



Sec 96: Impermissible Avoidance Agreement

IAA means an arrangement which satisfies two conditions:-

1. Main purpose/one of the main purpose of which is to obtain a tax benefit ; and
2. It:
 - ☛ Creates rights/obligations which are not ordinarily created between persons dealing arm's length or
 - ☛ Results (directly or indirectly) in misuse or abuse of provisions of Act or
 - ☛ Entered/carried in a manner, which are not ordinarily employed for bonafide purposes or
 - ☛ Lacks commercial substance or
 - ☛ Deemed to lack commercial substance.

Transaction shall be deemed to lack commercial substance

S.No.	Nature Of Transaction	Example
1.	Substance of the transaction differs significantly from its Form (Form v/s Substance)	A transaction has been stated to be a sale and lease transaction, but in substance it is only a make and believe story.
2.	The only purpose of selection of such Location of asset/transaction/place of residence of any party is to obtain tax benefit and there is no substantial commercial purpose for selecting such Location of asset/transaction/place of residence of any party.	A transaction between A Ltd. of Netherlands and B Ltd. of Hongkong is executed through a conduit C Ltd. in a Tax Heaven.
3.	Arrangement does not significantly affect business risk/net cash outflows of any party to the arrangement but only attributes tax benefits	X Ltd. Located in tax holiday area taken a P&M on rent of ₹ 4 Crores from sister concern and given it on rent to another sister concern for rent of ₹ 10 Crores.
4. (i)	Transaction involves: Round Tripping, which includes any arrangement in which, through series of transactions :- (a) funds are transferred among parties (b) such transactions have no substantial commercial purpose other than obtaining tax benefit. It is irrelevant that: ☛ funds involved in round trip financing can be traced to any funds transferred/ received (direct nexus not relevant) ☛ time or sequence in which funds are transferred/received	(a) A group company in profit, obtains loan from market and gives loan to sister concern interest free; and claims it to be for business purposes. (b) A company (X Ltd.) purchases shares of group company, from another group company at a high value and sells it to another group company at low value. This results in a loss to X Ltd. This transaction can be vice-versa. (c) A group company in profit, obtains loan from market. Uses the loan for business, and gives loan to sister concern out of own funds. (direct nexus not relevant)



	☛ Manner/Mode in which funds are transferred/received	
ii	An accommodating party i.e. a party, the main reason for whose participation is to obtain (directly or indirectly) a tax benefit. It is irrelevant that the accommodating party is associated person or not.	A Ltd. sells shares to subsidiary company B Ltd. at a lower value and books a loss (A Ltd. wanted a loss). B Ltd. transfers the shares at a higher value in the market and books a profit (Subsidiary wanted a profit). Here B Ltd. is the accommodating party.
iii	Elements have the effect of offsetting or cancelling each other	Cross transfer in Clubbing Topic.
iv	A transaction conducted through one or more persons and disguises the value/location/source/ownership/control of funds	A share capital is invested in India by a company in Mauritius, the source of investment in Indian company is not disclosed.

Further, it has been provided that following shall be irrelevant for deciding whether a transaction lacks commercial substance or not: -

- ✓ Period/time for which arrangement exists.
- ✓ Fact of payment of taxes, directly or indirectly, under the arrangement.
- ✓ Fact that an exit route (including transfer of any activity/ business/ operations) is provided by the arrangement.

While treating a transaction as IAA:

- ✓ An equity may be treated as debt or vice-versa
- ✓ Capital receipt may be treated as revenue receipt or vice-versa.
- ✓ Expenditure/ deduction/ relief/ rebate may be recharacterised.

Sec 98: Consequence of IAA

If any arrangement is declared to be IAA, then the **consequences** shall be determined in such manner as is **deemed appropriate**, in the circumstances of the case. Circumstances of case may results in denial of any tax benefit or benefit under DTAA. The impact of treating a transaction as IAA may result into following illustrative situations: -

- (a) disregarding, combining or re-characterising any step in, or a part or whole of, the IAA;
- (b) treating the IAA 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 [treating accommodating party as benami];
- (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; [holding concerns as benami]
- (e) reallocating amongst the parties to the arrangement-
 - ☛ any accrual, or receipt, of a capital or revenue nature; or
 - ☛ any expenditure, deduction, relief or rebate;



(f) Treating-

- ☞ the place of residence of any party to the arrangement; or
- ☞ the situs of an asset or of a transaction, at a place other than the place of residence or location of the asset or location of the transaction as provided under the arrangement;

(g) considering or looking through any arrangement by disregarding any corporate structure [lifting of corporate veil/ disregarding the alter-ego]

Important Definitions

➤ Arrangement: - Means whole/part/step in of any transaction/operation/scheme/agreement/understanding. It covers transactions, whether enforceable or not.

➤ Associated person

Type of Assessee	Associated Person (AP)
Individual	Relative (same as u/s. 56(2)(x))
HUF, Company, Firm/ AOP/ BOI, Other Persons	Same as given in section 40A(2) of PGBP

➤ "Tax benefit" means: -

- (a) Reduction/avoidance/ deferral of tax under domestic law/DTAA
- (b) Increase in refund under domestic law/ DTAA
- (c) Reduction in total income/ increase in loss.

➤ "Party" also covers Permanent Establishment (PE).

Sec 144BA: Power to treat a transaction as IAA - Procedural Provisions

PC/C : Principal Commissioner/Commissioner

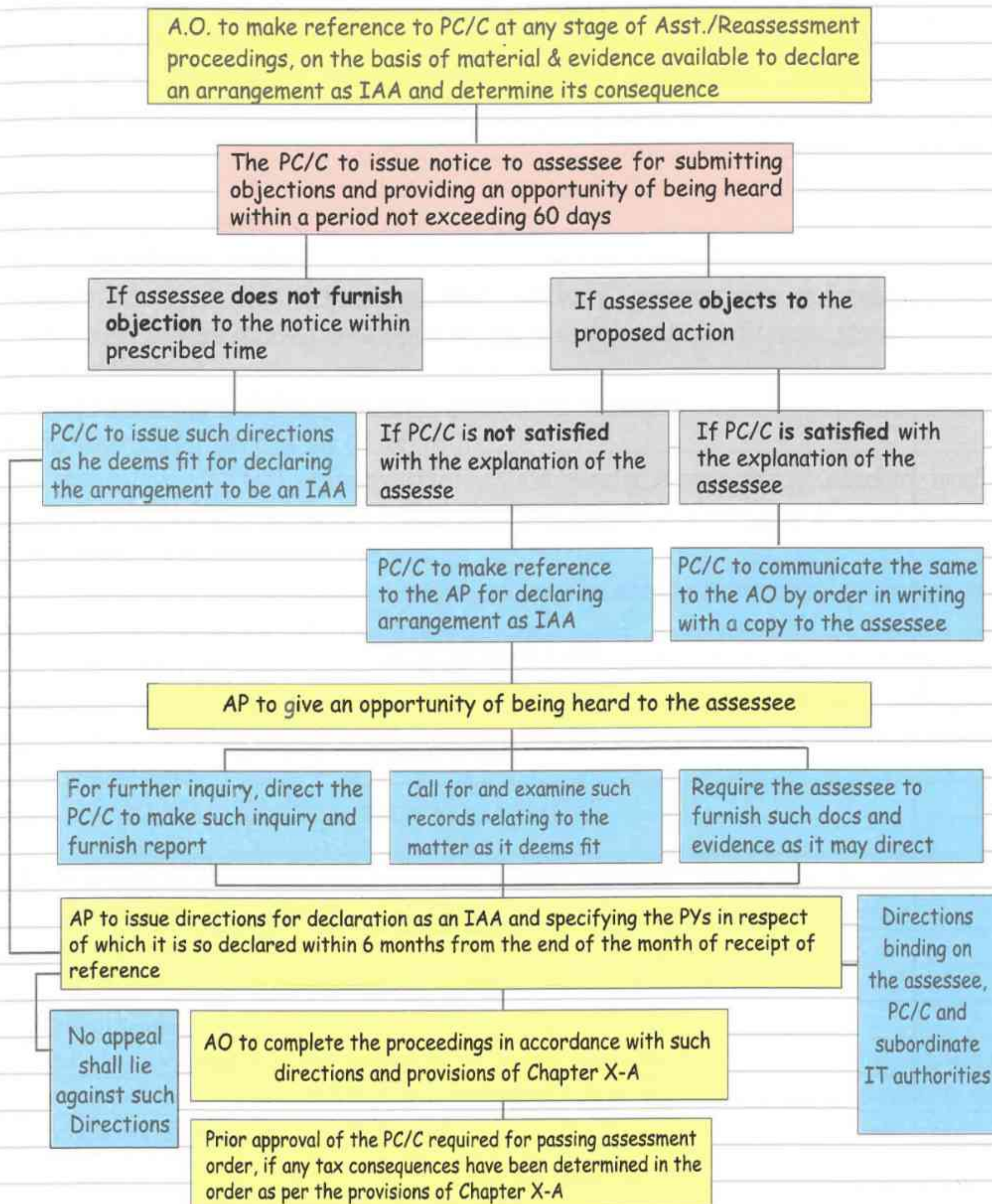
AP : Approving Panel

AO: Assessing Officer

IAA: Impermissible Avoidance Agreement

Approving Panel (AP)

- ☞ Constitution: CG may constitute one or more Approving Panels.
- ☞ Composition: Each AP may shall consist of 3 members including a Chairperson.
- ☞ Qualification: - Chairman shall be a person who is or has been a judge of a High Court
 - 1 member shall be a member of IRS not below the rank of PCCIT/CCIT
 - 1 member shall be an academic or scholar having special knowledge of matters such as direct taxes, business accounts and international trade practices.
- ☞ Term: Ordinarily for 1 year; May be extended from time to time upto a period of 3 years.



Notes



Sec 115BBH: Tax on Income from VDA [Applicable from AY 23-24 i.e. 01/04/2022]

Income on transfer of VDA taxable @30%.

Notes:

- Any expenses, allowance or set-off of any loss **not allowed** while calculating income on transfer of VDA **except cost of acquisition of VDA**.
- Loss on transfer of VDA **not allowed to set off against any other income** and also assessee **cannot carry forward** such losses.
- "Virtual digital asset" means—
 - any information or code or number or token (not being Indian currency or foreign currency), generated through cryptographic means or otherwise and can be transferred, stored or traded electronically;
 - a non-fungible token (NFT) or any other token of similar nature;
 - any other digital asset, as the CG may notify.
- NFT shall not include a NFT whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.
- Following **shall not be treated** as VDA
 - Gift card or vouchers**, being a record that may be used to obtain goods or services or a discount on goods or services;
 - Mileage points, reward points or loyalty card**, being a record given without direct monetary consideration under an award, reward, benefit, loyalty, incentive, rebate or promotional program that may be used or redeemed only to obtain goods or services or a discount on goods or services;
 - Subscription to websites** or platforms or application.

Sec 194S: TDS on payment of VDA [Applicable from 01/07/2022]

Nature of Payment	Payer	Payee	Limit	Rate
Consideration for transfer of VDA	Any Person	Resident Person	Consideration > ₹ 10,000	1% of Consideration

Additional Points

- In case of **payer** being **Ind/HUF** not having any income under the head **PGBP** or having Business or profession but last year T/O or G/R does not exceed ₹ 1 Cr in case of business or ₹ 50 Lakhs in case of profession required to deduct TDS only if **consideration is more than ₹ 50,000**. In this case **payer not required to obtain TAN & section 206AB also not applied**.
- If the consideration for transfer of VDA is wholly in kind or in exchange of other VDA or it is partly in kind & partly in cash and the cash balance is not sufficient enough to meet the TDS liabilities, then Payer shall **release the consideration only after ensuring that tax is paid on such consideration**.
- If provision of section **194-O** and **194S** both apply then TDS deducted u/s **194S**.



Note: In section 194S specified person (Ind/HUF ref. in point 1) required to pay TDS within 30 days from end of the month in which TDS deducted along with statement in form 26QE.

#CBDT Guidelines

1. TDS applicable on consideration excluding GST and commission.
2. In transaction payment made using payment Gateway then Payment Gateway not required to deduct TDS u/s 194S.
3. Sec 194Q not applicable when TDS deducted u/s 194S.
4. If transaction took place outside the exchange then Buyer required to deduct TDS of seller.
5. TDS applicability when Transaction took place through Exchange (e.g. WazirX)
 - (i) Mr. Hari (Buyer) buys VDA through WazirX and VDA own by Mr. Devam (Seller): In this case WazirX will deduct TDS of Mr. Devam when paying or crediting consideration.
 - (ii) Mr. Hari (Buyer) buys VDA through WazirX and VDA own by WazirX only: In this case Hari will deduct TDS of WazirX. If WazirX entered into agreement with Hari, that, WazirX will pay TDS to Govt., then Hari not required to deduct TDS.
6. TDS applicability when consideration is any other VDA
 - (i) The buyer will release the consideration in kind after seller provides proof of payment of such tax (e.g. Challan details etc.). Where VDA "BTC" is being exchanged with another VDA "DOGE", both the persons are buyer as well as seller. One is buyer for "BTC" and seller for "DOGE" and another is buyer for "DOGE" and seller for "BTC". Thus, both need to pay tax with respect to transfer of VDA and show the evidence to other so that VDAs can then be exchanged.
 - (ii) If this transaction took place through exchange say WazirX then alternatively TDS can be deducted by WazirX in following manner: -
 - (a) WazirX would be required to deduct TDS for both legs of the transactions.
 - (b) At the time of transaction, the WazirX will deduct TDS in the pair being traded. For e.g. in case of trade for Monero to Deso, 1% of Monero and 1% Deso will be deducted as TDS by the WazirX and balance shall be transferred to the customer. The trail of transactions evidencing TDS of 1% of consideration for every VDA to VDA trade shall be maintained by the Exchange.

- (c) The WazirX shall immediately execute a market order for converting this TDS (1% Monero/ 1% Deso in the above example) to one of the primary VDAs (BTC, ETH, USDT, USDC) which can be easily converted into INR. This step will ensure that the TDS in the form of non-primary VDAs like Deso/Monero is converted to an equivalent of primary VDAs which have a ready INR market. Time stamps of timing of orders to be maintained to ensure such conversion of VDAs withheld to be done on immediate basis by the WazirX. If the taxes are withheld in primary VDAs, this step would be ignored.
- (d) All the TDS in the form of primary VDAs will be accumulated for the day. Time limit will be from 00:00 hours to 23:59 hours. VDA accumulation by the Exchange shall be verifiable from the trail of orders for VDA-to-VDA trades executed during the day.
- (e) The accumulated balance of primary VDAs at 00.00 hours will be converted into INR based on the market rate existing at that time. The WazirX are required to place market order at 00:00 hours for the TDS in form of primary VDAs for conversion into INR. These sell market orders shall be executed based on the open buy orders in the market.
- (f) It is clarified that there would not be any further TDS for converting the tax withheld in kind in the form of VDA into INR or from one VDA to another VDA and then into INR.



Notes

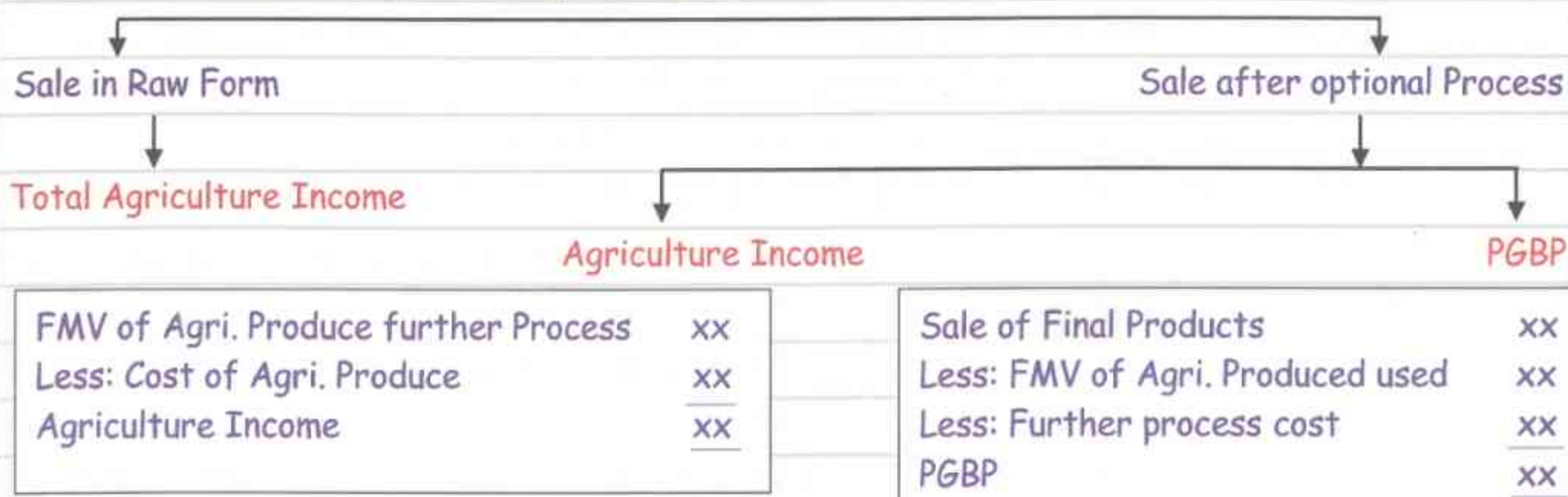


- Sec 10(1) Agriculture Income - It is exempt from Tax if its from agriculture land in India.

As per section 2(1A), Agriculture income means -

- (a) Rent from agriculture land (used for agriculture purpose).
- (b) Income from sale of agriculture produce. (Note 1)
- (c) Rent from house (use as dwelling house, store house).
- (d) Income from nursery.

Note 1: Rule 7- Sale of agriculture produce



- Special Rules for Tea, Coffee & Rubber

Rules	Activity	Agri. Income	PGBP
8	Growing and Manufacturing of Tea	60%	40%
7B	Growing & Manufacturing of Coffee		
	(a) Grown & cured	75%	25%
	(b) Grown, Cured, Roasted & Grounded	60%	40%
7A	Growing & Manufacturing of Rubber	65%	35%

Remember:- Higher% represents income from Agriculture

- Partial Integration in case of Agricultural Income

Agriculture income is exempt from tax but for computation of tax it shall be considered if following conditions are satisfied

- (i) Assessee is Individual, HUF, AOP, BOI, AJP.
- (ii) Agriculture income more than ₹ 5,000.
- (iii) Non-agriculture income more than Basic exemption.

Computation of Tax Liability	₹
Non-Agriculture Income (Total Income) [A]	xx
Agriculture Income [B]	xx
Total [C]	xx
Tax Payable on "C" [D]	xx
Aggregation of "B" and Basic Exemption [E]	xx
Tax payable on "E" [F]	xx
Net Tax payable "D-F" [G]	xx



- Sec 14A: For computing total income under the five heads of income, No deduction shall be allowed in respect of expenditure incurred by assessee in relation to Exempt Income.

Manner of computation of disallowance: Rule 8D

1. Where A.O. is satisfied with the correctness of the claim of expenditure - No action is required.
2. Where A.O. is not satisfied with correctness of the claim - expenses attributed to exempt income shall be computed with Rule 8D of income tax rules.

Rule 8D: Expenditure relating to exempt Income

	₹
(a) Amount of expenses directly relating to exempt income	xx
(b) Amount equal to 1% of this annual average of the monthly average of the opening & closing balance of investment, income from which is exempt	xx
Total amount disallowable u/s 14A	xx

Notes

1. Provided that amount referred in (a) and (b) shall not be more than total expenditure claimed by assessee.
2. Sec. 14A read along with Rule 8D provides for disallowance of expenditure even where the taxpayer has not earned any exempt income in a particular PY.

Kribhco (2012)(Delhi): Sec. 14A is applicable only if an income is exempt as per Chapter -III of the IT ACT 1961.

- Deductions under chapter VI-A are different from the exemptions.
- as per section 14A, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to such income which does not form part of the total income (Exempt Income).

No disallowance can be made u/s 14A in respect of income included in total income in respect of which deduction is allowable u/s 80C to 80U

E.g.: Mr. BB invested in securities & expenditure related to such investment is ₹ 2,00,000. Out of above securities, income from some securities is exempt & from other securities taxable. Expenditure directly attributed to exempt securities is ₹ 30,000. Investment Value in securities from which income is exempt: ₹ 60,00,000 (Monthly Avg. of opening and closing & after that annual average)

Answer:

Expenditure related to Exempt Income	₹
(i) Directly related to Exempt Income :	30,000
(ii) 1 % of Exempt Income (60,00,000 × 1 %) :	60,000
Disallowed Expenditure	90,000

Conclusion: So in this question ₹ 1,10,000 expenditure is allowed as deduction.



If Indian co (has place of effective management in India) engaged in business of operating ships can compute its income on the basis of tonnage tax scheme if company owning at least one qualifying ship. This scheme is optional.

➤ **Sec 115VG: Computation of Tonnage Income**

Income = Daily tonnage income × No. of days the ship is operated in P.Y

Qualifying ship having net tonnage	Daily Tonnage Income
Upto 1,000 tons	₹ 70 for each 100 tons
> 1,000 upto 10,000 tons	₹ 700 + ₹ 53 for each 100 tons
> 10,000 upto 25,000 tons	₹ 5,470 + ₹ 42 for each 100 tons
> 25,000 tons	₹ 11,770 + ₹ 29 for each 100 tons

1. Tonnage shall be rounded off to the nearest multiple of 100 tons.
2. Deductions, set-off any loss shall not be allowed against tonnage income.
3. Tonnage tax income shall not be liable to MAT.
4. **Qualifying Ship:** seagoing ship or vessel of 15 net tonnage or more but exclude (i) a seagoing ship or vessel if the main purpose for which it is used is for the provision of goods or services of a kind normally provided on land (ii) factory ships (iii) fishing vessels (iv) harbour and river ferries (v) pleasure craft (vi) offshore installations (vii) qualifying ship which is used as a fishing vessel for a period of more than thirty days during a P.Y.
5. Exercising the above scheme is optional. Where an assessee opts for tonnage tax but wishes to opt out of the same within 10 years from the date on which he exercised option, he shall not be eligible to opt into tonnage tax for a period of 10 years from date of opting out.
6. Company should not charter in more than 49% of net tonnage of qualifying ship operated by it. If it crossed that limit then in that year this scheme not applicable.
7. Company shall maintain separate books of account and obtain a report from CA and furnish it before the due date specified u/s 44AB.
8. Company shall credit to Tonnage Tax reserve a/c (TTRA) atleast 20% of the book profits derived from core and eligible incidental activities every year which shall be utilised only for acquiring a new ship before expiry of 8 years. (BP same as 115JB).
9. If any amount mis-utilised then proportionate income shall be taxable as per normal provision of Act.
10. If there is any shortfall in the amount credited to the TTRA, then the following amount taxable under the other provisions of the Act:

$$\text{Taxable amount} = \frac{\text{Relevant shipping income} \times \text{Shortfall in credit to reserves}}{\text{Minimum reserve to be credited}}$$
11. Failure to create TTRA for 2 consecutive PY's will render tonnage scheme invalid from 3rd PY.
12. If ship transferred within 3 years from end of PY in which it acquired, it proportionate amount shall deemed as income in year of transfer.
13. If amount not utilized within 8 years, it shall be deemed as Income of 9th year.
14. Income from incidental activities shall not be considered only up to 0.25% of Turnover from core activities. Any excess, shall be taxable under normal provisions of the Act.

Notes



Sec 2(15): Charitable Purpose

- ☞ Relief of poor,
- ☞ Education,
- ☞ Yoga,
- ☞ Medical relief,
- ☞ Preservation of Environment (including watersheds, forests & wild life),
- ☞ Preservation of monuments or places or objects of Artistic or Historic interest,
- ☞ ***Advancement** of any other object of General public utility.

* **Advancement** of any other object of General public utility not be charitable purpose, if it involves any activity related to trade, commerce or Business but it is treated as charitable purpose if **aggregate receipt from Business activity is not more than 20% of the total receipts.**

CBDT Clarifications

1. No need to cancel registration just because business receipts is > 20%, exemption will not be available for that year.
2. Promotions of Games & sports also treated as charitable purpose.

Sec 11(1): Income of the Charitable or Religious Trust

Following incomes of the Trust shall be exempt from tax :-

- (i) **Corpus** Donation [if it is deposited in mode prescribed u/s 11(5)].
- (ii) **15% of Gross Income** (Set aside/Standard deduction).
- (iii) Income **applied** for charitable or religious purpose in India (out of remaining 85% on Income).

➤ **Explanation - 1:** If 85% of income could not applied in current P.Y. :-

(a) For the reason that whole or any part of income has not received during PY (outstanding) - Assessee submit a declaration (Form 9A) to **AO at least 2 months before due date of ROI u/s 139(1)** that, such income shall be actually applied in the **year of receipt or in the immediately next year**, then such amount is treated as **deemed to be applied in current P.Y.**

If such amount **not applied** in the year of receipt or in the immediately next year then such amount shall be treated as income of the next year in which such amount received and **taxable @30% u/s 115BBI.**

Note: This option is possible only when assessee follow accrual system of accounting wherein the income has been recognised but not received

(b) For any other reason - Assessee submit a declaration (Form 9A) to AO at least 2 months before due date of ROI u/s 139(1) that income could not apply in current PY due to any reason (like bumper donation received in last month) and such income will be actually applied in the next PY then such amount is treated as deemed to be applied in current PY.

If such amount not applied in the next year, then such amount shall be treated as income of the next year and taxable @30% u/s 115BBI.

➤ Explanation - 2: Any amount donated to any other trust registered u/s 12AA/12AB or institution u/s 10(23C) shall be treated as application but if such amount is donated as Corpus of such trust institution then it is not treated as application.

➤ Explanation - 3: For the purpose of computing application of Trust, PGBP provisions of section 40A(3), 40A(3A) and 40(a)(ia) shall apply here also.

☞ 40A(3)/ 40A(3A)- Expenditure paid in a single day to a single person more than ₹ 10,000 in any mode other than A/C payee cheque or DD or ECS not treated as application. If deduction allowed in earlier year on due basis and in current year if payment made more than ₹ 10,000 in cash then such amount will be treated as income of current PY.

