment for supply of know-how, being an intangible property. Sakura Industries Ltd. is currently paying a royalty of USD 3 million per annum to PCIL for supply of know-how. For similar supply of know how

to Hikari Ltd., a wholly owned Government Company in Japan, PCIL receives annual royalty of USD 4 million.

Under CUP Method, ALP has to be taken as USD 4 million. Understatement of royalty is 1 million USD, i.e., 1 M USD x ₹ 82 = ₹ 820 lakhs.

Transaction with Orion Capital Inc.

As per section 92A(2), if one enterprise advances loan to the other enterprise of an amount of 51% or more of the book value of the total assets of such other enterprise, the two enterprises would be deemed to be associated enterprises.

As on the date of borrowing, the amount advanced is ₹ 220 crores out of ₹ 330 crores, which comes to 66.67%. Hence, Orion Capital Inc., is deemed to be an associated enterprise of PCIL. Interest payments are also covered by the term "international transaction".

Orion Capital Inc., has charged interest at 8% and PCIL has paid interest of ₹ 17.6 crores for the year ended 31.3.2025. Interest rate charged to other parties is 7%. This has to be taken as the ALP rate.

In view of this, the interest payment should have been 17.6 x 7/8 i.e., ₹ 15.4 crores. An excess payment of 2.2 crores over the ALP has been made.

Transaction with PBC

In PBC, PCIL holds 22/92 i.e., 23.91% of the voting power. Since PCIL holds less than 26% of the voting power, PBC is not an associated enterprise. Hence, the transfer pricing provisions would not be applicable on sales made by PCIL to PBC.

5. (a) (i) The time limit for service of notice under section 143(2) is three 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 2024-25 was filed by the assessee on 25th October, 2024. Therefore, the notice under section 143(2) has to be served by 30th June, 2025. However, the notice was served on the assessee only on 9th July, 2025. 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, Novatech Industries Pvt. Ltd, had raised an objection to the proceeding, on the ground of non-service of the notice under section 143(2) on time, then, the validity of the assessment order can be challenged. In absence of such objection, the assessment order cannot be challenged.

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

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

Analysis and Conclusion: Section 90(2) provides that the provisions of the DTAAs would override the provisions of the Act in cases where the provisions of DTAAs are more beneficial to the assessee. Even the charging sections 4 and 5 of the Act, which deal with the principle of ascertainment of total income under the Act, are also subordinate to the principle enshrined in section 90(2).

Thus, in so far as the applicability of the scope/rate of taxation with respect to the impugned payments made to the non-residents is concerned, no fault can be found with the rate of taxation invoked by the assessee based on the DTAAs, which prescribed for a beneficial rate of taxation. The provisions of tax withholding, i.e., section 195 of the Act, would apply only to sums that are otherwise chargeable to tax under the Act. The provisions of DTAAs, along with sections 4, 5, 9, 90 & 91 of the Act, are relevant while applying the provisions of tax deduction at source.

Therefore, section 206AA of the Act cannot be understood to override charging sections 4 and 5 of the Act.

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

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

(iii) **Issue Involved:** The issue under consideration is whether prosecution proceedings can be initiated where tax deducted has been deposited by the assessee suo moto, after the time prescribed under the Act but before receiving notice from the income-tax department, along with interest under section 201(1A) and the assessee has shown reasonable cause for such delay.

Relevant provisions of law: Prosecution proceedings are attracted under section 276B, if a person fails to pay to the credit of the Central Government, the tax deducted at source by him as required under the provisions of the Act. The punishment is rigorous imprisonment for not less than 3 months but which may extend to 7 years and with fine. Section 278AA, however, provides that no person would be punishable for such failure if he proves that there was reasonable cause for the same.

Analysis & Conclusion: The CBDT has, vide Circular No. 24/2019 dated 9.9.2019, in exercise of the powers under section 119, listed out the offences covered under Chapter XXII of the Income-tax Act, 1961 in respect of which prosecution proceedings shall be launched by Approving Authority being the Sanctioning 15 Authority where the quantum of offences exceed the prescribed monetary threshold. Accordingly, in case of failure to pay TDS under section 276B or failure to pay TCS u/s 276BB, no prosecution will be processed if the TDS/TCS amount does not exceed ₹ 25 lakhs and delay in deposit is less than 60 days. In this case, the company has reasonable and sufficient cause since it was facing financial hardship on account of large sum of money stuck up with the debtors and also with the income-tax department on account of refunds. Inspite of the financial crisis, the company has *suo moto* deposited the TDS along with interest under section 201(1A) of the Act, before receiving any notice from the income-tax department in this regard. Since it has deposited the TDS along with interest *suo moto* before receiving any notice from the department and it has also shown reasonable cause for such delay in

deposit, the company cannot be punishable for the delay in deposit of TDS. The initiation of prosecution proceedings under section 276B against the company and the directors is, therefore, not correct.