☞ 40(a)(ia)- If any amount paid or credited to resident and if TDS not deducted in PY or deducted but not paid to Govt. upto due date of ROI then 30% of such expenditure not allowed as application for trust. The same would be treated as application in the year in which TDS deposited.

➤ Explanation - 3A: If trust having temple, mosque, gurdwara, church or other place notified u/s 80G(2)(b), received any donation for repair or renovation of such places then trust may treat such sum as corpus donation if following conditions are satisfied; -

(a) Such amount should be utilised only for repair or renovation,

(b) Such amount should not be donated to any person,

(c) Maintains such corpus as separately identifiable, and

(d) Invested/deposited in modes specified u/s 11(5).

If any of condition mentioned above violated then such sum shall be treated as income of the PY in which violation takes place.

[Added by FA 22 w.e.f. AY 21-22]

Explanation - 4: [Added by FA 21 w.e.f. AY 22-23]

(i) Amount applied out of Corpus Fund shall not be treated as application in current year.

However, when the income of any subsequent PY is utilised to invest or deposit back into specified mode u/s 11(5) for such corpus, then such amount shall be allowed as application in the PY in which it is invested or deposited back to corpus and to the extent it is deposited back. It is treated as application only if following conditions are satisfied;-



- ✓ Application should be in India,
- ✓ Application should not be by way of donation to the corpus of another trust or institution.
- ✓ Section 40A(3) & 40(a)(ia) satisfied on application.
- ✓ Carry forward and set off of excess application is not allowed.
- ✓ Application should not for the benefit of any person in section 13(3).
- ✓ Invests or deposits back into corpus within 5 years from end of FY in which amount applied from corpus.

E.g.: Balaji Trust applied ₹ 50 lakhs in PY 24-25 for religious purpose out of corpus fund of Trust. In this case ₹ 50 lakhs not treated as application for PY 24-25.

Suppose in PY 26-27 Trust deposited back ₹ 35 lakhs in corpus fund out of income of PY 26-27 then ₹ 35 lakhs treated as application for PY 26-27.

(ii) Amount applied from any **loan or borrowing** shall **not be treated as application** in current year. However, when such loan or borrowing is repaid from the income of any subsequent PY, such repayment shall be allowed as application in the PY in which it is repaid and to the extent it is repaid. It is treated as application only if following conditions are satisfied:-

- ✓ Application should be in India,
- ✓ Application should not be by way of donation to the corpus of another trust or institution.
- ✓ Section 40A(3) & 40(a)(ia) satisfied on application.
- ✓ Carry forward and set off of excess application is not allowed.
- ✓ Application should not for the benefit of any person in section 13(3).
- ✓ Repayment of loan made within 5 years from end of FY in which amount applied from loan.

E.g.: During PY 24-25 Balaji Trust constructed a building for ₹ 80 lakhs out of loan taken from HDFC bank. In this case ₹ 80 lakhs not treated as application for PY 24-25. Suppose in PY 25-26 Trust repaid loan of ₹ 30 lakhs out of income of PY 25-26 then ₹ 30 lakhs treated as application for PY 25-26.

(iii) Any amount **donated to any other trust** registered u/s 12AA/12AB or institution u/s 10(23C) [other than referred in Explan 2], shall be treated as application for charitable or religious purposes only to the extent of 85% of such amount donated. [Added by FA 23 w.e.f. AY 24-25]

E.g.: During PY 24-25 Balaji Trust donated ₹ 50 lakhs to Siddhivinayak trust (registered u/s 12AB) then Balaji Trust can claim application of only ₹ 42.5 lakhs.

➤ **Explanation - 5:** If any excess application of earlier PY's shall not be allowed to set-off in current PY. It means excess application shall not allowed to be C/F and Set-off. [Added by FA 21 w.e.f. AY 22-23]



- Explanation added for whole section 11: Any sum payable by any trust or institution shall be considered as application of income in the PY in which such sum is actually paid by it (irrespective of method of accounting followed by trust). Where during any PY, any sum has been claimed to have been applied, such sum shall not be allowed as application in any subsequent PY.

E.g.: Balaji Trust regularly follow accrual system of accounting. Trust purchased computer for trust purpose on 28/03/25 for ₹ 20 lakhs and payment to vender made on 16/07/25. In this case application of ₹ 20 lakhs are allowed in PY 25-26. [Added by FA 22 w.e.f. AY 22-23]

Sec 11(2): Exemption if income accumulated for specific purpose

Where 85% of income is not applied during the P.Y. but accumulated or set apart, then such set apart income is not included in Income if following conditions are satisfied:

1. Assessee should furnish a statement to A.O. [Form 10] stating the **purpose & period** for which such income is accumulated [Maximum period can be 5 years].
2. Statement should be furnish **at least 2 months before due date** of ROI u/s 139(1)
3. Such money should be deposited in **Sec 11(5) modes (Safe investments)**.
4. Such money should **not be donated to any other Trust**.

➤ Provided that in computing the period of 5 years, the period during which the income **could not be applied** for the purpose, due to an order of any court, **shall be excluded**.

Sec 11(3): Exemption withdrawn if conditions not satisfied

Any income referred u/s 11(2) -

- (i) Is applied to purposes **other than the purposes** for which it was accumulated, then it shall be taxable in **the P.Y. in which it is so applied**, or
- (ii) **Ceases** to remain invested in modes **as per Sec. 11(5)**, then it shall be taxable in the P.Y., in which it so ceases, or
- (iii) Is **not utilised within specific time** then it shall be taxable in the **last year of specific period**, or
- (iv) If donated to any trust then taxable in the year in which **it is so donated**.

Note: Income taxable u/s 115BBI@ 30% in the year of violation.

- Sec 13(9): Denial of exemption if return not filed up to due date

Exemption u/s 11(2) shall not be available, if

- (a) Statement to A.O. not filed up to due date of ROI, or
- (b) Return of income not filed up to due date of ROI.

CBDT Circular No.6/2023 clarifies that the statement in Form No. 10/9A is required to be furnished at least 2 months prior to due date of ROI so that it may be taken into account while auditing the books of account. However, the accumulation/deemed application shall not be denied to a trust as long as the statement of accumulation/deemed application is furnished on or before the due date of furnishing the return u/s 139(1).



Sec 11(4)/(4A): Business income of Trust

If Business is **incidental to the attainment of main objective** of Trust & separate books of A/c's are maintained, then exemption u/s 11(1) & 11(2) can be claimed on Business income. In Assessment, If A.O. finds any **concealed income** in respect of Business, then exemption u/s 11(1)/11(2) shall **not be available** in respect of such concealed income.

Sec 11(5): Safe Investment mode for Trust

- Investment in Government Saving Certificates, Units of UTI, CG/SG securities, debentures of any company which is guaranteed by Govt., Units of Mutual Fund, equity shares of a 'depository', Stock Certificate as defined in Sovereign Gold Bonds Scheme, 2015, Shares of NSDC, shares of stock exchange or subsidiary of stock exchange.
- Deposits with Post Office Savings Banks, Schedule Banks or Co. Op Banks. or Industrial Development Bank
- Investment or deposits in any public sector company. (If PSC cease to be PSC then investment in shares of that company should be treated as legitimate investment till 3 years from the date of cessation and in any other investment till the time of maturity).
- Investment in bonds of approved financial corporation / public companies providing long term finance.
- Investment in immovable property.
- debt instruments issued by any infrastructure Finance Company registered with RBI.
- "Stock Certificate" as defined in Sovereign Gold Bonds Scheme, 2015.
- Investment by way of acquiring units of POWERGRID Infrastructure Investment Trust.

Sec 11(6): Depreciation not allowed

If cost of asset is already claimed as application, then depreciation on such asset shall not be considered as application while computing income of P.Y.

Sec 11(7): Exemption u/s 10 not available

Where trust claim exemption u/s 11, then exemption u/s 10 [other than 10(1), 10(23C), 10(23EA), 10(23EC), 10(23ED), 10(46), 10(46A) & 10(46B)] shall not be allowed to trust means trust can claim exemption u/s 10(1) [Agriculture income] with Sec 11 exemption but other exemption of Sec 10 not available.

Provided that registration shall u/s 12AA/12AB become inoperative from the date on which the trust or institution is approved u/s 10(23C)(iv)/(v)/(vi)/(via) or notified u/s 10(23EA), 10(23EC), 10(23ED) or 10(46), as the case may be.

Note: So either trust/institution can claim exemption u/s 11/12 or u/s 10(23C)(iv)/(v)/(vi)/(via).

Sec 12A: Conditions for Applicability of sec 11 & 12

Exemption u/s 11 & 12 available if:

- Trust should be registered u/s 12AB.
- If total income (before claiming exemption u/s 11&12) is more than Basic exemption then trust required to maintain books of account & documents and get it audited from auditor and furnish report within time given u/s 44AB.
- Return of the trust filed u/s 139(4A) upto due date of return filing given u/s 139(1)/(4).

Requirement for obtaining registration u/s 12AB w.e.f. 01.04.2021

Case	Scenario	Time limit for making application	Time limit for grant of Registration	Period of Reg.	From which Year Exemption u/s 11 & 12 Available
1.	Exiting Trusts already registered u/s 12A/12AA	3 months from 01/4/21 i.e. 30/6/21 - FORM 10A [as per circular it's extended till 30/6/24]	3 months from the end of month in which application was received	5 Years (without inquiries)	From the AY for which trust earlier granted registration
2.	New trust applying for Fresh registration u/s 12AB (Note)	1 month prior to the commencement of PY relevant to AY for which registration is sought FORM 10A	1 months from the end of month in which application was received	3 Years (Provisional Registration) (without inquiries)	From the AY relevant to the FY in which application is made
3.	Trust granted provisional registration, now applying for final registration	6 months prior to expiry of approval or 6 months from the commencement of activity, whichever is earlier FORM 10AB	6 months from the end of month in which application was received [6 months from end of quarter in which application recd w.e.f. 1/10/24]	5 Years (From AY for which provisional registration granted) (with inquiries)	From the first of the AY's for which it was provisionally registered.
4.	Trusts registered u/s 12AB	6 months prior of expiry of registration FORM 10AB		5 Years (with inquiries)	From the AY relevant to the FY in which application is made
5.	Trust adopted modification of objects which do not confirm the conditions of registration	30 days from date of adoption or modification FORM 10AB		5 Years (with inquiries)	From the AY relevant to the FY in which application is made
6.	Trust registration becomes inoperative due to sec. 11(7)	6 month prior to commencement of AY from which registration sought	6 months from the end of month in which application was received	5 Years (with inquiries)	From the AY relevant to the FY in which application is made



to be made
operative **Form 10AB**

Note - With effect from 1.10.23, a trust which has already commenced its activities and has not availed exemption in any P.Y. before the date of application, need not apply for provisional registration. It can at any time after the commencement of activities directly apply for final registration in Form 10AB. Thus, w.e.f. 1.10.2023 only the trust/institutions which have not commenced activities are required to get provisional registration.

Note: Provided that where the application is filed beyond the time limit given in above table CIT/PCIT may, if he considers that there is a reasonable cause for delay in filing the application, condone such delay and such application shall be deemed to have been filed within time. [Added by FA 24 w.e.f. 1/10/24]

Sec 12AB: Procedure of Registration

1. CIT/PCIT on receipts of application shall pass an order for registering the trust for 5 years (in case 1 of above table).
2. CIT/PCIT on receipts of application shall pass an order for provisional registration for trust for 3 years (in case 2 of above table).
3. CIT/PCIT on receipts of application shall call for documents or information and satisfy himself about genuineness of activity of trust and 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. (in case of 3,4,5,6 of above table)
4. After satisfying he may pass order for registration of trust or refusing registration or cancelled the registration (cancelled in case of provisional registration) within time limit given in above table.
5. Where registration or provisional registration granted u/s 12AB and subsequently: -
 - (a) CIT /PCIT noticed occurrence of **specified violation** during any PY;
 - (b) CIT/PCIT has received a **reference from the AO** under the 2nd proviso of sec. 143(3) for any PY; or
 - (c) Case has been **selected as per risk management strategy** of CBDT, for any PY;
 then the CIT /PCIT shall-
 - (i) **Call for such documents** or information, or make such inquiry as he thinks necessary,
 - (ii) If **he is satisfied that specified violation took place** then he will pass an order for cancelling the registration, after giving an opportunity of being heard, for such PY and all subsequent PY's.
 - (iii) If he is **not satisfied** about the occurrence of specified violation then pass an order in writing, refusing to cancel the registration.
 - (iv) Order shall be passed **within 6 months from end of quarter** in which the first notice is issued by CIT/PCIT, calling for any document or information, or for making any inquiry.
 - (v) **Forward a copy** of the order to the **AO and such trust**.

6. "Specified violation" means; -
- Where any income has been applied, other than for the objects of the trust ; or
 - Where trust has income from business which is not incidental to the attainment of its objective or separate BOA are not maintained for the business which is incidental to the attainment of its objectives; or
 - Where the trust has applied any part of its income for private religious purposes; or
 - Where the trust has applied any part of its income for the benefit of any particular religious community or caste; or
 - Any activity of trust is not genuine or not carried out in accordance with conditions subject to which it was registered; or
 - Trust has not complied with the requirement of any other law, and the order, holding that such non-compliance has occurred, has either not been disputed or has attained finality.
 - Application for registration is not complete or it contains false or incorrect information. [This is considered as specified violation w.e.f. 1.4.23]

Sec 13(1): Denial of Exemption u/s 11 & 12

Exemption u/s 11 & 12 NOT available in following cases;

- Income from trust for private religious purposes.
- Income from trust for the benefit of any particular religious community or caste.
- Income of trust for the benefit of specified person (relative), such part of the income.
- Fund of the trust deposited or invested in modes other than 11(5), to the extent of such deposit or investments.

Sec 13(3): Meaning of specified Person (Relative)

- ☞ Author/Founder of Trust.
- ☞ Person who made donation of > ₹ 50,000 in PY.
- ☞ Where the founder /donor is HUF, Member of HUF.
- ☞ Trustee or Manager of Trust.
- ☞ *Relative of any founder, donor, Member, trustee, manager.
- ☞ Any concern in which any of the above person has a substantial interest.
- *Relative means person's referred u/s 56(2)(x)

13(6): Educational and Medical Facility to Specified person

Any educational or medical facility is provided by educational or medical trust to specified person then market value (FMV) of such facility shall be treated as income and exemption u/s 11 & 12 not available on such income.



Sec 11(1A): Capital gain deemed to be applied for charitable purpose

Where any capital asset is transferred by trust & Net consideration is utilized for acquisition of another capital asset then following capital gain shall be exempt,

- a) If Net consideration **fully utilized** then capital gain **fully exempt**.
- b) If Net consideration partly utilized then,
(Cost of New Asset - Cost of old Asset) shall be exempt

Sec 115BBI: Tax on Specified Incomes

Following specified Incomes are taxable @ 30%; -

- (a) Income accumulated or set apart in excess of 15% where such accumulation is not allowed under any specific provision.
- (b) Deemed Income as per Explanation-1 of section 11(1).
- (c) Deemed Income as per section 11(3).
- (d) Income applied for the benefit of specified person as per section 13(1).
- (e) Income not deposited/invested in modes specified in 11(5) as per section 13(1).
- (f) Income used for any purpose outside India.

Note: In this section income computed without any deduction in respect of any expenditure or allowance or set off of any loss.

Sec 13(10): Calculation of Income in case of certain violations

Where the commercial receipts > 20% of gross receipts in case of advancement of any other objective of general public utility OR BOA of trust not maintained OR not audited OR return not filed on time u/s 139(1)/(4), trust 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, subject to fulfilment of the following conditions, namely: -

- (a) Such expenditure is **not from the corpus** standing as on the end of last year;
- (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 in any PY; and
- (d) Such expenditure is **not in the form of any contribution or donation** to any person.

Notes:

1. For the purpose of computing income of Trust, PGBP provisions of section 40A(3), 40A(3A) and 40(a)(ia) shall apply here also.
2. For the purposes of computing income, no deduction in respect of any expenditure or allowance or set-off of any loss shall be allowed under any other provision of this Act.

Sec 115BBC: Tax on Anonymous donation received by trust or institutions

Anonymous donation means any donation where person receiving such contribution does not maintain record of donor.

- (i) Income tax @ 30% on the **anonymous donations** received in excess of the **higher** of following
- | | |
|---|-----|
| ↑ (i) 5% of Total Donation (including corpus & Govt. grant) | xxx |
| ↑ (ii) ₹ 1,00,000 | xxx |
- (ii) Balance Income of trust/institution is taxable as per normal tax rate.

➤ Anonymous Donation received by wholly Religious Trust - **Not Taxable u/s 115BBC** [subject to sec 11 & 12].

➤ Anonymous Donation received by charitable Trust - **Taxable u/s 115BBC**

➤ Anonymous Donation received by wholly religious & charitable purpose - **Not taxable u/s 115BBC** if it is made with specific direction that such donation should be used for educational institution / medical institution / Hospital run by such trust.

Note: If Anonymous donation not taxable u/s 115BBC, then such donation shall be taxable as per normal provision of income tax & subject to Sec 11 & 12.

➤ In simple word	₹
Actual amount of Anonymous donation	xxx
Less: ↑ (i) 5% of Total Donation	xx
↑ (ii) ₹ 1,00,000	xx
	(xxx)
This is taxable as per 30%	xxx

This amount is added to other income & will be chargeable @ Normal tax rate.

➤ Format to Solve Questions

Particulars	₹
Gross Receipts of Trust (other than Corpus donation & anonymous donation taxable u/s 115BBC)	xx
Capital Gain on Transfer of Capital Asset	xx
Total	xx
Less: 15% accumulated and set apart (Std. deduction)	(xx)
Balance	xx
Less: Application of Income for Trust Purpose	(x)
Less: Capital Gain deemed applied u/s 11(1A)	(x)
Less: Deemed application (O/s or any other reason)	(x)
Less: Income Accumulation u/s 11(2)	(x)
Income Taxable at Normal Tax Rates	xx
Add: Anonymous Donation Taxable at Special Rate of 30%	xx



Add: Income Taxable u/s 115BBI at special rate of 30%

xx

Total Income

xx

Sec 10(23C): Income of certain Universities, Hospitals, Educational Institution, Medical Institution

1. Income of any university or educational institution or any hospital or other institution **wholly or substantially financed by the Govt. (Govt grant is > 50% of total receipts)** which exists solely for educational or medical purposes and not for profit, shall be fully exempt from tax.

[10(23C)(iiiab)/(iiiac)]

2. Income of any university or educational institution or any hospital or other institution which exists solely for educational or medical purposes and not for profit and aggregate **annual receipts is upto ₹ 5 crore**, shall be fully exempt from tax.

[10(23C)(iiid)/(iiiae)]

Note: If any person has receipts from university/education institution as well as from hospital/medical institution then exemption under these section shall not apply if aggregate receipts from such institutions more than ₹ 5 crores. **[₹ 5 crores limit apply for aggregate receipts for section 10(23C)(iiid) & (iiiae)]**

3. Income of any approved fund/Trust/institution for charitable or religious purpose university or educational institution or any hospital or other institution approved by CIT/PCIT which exists solely for educational or medical purposes and not for profit, shall be exempt from tax subject to certain conditions.

[10(23C)(iv)/(v)/(vi)/(via)]

Notes: Sec 10(23C)(iv)/(v)/(vi)/(via) are similar to sections 11/12/13 so all the provision we have discussed with section 11,12,12A,12AB,13,115BBC,115BBI are applicable for sec 10(23C) also.

Amendment: Approval u/s 10(23C)(iv)/(v)/(vi)/(via) not applicable w.e.f. 1/10/2024. Now every trust or institution has to apply for registration u/s 12AB only w.e.f. 1/10/2024.

New Noble Educational Society (2022)(SC): Whether the requirement u/s 10(23C) to solely engage itself in education mean that such institution cannot have objects not related to education. Also, is it necessary that profits of business incidental to educational activity and not any other activity.

Analysis & Decision: The SC, made the following observations and conclusions:

(a) "solely" engage itself in education or educational activities, and not engage in any activity of profit, means such institutions cannot have objects which are unrelated to education. In other words, all objects must relate to imparting education or be in relation to educational activities. The term "solely" is not the same as "predominant/mainly". The term "solely" means to the exclusion of all others.

(b) Sec. 11(4A) refer to profits which may be "incidentally" generated or earned by the charitable institution. In the present case, the same is applicable only to those institutions which impart education or are engaged in activities connected to education.

(c) "Business" and "profits" in 11(4A) merely means that the profits of business which is "incidental" to educational activity—i.e., relating to education such as sale of text books, providing school bus facilities, hostel facilities, etc. However, where institutions provide their premises or infrastructure to other entities,

trusts, societies, etc., for the purposes of conducting workshops, seminars or even educational courses (which the concerned trust is not actually imparting) and outsiders are permitted to enrol in such seminars, workshops, courses, etc., then the income derived from such activity cannot be characterised as part of education or "incidental" to the imparting education.

Ahmedabad Urban Development Authority (and other appeals)(2022)(SC): When an activity can be considered as trade, commerce or business for attracting proviso to section 2(15) when assessee's objective is to "any other objective of general public utility"

As per SC neither precludes any assessee advancing objects of general public utility, from claiming exemption, nor the taxing authorities from denying exemption, in the future, if the receipts of the relevant year exceed 20%. AO must on a yearly basis, scrutinize the record to discern whether the nature of the assessee's activities amount to "trade, commerce or business" based on its receipts and income (i.e., whether the amounts charged are on cost-basis, or significantly higher).

St. Peter's Educational Society (2016) (SC): Institutions engaged in providing specialized training in certain fields (like communication, advertising etc) and awarding diplomas and certificates are also eligible for tax exemption in terms of section 10(23C)(vi). It is not mandatory for such institutions to conduct only recognized educational courses. Making of profit incidentally will not make the institution as existing for making profit.

Tax on Accreted Income of Trust or Institution [Exit Tax]

➤ Sec 115TD : Tax on Accreted Income

The "**Accreted income**" of trust registered u/s 12AA/12AB or Institution approved 10(23C)(iv)/(v)/(vi)/(via); shall be taxable @MMR if: i.e. **34.944% (30%+12%+4%)**

(a) **Conversion** of trust / Institution into a **form not eligible for Registration u/s 12AA/12AB 10(23C)**[Note 2]

(b) **Merger** into an entity **not having similar objects** and registered u/s 12AA/12AB/10(23C).

(c) **Non - distribution of assets on dissolution** to any other trust / Institution registered u/s 12AA/12AB/10(23C) **within 12 months** from end of the month in which dissolution takes place

Notes:

1. The exit tax shall be in addition to income taxable in hands of entity.

2. Deemed conversion into non- eligible form in following cases:

☞ **Registration** granted u/s 12AA/12AB /10(23C) has been **cancelled**.

☞ 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** u/s 12AA/12AB /10(23C) in that P.Y. or

⊗ It has applied for fresh registration u/s 12AA/12AB/10(23C) but application has been rejected.

☞ It has **failed to make an application** for : -

⊗ Re-registration; or

⊗ Renewal of Registration where the period of registration is due to expire; or

⊗ Final registration within the time specified u/s 12A, which expires in the said PY.

3. "Accreted Income" shall be computed on "specified date"

Meaning of Accreted Income	₹
Aggregate FMV of total Asset	xx
(-) Total liability of trust/institution	xx
Accreted Income	xx

Note: When the tax on the accreted income is levied on the FMV & if subsequent transfer of such asset, the cost of acquisition shall be the FMV of such asset.

Following assets & liabilities in respect of that assets shall not be considered in accreted income.

(a) Assets acquired out of agriculture income.

(b) Assets acquired by trust from the date of creation of trust / institution to the date from which registration/approval become effective u/s 12AA/12AB/10(23C).

[Where the benefit u/s 11 & 12 have been allowed to the trust or institution in respect of any P.Y. or years beginning prior to the date from which the registration u/s 12AA/12AB/10(23C) became effective, then, the registration shall be deemed to have become effective from the first day of the earliest P.Y.]

(c) Asset transfer on dissolution to other trust/institution registered u/s 12AA/12AB/10(23C) within 12 months from end of the month in which dissolution takes place.

Meaning of "Specified date" i.e. date of valuation of assets & liability

S.No.	Case	Valuation date
1.	Conversion of Trust / Institution into non - eligible form - Registration granted cancelled - Modification of objects - Fails to make application for re-registration, renewal or final registration	Date of cancellation Date of Modification Last date of making application
2.	Merger with any other non-charitable trust/institution	Date of merger
3.	Failure to transfer asset on dissolution within 12 months	Date of Dissolution

➤ Sec 115TD(4): Exit tax shall payable even if no income tax is payable by the Trust/Institution.

➤ Sec 12AC: Exit Tax not apply in case of merger [Added by FA 24 w.e.f. AY 25-26]

Where any trust or institution registered u/s 12AB or approved u/s 10(23C)(iv)/(v)/(vi)/(via) merges with another trust or institution, the provisions of Exit Tax not apply if-

(a) the other trust or institution has same or similar objects;



- (b) the other trust or institution is registered u/s 12AA or 12AB or approved u/s 10(23C)(iv)/(v)/(vi)/(via); and
- (c) the said merger fulfils such conditions as may be prescribed.

➤ Sec 115TD(5): Exit tax has to be paid to CG within 14 days from:-

S.No.	Cases	14 days from
A.	Conversion of trust/institution into non-eligible form (i) Registration granted has been cancelled	14 Days from the date on which: (a) the period for filling appeal to ITAT against the order cancelling the registration expires & No appeal has been filed by trust/institution OR (b) the order in any appeal confirming the cancellation of registration is recd. by trust /institution.
	(ii) Modification of objects & not applied for fresh registration (iii) Fails to make application for re-registration, renewal or final registration	14 days from end of P.Y.
	(iv) Modification of objects & applied for fresh registration but application rejected	14 Days from the date on which: a) the period for filling appeal to ITAT against the order of rejection expires & No appeal has been filed by trust/institution OR (b) the order in any appeal confirming the rejection is recd. by trust /institution.
B.	Merger with any other non-charitable trust/institution	14 days from the date of merger
C.	Failure to transfer asset to trust/ institution registered u/s 12AA/12AB/10(23C) within period of 12 months from end of the months in which dissolution took place.	14 days from the date on which period of 12 months (at the end of the month in which dissolution took place) expires.

- Sec 115TE: Interest for non-payment of tax within 14 days
Interest @1 % p.m. or part of the month from the 15th day till date on which the tax is actually paid.
- Sec 115TF: Trust/ Institution is deemed to be assessee in default.
If tax not paid then principal officer/trustee/trust/ institution shall be treated as assessee deemed to be default.



In case of transfer of assets upon dissolution of the trust to recipient, which is not a charitable trust, the recipient of asset shall also be treated as assessee in default. However, recipient's liability shall be limited to the extent to which the asset received by him is capable of meeting the liability.

➤ Rule 17CB: Calculation of FMV of Assets

Part A: Assets

Aggregate FMV of the total assets of the trust/institution in the balance sheet as reduced by-

- ⊗ Income-tax paid (TDS/TCS/Adv. Tax) after reducing income-tax refund (if any)
- ⊗ Unamortised amount of deferred expenditure.

FMV of Assets

1. Quoted Shares and securities: Average of Lowest & Highest price on valuation date on a recognize stock exchange

Note: If No trading on valuation date then average of last trading session.

2. Unquoted Equity shares:
$$\frac{A + B - L}{PE} \times PV$$

A: Book Value of All Assets (other than Covered in B) exclude TDS, Advance Tax after reducing IT refund & deferred expenditure shown in the asset side

B: FMV of bullion, jewellery, precious stone, artistic work, shares, securities and immovable property as determined as per this rule

L: Book value of liabilities, but not including the following amounts, namely:-

- ⊗ Paid up equity share capital.
- ⊗ Dividend amount set apart.
- ⊗ Reserves and surplus, other than depreciation reserve.
- ⊗ Provision for tax.
- ⊗ Provision for unascertained liabilities.
- ⊗ Contingent liabilities other than arrears of dividends of cumulative preference shares.

PE: Total amount of paid-up equity share capital as shown in the B/s.

PV: The paid-up value of such equity shares

3. Unquoted Shares or Security (other than equity shares):

FMV on Valuation Date on the basis of valuation report of merchant banker or an accountant.

4. Immovable Property: SDV or FMV, whichever is higher.



5. A business undertaking: $(A+B-L)$
6. Any other assets: FMV on Valuation Date

Part: B- Liabilities

Book value of total liabilities in the B/s but not including the following amounts, namely :-

- ⊗ Capital fund or accumulated funds or corpus, by whatever name called.
- ⊗ Reserves and surplus.
- ⊗ Provision for tax.
- ⊗ Provision for unascertained liabilities.
- ⊗ Contingent liabilities.



Sec 44AB: Compulsory Audit of books of accounts

Following persons are required to furnish audit report by 1 month before the due date of filing ROI u/s 139(1) in a prescribed form (3CA/3CB/3CD):

A	B	C
Specified profession	Business	Special Cases
G.R. > ₹ 50 Lac	T.O./G.R. > ₹ 1 crore In case of business, T.O. Limit shall be ₹ 10 crores instead of ₹ 1 crore if: i) *Cash receipts out of total receipts is upto 5% during the PY and ii) *Cash payment out of total payments is upto 5% during the PY.	- Assessee claiming lower income u/s 44AD or 44ADA and NTI > Basic exemption - Assessee claiming lower income u/s 44AE, 44BB, 44BBB

*cheque/DD, which is not account payee, shall be treated as Cash

➤ Non-applicability of Sec 44AB:

- Person declaring income u/s 44AD or 44ADA.
- Person deriving income of the nature referred to in section 44B (ship) & 44BBA (aircraft).

➤ Penalty u/s 271B: if assessee fails to get accounts audited:

- ↓
- 0.5% of T.O. or G.R. or
 - ₹ 1,50,000

Whichever is lower

➤ Computation of Turnover to determine eligibility of Tax Audit

- Discount allowed in sales invoice deducted from T/o.
- Cash discount not allowed in a cash memo/sales invoice is in nature of a financing charge and is not related to turnover. Therefore, should not be deducted from the T/o.
- Turnover discount is normally allowed to a customer if sales made to him exceed a particular quantity. As per trade practice, it is in nature of trade discount and should be deducted from the T/o.
- Special rebate allowed to customer can be deducted from sales if it is in nature of trade discount. If it is in nature of commission on sales, then it cannot be deducted.
- Price of goods returned should be deducted from turnover even if returns are from sales made in earlier year/s.
- Sale proceeds of any shares, securities, debentures, etc., held as investment will not form part of turnover. However, if shares, securities, debentures etc., are held as stock-in-trade, sale proceeds thereof will form part of T/o.

Note: If assessee having more than one business then all the businesses T/o shall be aggregated for the purpose of checking audit requirement. However in case of business covered u/s 44B or 44BBA

then T/o of such business shall be excluded.

Tax Audit Report u/s 44AB Read with Rule 6G

Form 3CA + 3CD	Accounts of assessee already audit under any other law like Companies Act, 2013 or LLP Act, 2008
Form 3CB + 3CD	Accounts of assessee not audited under any other law
Revised TAR	TAR may (option) be revised by the person (assessee) by getting revised report of audit from CA and furnish it before the end of the AY for which the report pertains, if there is payment by such person after furnishing of TAR which necessitates recalculation of disallowance u/s 40 or 43B. TAR can be revise multiple times.
Considerations while furnishing particulars in Form 3CD	- If item of income/expenditure is covered in more than one clauses suitable cross reference to such items be given at appropriate places. - If there is difference in opinion of tax auditor and assessee in respect of any info furnished in Form, auditor should state both viewpoints and relevant info to enable tax authority to decide in the matter. - If any clause is not applicable, he should state that same is not applicable. - In computing allowance or disallowance, he should keep in view law applicable in relevant year, even though form of audit report may not have been amended to bring it in conformity with amended law. - Info. in Form should be based on BOA, records, documents, information and explanations made available to tax auditor for examination. - In case auditor relies on Case Law, he may mention the fact.

Clause by clause analysis of Form 3CD

Clause - 1	Name of the Assessee Notes - Branch Name along with Assessee name in case of Tax Audit of Branch
Clause - 2	Address: As communicated to ITO for assessment, in case of company also mention registered office if it is different
Clause - 3	Permanent Account Number
Clause - 4	Whether the assessee is liable to pay indirect tax like excise duty, service tax, sales tax, goods and service tax, customs duty, etc. if yes, please furnish the registration number or GST number or any other identification number allotted for the same. Notes - All the GSTIN numbers allotted to the assessee need to be mentioned.
Clause - 5	Status like Individual, HUF, Firm etc.
Clause - 6	Previous Year
Clause - 7	Assessment Year
Clause - 8	Indicate the Relevant clause of Sec 44AB under which the audit has been conducted
Clause- 8A	Whether the assessee has opted for taxation under any of the sections 115BA, 115BAA, 115BAB, 115BAC, 115BAD & 115BAE. Auditor has to verified that Form 10-IB, 10-IC, 10-ID, 10-IF or 10-IEA has been furnished.



Clause - 9	(a) Firm or AOP/BOI, indicate names of partners/members & their PSR. (b) If there is any change in the partners or members or in their PSR since the last date of the last year, the particulars of such change.
Clause - 10	(a) Nature of business or profession (if more than one, nature of every business or profession). (b) If there is any change in the nature, the particulars of such change.
Clause - 11	(a) Whether BOA are prescribed u/s 44AA, if yes, list of books so prescribed. (b) List of BOA maintained and the address at which the books of account are kept. (In case BOA are maintained in a computer system, mention the BOA generated by such computer system. If BOA are not kept at one location, please furnish the addresses of locations along with the details of BOA maintained) (c) List of books of account and nature of relevant documents examined.
Clause - 12	Whether the profit and loss account include any profits and gains assessable on presumptive basis, if yes, indicate the amount and the relevant section (44AD, 44ADA, 44AE, 44AF, 44B, 44BB, 44BBA, 44BBB, Chapter XII-G, First schedule or any other relevant section)
Clause - 13	(a) Method of accounting employed in the previous year. (b) Whether there had been any change in the method employed vis-a-vis the method employed in the immediately last PY, if yes then give details of change and impact on profit & loss. (c) Whether any adjustment is required to be made to the profits or loss for complying with the provisions of ICDS and impact on profit & loss.
Clause - 14	Method of valuation of closing stock employed in the PY. Details of deviation, if any, from the method of valuation prescribed u/s 145A and the effect thereof on the profit or loss.
Clause - 15	Give the following particulars of the capital asset converted into stock-in-trade - ☞ Description of capital asset; ☞ Date of acquisition; ☞ Cost of acquisition; ☞ Amount at which the asset is converted into stock-in-trade.
Clause - 16	Amounts not credited to the profit and loss account, being, - ☞ items falling within the scope of section 28; ☞ the proforma credits, drawbacks, refund of duty of customs or excise or service tax, or refund of sales tax or value added tax, where such credits, drawbacks or refunds are admitted as due by the authorities concerned; ☞ escalation claims accepted during the previous year ☞ any other item of income; ☞ capital receipt, if any
Clause - 17	Where any immovable property is transferred during PY for a consideration less than SDV u/s 43CA or 50C. Details of property, SDV, Consideration and whether Sec 43CA/50C applicable or not shall be furnished.
Clause - 18	Particulars of depreciation allowable as per IT Act, 1961 in respect of each asset or block of assets, as the case may be, in the following form:- (a) Description of asset/block of assets. (b) Rate of depreciation. (c) Actual cost or WDV. (d) Additions/deductions during the year with dates; in the case of any addition of an asset, date put to use; including adjustments on account of - (i) CENVAT credits claimed and allowed under the Central Excise Rules, 1944, in respect of assets acquired on or after 1st March, 1994,

	(ii) Change in rate of exchange of currency, and (iii) Subsidy or grant or reimbursement, by whatever name called. (e) Depreciation allowable. (f) WDV at the end of the year.
Clause - 19	Amounts admissible under sections: 33AB, 33ABA, 35(1)(i), 35(1)(ii), 35(1)(iia), 35(1)(iib), 35(1)(iv), 35(2AA), 35(2AB), 35ABA, 35ABB, 35AD, 35CCA, 35CCC, 35CCD, 35D, 35DD, 35DDA, 35E or any other relevant section.
Clause - 20	(a) Sum paid to an employee as bonus or commission. [Sec. 36(1)(ii)]. (b) Details of Contributions received from employees for various funds as referred to in section 36(1)(va).
Clause - 21	(a) Please furnish details of amount debited to P&L A/c, being in nature of capital, personal expenditure, advt. expenditure in documents of political party, illegal exps (as given in section 37) etc. (b) Amounts inadmissible u/s 40. (c) Amounts debited to P&L being interest, salary, bonus, commission or remuneration inadmissible u/s 40(b)/40(ba) and computation thereof. (d) Disallowance/deemed income u/s 40A(3). (e) Provision for payment of gratuity not allowable under sec.40A (7). (f) any sum paid by the assessee as an employer not allowable u/s 40A (Payment to unregistered gratuity / PF) (g) Particulars of any liability of a contingent nature. (h) Amount of deduction inadmissible in terms of sec. 14A in respect of the expenditure incurred in relation to income which does not form part of the total income; (Expenditure on exempted income) (i) Amount inadmissible under the proviso to sec. 36(1)(iii) (Interest on loan for CAPEX till it is put to use)
Clause - 22	Amount of interest inadmissible u/s 23 of the Micro, Small and Medium Enterprises Development Act, 2006 or any other amount not allowable u/s 43B(h).
Clause - 23	Particulars of payments made to persons specified under section 40A (2) (b). (All Payment to relatives, if they excessive they will be disallowed under 40A(2)(a))
Clause - 24	Amount deemed to be profits & gains u/s 33AB /33ABA. (Withdrawal / Closure of deposit is taxed)
Clause - 25	Any amount of profit chargeable to tax under section 41 & computation thereof.
Clause - 26	Amount allowed and disallowed as per section 43B.
Clause - 27	(a) Amount of CENVAT/GST credits availed of or utilized during the PY and its treatment in P&L A/c and treatment of outstanding CENVAT/GST credits in the accounts. (b) Particulars of income or expenditure of prior period credited or debited to the P&L A/c.
Clause - 29	Whether during the previous year the assessee received any consideration for issue of shares which exceeds the FMV of the shares u/s 56(2)(viib). If yes, please furnish the details of the same.
Clause - 29A	Whether any amount is to be included in IFOS u/s 56(2)(ix) [Adv. Money forfeited]
Clause - 29B	Whether any amount is to be included in IFOS u/s 56(2)(x) [Gift]
Clause - 30	Details of any amount borrowed on hundi or any amount due thereof (including interest on the amount borrowed) repaid, otherwise than a/c cheque [Section 69D]
Clause - 30A	(a) Whether primary adjustment to transfer price u/s 92CE, has been made during the previous year? (Yes/No) (b) If yes, please furnish the following details: -



	- Under which clause primary adjustment is made? - Amount of primary adjustment. - Whether the excess money available with AE is required to be repatriated to India? (Yes/No) - If yes, whether the excess money has been repatriated within the prescribed time (Yes/No) - If no, the amount (in Rs.) of imputed interest income on such excess money which has not been repatriated within the prescribed time.
Clause - 30B	(a) Whether the assessee has incurred expenditure during the PY by way of interest or of similar nature exceeding 1 crore u/s 94B? (Yes/No) (b) If yes, please furnish the following details: - - Amount of expenditure by way of interest or of similar nature incurred - Earnings before interest, tax, depreciation and amortization (EBITDA) during the PY - Amount of expenditure by way of interest which exceeds 30% of EBITDA. - Details of interest expenditure B/F as per section 94B. - Details of interest expenditure C/F as per section 94B.
Clause - 30C	(a) Whether the assessee has entered into an impermissible avoidance arrangement u/s 96, during the previous year? (Yes/No.) (b) If yes, please specify: - - Nature of impermissible avoidance arrangement. - Amount of tax benefit in PY arising, in aggregate, to all the parties to the arrangement
Clause - 31	(a) Reporting of each loan or deposit in an amount exceeding the limit specified in Section 269SS/269T taken or accepted or repaid during the PY. (b) Reporting of each receipt or payment in an amount exceeding the limit specified in section 269ST, in aggregate from a person in a day or in respect of a single transaction or in respect of transactions relating to one event or occasion from a person, during the previous year, where such receipt is otherwise than by a cheque or bank draft or use of electronic clearing system through a bank account.
Clause - 32	(a) Details of b/f loss or dep. allowance, to the extent its available. (b) Whether a change in shareholding of the company has taken place in the PY due to which the losses incurred prior to the PY cannot be allowed to be c/f u/s 79. (c) Whether the assessee has incurred any speculation loss u/s 73 during the PY, if yes, please furnish the details of the same. (d) Whether the assessee has incurred any loss u/s 73A in respect of any specified business during the PY, if yes, please furnish details of the same.
Clause - 33	Section-wise details of deductions, if any, admissible u/c VIA or Chapter III (Section 10AA)
Clause - 34	Whether the assessee is required to deduct or collect tax as per the provisions of Chapter XVII-B or Chapter XVII-BB. If Yes, please furnish details. whether the assessee is required to furnish the statement of tax deducted or tax collected. If yes, please furnish the details. whether the assessee is liable to pay interest u/s 201(1A) or 206C(7). If Yes, please furnish.
Clause - 35	In the case of a trading concern, give quantitative details of principal items of goods traded: (i) Opening stock; (ii) Purchases during the PY; (iii) Sales during the PY; (iv) Closing stock; (v) shortage / excess, if any. In the case of a manufacturing concern, give quantitative details of the principal items of raw materials, finished products and by-products.

Clause-36A	(a) Whether the assessee has received any amount in the nature of dividend u/s 2(22)(e) (Yes/No) (b) If yes, please furnish the following details: - (i) Amount received, (ii) Date of receipt.
Clause - 37	Whether any cost audit was carried out, if yes, give the details if any, of disqualification or disagreement on any matter/ item/ value/ quantities may be reported/identified by the cost auditor.
Clause - 38	Whether any audit was conducted under the Central Excise Act, 1944, if yes, give the details if any, of disqualification or disagreement on any matter/ item/ value/ quantity as may be reported/identified by the auditor.
Clause - 40	Details regarding turnover, gross profit, (Ratio) etc., for the previous year and preceding PY (a) Total Turnover (b) Gross Profit/Turnover (c) Net Profit/Turnover (d) Stock in trade/Turnover (e) Material Consumed/Finished Goods Produced
Clause - 41	Please furnish the details of demand raised or refund issued during the PY under any tax laws other than Income Tax Act, 1961 along with details of relevant proceedings
Clause - 42	(a) Whether the assessee is required to furnish statement in Form No.61 or Form No. 61A or Form No. 61B? (Yes/No) [SFT & Reportable accounts] (b) If yes, please furnish details.
Clause - 43	(a) Whether the assessee or its parent entity or alternate reporting entity is liable to furnish the report u/s 286 (Yes/No) [Cbc Reporting] (b) if yes, please furnish the following details: ☞ Whether report has been furnished by the assessee or its parent entity or an alternate reporting entity ☞ Name of parent entity ☞ Name of alternate reporting entity (if applicable) ☞ Date of furnishing of report
Clause - 44	Break-up of total expenditure of entities registered or not registered under the GST. Specifying total amount of expenditure incurred during the year, expenditure in respect of entities registered under GST relating to goods or services exempt from GST, relating to entities falling under composition scheme, relating to other entities and total payment to registered entities. Expenditure relating to entities not registered under GST also need to be specified.



Sec. 92: Income from International or Specified Domestic Transactions

Any income, expenditure, interest & allocation of cost in relation of **International transaction or specified domestic transaction** shall be computed having regard to **Arm's length price**.

ALP means - **Correct market price, Fair price**.

- ⊗ If due to ALP there is **reduction in the income or increasing the losses** then transfer pricing provisions **shall not apply**.

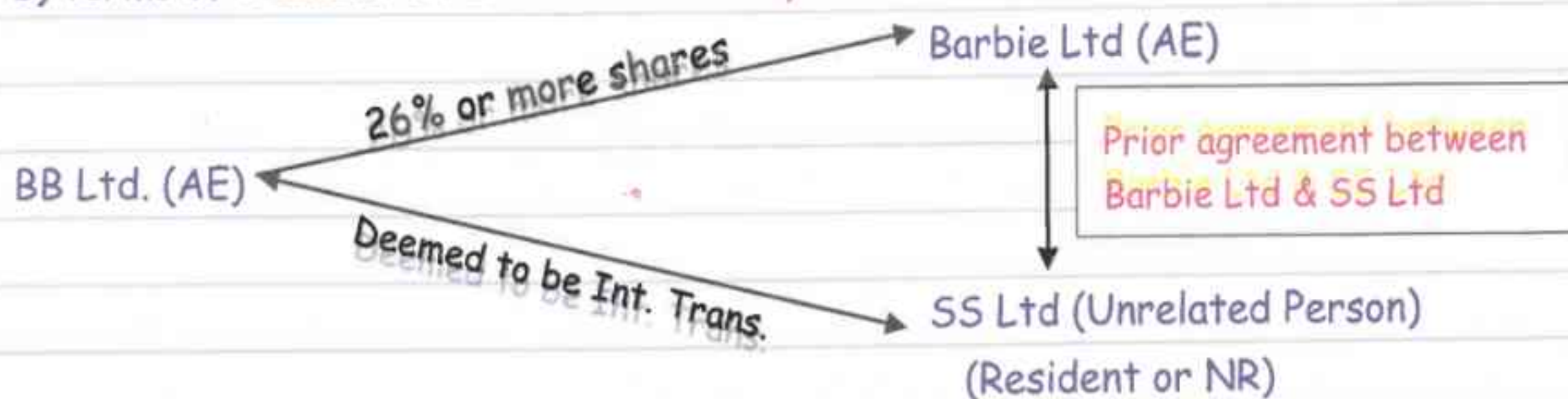
Sec. 92B: International Transactions

It means - (a) Transaction between two or more **Associated Enterprises (A.E)** &
(b) At least **one** must be **Non-Resident (NR)**.

Notes:

1. Transaction should be in the nature of purchase, sale, lease of property, provision of service, lending or borrowing of money etc.
2. If both AE's are NR, then TP shall only apply if income of one of the NR is taxable under IT Act.
3. Transaction between enterprise & unrelated person shall be **deemed to be international transaction**, if :

- a) there exists a **prior agreement** between AE & unrelated person, or
- b) terms of **transaction are determined by A.E.**



In the above example, the transaction between BB Ltd. & SS Ltd is not an international transaction but if there is prior agreement between Barbie Ltd & SS Ltd. related to transaction between BB Ltd & SS Ltd & terms are determined by Barbie Ltd. then the transaction between BB Ltd. & SS Ltd. is treated as deemed to be international transaction.

Sec. 92A: Associated Enterprise

Two enterprises shall be treated as AE's if **at any time during the P.Y.:-**

- a. One enterprise holds at least **26% shares** (voting power) of other enterprise.
- b. Any person holds at least **26% shares** of each of such enterprise.

Note: Above relationship covered direct as well as indirect control.

Ex:1 Tata Ltd. holds 33% of Voting Power in Tata Motors Ltd. and Tata Motors Ltd. holds 80% Voting Power in JLR Ltd.

In above situation, Tata Ltd. holds 26% or more voting power in Tata Motors Ltd., directly and in JLR Ltd. indirectly (through Tata Motors). Therefore, both Tata Motors Ltd. & JLR Ltd. are AE's.



Ex:2 Mr. Tata holds 40% of voting power in both TCS Ltd. and Titan Ltd. where neither TCS Ltd. has any holding in Titan Ltd. nor Titan Ltd. has any holding in TCS Ltd.

In this situation, since Mr. Tata directly holds 40% of voting power in both TCS Ltd. and Titan Ltd., TCS Ltd. & Titan Ltd. will be AE's.

- c. One enterprise appoints **more than half of the BOD** or **one or more Executive** Director of other enterprise.
- d. Any person appoints more than half of the **BOD** or **one or more Executive** Director of **each of such enterprise**.

Ex:1 JLR Ltd. has 15 directors on its Board. Out of that, Tata Motors Ltd. has appointed 8 directors. In such case, JLR Ltd. and Tata Motors Ltd. are AE's.

Ex:2 Mr. Ambani appointed 9 directors out of 15 directors of Jio Ltd. and appointed 2 executive directors on the board of RIL Ltd. In such case, since a common person i.e. Mr. Ambani appointed more than half of the directors in Jio Ltd. and appointed 2 executive directors in RIL Ltd., both Jio Ltd. and RIL Ltd. are AE's.

- e. A loan given by one enterprise to other enterprise, at least **51% of the Book Value Total assets** of other enterprise.

Ex: Book Value of total assets of KK Ltd. is ₹100 crores. BB Ltd. advances loan of ₹ 60 crores to KK Ltd.

In this case, BB Ltd. advances loan of ₹60 crores to KK Ltd, which is 60% of the book value of total assets of KK Ltd. Hence, BB Ltd. & KK Ltd. are AE's.

- f. One enterprise guarantees **at least 10%** of the Total **Borrowing** of the other enterprise.

Ex: P Inc. has total loan of 1 million dollars from XYZ Bank of America. Out of that, A Ltd., an Indian company, guarantees 20% of total borrowings in case of any default made by P Inc. In such case, since A Ltd. guarantee 20% of total borrowings of P Inc., P Inc. and A Ltd. are AE's.

- g. The Business of one enterprise is **wholly dependent** on **knowhow, patent, copy right etc.** of other enterprise.

Ex : Kia Motors India Ltd. manufactures cars in India using Knowhow of Hyundai Motors Ltd. south korea.

In this case, Kia Motors India Ltd. business is totally (100%) depends on Knowhow of Hyundai Motors Ltd. Hence, Kia Motors India Ltd. & Hyundai motors Ltd. are AE's.

- h. **90% or more of raw material** required by one enterprise is supplied by other enterprise and the prices and other conditions relating to the supply are influenced by such other enterprise.



Ex : Sam Ltd. USA supplies raw material of ₹ 91 Lakhs to BB Ltd. India and Total RM used by BB Ltd. is 100 lakhs. In this case Sam Ltd. & BB Ltd. are AE's if price influenced by Sam Ltd.

- i. Goods manufactured by one enterprise are **sold to** other enterprise & **price & other** condition are **influenced** by other enterprise.

Ex: BB Ltd. of India sells good to Martin Ltd. of Canada. In this case BB Ltd. & Martin Ltd. are AE's if price & other conditions related to sales is influence by Martin Ltd.

- j. One enterprise is **controlled** by **individual** & other enterprise is **controlled by such individual or his relative** or jointly by individual & relative.

Ex : Mr. A and Mr. B are relatives. Mr. A has control over X Ltd. and Mr. B has control over Y Ltd. Therefore, both X Ltd. and Y Ltd. will be deemed associated enterprises.

- k. One enterprise is **controlled by HUF** & other enterprise is controlled by **member, relative of member** or jointly by member & relative.

- l. One enterprise has **at least 10% interest** in another enterprise being **partnership Firm, AOP, BOI**.

- m. Any relationship of mutual interest, as may be prescribed.

Sec. 92C: Computation of Arm's Length Price (ALP)

ALP shall be computed as per the **most appropriate method** out of the following.

1. Comparable uncontrolled Price Method (CUP)	₹
Price charged/paid in comparable un-controlled transaction	xx
(+)/(-) Adjustment for difference between international Transaction & comparable uncontrolled transaction	xx
ALP	xx

Note: Normally CUP is applicable when **comparable uncontrolled transaction is available**.

2. Resale Price Method (RPM)	₹
Price charged for goods sold to unrelated enterprise (Resale price)	xx
(-) Normal G.P. margin in similar transaction	(xx)
	xx
(-) Purchase related expense	(xx)
ALP	xx

Note: Normally RPM is Applicable when **goods purchased from A.E** is transferred (sale) to **unrelated person**.



3. Cost Plus method (CPM)

	₹
Direct cost + Indirect cost of production	xx
(+) Normal G.P margin in similar transaction	xx
	xx
(+)/(-) Adjustment for difference between international Transaction & comparable uncontrolled transaction	xx
	xx
ALP	xx

Note: Normally CPM is applicable when goods manufactured by one A.E & sold to other A.E.