Note - *The facts given in the question are similar to the facts in ACIT v. AT-Dev Prabha (JV) and others (2023) 454 ITR 59, wherein the above issue came up before the Supreme Court. The above answer is based on the rationale of the Supreme Court in the said case read along with the CBDT Circular.*

(b) **(i)** In order to complete tax cases, a country may require certain information which may be available with the treaty partner. Article 26 provides for the information which may be exchanged and the manner in which such a request has to be made. The OECD and UN Model Conventions are similar with respect to this Article.

Importance of Article 26:

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

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

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

6. **(a)** In the given case, M/s. DesignSphere Inc., a company incorporated in Country Z9, entered into a contractual arrangement with Serenity Estates Pvt. Ltd., an Indian company, for rendering architectural design services in India.

M/s DesignSphere Inc. constituted a partnership firm in its home country with one of its directors as a nominal partner in order to avoid tax liability in India. The newly formed firm entered into the agreement with the Indian client, while the actual manpower and resources were seconded from the company. The firm thereafter claimed that the payment was not taxable in India under the India–Z9

tax treaty, as it had no fixed base and its partners/employees did not stay in India beyond the 180-day limit.

It is obvious that there was no commercial necessity to create a separate firm except to obtain the tax benefit. The firm was only on paper as the manpower was drawn from the company. The firm did not have any commercial substance. Moreover, it is a case of treaty abuse. Hence, GAAR may be invoked to disregard the firm and tax payment for architectural services as fee for technical services. However, the rate of tax on such payment shall be as applicable under the treaty, if more beneficial.

(b) A resident can make an application for advance ruling in relation to his tax liability arising out of one or more transactions valuing ₹ 100 crore or more in total which has been undertaken or is proposed to be undertaken.

Since the value of transactions between M/s Unicorn Ltd and M/s Orange Inc for providing technical knowhow exceeds ₹ 100 crores, Unicorn Ltd. can make an application for advance ruling with the Board for Advance Rulings.

As per section 245U, the Board for Advance Rulings shall have all the powers of the Civil Court in respect of discovery and inspection, enforcing the attendance of any person, including any officer of a banking company and examining on oath, issuing commissions and compelling the production of books of accounts and other documents.

Accordingly, the Board can ask for the production of books of accounts before passing advance ruling for Unicorn Ltd.

(c) As per section 40A(3), where the assessee incurs any expenditure, in respect of which payment or aggregate of payments made to a person in a day otherwise than by an account payee cheque drawn on a bank or by an account payee bank draft or use of electronic system through bank account or through such other prescribed electronic modes exceeds ₹ 10,000, such expenditure shall not be allowed as a deduction.

Clause 21(d) of Form 3CD requires the tax auditor to report, on the basis of the examination of books of account and other relevant documents/evidence, whether the expenditure covered under section 40A(3) read with rule 6DD were made by account payee cheque drawn on a bank or account payee bank draft; and if not, to furnish details mentioned thereunder, namely, date of payment, nature of payment, amount etc.

The Guidance Note on Tax Audit issued by ICAI states that there may be practical difficulties in verifying whether each payment is made through account payee

cheque or bank draft or ECS or other prescribed electronic modes. Where the reporting has been done on the basis of the certificate of the assessee, the fact has to be reported as an observation in para 3 of Form 3CA.

The tax auditor is required to point out in tax audit report, the violation of the provisions of section 40A(3) thereof involving expenditure to a person in a day exceeding ₹ 10,000 otherwise than by way of account payee cheque/bank draft, ECS and other prescribed electronic modes. However, in this case, the tax auditor has certified that there was no such instance, though such instances aggregate to a large quantum of ₹ 18 crores.

The tax auditor should have considered the nature of business i.e., jewellery business of the assessee and accordingly undertaken necessary checks to verify whether there are cash payments in violation of section 40A(3). He should have made use of the audit tools which are available to find out such payments expeditiously and accurately where the data is voluminous.

In this case, considering the nature of business of the assessee, namely, jewellery business, the onus was on the tax auditor to verify the same before reporting in Form 3CD. Mere reliance on certificate issued by the management is not acceptable in such a case. Also, even in a case where the reporting has been done on the basis of the certificate of the assessee, the fact has to be reported as an observation in para 3 of Form 3CA, which he had failed to do.

Thus, in the case, the tax auditor had failed to exercise due diligence in the conduct of his professional duties. He had also failed to obtain sufficient information which is necessary for expression of opinion. On account of such failure, clauses (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949 may be invoked.