4. Profit split method (PSM)

Normally PSM is applicable where assessee executes an order in joint venture with its associate enterprise. First find out Total profit earned in Joint venture & after that divide that profit between AEs in the ratio of manpower employed, functions performed, risk taken, etc.

	₹
Cost incurred by Assessee	xx
(+) Share of profit of such enterprise	xx
	xx
ALP	xx

Ex. MM Ltd incorporated in UK received order to develop a software for Nano Inc. USA and consideration for same is \$ 2,00,000. MM Ltd executed such order in joint venture with BB Ltd & Modi Ltd, India based companies. Modi Ltd holds 30% equity shares of BB Ltd and 27% equity shares of MM Ltd. Consideration of \$ 2,00,000 is distributed amongst MM Ltd, BB Ltd. & Modi Ltd., \$ 1,00,000, \$ 50,000 & \$ 50,000 respectively.

Cost incurred to develop the software is \$1,60,000. Contributions by MM Ltd, BB Ltd & Modi Ltd. to the earning of such combined net profit on the basis of functions performed, risks assumed and assets employed by each enterprise is 40:40:20. This evaluation is to be made on the basis of reliable external market data which can indicate how such contribution would be evaluated by unrelated enterprises performing similar functions. Cost incurred by BB Ltd. is \$ 42,000. Calculate ALP for BB Ltd.

Solution : Total Profit from Joint Venture (\$2,00,000 - \$1,60,000) = \$40,000

Distribution of Profit on relevant contribution ratio:

MM Ltd: \$ 40,000 × 40% = \$16,000

BB Ltd : \$40,000 × 40% = \$16,000

Modi Ltd: \$ 40,000 × 20% = \$8,000

ALP for BB Ltd.: Cost Incurred: \$42,000 + Profit \$16,000 = ALP \$58,000

Profit to be increase of BB Ltd: \$58,000 - \$50,000 = \$8,000



5. Transactional Net margin method (TNMM)

Under this method, Profit (Net profit) earned by other players in the same industry under same or similar consideration taken into account for computing ALP.

➤ Sec 92C (2): More than one ALP

If more than one price is determined as per the most appropriate method then the Avg. (arithmetic mean) of such price shall be ALP (Arm's length price).

If the difference between Actual Transaction Price & ALP is upto 3% (1% in case of wholesale trading) of actual transaction price then such difference shall be ignored & actual transaction price shall be treated as ALP. If such difference is more than 3% of actual transaction price then entire difference shall be added to the income of assessee.

"Wholesale trading" means an international transaction or specified domestic transaction of trading in goods, which fulfils the following conditions, namely: -

- (i) Purchase cost of finished goods is 80% or more of the total cost of trading activities; and
- (ii) Avg. monthly closing stock of goods is 10% or less of sales of trading activities.

Example: Actual Transaction Price : 150

ALP as per Most Appropriate Method

1. 145

2. 152

3. 157

4. 160

Average of ALP: 153.5

Allowed difference (Tolerance Band) is 3% of Actual Transaction Price i.e. $150 \times 3\% = 4.5$

In this case difference between ALP & Actual Price is up to 3% so Actual Transaction price i.e. 150 is treated as ALP.

➤ Sec 92C(3): Determination of ALP by A.O.

In the following cases ALP shall be computed by A.O.

- (i) Assessee fails to compute ALP as per most appropriate method.
- (ii) Data used for computing ALP is not reliable or not correct.
- (iii) Documents are not maintained by Assessee as per Sec 92D.
- (iv) Assessee fails to furnish info & docs required u/s 92D.

Provided that an opportunity of being heard shall be given by A.O. to the Assessee.

➤ Sec 92C(4): Effect of ALP determined by A.O.

If ALP is computed by A.O. under sub-section (3) then



- a. If income of one enterprise is increased by A.O. the income of the other Associated enterprise shall **not change** [unaffected].

Hero Ltd. (India)

→ Honda Inc. (Japan)

Royalty Paid ₹200 Cr. for Knowhow

Hero Ltd paid royalty to Honda after deducting TDS, in this case suppose ALP determine by AO for royalty is ₹150 Cr., Royalty exps. allowed to Hero is only ₹150 Cr. but **Royalty Income taxable in hands of Honda is ₹200 Cr.**

- b. If income of one Associated Enterprise is increased by A.O. then deduction u/c VI-A & Sec 10AA shall **not be allowed** against increased part of its income.

BB Ltd. engaged in software development and working in SEZ	As per ROI	As per AO (↑Profit)
PGBP (GTI)	100 Cr	120 Cr.
(-) Deduction u/s 10AA [50% of Export profit]	(50 Cr.)	(50 Cr.)
NTI	50 Cr.	70 Cr.

➤ Rule 10CA: Range concept

- Arrange the values in the data set in **Ascending** order.
- Arrive at a **range starting from "35th Percentile" & ending at "65th Percentile"** of the data set.
- In case the actual transaction price **falls within the range** (i.e. 35-65 percentiles) then actual transaction price shall be deemed to be the ALP.
- In case the actual transaction price **does not fall within** the computed range, the **Median of the data set (i.e. 50%)** shall be deemed to be the ALP.
- If 35%, 65%, 50% percentiles computed are not whole numbers then we have to consider higher number for range.
E.g. - $7 \times 35\% \text{tile} = 2.45$ we have to select 3rd Value in data set.
- If 35%, 65%, 50% percentiles computed are whole numbers then we have to consider mean of value assign at that number and next number.
E.g. - $20 \times 35\% \text{tile} = 7$ we have to take average of value given at number 7 & 8.

E.g. 1: Actual transaction Price (i.e. 150)

S.No.	1	2	3	4	5	6	7
ALP	162	158	136	145	170	152	154

Ans: - First arrange all dataset in ascending order

S.No.	1	2	3	4	5	6	7
ALP	136	145	152	154	158	162	170

Now, 35th & 65th Percentile of dataset shall be computed as follows: -

Total no. of values in data-set $7 \times (35/100) = 2.45$

Total no. of values in data-set $7 \times (65/100) = 4.55$



Since 2.45 & 4.55 are not whole numbers, we have to take next higher numbers i.e. 3 & 5. The arm's length range will be beginning at 152 (3rd number) & ending at 158 (5th number).

So, if actual transaction price is within the range (152-158) then the actual transaction price shall be treated as deemed to be ALP, but in our example, Actual Transaction price (i.e. 150) is not falling within Range so ALP shall be median of data-set.

Total no. of values in dataset $7 \times (50/100) = 3.5$ Since, this is not a whole no. & next higher value is 4 & ALP is 154.

E.g. 2:

1	2	3	4	5	6	7	8	9	10
92	95	100	103	107	111	119	120	121	125
11	12	13	14	15	16	17	18	19	20
127	130	132	135	139	142	144	145	150	152

Total entries in data-set = 20

35th Percentile = $20 \times (35/100) = 7$

Since this is a whole number, Avg of value at 7 & 8 shall be the 35th percentile = $(119+120)/2 = 119.5$

65th Percentile = $20 \times (65/100) = 13$

This is a whole number, Avg of value at 13 & 14 shall be the 65th percentile = $(132+135)/2 = 133.5$

Median = $20 \times 50/100 = 10$.

Since this a whole number, Avg of value at 10 & 11 shall be the Median = $(125+127)/2 = 126$.

If Actual Transaction price is between 119.5 to 133.5 then actual transaction price is considered as ALP otherwise ALP will be 126.

Notes:

1. Range concept is applicable in case of CUP, RPM, CPM & TNMM.
2. Sec 92C(2) is applicable only if number of values in the data set is less than 6. If number of values in the data-set is 6 or more than Range Concept shall apply i.e., Rule 10 CA.
3. In Range concept, if 'Multiple years' data is given, then we have to take weighted average of multiple year data (Current year + Last two years) in case of RPM, CPM, TNMM.

Method	Weight
RPM	Sales Quantum
CPM	Cost Incurred
TNMM	Costs Incurred or Sales effected or Assets employed

Ex. BB Ltd engaged in software development and declare operating profit to operating cost (OP/OC) is 10%. Data for the CY & last 2 years of the similar entities undertaking similar transactions is available at the time of filing of ROI. The weighted average shall be based upon the weight of OC as computed below:



Sr. No.	Name	AY 22-23	AY 23-24	AY 24-25 (CY)	Aggregation of OC & OP	Weighted Average
1	A Ltd.	OC=100 OP=12	150 10	225 35	475 57	12%
2	B Ltd.	OC=80 OP=10	125 5	100 10	305 25	8.2%
3	C Ltd.	OC=250 OP=22	230 26	250 18	730 66	9%
4	D Ltd.	OC=180 OP=(-9)	220 22	150 20	550 33	6%
5	E Ltd.	OC=140 OP=21	100 (-8)	125 (-5)	365 8	2.2%
6	F Ltd.	OC=160 OP=21	120 14	140 15	420 50	11.9%
7	G Ltd.	OC=150 OP=21	130 12	155 13	435 46	10.57%

From the above, the dataset will be constructed as follows:

S.No.	1	2	3	4	5	6	7
ALP	2.2%	6%	8.2%	9%	10.57%	11.9%	12%

Now, 35th & 65th Percentile of dataset shall be computed as follows: -

Total no. of values in data-set $7 \times (35/100) = 2.45$

Total no. of values in data-set $7 \times (65/100) = 4.55$

Since 2.45 & 4.55 are not whole numbers, we have to take next higher numbers i.e. 3 & 5. The arm's length range will be beginning at 8.2% (3rd number) & ending at 10.57% (5th number).

In present case actual profit is 10% i.e. within the range so no need of any adjustment.

Sec. 92CA: Reference to Transfer Pricing Officer (TPO)

- If **AO** considers it necessary, he may refer the computation of ALP to TPO, with previous approval of **CIT/PCIT**.
- TPO shall gather material for computation of ALP & shall require assessee to produce evidence.
- During the course of proceedings before T.P.O. if any other international transaction or **specified domestic transaction** (which was not referred by A.O) **comes to his knowledge**, then T.P.O. shall **consider** such transaction also.
- On the basis of material & evidence, T.P.O. shall compute the ALP & pass an order computing ALP.
- Order of T.P.O is **binding on A.O**.
- The T.P.O shall pass the order before **60 days prior to the last date for completion of Assessment** allowed u/s 153.
- If Assessment proceedings are stayed by any court or reference has been made u/s 90/90A, the time available to TPO for making an order [after excluding the time for which assessment



proceedings were stayed or time taken for receipt of information u/s 90/90A) less than 60 days, then remaining period shall be extended to 60 days.

- (h) If any case referred to T.P.O. then time limit allowed u/s 153 to AO shall be increased by 1 year.
- (i) Any Joint /Deputy/ Assistant Commissioner, authorised by CBDT, can be appointed as TPO.
- (j) CG may notify scheme for the purpose of Faceless determining ALP by TPO till 31st March, 2025.

Sec. 92CB: Safe Harbour Rules

For determination of income u/s 9(1)(i) or Arm's length price CBDT may notify safe harbour rules. "Safe harbour" means circumstances in which the income-tax authorities shall accept the transfer price declared by the assessee. [Still not notified for your exams]

Sec. 92CC: Advance Pricing Agreement (APA)

1. The CBDT with the approval of Central Govt, may enter into APA with any person for determination:
 - (a) ALP or specifying the manner in which the ALP is to be determined, in relation to an **international transaction (IT)** to be entered into by that person.
 - (b) Income referred to in sec. 9(1)(i), or specifying the manner in which income is to be determined, attributable to the operations carried out in India by NR.
2. The manner of determination of the ALP may be methods referred to in sec. 92C(1) or the methods provided by rules with such adjustments or variations, as may be necessary or expedient so to do.
3. APA is applicable for maximum **consecutive 5 years**.
4. The APA shall be binding on
 - (a) The **person** who entered into APA
 - (b) The **IT Authority** till level of CIT/PCIT
5. APA shall **not binding** if there is **change in law/facts**.
6. With the approval of CG, CBDT may declare an APA to be **void-ab-initio**, if it finds that the APA has been obtained by **fraud or misrepresentation of facts**.
7. APA may apply for any period **maximum 4 years preceding** the first of the P.Y. referred in APA (**Roll back provision**).
8. If APA apply then provisions of **sec. 92C & 92CA does not** apply.
9. Consequences of declaration of an APA as void ab initio:
 - Provisions of the **Act shall apply** as if such APA had **never been entered into**.
 - Period from the date APA signed till date of order declaring the APA as void ab initio, **shall be excluded** for the purpose of any time limit under Act (e.g. time limit of assessment completion u/s 153).
 - In case time limit after exclusion of the above-mentioned period is less than 60 days, such remaining period of limitation shall be extended to 60 days.
10. If an application is made for APA, then, the proceeding, in respect of such person, shall be deemed to be pending.



11. Conditions for applying for rollback provisions:

APA shall contain Rollback provision in respect of an IT subject to the following, namely: -

- (i) International transaction (IT) is same as the IT to which APA applies;
- (ii) Return for the relevant rollback year has been filed before the due date as per sec. 139(1);
- (iii) Report (CA Report) in respect of the IT had been furnished in accordance with sec. 92E;
- (iv) Rollback provision, in respect of an IT, has been requested by the applicant for all the rollback years in which the IT has been undertaken by the applicant.
- (v) Application has been made in Form 3CEDA with fees ₹ 5,00,000.

12. Non-applicability of Rollback provision: [Rule No. 10MA]

- (i) Determination of ALP of IT for the year has been subject matter of appeal before the ITAT and the ITAT has passed an order disposing of such appeal at any time before signing of APA; 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.

Sec. 92CD: Effect of APA

1. If prior to the date of entering APA, any ROI has already been furnished for any P.Y. to which APA applies, then such person shall furnish modified return as per APA within 3 months from the end of the month in which APA was entered into.
2. If assessment for any P.Y. to which APA applies are pending on the date of modified return, the AO shall complete assessment as per APA, AO will get extra 1 year for completion of Assessment.
3. If assessment for P.Y. to which APA applies already completed before filing of modified return then A.O. shall pass an order modifying the total income of that P.Y within one year from the end of FY in which time modified return was furnished.

➤ CBDT Circular: 10/2015- Some clarification on Rollback

1. Assessee cannot be selective on the years for which it wants to apply for rollback. He has to either apply for all 4 PY's or not apply at all. However, rollback would not apply to years which does not satisfy basic conditions mentioned above.
2. Rollback can be applied as long as original return was filed before the due date u/s 139(1), even if the applicant files a revised return u/s 139(5) later.
3. Rollback can be applied only when IT undertaken is of same nature, with same AE. Also, FAR analysis is materially same with APA entered into for future years. (Including choice of method, comparability analysis & tested party).
4. Although rollback cannot be applied in case it has the effect of reducing income or increasing losses as compare to returned income or loss. APA can be applied in case if its reducing income or increasing losses as compare to Assessed Income or Loss.



For example, if the returned income is ₹ 100, income adjusted by TPO is ₹ 120, and application of rollback results in income of ₹ 90, roll back for the year would be determined in manner that returned income of ₹ 100 is treated as final.

5. Applicant has the **option to withdraw rollback application** while maintaining the APA application for future years. However, reverse is not true. **Rollback cannot be accepted without accepting APA for future years.**
6. Rollback can only be availed only by person who entered into the IT. Hence, in case of merger of companies, amalgamated co. will not be entitled to roll back for transactions carried out by amalgamating co.
Ex. If A merges into B, only B will be entitled to roll back carried out by himself in earlier years.
Further. If A and B merge to form a new company C, nobody would be entitled to rollback.
7. Similarly, in case of de-merger, resulting co. will not be eligible for rollback as it was not in existence in rollback years.

➤ Compliance Procedure under APA

1. Person proposing to enter into APA shall make an **application to DGIT** (International Taxation) requesting for **pre-filing consultation**.
2. The Pre-filing consultation shall determine suitability of IT for APA scope & terms.
3. Person treated eligible may make an application for APA before the 1st April of PY relevant to first AY for which application is made or before undertaking transaction after payment of fees.

Value of International Transaction	Fees (₹)
Upto 100 Crores	10 lakhs
> 100 Crores upto 200 Crores	15 lakhs
> 200 Crores	20 lakhs

4. Application made can be **withdrawn any time before finalization of APA but fees shall not be refund.**
5. Person shall file an **annual compliance report in quadruplicate** (4 copies) for every year covered under APA within **30 days of due date of ROI or 90 days of entering into APA whichever is later.**
6. **TPO shall carry out compliance audit for every year covered under APA and furnish the same within 6 months from end of month in which compliance report is received from person.**

Sec. 92CE: Secondary Adjustment

- **"Primary adjustment"** means increase in Income or reduction in the losses due to ALP adjustment.
- **"Secondary adjustment"** means excess money with AE shall be treated as deemed to be Loan or Dividend to AE. India follows **deemed loan approach**.
 - ◆ Excess money means difference between ALP & Actual transaction price.



- Cases where secondary adjustment has to be made - Where the primary adjustment due to:-
- (i) has been made **suo moto** by the assessee in his ROI; or
 - (ii) **Made by the AO** has been accepted by the assessee; or
 - (iii) Is determined by an **APA entered into** by the assessee u/s 92CC on or after 1/4/17; or
 - (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 (MAP)** under DTAA u/s 90 or 90A for avoidance of double taxation.

- Non-repatriation of excess money by the AE deemed to be an advance - Where, due to primary adjustment, there is an increase in total income or reduction in the loss, the **excess money or part thereof which is available with its AE**, if not repatriated to India within the prescribed time shall be **deemed to be an advance (loan)** made by the assessee to such AE and the interest on such advance, shall be included in the income of the assessee.

Explanation: The excess money or part thereof may be repatriated from any of the NR AE's.

- "Excess money" means the **difference between ALP** as per primary adjustment and the price at which the international transaction has actually taken place.

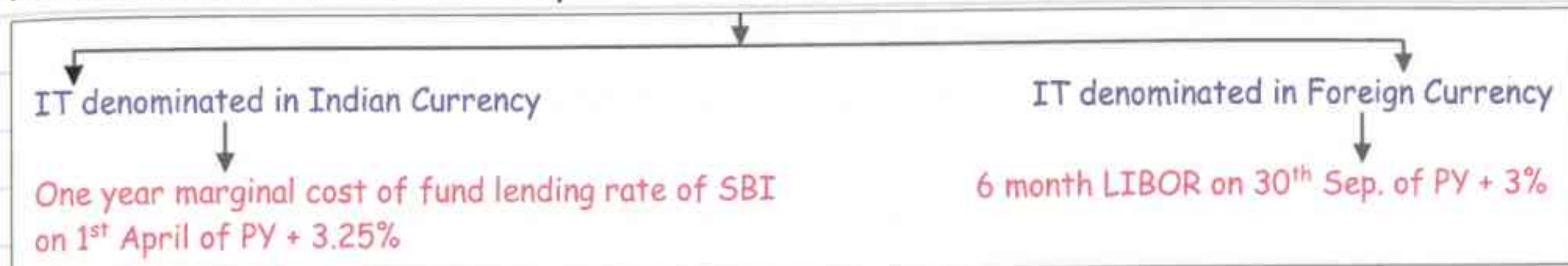
Example: BB Ltd entered into IT of sales with AE & actual Transaction Price is ₹ 3,000 lakhs ALP determined is ₹4,760 lakhs. So here excess money is ₹ 1,760 lakhs shall be first added to income of BB Ltd is known as Primary adjustment. BB Ltd have to repatriate ₹1,760 lakhs within 90 days otherwise treated as loan and the interest thereon shall be computed & added to the income until its repatriation is known as secondary adjustment.

- Time limit of repatriation and Interest Period

If primary adjustment is made by	Time limit for Repat.: 90 days	Interest period
Order of AO or appellate authority	From date of order of AO or appellate authority	From date of order of AO or appell. authority
APA -		
- entered upto due date of ROI in that PY	From Actual date of filing ROI	From due date of ROI
- entered after due date of ROI in that PY	From end of the month in which APA entered	From end of the month in which APA entered
Mutual agreement procedure	From the date of giving effect by AO to MAP	From the date of giving effect by AO to MAP
Other reasons	From Due date of ROI	From Due date of ROI



➤ Rate of Interest on "Excess Money"



- No requirement of secondary adjustment if primary adjustment in any PY does not exceed ₹ 1 crore or the primary adjustment is made in respect of A.Y. 2016-17 or an earlier assessment year.

Ex: 1 BB Ltd of India holding 36% equity shares of Trump Inc. USA. In PY 22-23 BB Ltd exported goods worth ₹ 6,00,00,000 to Trump Inc. The ALP of such transaction is ₹ 8,20,00,000. Due date of BB Ltd is 30th Nov. 2023. Transaction designated in Indian rupees. SBI one-year marginal cost of lending rate is 11.25% on 1st April 2023.

Solution: In this case excess money is 2.20 Crore. BB Ltd should repatriate such money within 90 days from the due date of ROI. i.e. till 28.02.2024 (30th Nov 2023 + 90 days)

If excess money not repatriate in India upto 28.02.2024 then following shall be treated as income of BB Ltd. for PY 23-24 (AY 24-25)

$2.20 \text{ Crore} \times 14.50\% \times 122 \text{ days} / 366 \text{ days (1st Dec. 23 to 31st March 24)} = 10,63,333.$

- Suppose in above example excess money not repatriated till 31st March 25 then following income shall be added for PY 24-25 (AY 25-26). SBI one-year marginal cost of lending rate is 11.25% on 1st April 2024 = ₹ 2.20 Crore $\times$ 14.50% = ₹ 31,90,000.

Note: Interest income is computed for every year till excess money repatriated in India.

◆ Sec. 92CE(2A): Additional Income Tax instead of Secondary adjustment

- Where the excess money or part thereof has not been repatriated in time, the assessee will have the **option** to pay additional income-tax at the rate of **18% + Surcharge of 12% + HEC 4% (eff. rate is 20.9664%)** on such excess money or part thereof in addition to the existing requirement of calculation of interest till the date of payment of this additional tax.
- Tax so paid shall be final payment of tax and **no credit shall be allowed in respect** of such tax.
- Deduction in respect of the amount on which such tax has been paid, shall not be allowed under any other provision of this Act; and
- If assessee pays the additional income-tax, he will **not be required** to make secondary adjustment or compute interest from the date of payment of such tax.

E.g.: Suppose in above example, BB Ltd not repatriated excess money and wants to pay additional tax on 1st July 2025.



In this case BB Ltd required to pay addition tax on 1st July 25 at 18% (+12%+4%) Additional Tax = ₹ 2,20,00,000 × 20.9664% = ₹ 46,12,608.

In this case following interest income shall be included in Total Income of PY 25-26. SBI one-year marginal cost of landing rate is 12% on 1st April 2025.

₹ 2,20,00,000 × 15.25% × 91/365 days (1st April 25 to 30th June 25) = ₹ 8,36,452

Sec. 92D: Maintenance of information & Documents

- (i) Assessee entering into International Transaction (IT) or Specified Domestic Transaction (SDT) required to maintain documents as **specified by CBDT (TP study report or Local file)**.
- (ii) **Constituent entity** of an international group, shall keep and maintain such information and document in respect of an international group as may be prescribed (**master file**).
- (iii) The **AO or the CIT (A)** may, require any person referred to point (i) to furnish TP study report within **10 days from the date of receipt of a notice**. (It may be extended by further 30 days)
- (iv) **Constituent entity** shall furnish the master file to the authority prescribed u/s 286 within the time and manner as may be prescribed. [Discussed later]

Notes:

1. Documents are required to be maintained only if value of IT is **more than ₹ 1 cr.**
2. Documents are required to be kept for **8 years** from the end of relevant A.Y.

Sec. 92E: Audit Report of CA

Assessee who entered into IT or SDT is required to file report of CA in the Form No. **3CEB** upto 31st Oct. of A.Y. [one month before due date of ROI]

➤ Penalties

Section	Default	Penalty
271AA	i. Fails to keep & Maint. Documents (TP Study Report) ii. Fails to Report Transactions iii. Fails to Maintain/Furnish Correct Info./ Doc. _____ iv. Fails to furnish info & doc. (Master File)	→ 2% of Transaction Value → 5,00,000
271G	Failure to furnish info & documents (TP study Report)	2% of Transactions Value
271BA	Failure to furnish report of CA as per Sec 92E .	₹ 1,00,000
270A	Failure to report any transactions would constitute 'misreporting of income'	Penalty of 200% of Taxes apply

Note: However, the amount of underreported income (URI) represented by any addition made in conformity with the ALP determined by the TPO would not be included within the scope of URI u/s 270A, where the assessee had maintained information and documents, as per 92D, declared the international transactions and disclosed all material facts relating to the transaction.



Sec. 92BA: Specified Domestic Transactions

Any of the following transactions, if the agg. value of such trans. in the P.Y. is **more than ₹ 20 cr.**

- (i) Inter-unit transfer of goods and services referred to in Sec 80A & 80-IA(8).
- (ii) Business Transacted between assessee and his closely connected person referred u/s 80IA(10).
- (iii) Transaction referred to in any other section of Chapter VI-A or 10AA to which provisions of sec 80IA(8) or(10) apply.
- (iv) Business transacted between assessee and his closely connected persons referred u/s 115BAB(6) & 115BAE(4).
- (v) Any other transaction as may be prescribed.

Note: The above sections refer to transactions between eligible business/units (claiming deduction u/s 10AA or Income based deductions u/c VI-A or opting for concessional tax rates u/s 115BAB/ 115BAE) and non-eligible business/units where the consideration for transactions does not correspond to the market value resulting in higher profits in the eligible business/units.

Country-by-country Report: Reporting Requirements of MNES

The Country-by-Country (CBC) report has to be submitted by parent entity of an international group **to the prescribed authority in its country of residence.** This report is to be based on consolidated financial statement of the group.

- MNEs have to report annually and for each tax jurisdiction in which they do business, the **amount of revenue, profit before income tax and income tax paid and accrued.**
- MNEs have to report their **total employment, capital, accumulated earnings and tangible assets** in each tax jurisdiction.

Sec 286: Furnishing of Report (Cbc) in respect of International Group

1. If **parent entity** of the international group/alternate reporting entity is **resident in India** shall be required to furnish CbC report (if the **group revenue as per CFS of last year ₹ 6400 crore or more**) in respect of the group in Form 3CEAD to JDIT designated by DGIT/PDGIT (system) **within 12 months from the end of the relevant accounting year.**

Note: Rate of exchange for the converting revenue into Indian ₹ shall be TTBR of last day of the **last** accounting year.

2. Every **resident constituent entity** of the international group, whose parent entity is NR, shall **notify in Form 3CEAC, at least 2 months prior to due date** for furnishing CbC report stating:
 - ✓ **whether it is the alternate reporting entity** of the international group, or
 - ✓ **details of parent entity /alternate reporting entity** of the international group & the country of which the said entities are resident.



3. Resident constituent entity (other than parent entity/alternate reporting entity) shall to furnish CbC report in India, if parent entity of the group is resident of a country :
- ✓ In which it is not obligated to file CbC report
 - ✓ With which India does not have an arrangement for exchange of the CbC report; or
 - ✓ Which is not exchanging info. with India even though there is an agreement (systemic failure), and this fact has been intimated to the entity by JDIT- CbC shall be file within 6 months from the end of the month in which systemic failure has been intimated.
- Within 12 months from end of accounting year
4. If there are more than one resident constituent entity of the group, then the group can nominate one constituent entity in Form 3CEAE who shall furnish the CbC report on behalf of the group.
5. If the NR parent entity had designated an alternate entity for filing CbC report in the tax jurisdiction of the alternate entity & alternate entity has furnished such report on or before date specified by that country, then the resident constituent entities would not be obliged to furnish the report if it can be obtained by Indian tax authorities under the agreement of exchange with that country.
6. JDIT can call for documents and information from the entity furnishing the report for the purpose of verifying the accuracy & they shall produce the same within a period of 30 days from the date of receipt of a notice (Can be further extended by maximum 30 days).

Notes:

1. "Alternate reporting entity" means an entity which has been designated by the group to file CbC report in place of the parent entity.
2. "Accounting year" means:

If Parent entity is resident in India	Previous year i.e. 1 st April - 31 st March
If Others	Accounting period for which parent entity prepares its FS under laws or AS of its country.

3. Sec 271GB(1)/(3): Penalty for Not furnishing report u/s 286

Period of Delay	Penalty
a. Upto a month	₹ 5,000 Per day
b. beyond one month	₹ 15,000 per day after one month
c. Continuing default even after service of order levying penalty either under (a) or under (b)	₹ 50,000 per day of continuing failure beginning from the date of service of order

4. Sec 271GB(2): Penalty for Not furnishing information and documents (discussed in point 6 of 286)

Period of Delay	Penalty
a. Fails to produce info. within time allowed	₹ 5,000 Per day after such period expire
b. Continuing default even after service of order levying penalty	₹ 50,000 per day of continuing failure beginning from the date of service of order



5. Sec 271GB(4) : Penalty for submission of inaccurate information in the CBC report
If the reporting entity has provided any inaccurate information in the report, the penalty would be ₹ 5,00,000 if, -
 - (a) Entity has knowledge of the inaccuracy at the time of furnishing the report; or
 - (b) Entity discovers the inaccuracy after the report furnished but fails to inform the prescribed authority and furnish correct report within 15 days of such discovery; or
 - (c) Entity furnishes inaccurate info. or document in response to notice of the prescribed authority.
 6. Sec 273B: Penalty u/s 271GB not applicable if there was reasonable cause for such failure.
- Maintenance and furnishing of Master file [Rule 10DA]
1. Master file contains list of all entities of the international group along with their addresses, legal status of the constituent entity and ownership structure of the entire international group, description of the business of international group, list and brief description of important service arrangements etc.
 2. constituent entity of an international group shall -
 - (i) if the consolidated group revenue as per CFS of the group for the accounting year, exceeds ₹ 500 crore; and
 - (ii) the aggregate value of international transactions -
 - (a) during the accounting year, as per the BOA's, exceeds ₹ 50 crore, or
 - (b) in respect of purchase, sale, transfer, lease or use of intangible property during the accounting year, as per the BOA's, exceeds ₹ 10 crore.

Note: Rate of exchange for the converting revenue into Indian ₹ shall be TTBR of last day of the accounting year.
 3. Master file shall be furnished to the JDIT in Form 3CEAA on or before the due date for furnishing the return of income.
 4. Constituent entity shall mandatorily furnish Part A of Form 3CEAA whether or not the limits specified above are satisfied (i.e. File Part A of Form 3CEAA mandatory every year. Fill Part B only if above limits are satisfied).
 5. Where there are more than one constituent entities of group resident in India. Form 3CEAA may be furnished by any one constituent entity if
 - i. international group has designated such entity for this purpose and
 - ii. information has been conveyed in Form 3CEAB to the JDIT in this behalf at least 30 days prior to the due date of furnishing Form 3CEAA.
 6. Documents should be kept & maintained for 8 years from the end of AY.

Sec. 94A: Special Provision in respect of transaction with person located in NJA
CG may notify any country or territory outside India to be a notified Jurisdictional area (NJA).
If Assessee enters into transaction with any person located in NJA then :



- (i) All the parties shall be deemed to be associated enterprises (as per 92A).
- (ii) The transaction shall be deemed to be an international transaction (as per 92B).
- (iii) The provision of Transfer pricing shall apply to Assessee (except tolerance band of 3%).
- (iv) Assessee have to submit documents & information required by IT Authority.
- (v) If any payment made to person located in NJA then min. TDS rate will be 30%.
- (vi) If Assessee recd any sum from person located in NJA then assessee have to offer explanation about the source of the fund in the hands of that person or in hands of beneficial owner (if that person is not beneficial owner). If assessee doesn't offer explanation or explanation is not satisfactory, then such sum shall be treated as income of Aseessee.

Sec. 94B: Limitation on Interest Deduction in certain cases

1. Interest expenses or similar nature (like guarantee commission etc) incurred by an Indian company or a permanent establishment of a foreign company in India in respect of any debt issued by a non-resident, being an associated enterprise shall be disallowed while calculating income under the head PGBP to the extent "Excess interest" (Excess interest shall be disallowed)
2. Calculation of Excess Interest
 - (i) Total Interest - 30% of EBITDA (Earning before Interest, Tax, Depreciation, amortisation)
 - (ii) Interest paid to Associate EnterpriseWhichever is Lower
 - Alternate Views: Allowed interest to AE is 30% of EBITDA
3. If the debt is issued by a lender which is not associated but an AE 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 AE.
4. Above provision is applicable only if interest to AE is more than ₹ 1 crore rupees.
5. This Section shall NOT apply to an Indian company or a PE of a foreign company which is engaged in the business of banking or insurance or finance company located in IFSC or interest paid in respect of a debt issued by a lender which is a PE in India of a NR, being a person engaged in the business of banking or such class of NBFC as may be notified.
6. The amount of interest expenditure disallowed under this provision, shall be carried forward to the following AY's, and it shall be allowed as a deduction against the profits and gains, if any, of any business or profession for that assessment year to within the limit of this section. This interest can be carried forward upto 8 AY's immediately succeeding the assessment year for which the excess interest expenditure was first computed.



Sec. 6: Residential Status

Total income of an assessee cannot be determined without knowing his residential status. Scope of Total income is based on Residential status. If any person become **Resident** then his **whole world income is taxable** in India but if person become **Non-Resident**, then **only Indian Income** is taxable for that person. Residential status shall be determined for **every person for each previous year** independently.

Residential Status of Individual

Basic Conditions as per Section 6(1)	No. of days stay in India	Satisfied or Not satisfied
1. Stay in India for 182 days or more in P.Y. (Current PY)		
OR		
2. Stay in India for 60 days or more in P.Y. and 365 days or more in Last 4 P.Y.'s		
Additional Conditions Section 6(6)		
1. Resident for 2 P.Y. or more in Last 10 P.Y.'s		
AND		
2. Stay in India for 730 days or more in Last 7 P.Y.'s		

If any individual satisfies **any One Basic condition** (at least one) then he is treated as Resident in India otherwise Non-Resident in India. If any individual become **Resident in India**, then we have to check that such person is **Resident and ordinarily resident (ROR)** in India or **Resident but Not ordinarily (R but NOR)** Resident in India. If the such assessee satisfy **both the additional conditions** then he is treated as R and OR otherwise R but NOR.

Notes:

- The day on which he **enters India**, as well as the day on which he leaves India, shall be taken into account as the **stay of Individual in India**.
- In the following cases only Basic condition no. 1 is applicable for Determination of residential status (2nd Basic condition should be Ignored).
 - Indian Citizen**, Leave India during the P.Y. for an **employment outside India**.
 - Indian Citizen** being a **crew member** of Indian Ship, **leave India** during the P.Y.
 - Indian Citizen or Person of Indian origin** engaged outside India in any employment or a Business or Profession, and **Visiting India** during P.Y. & **his total income** (excluding income from foreign source) is **upto ₹ 15 Lakhs in P.Y**

Note : Person of Indian Origin means, he or either of his parents or either of his grandparents were born in undivided India.



- In case of Indian citizen or person of Indian origin having total income (other than foreign source income) of **more than ₹ 15 lakhs** then **2nd** basic condition applicable and instead of **60 days in PY**, **120 days are considered**, if stay in India 120 days or more but less than 182 days in current PY & stay in India for 365 days or more in last 4 PY's then he will be treated **as resident but not ordinary resident**. (In this case no need to check additional conditions)

Note: Income from foreign sources (FSI) means income which **accrues or arises outside India** except income derived from a business controlled in or a profession set up in India.

- **Summary - How many days an Indian Citizen or a Person of Indian origin visits in India during PY**

Less than 120 days	120 days or more but upto 181 days	182 days or more irrespective of Total Income
NR in India	If he satisfied both the conditions then R but NOR otherwise NR (i) Stay in India for 365 days or more in last 4 PY, and (ii) His Total Income (other than foreign income) more than ₹ 15 Lakhs.	If he satisfied both the conditions then R&OR otherwise R but NOR (i) Resident in India for 2 PY or more in last 10 PY's, and (ii) Stay in India for 730 days or more in last 7 PY's

- In case of **Indian citizen**, crew member of a foreign bound ship (originated from India and destination outside India or vice versa) leaving India, followings days shall **be treated as stay outside India**; - "From the **date entered into the continuous discharge certificate (CDC)** in respect of **joining** the ship & ending on the date entered into CDC in respect of **signing** of the ship."

Sec. 6(1A): Deemed Resident

In case of **Indian citizen**, having **total income (other than foreign source income)**, **exceeding ₹ 15 lakhs** during the PY shall be **deemed to be resident** in India in that PY, if 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 & he is **always treated as R but NOR**.

- ⊗ However, this provision will not apply in case individual resident in PY as per section 6(1).
- ✓ **Liable to tax means** that there is an **income-tax liability on such person** under foreign country tax law. It also **includes a person** who has subsequently been **exempted from such liability** under the law of that country.

Sec. 6(2): Residential Status of Hindu Undivided Family (HUF)

If Control and Management of its affairs is

Wholly or Partly in India
Resident

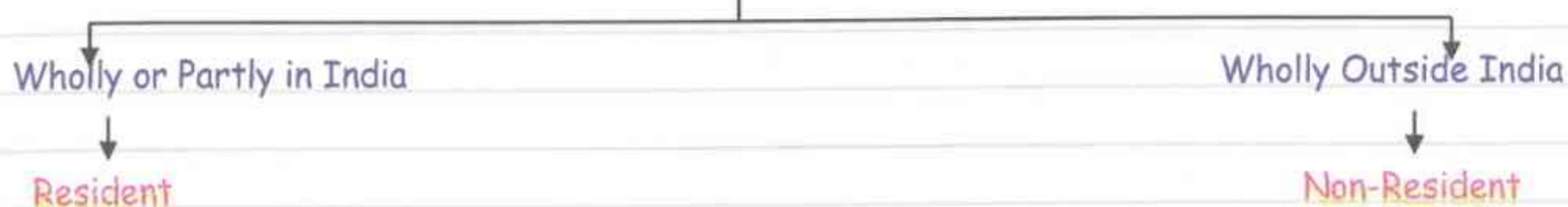
Wholly Outside India
Non-Resident



Note: If Karta of HUF is satisfying both the additional Conditions as per sec 6(6) the HUF is treated as R and OR otherwise R but NOR.

Sec. 6(2): Residential Status of FIRM/AOP/BOI/Local Authority/AJP

If Control and Management of its affairs is



Sec. 6(3): Residential Status of Company



➤ POEM means a "place where key management & commercial decisions that are necessary for the conduct of the business of an entity as a whole are in substance made".

➤ Determination of POEM (Applicable only if Turnover > ₹ 50 crore) [Circular 06 & 08/2017]

A. Company having Active Business outside India (ABOI)

If both the conditions are satisfied then POEM is not in India.

- Active Business outside India (ABOI), and
- Majority Board meetings held outside India.

"ABOI" means: If all conditions are satisfied:-

- If passive income is upto 50% of its total income, and
- Less than 50% of its total asset are situated in India; and
- Less than 50% of total number of employees are situated in India or are resident India; and
- Payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.

▪ Meaning of Certain Terms:

☞ Passive Income means:

- Income from Transaction where both Purchase & sales of goods is from/to its Associated Ent.
- Income by way of Royalty, Dividend, Capital Gain, Interest (except for Banking Company or PFI) or Rental income.

- ☞ **Income:** Income as per Tax Law of country of incorporation. If Tax Law does not required computation of Income, then Income as per Books of Accounts.
- ☞ **Value of Assets:**
 - a. Depreciable asset: **Average of opening and closing WDV** of such asset or block of asset as per Tax Law of that country.
 - b. Other Asset: Value as per Books of Account.
- ☞ **Number of Employees:** **average of the no. of employees** at the **beginning and at the end of the year** and shall include persons, who though not employed directly by the Company (contract employees), perform tasks similar to those performed by the employees.
- ☞ **Pay roll:** Cost of salaries, wages, bonus and all other employee compensation including related pension and social costs borne by the employer.
- Notes:**
 - In case the **Board is not exercising its powers** of management and such powers are being exercised by either the holding company or any other person, resident in India, then **POEM shall be considered to be in India.**
 - Merely **BOD follows general & objective principles of global policy** of the group in relation to pay roll, Accounting, HR, IT infrastructure and network platforms, Supply chain, Routine banking, operational procedures etc. **it would not constitute that BOD as standing aside & not exercising its powers.** Provisions of GAAR can be triggered in cases where it is found to be used abusive/aggressive tax planning.
 - For the ABOI test average of the data of PY and last 2 PY shall be considered. If company has not been in existence for that long then data of period that the company has been in existence shall be considered. If accounting year for tax purposes, in accordance with laws of country of incorporation, is different from the PY, then, data of the accounting year that ends during the relevant PY and two accounting years preceding it shall be considered.
Example: Suppose company incorporated in USA & they follow calendar year for tax purpose. For determination of residential status for PY 2023-24 data of calendar year 2023, 2022 & 2021 shall be considered.



B. Other Company (ABOI test not fulfilled)

Determination of POEM would be Two Stage Process

1. Identification or ascertaining the persons who actually make the key management and commercial decision for conduct of the company's business as a whole.
2. Determine of place where decisions are infact being made

☞ The place where decisions are taken would be more important than the place where such decision are implemented. For the purpose of determining POEM, it is the substance would be conclusive rather than the form.

S.No.	Situation	POEM
1.	When the BOD exercise authority & takes key commercial decisions in substance.	Place where key decisions are taken
2.	Powers are delegated by the Board to Senior management or other persons.	Place where such persons make decision
3.	Powers are delegated by the Board to Executive committee	Location where executive based & where committee make decisions
4.	In case of Circular resolution & round robin voting.	Location of the person who has the Authority to take decisions.
5.	Decisions made by shareholder on Matters which are reserved for shareholder decisions.	Location where such decisions are Taken not relevant for determination of Poem
6.	Senior persons located in Principal place of business	Such Principal place of business
7.	Decentralised Company (Multiple locations)	Location where senior managers are primarily based, return to travel to other location or meet when formulating or deciding key strategies and policies for the company as a whole.
8.	Senior management may operate from different locations and participate in various meetings via telephone or video conferencing	The location where highest level of management (for example, the MD and Financial Director) and their direct support staff are located.

- CBDT clarified that POEM guidelines shall not apply to a company having turnover or gross receipts of ₹ 50 crores or less in a financial year.

Sec. 115JH: Transition Mechanism for Foreign company

Foreign company which has not been assessed to tax in India earlier and has become POEM resident in India for 1st time then transition mechanism shall apply.

- Central Govt. Notification No. 29/2018, dated 22 June, 2018 [Applicable from 1st April, 2017]

Let's understand the notification with the help of an example. Say, a foreign company (FCO) is incorporated in Singapore and is a tax resident of that country. FCO becomes a POEM resident in India for FY 2023-24

1. Determination of opening WDV

Whether FCO is assessed to tax in Singapore	Yes		No
Whether depreciation is considered for taxability in Singapore	Yes	No	Not applicable
Then, opening WDV of FCO for FY 24-25 shall be	WDV as on 1 st April 24 as per Singapore tax records	WDV as on 1 st April 24 assuming that depreciation is actually allowed	WDV as on 1 st April 24 as per FCO's books of account maintained as per Singaporean laws

2. Brought forward loss and unabsorbed depreciation

Whether FCO is assessed to tax in Singapore	Yes		No
Then, L&D of FCO as on 1 st April 24 shall be	L&D of FCO as on 1 st April 24 as per Singapore tax records.	L&D of FCO as on 1 st April 24 as per FCO's BOA as per Singaporean laws	

Notes

- Losses shall be allowed to be carried forward under Income Tax Act only for the remaining period.
- Losses and Unabsorbed dep. of foreign company shall be allowed to setoff only against incomes which has become taxable in India due to it becoming resident due to POEM.
- In case of different accounting period followed by company, Losses and depreciation shall be allocated on proportionate basis.

3. Period of P&L A/c and B/S in cases where accounting year of FCO does not end on 31st March

☞ FCO is required to prepare P&L A/c and B/S for the period starting from the date on which the accounting year immediately following said accounting year begins, upto 31st March of the year immediately preceding the period beginning with 1st April and ending on 31st March during which the FCO has become resident.

☞ The foreign company is also required to prepare P&L A/c and B/S for succeeding periods of 12 months, beginning from 1st April and ending on 31st March, till the year the FCO remains resident in India on account of its POEM.



E.g. 1: If the accounting year of the FCO is a calendar year and the company become resident in India during P.Y. 24-25 for the first time due to its POEM being in India, then, the company is required to prepare P&L A/c and B/S for the period 1st Jan., 24 to 31st March, 24. It is also required to prepare P&L A/c and B/S for the period 1st April, 24 to 31st March, 25.

For the purpose of C/F of loss and unab. dep. in cases where the accounting year followed by the FCO does not end on 31st March and the period starting from the date on which immediately following year begins upto 31st March of the year, immediately preceding the period beginning with 1st April and ending on 31st March during which it has become resident, is, —

(a) **less than 6 months**, it shall be included in that accounting year;

(b) equal to or **more than 6 months**, that period shall be treated as a **separate accounting year**.

E.g. 2: For the purpose of C/F of loss and unab. dep. in this case, since the period 1st Jan, 24 to 31st March, 24 is less than 6 months, it is to be included in the last accounting year. Accordingly, the P&L A/c and B/S of the 15 months period from 1st Jan, 23 to 31st March, 24 is to be prepared.

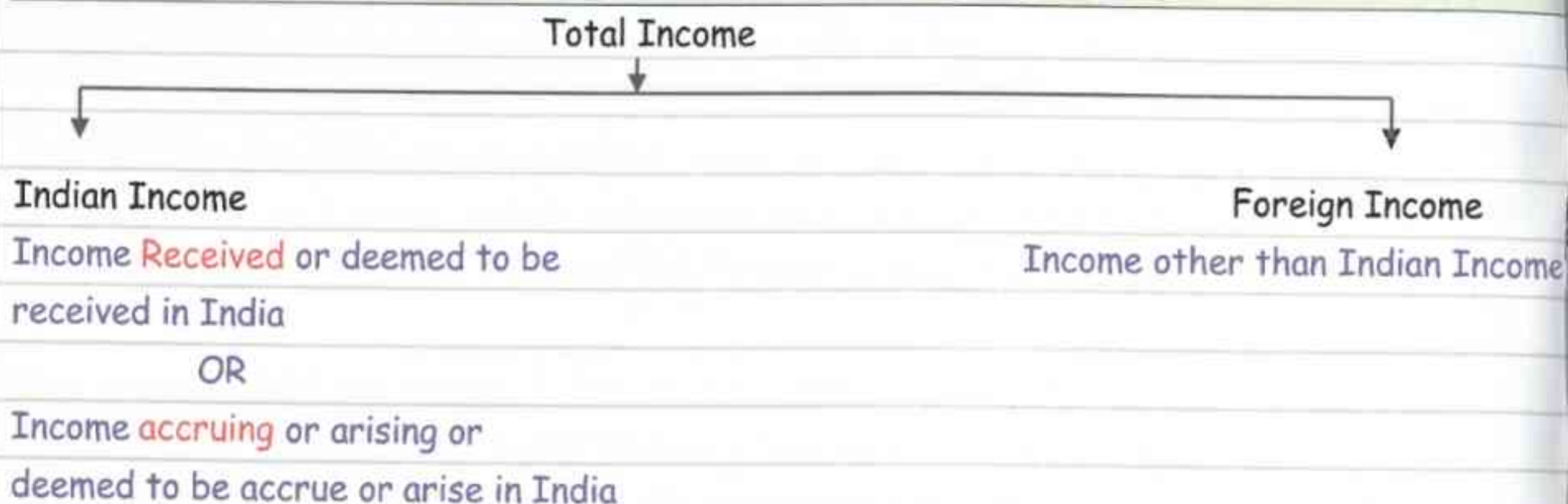
E.g. 3: If the accounting year is from 1st July to 30th June and the FCO becomes resident during P.Y. 24-25, then, the company is required to prepare P&L A/c and B/S for the period 1st July, 23 to 31st March, 24. It is also required to prepare P&L A/c and B/S for the period 1st April, 24 to 31st March, 25

For the purpose of C/F of loss and unab. dep. in this case, since the period is 6 months or more, it is to be treated as a separate accounting year. The loss and unab. dep. as per tax record or books of account, as the case may be, of the foreign company shall, be allocated on proportionate basis.

4. **Applicability of TDS provisions:** If more than one provision of TDS applies to the FCO as resident as well as foreign company, the provision applicable to the foreign company alone shall apply.
5. **Availability of deduction u/s 90 or 91 (Foreign tax credit):** Foreign Co. is eligible for the relief/deduction of foreign taxes paid as per Sec 90 or 91 of the Act.
6. **Non-applicability of the notification:** This notification does not apply to income of the FCO which was taxable in India even if foreign co had not become a resident.
7. **Applicability of other Provisions relating to FCO:** FCO shall continue to be treated as a foreign company even if it is said to be resident in India and all the provisions of the Act shall Apply accordingly. Consequently, the provisions specifically applicable to, —
 - (i) a foreign company, **shall continue to apply** to it;

- (ii) NR persons, shall **not apply** to it; and
- (iii) Provisions specifically applicable to resident, **shall apply** to it.
8. Applicability of tax rate on foreign company: Tax Rate of 40% shall remain the same, i.e., rate of income-tax applicable to the foreign company even though residency status of the foreign company changes from NR to resident on the basis of POEM.
9. Meaning of Foreign jurisdiction: The place of incorporation of the foreign company.

Sec. 5: Scope of Total Income



➤ Taxability of Income for Individual & HUF

S.No.	Income	R & OR	R but NOR	NR
1.	Indian Income	Taxable	Taxable	Taxable
2.	Foreign Income	Taxable	Taxable	Not Taxable
	- Income from Business or Profession Controlled / setup from India			
	- Other foreign Income	Taxable	Not Taxable	Not Taxable

➤ Taxability of Income for Other Assessee

S.No.	Income	Resident	NR
1.	Indian Income	Taxable	Taxable
2.	Foreign Income	Taxable	Not Taxable

Notes:

- Income received means, **received** for the **first time**. After receiving income outside India, subsequently if it is remitted into India, it **cannot be treated as Receipt of Income**.
- Income may be in **Cash or in Kind**.
- Any income already taxed on accrual basis, consequently remitted to India, is not chargeable to tax at the time of remittance irrespective of the residential status.

4. Income **accrual** in India means, income **generated in India** or **source of Income** situated in India.

Sec. 7: Income deemed to be received in India

- (i) Contribution in excess of **12% of salary to Recognised provident fund** or interest credited in excess of 9.5% p.a (Annual accretion to the credit of RPF).
- (ii) Contribution by employer under a pension scheme referred u/s 80CCD (NPS).
- (iii) Amount transferred from URPF to RPF (being the employer's contribution and interest thereon).

Sec. 9: Income deemed to accrue or arise in India

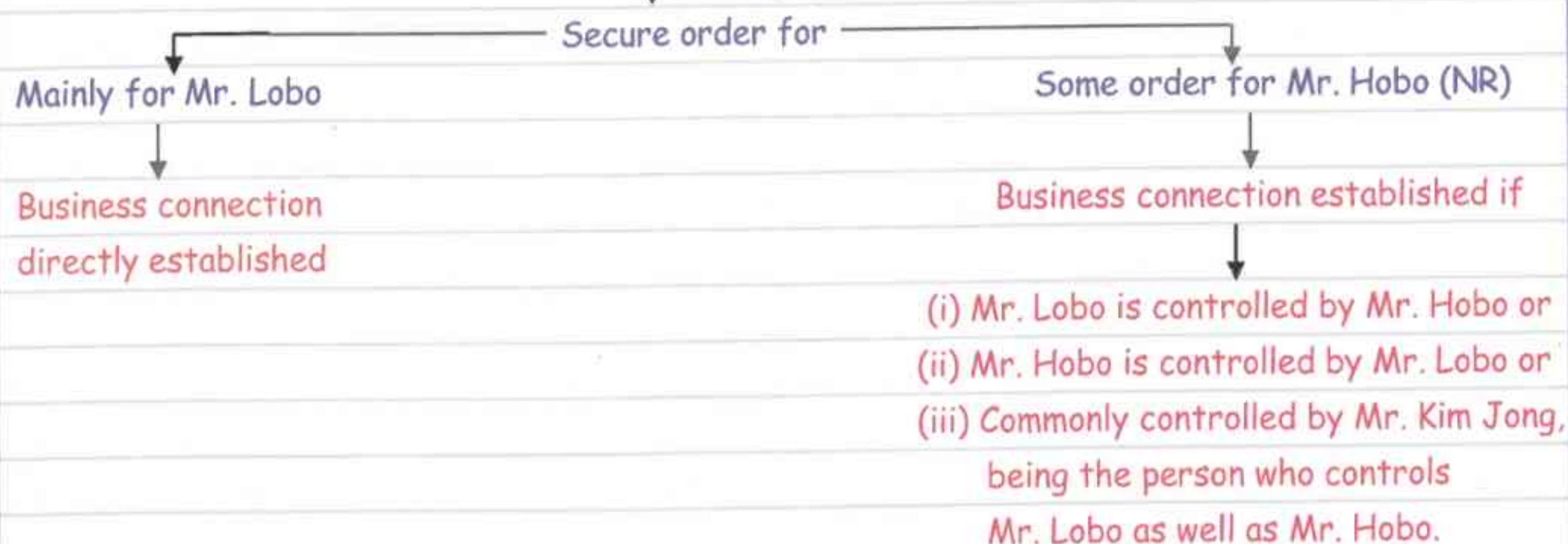
- Sec 9(1)(i): Through or from any Business Connection in India or any property in India or any asset or source of income in India or transfer of a capital asset situated in India

☞ "Business Connection" means a **person acting on behalf of NR :-**

- a. Must have an **authority**, which is **habitually** exercised in India, to **conclude contracts** on behalf of the non-resident or habitually concludes contracts or plays the principal role leading to conclusion of contracts by that NR and such contracts are
 - in the name of the NR; or
 - for the transfer of the ownership of, or for the granting of the right to use, property owned by that NR or that NR has the right to use; or
 - for the provision of services by that NR.
- b. **Habitually maintain a stock** from which he regularly delivers on behalf of NR.
- c. **Habitually secure order** in India mainly or wholly for NR.

Further in following case Business connection also establish

Mr Raj acting on behalf of Mr. Lobo (NR)



- ✓ Significant economic presence of a NR in India shall also constitute business connection in India

S.No.	Nature of Transaction	Condition
(a)	Transaction in respect of any goods, services or property carried out by a NR with any person in India including provision of download of data or software in India,	Aggregate of payments arising from such transactions during the PY exceeds ₹ 2crores.
(b)	Systematic and continuous soliciting of business activities or engaging in interaction with users in India	Numbers of users should be atleast 3 Lakhs.

Further, the above transactions or activities shall constitute SEP in India, whether or not agreement for such transactions or activities is entered in India or NR has a residence or place of business in India or NR renders services in India.

However, only so much of income as is attributable to the transactions referred to in (a) or (b) above shall be deemed to accrue or arise in India.

- ⊗ Agents having independent status are not included in Business Connection: Where the NR carries on business through a broker, general commission agent or any other agent having an independent status, if such a person is acting in the ordinary course of his business. Independent status where agent does not work mainly or wholly for the NR.

Where business connection established then only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India. [Expl. 3]

- ✓ Explanation 3A added by FA 20 w.e.f. AY 21-22

The income attributable to the operations carried out in India, shall include income from—

- Advertisement which targets a customer who resides in India or a customer who accesses the advertisement through internet protocol (IP) address located in India;
- Sale of data collected from a person who resides in India or from a person who uses IP address located in India; and
- Sale of goods or services using data collected from a person who resides in India or from a person who uses IP address located in India.

- ⊗ Following shall not be treated as Business Connection in India

- Purchase of goods in India for export.
- Collection of news and views in India for transmission out of India.
- Shooting of cinematograph films in India if such NR is Individual, who is not a citizen of India or a firm which does not have any partner who is a citizen of India or who is resident in India or a company which does not have any shareholder who is a citizen of India or who is resident in India.
- In case of a foreign co. engaged in the business of mining of diamonds, from the activities which are confined to display of uncut and unassorted diamonds in any special zone notified by the CG.



☞ Income from property, Asset or source of Income is situated in India, then it is treated as deemed to be accrued or arise in India.

☞ Income through transfer of Capital asset situated in India whether registration of documents of transfer in India or outside India or consideration received in India or outside India.

Indirect Transfer [Introduced to override SC Judgment in Case of Vodafone]

Expln. 5: It is hereby clarified that 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.

So shares of foreign company deemed to be located in India if such shares derived its value from assets located in India. Capital gains applicable on transfer of such shares of foreign company.

✓ The shares of foreign entity derived its value **substantially from Indian assets** if on specified date (valuation date) :

- **FMV of Indian assets** held by foreign company is **more than 10 Crores**; and
- It represents **atleast 50%** of value of **all assets owned by foreign company**.

⊗ **Exception:** Income **shall not be deemed to accrue or arise** to a NR from transfer interest in an foreign entity if the transferor along with its associated enterprises does not hold, the right of management or control in foreign entity or voting power/share capital more than **5% of the total voting power/share capital** in the foreign entity **at any time during the 12 months preceding the date of transfer**.

Notes:

1. Valuation date: last day of accounting year (**last b/s date**) preceding the date of transfer. However, Book Value of assets on date of transfer is higher by **15% or more** of the book value of assets as on last day of last accounting year then valuation date shall be **date of transfer**.
2. FMV of assets: FMV of assets on valuation date **without reduction of liabilities**.
3. Accounting year: Each 12 months periods end on 31st March. If company follow any other period as accounting year (like cal. year) as per foreign country law then that period shall be accounting year.
4. Where **all the assets owned by the foreign entity are not located in India**, only so much of income as is **proportionate** to the assets located in India shall be deemed to accrue or arise in India.
5. Assets held by a **NR** directly or indirectly in **Category I foreign portfolio investor** shall not be deemed to be situated in India even if deriving its value substantially from assets located in India.

Example:

Orange Ltd a USA based company hold 100% shares Grapes Ltd, a Singapore based company acquired for ₹ 1000 crores. Grapes Ltd has a subsidiary in India i.e. Mango Ltd. Grapes Ltd also has subsidiaries in Sri Lanka, Taiwan and China. Grapes Ltd hold 90% shares of Mango Ltd. Orange Ltd. transferred its entire stake in Grapes Ltd to UK based company Kiwi Ltd. on 01/09/24 for ₹ 2100 crores.

(1) Financial year followed by each of the above companies

Company	Financial Year
Orange Ltd., USA	1 st July to 30 th June
Grapes Ltd, Singapore	1 st January to 31 st December
Mango Ltd, India	1 st April to 31 st March

(2) B/S of Grapes Ltd as on the date of transfer and as on previous accounting year end date:

Liabilities	31/12/23	01/09/24	Assets	31/12/23	01/09/24
	Amount in crores			Amount in crores	
Capital & reserves	2500	2000	Investment in Mango Ltd	1000	1000
			Investment in China, Sri Lanka and Taiwan	500	500
Liabilities	-	-	Other assets	1000	500
Total	2500	2000	Total	2500	2000

(3) B/S of Mango Ltd as on the date of transfer and as on previous accounting year end date:

Liabilities	31/03/24	01/09/24	Assets	31/03/24	01/09/24
	Amount in crores			Amount in crores	
Capital	500	800	Investments	300	300
Liabilities	500	400	Immovable property	200	200
			Other assets	500	700
Total	1000	1200	Total	1000	1200

(4) Fair Market Value of assets Income-tax Rules, 1962:

Date	Grapes Ltd	Mango Ltd
	Amount in crores	
31 st Dec 2022	5000	3000
31 st March 2023	5300	3300
1 st Sep 2023	6000	4000



1. Determination of Valuation Date

BV of assets of Grapes Ltd as on last B/S date i.e. on 31/12/23 = ₹ 2500 crores

BV of assets of Grapes Ltd as on the date of transfer i.e. on 31/09/24 = ₹ 2000 crores

Is there an increase in book value of asset by 15% = No. In fact, there is decrease in BV of asset

Valuation date = 31/12/2023

2. Determining whether 50% threshold is met on the Valuation date

FMV of all assets of Grapes Ltd as on valuation date = ₹ 5000 crores

FMV of Indian assets held by Grapes Ltd (3,000 Cr. X 90%) = ₹ 2700 crores

Percentage of India asset as compared to all assets of Grapes Ltd = 54%

Since, the value of Indian assets more than ₹ 10 crores; and represents 54% of the value of all assets owned by Grapes Ltd., the shares of Grapes Ltd. shall be deemed to derive its value substantially from the assets located in India.

3. In this case capital gain applicable in hands of orange Ltd. on transfer of shares of grapes Ltd.

Computation of Capital Gain ₹

Full Value of Consideration 2100 crores

Less: Cost of Acquisition 1000 crores

Capital Gain 1100 crores

Out of ₹ 1100 crores of capital gain only proportionate capital gain taxable in India. As per rule no.

11UC = ₹ 1100 × FMV of Indian assets held by foreign company

FMV of Total Assets of foreign Company

i.e. $1100 \times 2700 \text{ crores} / 5000 \text{ crores} = ₹ 594 \text{ crores}$ capital gain taxable in India.

➤ Sec 9(1)(ii): Salary Income for service rendered in India, whether such Income before or after service rendered like Gratuity, Pension, Profit in lieu of Salary.

➤ Sec 9(1)(iii): Salary received by Indian Citizen from Govt. for service rendered outside India.

✓ As per section 10(7) perquisite & allowances are **Exempt**.

➤ Sec 9(1)(iv): Dividend paid by Indian Company Outside India

➤ Section 9(1)(viii) : Deemed accrual of gift made to a person outside India

Gift of any money made by resident to:-

- NR or foreign company on or after 5th July 2019 or

- R but NOR on or after 1st April 2023,

shall be deemed to be accrued or arise in India.

➤ Sec 9(1)(v): If interest is payable by: -

- a. Government, or
- b. Resident person [Exception: where money borrowed and used, for the purposes of a business or profession carried on by him outside India or for the purposes of earning any income from any source outside India], or
- c. NR when money borrowed used for the purpose of business or profession carried in India by him,
 - then such interest is treated as deemed to be accrued or arise in India.

E.g.: If a NR 'Lobo' borrows money from a NR 'Hobo' and invests the same in shares of an Indian company, interest payable by 'Lobo' to 'Hobo' will not be deemed to accrue or arise in India.

Note: Interest payable by PE of NR engaged in Banking Business, to HO or any PE of such NR outside India, shall be deemed to accrue or arise in India.

HSBC Branch in India Interest → HCBC Bank Hongkong

Interest received by HCBC Hongkong from HCBC Branch in India Shall be deemed to be Accrue or arise in India.

➤ Sec 9(1)(vi): If royalty payable by: -

- a. Government, or
- b. Resident person [Exception : Where it is payable for the transfer of any right or the use of any property or information or for the utilization of services for the purposes of a business or profession carried on by such person outside India or for the purposes of earning any income from any source outside India]
- c. NR in respect of transfer of any right, use of any property or information or utilization of service for purpose of business or profession carried in India or earning any Income from any source in India
 - then such Royalty is treated as deemed to be accrued or arise in India.

Notes:

1. Lumpsum Royalty by resident to NR for supply of computer software along with computer hardware under the scheme of CG shall not be treated as deemed to be accrued or arise in India.
2. If transfer of property is already taxable "Capital gain" then it is not covered under "Royalty".
3. "Royalty" means consideration (including any lump sum consideration) for —
 - (i) Transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;
 - (ii) Imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;



- (iii) **Use of** any patent, invention, model, design, secret formula or process or trade mark or similar property;
- (iv) Imparting of any **information** concerning technical, industrial, commercial or scientific **knowledge, experience or skill**;
- (v) **Use** or right to use any **industrial, commercial or scientific equipment** but not including the amounts referred u/s 44BB;
- (vi) Transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting;
- (vii) Rendering of any services in connection with the activities referred in above clauses.

4. Consideration for use or right to **use of computer software is covered under Royalty.**

Notif. No. 21/2012: Exempted certain software payments from the applicability of TDS u/s 194J. Accordingly, where payment is made by the transferee for acquisition of software from a resident-transferor, the sec 194J **would not be attracted** if -

- ✓ the software is acquired in a subsequent transfer without any modification by the transferor;
- ✓ tax has been deducted either u/s 194J or 195 on payment in previous transfer of such software;
- ✓ the transferee obtains a declaration from the transferor that TDS has been so deducted along with the PAN of the transferor.

➤ Sec 9(1)(vii): If fees for technical service (FTS) payable by: -

- a. Government, or
- b. Resident person [Exception : Where the fees is payable in respect of technical services utilised in **a business or profession carried on by such person outside India or for the purpose of earning any income from any source outside India.**]
- c. NR in respect of Technical service **utilised** in business or profession carried on by such person **in India or such service utilise for earning any income from any source in Indian,**
 - then such FTS is treated as **deemed to be accrued or arise in India.**

FTS means: any consideration (including any lumpsum consideration) for the **rendering of any managerial, technical or consultancy services** (including providing the services of technical or other personnel). However, it does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head 'Salaries'.

Sec. 9A: Presence of Eligible Fund Manager in India not to constitute Business Connection

1. In case of an **Eligible investment fund**, the fund management activity carried out through an **eligible fund manager** acting on behalf of such fund shall **not constitute business connection** in India of that fund.
2. EIF shall not be treated as resident in India merely because manager undertaking fund management activities on its behalf is located in India.
3. EIF **means** a fund established or incorporated or registered outside India, which collects funds from its members for investing it for their benefit & fulfil the following conditions:
 - (a) Fund should **be NR**;
 - (b) Fund should be a resident of a country with **which India entered into DTAA**;
 - (c) Aggregate participation or investment in the fund, directly or indirectly, by resident persons should not **exceed 5% of the corpus of the fund**;

For the purposes of calculation of participation or investment, any contribution made by fund manager during the first 3 years of operation of the fund, **not exceeding ₹ 25 crore, shall not be taken into account.**

 - (d) Fund and its activities should be subject to applicable investor protection law in the country where it is established or incorporated or is a resident;
 - (e) Fund should have **minimum 25 members who are, directly or indirectly, not connected persons**;
 - (f) Any **member of the fund** along with connected persons **shall not** have any participation interest, directly or indirectly, in the **fund exceeding 10%**;
 - (g) Aggregate participation interest, directly or indirectly, **of ten or less members along with their connected persons in the fund, shall be less than 50%**;
 - (h) Investment by fund in any entity shall **not exceed 20% of the corpus** of the fund;
 - (i) No investment shall be made by the **fund in its associate entity**;
 - (j) **Monthly average of the corpus of the fund shall not be less than ₹ 100 crore.**

If fund has been established in the PY, the corpus of fund shall not be less than ₹ 100 crore at the end of a period of 12 months from the end of the month of its establishment, However, this condition shall not be applicable to a fund which has been wound up in the PY.

 - (k) Fund shall not carry on or control and manage, directly or indirectly, any business in India;
 - (l) Fund **should neither be engaged in any activity which constitutes a business connection in India nor should have any person acting on its behalf whose activities constitute a business connection in India** other than the activities undertaken by fund manager.
 - (m) Remuneration of fund manager in respect of fund management activity undertaken on its behalf **should not be less than** the amount calculated in such manner as may be prescribed.

Note: Conditions mentioned in point (e), (f) & (g) shall not apply in case of fund set up by Govt. or Central Bank of a foreign State or a sovereign fund or such other fund notified by CG (i.e., an

investment fund set up by a Category-I or Category-II Foreign Portfolio Investor registered under the SEBI (Foreign Portfolio Investors) Regulations, 2014, made under the SEBI Act, 1992.

4. **Eligible fund manager**, means any person who is engaged in the activity of fund management and fulfills the following conditions:
 - (a) Person should **not be an employee of the fund or a connected person** of the fund;
 - (b) Person should be **registered as a fund manager or investment advisor as per** regulations;
 - (c) Person should be **acting in the ordinary course of his business** as a fund manager;
 - (d) Person along with his connected persons **shall not be entitled, directly or indirectly, to more than 20% of the profits** accruing to fund from the transactions carried out by such fund manager.
5. Fund shall, in respect of its activities, furnish **within 90 days from the end of the FY**, a statement in the prescribed form. If fails to file then penalty of **₹ 5,00,000** may attract. **[Section 271FAB]**
6. This special taxation regime would not have any impact on taxability of any income of fund which would have been chargeable to tax irrespective of whether the activity of fund manager constituted business connection or not. Further, the said regime shall not have any effect on the scope of total income or determination of total income in the case of the eligible fund manager.

Meaning of certain terms:

- (i) **Associate**: An entity in which a director or a trustee or a partner or a member or a fund manager of the fund or a director or a trustee or a partner or a member of the fund manager of such fund, holds, either individually or collectively, share or interest, being more than 15% of its share capital or interest, as the case may be.
- (ii) **Corpus**: Amount of funds raised for the purpose of investment by fund as on a particular date.
- (iii) **"Connected Person"** same as Specified person as per sec. 40A(2).

Note: CG may, specify that any one or more of the conditions specified point (3) or (4) shall not apply or shall apply with such modifications, in case of fund and its fund manager, if such fund manager is located in an IFSC, and has commenced its operations on or before the 31st March, 2024.

CG Notification:

- (a) Eligible investment fund, the conditions specified in,—
 - (i) clause (e), (f) and (g) of point (3) shall not apply;
 - (ii) clause (k) shall be modified, namely:— (k) Fund shall not carry on, or participate in, the day to day operations of any person in India and for this purpose the monitoring mechanism to protect the investment in such person including the right to appoint directors or executive director shall not be considered as participation in day to day operations of such person in India.
- (b) Fund manager, the conditions of clause (b) of point (4) shall be modified, namely: — (b) the person is registered as a portfolio manager or an investment advisor in accordance with the IFSC Act.

Some Exempt Income

Section	Income	Eligible Assessee
10(4)(ii)	Interest on money standing to the credit in a Non-resident (External) account in India	Person resident outside India (under FEMA Act) or a person who has been permitted to maintain said a/c by RBI
10(4C)	Interest payable by Indian company or Business trust in respect of monies borrowed from outside India by way of Rupee Denominated Bond, as referred in Sec 194LC, during the period beginning from the 17/09/18 and ending on the 31/03/19	NR or Foreign Company
10(4D)	➤ Capital Gains on transfer of assets referred u/s 47(viiab) on a recognised stock exchange located in IFSC and consideration payable in foreign currency; ➤ Capital Gains on transfer of security (other than shares of company resident in India); ➤ Any income from security issued by NR (not being a PE of NR in India); ➤ Income from securitisation trust chargeable under PGBP.	Specified fund (Notes) Such income exempts to the extent it is attributable to units held by NR (not being the PE of a NR in India) or is attributable to the investment division of offshore banking unit.
10(23FBC)	Any Income by Unit holders from specified fund or on transfer of Units of specified fund.	Unit Holder of Specified Fund

Notes:

- "Specified fund" means
 - Fund established in India in the form of trust or company or a LLP,—
 - Which has been granted a certificate of Category-III Alternative Investment Fund or granted a certificate as retail scheme or exchange traded fund.
 - Which is located in any International Financial Services Centre (IFSC); and
 - of which all the units other than unit held by a sponsor or manager are held by NR; or

Note: Condition specified in (c) shall not apply where any unit holder, being NR during the PY when such units were issued, becomes resident u/s 6(1) or 6(1A) in any PY subsequent to that year, if the aggregate value and number of the units held by such resident unit holder or holders do not exceed 5% of the total units issued. Unit holder, who becomes a resident during any PY, shall cease to be a unit holder of such specified fund within a period of 3 months from the end of the PY in which he becomes a resident.
 - Investment division of an OBU, which has been granted a certificate of registration as a Category-I foreign portfolio investor under the SEBI (FPI) Regulations, 2019.

2. "Investment division of offshore banking unit (OBU)" means an investment division of a banking unit of a NR located in an IFSC, as referred in sec 80LA(1A) and which has commenced its operations on or before the 31st March, 2024.

10(4E)	Any income accrued as a result of— (i) transfer of non-deliverable forward contracts or offshore derivative instruments or over-the-counter derivatives; or (ii) distribution of income on offshore derivative instruments, entered into with OBU of IFSC.	Non Resident
(i) "A non-deliverable forward contract" shall mean a contract for the difference between an exchange rate agreed before and the actual spot rate at maturity, with the spot rate being taken as the domestic rate or a market determined rate and such contract being settled with a single payment in a foreign currency. (ii) Offshore derivative instrument shall have same meaning as assigned to it in SEBI Foreign Portfolio Investor Reg. (iii) over-the-counter derivatives" shall mean a derivative contract that is not traded on an exchange but instead is privately negotiated between a purchaser and a seller.		
10(4F)	Royalty or interest , on account of lease of an aircraft or ship in a PY, paid by a unit of an IFSC, if the unit has commenced its operations on or before the 31 st March, 2024. "aircraft" means an aircraft or a helicopter, or an engine of an aircraft or a helicopter, or any part thereof of ship" means a ship or an ocean vessel, engine of a ship or ocean vessel, or any part thereof	Non-Resident
10(4G)	Any income received from,— (i) Portfolio of securities or financial products or funds, managed or administered by any portfolio manager on behalf of such NR; or (ii) Such activity carried out by such person, as may be notified by CG, in an account maintained with OBU in IFSC, to the extent such income accrues or arises outside India and not deemed to accrue or arise in India.	Non-Resident
10(4H)	Capital gains arising from transfer of equity shares of domestic company (Unit of an IFSC), engaged primarily in the business of lease of an aircraft which has commenced operations upto 31/03/26. Provided that this clause shall apply for CG from transfer of equity shares of such domestic company in a PY relevant to AY falling within the— (a) period of 10 AY's beginning with AY relevant to the PY in which the domestic company has commenced operations; or (b) period of 10 AY's beginning with AY commencing on 01/04/24, where the period referred to in clause (a) ends before 01/04/34. E.g. - If dom. company commences operation on 06/06/22, the first 10 AY's will be 23-24 to 32-33 (in other words, this period ends before 01/04/34). Therefore, CG exemption will be available if CG arises during 10 AY's beginning with the AY 24-25. Conversely, if the aforesaid dom. Co. commences operations on 01/01/25, 10 AY's [for exemption u/s 10(4H)] will be 25-26 to 34-35.	Non-Resident or Unit of IFSC Engaged in the business of leasing of an Aircraft
10(34B)	Dividend from a company being unit of IFSC primarily engaged in the business of leasing of Aircraft.	Unit of IFSC Engaged in the business of leasing of an Aircraft

10(15)(ix)	Interest payable by a unit located in an IFSC in respect of monies borrowed by it on or after the 01/09/ 2019	Non-Resident
10(15B)	Any income from lease rentals of cruise ships received from a foreign company which operates cruise ship in India [pay tax as per section 44BBC]	Foreign Company
10(6)(ii)	Remuneration received by Foreign Diplomats/ Consulate and their staff Conditions: (a) The remuneration received by our corresponding Govt. official's resident in such foreign countries should be exempt. (b) The above-mentioned officers should be the subjects of the respective countries and should not be engaged in any other business or profession or employment in India.	Individual (not being a citizen of India)
10(6)(vi)	Remuneration received as employee of a foreign enterprise for services rendered by him during his stay in India, if: a) Foreign enterprise is not engaged in any trade or business in India; b) His stay in India does not exceed period of 90 days in such PY; and c) Such remuneration is not liable to deducted from the income of employer chargeable under this Act	Individual - Salaried Employee (not being a citizen of India)
10(6)(viii)	Salary received by or due for services rendered in connection with his employment on a foreign ship if his total stay in India does not exceed 90 days in the PY.	Individual (NR who is not a citizen of India)

10(48)	Income received in India in Indian currency on account of sale of Crude oil. Foreign company and agreement should be notified by the CG in national interest.	Foreign company on account of sale of crude oil. It should not be engaged in any other activity in India.
10(48A)	Income accruing or arising on account of storage of crude oil in a facility in India and sale of crude oil therefrom to any person resident in India. Foreign company and agreement should be notified by the CG in national interest.	Foreign company on account of storage of crude oil in a facility in India and sale of crude oil there from.
10(48B)	Income from sale of leftover stock of crude oil from facility in India after the expiry or termination of agreement referred u/s 10(48A).	Foreign company from sale of leftover stock of crude oil from the facility in India.
10(48C)	Income from arrangement for replenishment of crude oil stored in its storage facility in pursuance of directions of the CG in this behalf. Provided that this clause shall not apply to an arrangement, if the crude oil is not replenished in the storage facility within 3 years from the end of the FY in which the crude oil was removed from storage facility for the first time.	Indian Strategic Petroleum Reserves Limited, being a wholly owned subsidiary of the Oil Industry Development Board under the Ministry of Petroleum and Natural Gas.

- Sec 10(23FE): Exemption of Income of specified person from Investment in India
- ☞ Incomes: dividend, interest, any sum referred u/s 56(2)(xii) or LTCG from an investment made in India, in the form of debt/share capital/unit, if the investment—
- (i) is made between 1st April, 2020 to 31st March, 2024 &
- (ii) is held for at least three years.



☛ Eligible Investments

- (a) Business Trust (Invit); or
- (b) Entity carrying on the business of developing, or operating and maintaining, or developing, operating and maintaining any **infrastructure facility**; or
- (c) Category-I & II AIF regulated under the SEBI (AIF) Regulations, 2012, having minimum 50% investment in one or more of the entities referred to in item (b) or item (d) or item (e) or in an Business Trust (only Invit); or
- (d) Domestic company, set up and registered on or after the 1st April, 2021, having minimum 75% investments in one or more of the entities referred to in item (b); or
- (e) NBFC registered as an Infrastructure Finance Company as per RBI notification or in an Infrastructure Debt Fund, a NBFC, as referred to in the Infrastructure Debt Fund - NBFC (Reserve Bank) Directions, 2011, issued by the RBI, having minimum 90% lending to one or more of the entities referred to in item (b).

☛ **Taxability on failure to satisfy the conditions:** Where any income has not been included in the total income of the specified person due to the aforesaid provisions, and subsequently during any PY the assessee fails to satisfy any of the conditions, such income shall be chargeable to income-tax as the income of the person of that PY.

☛ Meaning of specified Person

- Wholly owned subsidiary of the Abu Dhabi Investment Authority
 - (i) It should be a resident of the United Arab Emirates, &
 - (ii) It makes investment, directly or indirectly, out of the fund owned by the Govt. of the Abu Dhabi.
 - Sovereign wealth fund (SWF)
 - (i) It should be wholly owned and **controlled**, by the **foreign Govt.**
 - (ii) It should be set up and **regulated under foreign country law.**
 - (iii) **Earnings** of the fund are credited either to the account of the Foreign Govt. or to any other account designated by that Govt. so that **no portion of the earnings inures any benefit to any private person.**
 - (iv) Asset of the said fund vests in the Foreign Govt. upon dissolution.
 - (v) It does participate in the day-to-day operations of investee but the monitoring mechanism to protect the investment with the investee including the right to appoint directors or executive director shall not be considered as participation in the day-to-day operations of the investee.
 - (vi) It is specified by the CG, by notification, for this purpose and fulfils prescribed conditions.
- Note:** provisions of (iii) and (iv) shall not apply to any payment made to creditors or depositors for loan taken or borrowing for the purposes other than for making investment in India.
- Pension fund
 - (i) It should be created or established under the law of a foreign country



(ii) It should not be liable to tax in such foreign country or if liable to tax, exemption from taxation for all its income has been provided by such foreign country

(iii) It does not participate in the day-to-day operations of investee but the monitoring mechanism to protect the investment with the investee including the right to appoint directors or executive director shall not be considered as participation in day-to-day operations of the investee

(iv) Specified by the CG, by notification, for this purpose and fulfils conditions specified in such notification.

Notes: loan and borrowing" means —

- (a) Loan taken or borrowing by SWF from, or any deposit or investment made in SWF by, any person other than the Govt. of the country in which the SWF is set up;
- (b) Loan taken or borrowing by pension fund from or any deposit or investment made in a pension fund by, any person but shall not include the deposit or investment which represents statutory obligations and defined contributions of one or more funds or plans established for providing retirement, social security, employment, disability, death benefits or any similar compensation to the participants or beneficiaries of such funds or plans, as the case may be.

➤ **Sec. 10(23FF): Exemption of Capital Gain for NR or Specified Fund**

Capital gains arising or received by a **NR** or **specified fund**, on transfer of share of a company resident in India, by the resultant fund or a specified fund to the extent attributable to units held by NR (not being a PE of a NR in India), and such shares were transferred from **original fund**, or from its wholly owned special purpose vehicle, to the **resultant fund in relocation**, and where capital gains on such shares were not chargeable to tax if that relocation had not taken place.

✓ **Exemption for relocation of an offshore fund to IFSC [Section 47(viiac)/(viiad)]**

47(viiac): Transfer, in a relocation, of a capital asset by the original fund to the resulting fund.

47(viiad): Transfer by a shareholder or unit holder or interest holder, in a relocation, of a capital asset being a share or unit or interest held by him in the original fund in consideration for the share or unit or interest in the resultant fund.

☞ **"Original fund" means—**

- (A) Fund established outside India, which collects funds from its members for investing it for their benefit and fulfils the following conditions, namely:—
 - (i) Fund is not a person resident in India;
 - (ii) Fund is resident of a country with which DTAA entered or is established in notified country;
 - (iii) Fund and its activities are subject to applicable investor protection regulations; and

(iv) fulfils such other conditions as may be prescribed.

(B) Investment vehicle, in which Abu Dhabi Investment Authority is the direct or indirect sole shareholder or unit holder or beneficiary or interest holder and such investment vehicle is wholly owned and controlled, directly or indirectly, by the Abu Dhabi Investment Authority or the Government of Abu Dhabi; or

(C) Fund notified by the CG & fulfils such other conditions.

Condition:

The original fund, in a case where a capital asset is transferred to a resultant fund being a Category III AIF, shall fulfil the condition that the aggregate participation or investment in the original fund, directly or indirectly, by persons resident in India shall not exceed 5% of the corpus of such fund at the time of such transfer.

☞ "Relocation" means transfer of assets of the original fund, or of its wholly owned SPV, to a resultant fund upto 31st March, 2025, where consideration for such transfer is discharged in the form of share or unit or interest in the resulting fund to,—

(i) shareholder or unit holder or interest holder of the original fund, in the same proportion in which the share or unit or interest was held by such shareholder or unit holder or interest holder in such original fund, in lieu of their shares or units or interests in the original fund; or

(ii) Original fund, in the same proportion as referred to in (i), in respect of which the share or unit or interest is not issued by resultant fund to its shareholder or unit holder or interest holder;

☞ "Resultant fund" means a fund established or incorporated in India in the form of a trust or a company or a limited liability partnership, which—

(i) has been granted a certificate of registration as a Category I or II or III AIF, and is regulated under the SEBI (AIF) Regulations, 2012 or IFSC Authority Act, 2019; and

(ii) is located in any IFSC.

✓ **Sec 49 Cost of Acquisition**

(i) the COA of a capital asset for the resulting fund would be the COA of the original fund.

(ii) the COA of a share or unit or interest in resulting fund would be the COA of the share or unit or interest in the original fund.

Taxation of NRI (Chapter XII-A)

➤ Sec. 115C: Meaning of Certain Terms

a) NRI means **NR + Indian citizen/Person of Indian origin.**

"Person of Indian Origin means if he, or either of his parents or any of his grandparents, was born in undivided India"

b) "Foreign Exchange Assets" means

Any of the following assets **acquired/purchased in foreign exchange (FOREX); -**

- ✓ Shares of Indian company (Public/ Private)
- ✓ Debenture of Indian public company
- ✓ Deposits with an Indian Public company
- ✓ Securities of Central Govt
- ✓ Any other asset as may be notified by CG

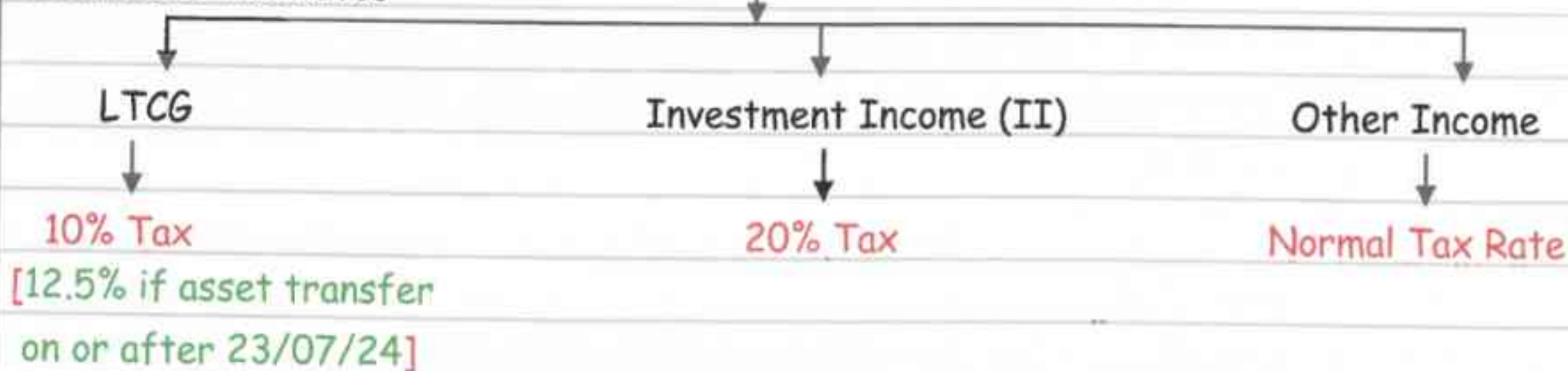
c) LTCG = LTCG from foreign exchange assets.

Investment Income (II) = Any income derived from foreign exchange assets.

➤ Sec. 115D: Method of computation

- ☞ Investment Income: Sec 28 to 44C, Sec 57 & chapter VI-A are **not available.**
- ☞ LTCG: Chapter VI-A **not available.**
- ☞ First proviso to Sec 48: **Available.**
- ☞ Second Proviso to Sec 48(Indexation): **Not available.**
- ☞ Other incomes = **Normal Provisions.**

➤ Sec. 115E: Tax Rates



➤ Sec. 115F: Exemption on LTCG

LTCG on FOREX asset shall **be exempt** if net consideration is utilized for acquiring other FOREX assets or Saving Certificate u/s 10(4B) within **6 Months** from the date of transfer.

Exempt amount:
$$\frac{\text{LTCG} \times \text{Cost of New Asset}}{\text{Net Consideration}}$$

Note: New asset should not be transferred or converted into money within 3 years from the date of acquisition, if it is transferred then exempted LTCG earlier shall now be taxable as LTCG in the year in which new asset transferred or converted into money.



➤ **Sec. 115G: Exemption from the Filing of Return of Income**

ROI **not required** to be filed if :

- Total Income include only investment income & LTCG.
- TDS already deducted.

➤ **Sec. 115H: Above provision apply even if NRI becomes Resident**

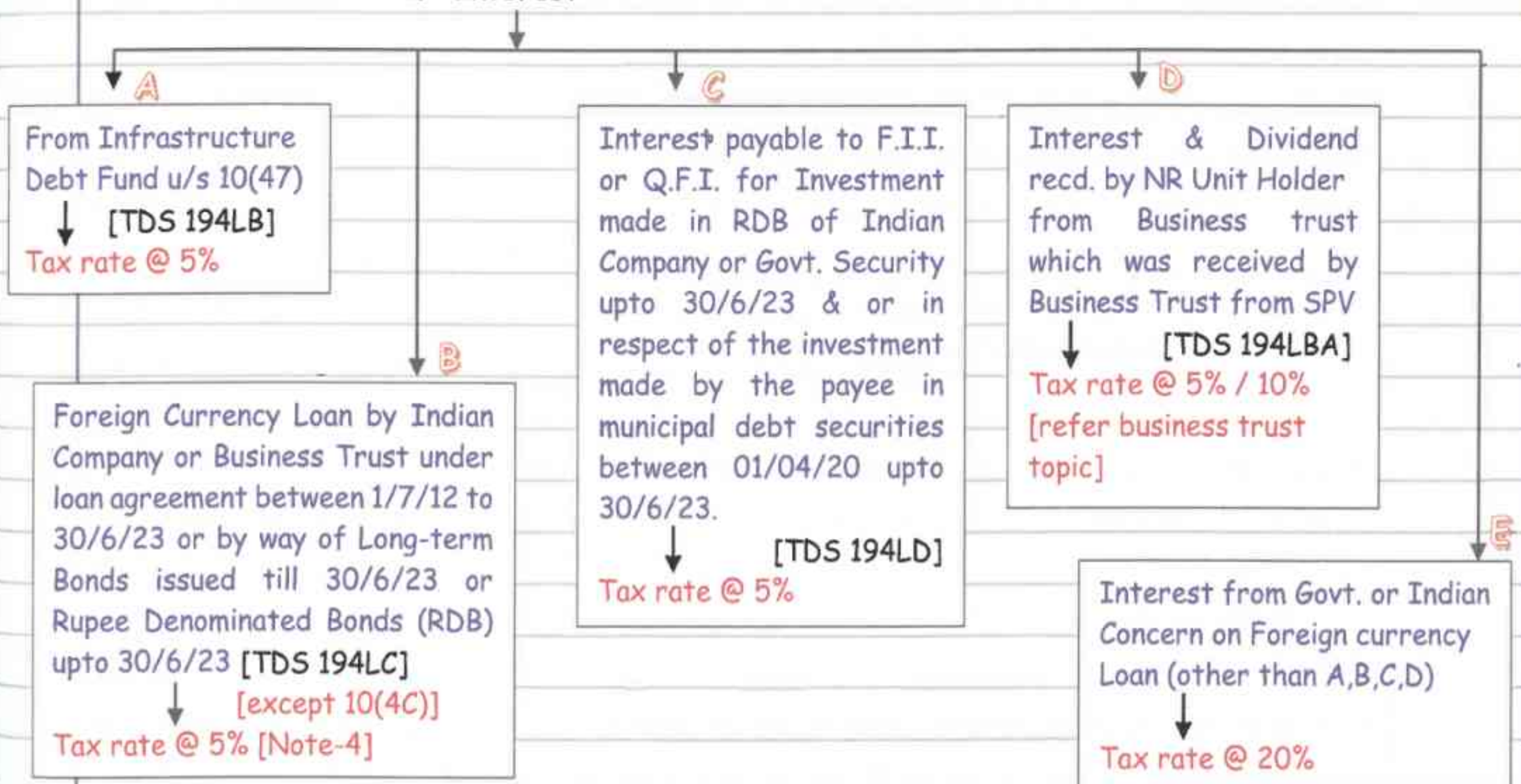
NRI becomes Resident, can file declaration with ROI of AY in which he becomes Resident that he wants to be governed by provision of this chapter. It means **investment income** continue to be taxed @ 20%. This chapter will apply till transfer or converted into money of such forex assets.

➤ **Sec. 115-I: The above provisions are optional** means assessee can pay Normal tax on LTCG & investment income instead of 10% & 20%.

Special Rates of Tax for NR

➤ **Sec 115A: Interest, Royalty, Fees for Technical Service received by NR/Foreign Company**

1. Interest

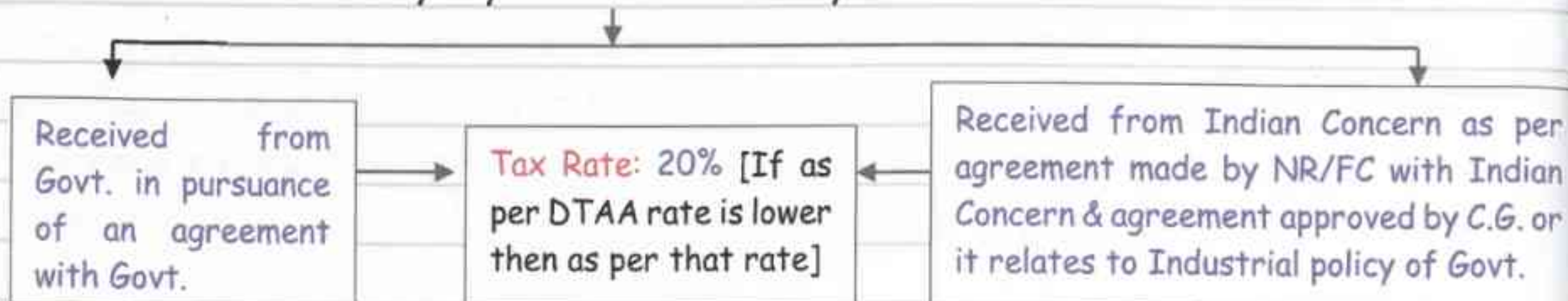


Notes:

- Dividend received by NR/FC: **20% Taxable**. [10% if dividend recd. from IFSC Unit]
- Income received from UTI/MF: **20% taxable**.
- F.I.I./Q.F.I.: Foreign Institutional Investor or Qualified Foreign Investor.
- Tax & TDS rate shall be 4% instead of 5% in respect of monies borrowed by it from a source

Outside India by way of issue of any long-term bond or RDB on or after the 01/04/20 upto 30/06/23, which is listed only on a recognised stock exchange located in any IFSC and 9% rate if bond or RDB issued on or after 01/07/23.

2. Royalty & FTS received by NR/FC



- Notes :
1. Royalty/FTS received by NR/FC having PE in India shall be taxable at normal tax rate (refer sec 44DA in PGBP) and **not having PE** in India then taxable at **20% as per section 115A**.
 2. It shall **not be necessary** for the assessee to furnish a **return of income** if the following conditions are satisfied:

- (a) Total income consists of the **Interest or Dividend or Royalty & FTS** income referred above
- (b) TDS has been deducted from such income.

- **Sec 115AB : Income & LTCG to "Overseas financial Organization"** on units of UTI/MF acquired in foreign currency - **10% Taxable**. [Tax on LTCG @ 12.5% if asset transfer on or after 23/07/24]

"Overseas Financial Organisation" means any fund, institution, association or body, established under the foreign laws, which has entered into an arrangement for investment in India with any public sector bank or PFI or mutual fund. Such arrangement should be approved by the SEBI.

- **Sec 115AC: LTCG & Interest / Dividend from Bonds & GDR**

Income received by **Non-Residents** on **Bonds of Indian co, or GDR** acquired in foreign currency.

LTCG : **10% Tax** [Tax on LTCG @ 12.5% if asset transfer on or after 23/07/24]

Interest/Dividend : **10% Tax**

Notes:

1. Where the assessee acquired GDR or bonds in an amalgamated or resulting company by virtue of his holding GDR or bonds in the amalgamating or demerged company, the concessional tax treatment would apply to such GDR or bonds.
2. It shall not be necessary for the assessee to furnish a return of income if:-
 - (a) The Total income consists of only the **interest or dividend** income referred above
 - (b) TDS has been deducted from such income.



➤ **Sec 115ACA: Tax on income/CG from GDRs purchased in foreign currency**

Income received by **resident employees** of an Indian company or its subsidiary engaged in specified industry & GDR issued as per ESOP'S

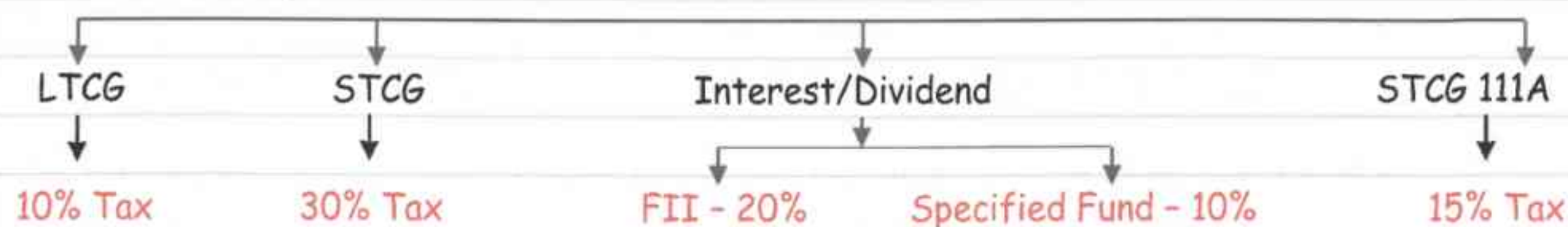
LTCG : 10% Tax [Tax on LTCG @ 12.5% if asset transfer on or after 23/07/24]
Dividend : 10% Tax

Notes:

1. Specified industry means IT software/service, entertainment service, pharmaceutical industry, biotechnology industry & any other may be notified.
2. "GDR" means any instrument in the form of a depository receipt or certificate created by the Overseas Depository Bank outside India or in an IFSC and issued to investors against the issue of,—
(i) Ordinary shares of company listed on a RSE 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 IFSC.
3. This section is applicable to Resident person. We have included in this topic is only to maintain sequencing of sections.

➤ **Sec 115AD: Capital Gain & Interest/dividend on Security of FII /Specified fund**

Income received by **Foreign Institutional Investors (FII) or specified fund** on securities (other than units of UTI/MF).



[@12.5% if asset transfer on or after 23/07/24]

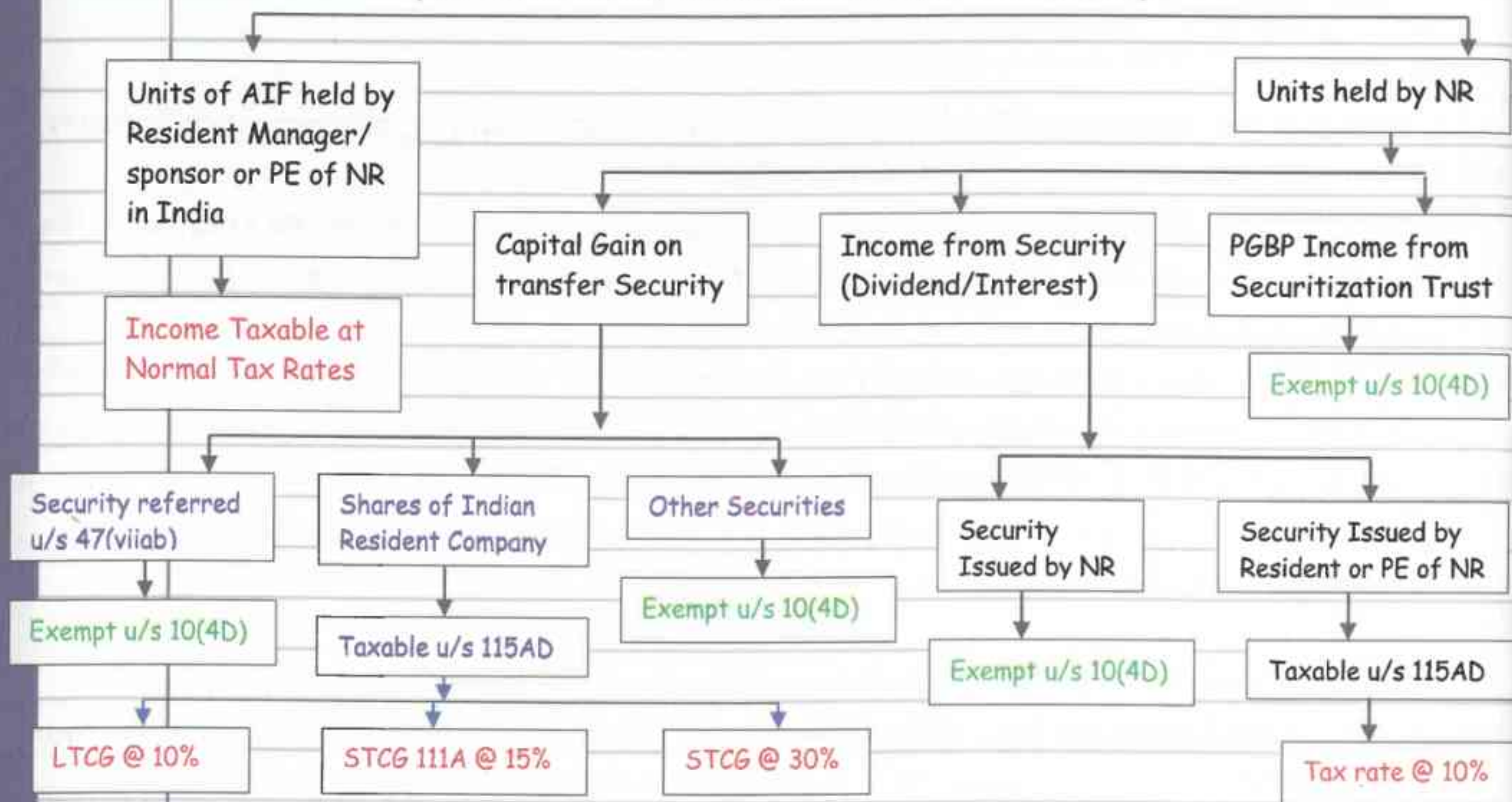
[@20% if asset transfer on or after 23/07/24]

Notes:

1. In case of LTCG u/s 112A, income tax @10%/12.5% on income exceeding ₹ 1.25 lakh.
2. Higher Surcharge @ 25% and 37% not applicable in case of above dividend & Capital Gain (STCG & LTCG). It means maximum surcharge rate on dividend & above capital gain is 15% in case of AOP/BOI.
3. In case of specified fund, the provision of this section shall apply only to the extent of income that is attributable to units held by NR (not being a PE of a NR in India).
4. Specified Fund means same as assign in sec. 10(4D).
5. In case of specified fund is investment division of an OBU, the provisions of this section shall apply only to the extent of income that is attributable to the investment division of such OBU.

Taxability of Specified Fund

(AIF-III in IFSC or Investment division of OBU in IFSC)



Rule 21AI/ 21AJ: Calculation of Proportionate shares of NR for the purpose of Sec 10(4D) and 115AD

1. Capital Gain

Capital Gain x $\frac{\text{Aggregate of Daily "AUM" held by NR unit holders from the date of acquisition till the date of transfer of capital assets}}{\text{Aggregate of Daily "AUM" of Specified Fund from the date of acquisition till the date of transfer of capital assets}}$

2. Income from security (Dividend/Interest) / PGBP from securitization Trust

Income x $\frac{\text{"AUM" held by NR unit holders as on the date of receipt of Income}}{\text{"AUM" of Specified Fund as on the date of receipt of Income}}$

> Sec. 115BBA: Income of NR Sports Person, Sports Association & Entertainer

Income received by Non-Resident sports man, NR Sports Association, NR Entertainer - Tax Rate @ 20%

(a) A sportsman (including an athlete), who is not a citizen of India and is a NR

Any income received or receivable by way of—

- ✓ Participation in any game or sports in India (other than casual income like card game etc.); or
- ✓ Advertisement; or



- ✓ Contribution of articles relating to any game or sport in India in newspapers, magazines or journals;
- (b) A non-resident sports association or institution: Guaranteed amount to be payable to such institution in relation to any game or sport played in India.
- (c) An entertainer who is not a citizen of India and is a NR: Any from his performance in India.

The assessee is not required to file return of his income if—

- (a) His total income consisted only of income referred to in (a) or (b) or (c) above; and
- (b) TDS has been deducted from such income.

Note: Calcutta High Court held that although the payments made to NR umpires and the match referees are "income" which has accrued in India, the same are **not taxable** u/s 115BBA and thus, the assessee is not liable to deduct TDS u/s 194E. It may be noted that since income has accrued to NR umpires and match referees, the TDS u/s 195 would be attracted and tax would be deductible at the rates in force.

Notes for all above sections (115A to 115BBA):

1. Deduction u/s 28 to 44C or Sec 57 **not allowed** against above income.
2. Deduction under chapter VI-A (except 80LA) **not available** (except Royalty & FTS u/s 115A).
3. Indexation benefits & First Proviso to sec 48 **not available** on capital gain taxable as per above rates.
4. Above provisions are **mandatory**.
5. Basic Exemption Benefit **NOT Available** against above income.
6. Deduction u/c VI-A available against Royalty and FTS referred in section 115A.

➤ **Sec. 285A: Furnishing of Information or documents by Indian Concern**

Where shares of **foreign entity** derives its value substantially from assets located in India & such entity holds such assets in India in Indian concern then the Indian concern shall within **90 days** from end of **the FY in which transfer of shares of foreign entity** took place furnish **Form 49D** to the prescribed income tax authority providing information necessary for determination of income accruing or arising in India as per Sec 9(1)(i).

⊗ **Failure to furnish the same will attract penalty u/s 271GA of:**

- ☞ **2% of value of transaction**, if such transaction had the effect of transferring right of management control of Indian concern;
- ☞ **₹5,00,000** in any other case.

- **Sec 115JG: Conversion of Indian Branch of Foreign Company into Subsidiary Indian Company**
Where a foreign Company (foreign bank) engaged in the business of banking converts its Indian branch into Subsidiary company, capital gains on conversion would not be taxable if:
1. Indian branch amalgamates with Indian subsidiary as per the scheme of **amalgamation approved** by shareholders of the foreign company and the Indian subsidiary and **sanctioned by the RBI**.
 2. All assets and Liabilities of branch transfer to Indian subsidiary company.
 3. Assets and liabilities are transferred at **book values**.
- Note** - Any Revaluation would not be considered while determining the value of the assets
4. Foreign bank & nominees should holds **100% of share** capital of Indian subsidiary **till the end of the year of conversion** & at least **51% of the voting power** of Indian subsidiary for a period of **next 5 PY's**.
 5. Foreign company does not receive any consideration or benefit other than by **way of allotment** of shares in the Indian subsidiary.
- ❖ Provisions relating to Unab. depreciation, set off or c/f of losses, MAT Credit and the computation of income in case of foreign company and Indian subsidiary shall apply with Following modifications, exceptions and adaptation.

Provisions	Modification/exception/adaptation
Current year depreciation	In the year of amalgamation, Depreciation between Indian Branch and Indian subsidiary shall be apportioned based No. of days asset was use by each of them.
Set-off and carry forward of losses	Accumulated PGBP losses (Other than speculative loss) and unabsorbed of Indian Branch will be treated as losses and dep of subsidiary company for the year in which conversion took place. Note: Losses can be carried forward for fresh 8 years.
WDV of assets	Cost of block of assets of Indian subsidiary in the year of conversion shall be WDV of Indian Branch as per Income Tax Act on the date of conversion.
COA of capital assets	COA of assets acquired by Indian subsidiary in amalgamation = COA of Indian Branch.
POH of capital assets	POH of assets acquired by Indian subsidiary in amalgamation shall include POH of Indian Branch
MAT credit	MAT credit of Indian Branch can be carried forward and set-off by Indian subsidiary for a fresh period of 15 years.
VRS Expenditure amortisation	VRS allowed to Indian subsidiary for remaining period as per Sec 35DDA.
Provision for Bad and doubtful debts	Credit balance of Provision of bad and doubtful debts in books of Indian Branch as per Sec 36(1)(viii) will be deemed to be credit balance of Indian subsidiary.
Non-applicability of Sec 56(2)(x)	Sec 56(2)(x) shall not apply on the receipt shares by foreign bank from Indian subsidiary on conversion.

Note : Where any benefit/exemption/relief has been granted and thereafter there is failure to comply with any the conditions specified in scheme or notification then AO is empowered to recompute the total income of the assessee for by way of rectification u/s 154. The period of 4 years for rectification shall be considered from the end of the PY in which conditions violated.

**Godaddy.Com LLC (2023) (Delhi)**

Whether the fees received by a foreign company as consideration towards providing domain name registration services amounts to 'royalty' under section 9(1)(vi)?

The assessee is based in USA and does not have a PE or fixed place of business in India. It is an accredited registrar for the Internet Corporation for Assigned Names and Numbers (ICANN). The assessee provides services such as domain name registration, website design, and web hosting and charges a fee from its customers. Fees for facilitating domain name registration is shared in three ways. Part of the fee received from the customers is kept by the assessee whereas the remaining portion is shared with ICANN and the registry.

As per Explanation 2 to section 9(1)(vi), "royalty" 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") inter alia for the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trademark or similar property.

The Delhi High Court observed that assessee is not the owner of the domain name and hence it does not confer right to use or transfer the right to use of the domain name to its customers. A perusal of the clauses of the agreement show that what is agreed between the assessee and its customers is mere registration of a domain name, which does not create any proprietorship rights in the name used as the domain name or in the domain name registration either in the assessee or the customers or even any other third party. The assessee foreign company is not the owner of the domain name but merely facilitates the registration of domain name with registrar and charges a fees.

Accordingly, the High Court held that the fee received by the assessee for registration of domain names to its customers, cannot be treated as royalty.



Notes



- Double taxation means the same income **getting taxed twice** in hands of same assessee. Any country taxes income on basis of two rules i.e. **Residence Rule & Source Rule**. Double taxation is possible when assessee is Resident of one country & derives income from another country.

Suppose Mr. BB is Resident of India & deriving income from UK, then India will tax such income on the basis Resident rule and UK will tax such income on the basis of source rule.

- There are two type of Double taxation relief

Unilateral Relief

⊗ No DTAA
Sec. 91

Bilateral Relief

DTAA
Sec 90 & 90A

[Tax exemption method &
tax credit method]

Under Tax Exemption method, income is taxed in only **source country** and exempted in the residence country. Under Tax Credit Method Income is taxable in both countries in accordance with their respective tax laws read with double taxation avoidance agreement. The country of residence of the tax payer, however, allows him credit for the tax charged thereon in the country of source. India follows **credit method in majority** of its DTAA's.

Sec. 90: Agreement with Foreign countries (DTAA)

Central Govt, may enter into agreement with Govt of **foreign country** or **specified territory outside India**.

(a) For **granting relief for Doubly taxed income**, without creating opportunities for nontaxation 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).

(b) **Exchange of information** with each other for prevention of tax evasion transaction, investigation of such cases & **co-operation** with each other for **recovery of taxes**.

Notes:

1. **Provision of DTAA or Income Tax Act** whichever is **more beneficial** to the assessee shall apply [sec 90(2)]. However, provision of GAAR shall apply even if such provisions are not beneficial to assessee.
2. 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.
3. NR to whom DTAA applies, shall not be entitled to claim any relief under DTAA unless **TRC (Tax Residence Certificate)** of his being resident in any Foreign country is obtained by him from foreign Govt. [Sec 90(4)]



TRC produced by a resident of a contracting state will be accepted as evidence that he is a resident of that contracting state and IT Authorities in India will not go behind the TRC and question his residential status.

In addition to TRC the assessee would be required to provide such other documents & information as may be prescribed for claiming the treaty benefit:

- Status of assessee
- PAN of assessee (if allotted)
- Nationality (In case of Individual)
- Country or Specified territory for Incorporation or registration (In case of others)
- Assessee's Tax identification number in the country or specified territory of residence & in case there is no such number the unique number on the basis of which the person is identified by the Govt. or specified territory of which the assessee claim to be resident
- Period for which the residential status, as mentioned in the certificate
- Address of the assessee in the country or specified territory outside India.

However, the assessee may not be required to provide the information or any part thereof, if the information or the part thereof, as the case may be, is already contained in the TRC.

➤ As per Sec 90A "Specified Association" of India can enter into an agreement with "Specified Association" of foreign country. CG may adopt or implement such agreement. "Specified Association" means association functioning under any law (e.g. RBI).

➤ Meaning of Term Used in DTAA

- a. Term used in DTAA define in DTAA itself: It shall have meaning assigned in DTAA itself
- b. Term used in DTAA define in the Act: It shall have meaning assigned in the Act.
- c. Term used in DTAA & not defined in DTAA or the Act but assign a meaning on the notification issued by CG in Official Gazette, which is still in force. Term shall have meaning in the notification & shall have deemed to have effect from the date on which DTAA come into force.

Sec. 91: Double taxation relief if there is NO DTAA

- a. Assessee is Resident in India.
- b. Income derived from Foreign Country & income not deemed to be accrued or arise in India.
- c. Tax should have been deducted or paid in foreign country.
- d. There should be NO DTAA.



Amount of Relief

Step 1 : Compute **NTI** (Indian + foreign income)

2 : Find out **Gross Tax** (before claiming TDS/TCS, MAT/AMT credit, SA Tax, Advance tax but after adding surcharge & HEC)

3 : Find out "**Average rate of Tax**" on NTI

$$\text{ART} = \frac{(\text{Gross Tax} \times 100)}{\text{NTI}}$$

4 : Find out **Rate** at which tax paid/deducted in foreign country

5 : Find out **lower rate** from step 3 & 4

6 : Relief us $91 = \text{foreign income} \times \text{Rate in Step 5}$.

Note: How to calculate Foreign Tax Rate?

$$\frac{\text{Tax in foreign Country} \times 100}{\text{Income in foreign country as per their Tax Law}}$$

➤ Concept of Permanent Establishment (PE)

Permanent establishment means a fixed place of business through which the business of an enterprises is wholly or partly carried on. Every DTAA has a specific clause, which will deal with an explanation of permanent establishment for the purpose of such DTAA. **Business Income of a non-resident will not be taxed in India, unless such Non-resident has a permanent establishment in India.**

PE includes:

- (i) A place of management
- (ii) A branch
- (iii) An office
- (iv) A factory
- (v) A workshop
- (vi) A sales outlet
- (vii) A warehouse
- (viii) A mine, an oil or gas well, a quarry, or any other place of extraction of natural resources (not exploration)

As per DTAA business income of NR is taxable in India only if such NR has PE in India but as per Income Tax Act Business income of NR taxable in India if NR having Business Connection (Sec 9) in India.

➤ Taxation of Business Process Outsourcing (BPO) Units in India [CBDT Circular No.5/2004]

- (a) A NR 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 PE of NR entity, and the resident entity would have to be assessed to income tax as a separate entity.



- In such a case, the NR entity will not be liable under the IT Act, 1961.
- (b) However, it is possible that the NR entity may have a business connection with the resident Indian entity. In such a case, the resident Indian entity could be treated as the PE of the NR entity.
 - (c) NR entity or the foreign company will be liable to tax in India only if the IT enabled BPO unit in India constitutes its PE.
 - (d) NR or a foreign company is treated as having a PE in India if the said NR 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 NR principal. In such a case, the profits of the NR or foreign company attributable to the business activities carried out in India by the PE becomes taxable in India.
 - (e) If BPO units becomes PE in India then profit attributed to such PE shall be Taxable in India. Profit of PE shall be computed as if it were a distinct and separate entity. Transactions between PE and HO shall be computed on the basis of arm's length price.



Advance ruling means a decision taken in advance. If application is made to "The Board for Advance Ruling (BOAR)" then BOAR will give its ruling (Judgment) in relation to a transaction which has been already undertaken or is proposed to be undertaken by Assessee & such judgment may be related to any question of law/fact.

Sec 245N: Application to BOAR & Advance Ruling

S.No.	Applicant u/s 245N(b)	Advance Ruling u/s 245N(a) means determination by the BOAR in relation to
(i)	NR	A transaction which has been undertaken (u/t) or is proposed to be u/t by him.
(ii)	Resident	The tax liability of a NR arising out of a transaction which has been u/t or is proposed to be u/t by him with such NR and such determination shall include determination of any question of law or of fact specified in the application.
(iii)	Resident of class or category of persons notified by CG	The tax liability of a resident applicant, arising out of a transaction which has been u/t or is proposed to be u/t by such applicant and such determination shall include determination of any question of law or of fact specified in the application.
Note: CG has notified a resident, in relation to his tax liability arising out of one or more determinations valuing $\geq$ ₹ 100 crore in total.		
(iv)	Resident of class or category of persons notified by CG	An issue relating to computation of TI which is pending before any IT Authority or the ITAT and such determination or decision shall include determination or decision of any question of law or fact w.r.t. such computation of TI specified in the application.
Note: A Public sector undertaking has been notified by the CG		
(v)	Resident or NR	Whether an arrangement, which is proposed to be u/t by such applicant, is an impermissible avoidance arrangement (IAA) as referred to in Chapter X-A (GAAR) or not.

Sec 245Q: Application to BOAR

1. Make an application in prescribed FORM (34C/34D/34DA/34E/34EA) & manner stating question on which ruling is sought.
2. Application can be withdrawn within 30 days from date of application.
3. **Fees:**

	Assessee	Fees
(a) Public sector Company (Psu's) or person referred in point (v) of Sec 245N		₹ 10,000
(b) Other Assessee:		
Amount of transaction is upto ₹ 100 cr.		₹ 2,00,000
Amount of transaction > ₹ 100 cr upto ₹ 300 cr		₹ 5,00,000
Amount of transaction > ₹ 300 cr		₹ 10,00,000
4. Application should be signed digitally, if it is required to furnish his return of income under digital signature otherwise communicated through its registered e-mail address.

**Sec 245R: Procedure**

1. BOAR shall forward a copy of application to CIT/PCIT to ascertain whether the case is pending or not & if necessary, call for the records.
2. BOAR may allow or reject application but in following cases BOAR shall reject the application.
 - (a) In case of public sector co. (PSU) when question is already pending before **H.C. or S.C.**
 - (b) In case of **other assessee**, if question already pending before **IT Authority/ITAT/HC/SC.**
 - (c) Question **involves determination of FMV of any Property.**
 - (d) Question in the application related to a transaction which is designed prima facie for avoidance of tax (**except application made by PSU or application in relation to transaction is an impermissible avoidance arrangement or Not.**)
3. If the application is allowed then BOAR shall pronounce its ruling within **6 months** from the date of receipt of application of assessee.
4. Copy of ruling shall be forwarded to assessee & CIT/PCIT.
Note: If application is made by PSU, then IT Authority, ITAT shall not proceed further, means it will wait for the decision of BOAR.
5. Procedure of BOAR shall be in Faceless manners as per scheme notified by CBDT.

Sec 245T: Advance ruling to be void in certain circumstances

Where the BOAR finds, on representation made to it by the CIT/PCIT or otherwise, that an advance ruling has been obtained by applicant by fraud or misrepresentation of facts, it may, by order, declare such ruling to be void ab initio and all the provisions of this Act shall apply.

Sec 245-OB: Board for Advance Rulings

- (1) CG shall constitute one or more Boards for Advance Rulings, as may be necessary, for giving advance rulings under this Chapter on or after 01/09/2021.
- (2) BOAR shall consist of 2 members, each being an officer not below the rank of CCIT, as may be nominated by the Board.

Sec 245P: Vacancies, etc., not to invalidate proceedings

No proceeding before, or pronouncement of advance ruling by, the BOAR shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the BOAR.

Sec 245W: Appeal to HC

The **applicant**, if he is **aggrieved** by any ruling pronounced or order passed by the BOAR or the **AO**, on the directions of the CIT/PCIT, may appeal to **High Court** against such ruling or order of the BOAR within **60 days** from the date of the communication of ruling or order.



Provided that where the HC is satisfied, may grant further period of 30 for filing such appeal.

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➤ Submission of additional facts before the Board for Advance Rulings

1. BOAR may at its discretion permit or require the applicant to submit such additional facts as may be necessary to enable it to pronounce its advance ruling.
2. Where in the course of the proceedings before the BOAR, a fact is alleged which cannot be borne out by, or is contrary to, the record, it shall be stated clearly and concisely and supported by a duly sworn affidavit.

➤ Questions contained in the application

The applicant shall not, except by leave of the Board for Advance Rulings, urge or be heard in support of any additional question not set forth in the application, but in deciding the application the Board for Advance Rulings shall, at its discretion, consider all aspects of the questions set forth as may be necessary to pronounce a ruling on the substance of the questions posed for its consideration.

➤ Rectification of mistakes

1. BOAR may, with a view to rectifying any mistake apparent from the record, amend any order passed by it before the ruling pronounced by the BOAR has been given effect to by the AO.
2. Such amendment may be made suo motu or when the mistake is brought to its notice by the applicant or the PCIT or CIT, as the case may be, but only after allowing the applicant and the PCIT or CIT, as the case may be, reasonable opportunity of being heard.

➤ Difference of opinion

If the Members of BOAR differ in opinion on any point or points, the BOAR shall refer such point or points to the PCCIT (Int. Tax), who shall nominate one Member from any other BOAR and such point or points shall be decided according to the opinion of the majority of the Members.



Notes



1. OECD Model: OECD Model is essentially model treaty between **two developed nations**. This model advocates the residence principle, i.e., emphasis on the right of state of residence to tax the income.
2. UN Model: UN Model is a compromise between the source principle and the residence principle. However, it gives more **weight to 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.
3. US Model: This Model Convention is used by the United States while entering into tax treaties with various countries.

➤ OECD Model contains **VII chapters comprise of 32 articles** and UN Model also contains **VII chapters but comprise of 31 articles** and US Model comprises of 30 articles.

☞ Article 1: Persons Covered

OECD and UN Model Convention would apply to persons who are **residents of one or both of the Contracting States**.

Fiscally transparent entity - Income derived by or through a fiscally transparent entity under the tax law of either contracting states (CS) to be considered to be income of a resident of a CS, to the extent such income is treated, for purposes of taxation by that State, as the income of a resident of that State.

Example: - State A and State B have concluded a treaty identical to the MTC. State A considers that an entity established in State B is a company (opaque), and taxes that entity on interest that it receives from a debtor resident in State A. Under the domestic law of State B, however, the entity is treated as a FIRM (transparent entity), and the two members in that entity, who share equally all its income, are each taxed on half of the interest. One of the members is a resident of State B and the other one is a resident of a country with which States A and B do not have a treaty. In this case only half of the interest shall be considered, for the purposes of treaty benefit, to be income of a resident of State B.

☞ Article 2: Taxes Covered

Taxes on income and capital - MTC apply to **taxes on income and on capital** imposed on behalf of a CS or of its political subdivisions or local authorities, irrespective of the manner in which they are levied. Elements of income or capital including, gains from the alienation of property, total amounts of wages or salaries paid by enterprises, capital appreciation (wealth Tax).

It shall also apply to identical/substantially similar taxes imposed after date of signing of convention.

☞ Article 4: Residence

Residential status of any person shall be **determined as per domestic tax law** of that country. If any person become resident of both the country then his residential status shall determine as follows:



1. For Individual
 - (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 (MAP)**.
2. For Persons other than Individual- Residency shall be determined by competent authorities by way of MAP having regard to its POEM, place of incorporation etc.

Article 5: Permanent Establishment (PE)

- Article 5(1) states the "Basic Rule" for a PE and expresses the primary meaning of PE. PE exists if the following conditions are satisfied cumulatively:
 - ✓ There is an **"enterprise"**
 - ✓ Such enterprise is carrying on a **"business"**;
 - ✓ There is a **"place of business"**;
 - ✓ Such place of business is at the **disposal of the enterprise** (may be owned/rented but must be one which the enterprise has the effective power to use);
 - ✓ Place of business is **"fixed"**, that is, it must be established at a distinct place with a certain degree of permanence;
 - ✓ Business of the enterprise is **carried on** wholly or partially through this fixed place of business.
- As per Article 5(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.
- As per OECD MTC, a building site or construction or installation project constitutes a PE if it lasts more than **12 months**. UN MTC is wider as it covers "assembly and installation project" and "supervisory" activities in connection thereto and requires the activity in question to continue only for **6 months**.



- UN Model makes a specific reference to **Service PE** which is absent in the OECD Model. UN Model reads as follows - "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 CS for a period or periods **aggregating more than 183 days in any 12 months** period commencing or ending in the fiscal year concerned".
In the absence of a Service PE in OECD Model, the presence has to be ascertained through general principles under Article 5(1).
- Agency PE under OECD and UN targets activities done by a dependent agent of the enterprise in the Source State. The recent update expands the definition of dependent agent PE to include instances when an agent habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts routinely concluded without material modification by the enterprise.
- UN MTC** has an **additional Article 5(6) relating to insurance** which is absent in OECD Model. As per this Article, an insurance enterprise of a CS shall, except in regard to reinsurance, be deemed to have a PE in the other CS if it collects premiums in the territory of that other State or insures risks situated therein through a person.
In the absence of similar Article in the OECD, a PE of an insurance Enterprise has to be determined in accordance with provisions of Article 5(1) or 5(2) of the OECD model.

☞ Article 7: Business Profits

Business profits of an enterprise can only be taxed by the Residence State. Right of **Source State** to tax business profits of an enterprise only exists if **a PE exists in its jurisdiction**.

- As per OECD MTC, once PE is proven, Source State can tax only such profits as are attributable to the PE. UN MTC amplifies this attribution principle by a **limited Force of Attraction rule (FOA)**. FOA rule implies that when a foreign enterprise sets up a PE in State of Source, it brings itself within the fiscal jurisdiction of that State (State of Source) to such a degree that profits that the enterprise derives from Source State, whether through the PE or not, can be taxed by it (Source State).
- As per Article 7 of the UN MTC, if the enterprise carries on business in the other CS through a PE, profits of the enterprise may be taxed in the other State but only attributable to:
(a) that **PE**; (b) Sales in that other State of goods or merchandise of the same or similar kind as those sold through that PE; or (c) Other business activities carried on in that other State of the same or similar kind as those effected through that PE.

Article 11: Interest

Paragraph 1 provides the right to **Residence State to tax interest**. Paragraph 2, however, also confers right to the Source State to tax interest. Generally, the interest is taxed in the Source State at a given rate on gross basis. However, if the beneficial owner of the interest is a resident of the other CS, the tax so charged cannot exceed a specified percentage of the gross amount of the interest. OECD Model specifies the percentage as 10%, but the UN Model leaves this percentage to be established through bilateral negotiations.

It may be noted that the definition of interest in both the models is similar it 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 Govt. securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payment are not regarded as interest for the purpose of this Article.

Article 12: Royalties

As per the **OECD Model**, royalties arising in Source State and beneficially owned by resident of Residence State are taxable **only in Residence State**. However, the **UN Model** provides that royalties may be taxed in the Residence State. Hence, the UN Model departs from the principle of exclusive right to tax provided to Residence State in the OECD Model. Thus, under the UN Model, the **Source State may also tax royalties**. However, if the beneficial owner is a resident of the Residence State, the tax charged by the Source State **cannot exceed the specified percentage** of the gross amount of royalties.

Definition of 'royalties' under the OECD does not include the following: (a) rentals for films or tapes used for radio or television broadcasting and (b) equipment rentals like rentals for industrial, commercial or scientific equipment.

Article 12A of UN: Fees for Technical Services

In 2017, the UN Model has inserted a specific article pertaining to FTS. There is no specific reference to FTS in the OECD Model.

Paragraph 1 provides that the FTS may be taxed in the Residence State but does not provide that the FTS is exclusively taxable in the Residence State.

Paragraph 2 establishes the right of the country in which FTS arises to tax in accordance with its domestic law, subject to the limitation on the maximum rate of tax, if the beneficial owner is a resident of the other CS. The maximum rate of tax is to be established through bilateral negotiations



☞ Article 13: Capital Gains

The right to tax income from capital gains may be exclusively with the Residence State, or shared between the Residence and Source States. Capital gain shall be computed as per domestic law.

It contains rules for taxation of gains made from alienation of different assets such as immovable property, immovable property forming part of a PE, ships and aircrafts, etc. In respect of shares, both Models have been updated and are identical. Rights are conferred to the Source State if more than 50% of the value of shares during the preceding 365 days is derived from immovable property in such Source State.

☞ Article 14: Independent Personal Services [Only present in UN MTC]

Article 14 is only present now in the UN Model. It was deleted from the OECD Model. The Effect of deletion of Article 14 is that income derived from Professional Services etc., is now dealt with as 'Business Profits' (Article 7) under the OECD MC.

This Article deals with the taxation of income derived by a person for professional or specified services which are offered in the Source State through some presence.

1. Income derived by a resident of a CS 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 CS**:
 - a) If he has a **fixed base** regularly available to him in the other CS 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 CS; or
 - b) If his **stay in the other CS** 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. "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 21: Other Income

It deals with taxation of items of income which are not specifically taxable under any other Article. Key differences are as under: OECD approach envisages that the exclusive right to tax is with the Residence State.

UN Model contains an additional paragraph, Article 21(3), which provides that Source State may also tax other income.

Article 21(2) of both OECD and UN Model provides that for income effectively connected with a PE maintained in a CS by a resident of the other CS, taxation is governed by the provisions of Article 7 (Business Profits).

Additionally, UN Model provides that if the aforesaid income is effectively connected with a fixed base situated in a Contracting State by a resident of the other Contracting State, taxation would be governed by the provisions of Article 14 (Independent personal services).

☞ Articles 23A & 23B: Elimination of Double Taxation

This article provides tax exemption and tax credit method for elimination of double taxation.

☞ Article 25: Mutual Agreement Procedure

Where a taxpayer believes that the treatment by contracting states(s) is not in accordance with the provisions of the tax treaty competent authorities of both countries should endeavour to resolve the conflicts through bilateral negotiations. This would take place as follows

Particular	OECD	UN
Request of MAP	Tax payer can make the request to either contracting state	Alternative A: Taxpayer has to approach to his resident country Alternative B: Reference to arbitration process as a part of MAP. The decision arrived at is binding unless person directly affected does not accept it
Time Limit	2 years from the date when all information required in order the case needs to be provided to both states.	Arbitration may be initiated if competent authorities are unable to reach agreement on a case within 3 years from presentation of that case [alternative B]
Who can request for arbitration?	Arbitration must be requested by person who initiated the case	Arbitration may be requested by competent authorities of either state once such a request is made, taxpayer will be notified [Alternative B]
Departure from arbitration?	No specific provision	Competent authorities may depart from arbitration decision by agreement within 6 months after decision is communicated [alternative B]

☞ Article 26: Exchange of Information

In order to complete tax cases, a country may require certain info which may be available with the treaty partner. This provides for info which may be exchanged & the manner in which such a request has to be made.

▪ Importance of Article 26:

- facilitates effective exchange of information between CS's.



- 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.
-
- Similar provisions contained in OECD and UN MC's
 - A CS cannot be expected to provide confidential financial info to another CS unless it has confidence that the info will not be disclosed to unauthorized persons.
 - A CS can avoid the EOI obligations by showing that the info pertains to communication between an attorney and his client which is protected from disclosure under domestic law.
 - Lack of interest or use in such info cannot, however, form the basis for a CS to not cooperate with the EOI obligations.



Notes



➤ Sources of origin of International Tax Law

- a. **Multinational international agreements:** Agreement signed by more than 2 countries is called as "MIA". Example: Vienna Convention on Law of Treaties (VCLT)
- b. **DTAA:** It included protocols, memorandum of understanding, and exchange of information, etc. forming part of the DTAA
- c. **Customary international law and its general practices:** For example, principles of law recognised by civilized nations in their national legal systems, customary law and judicial decisions and the practices of international organizations.

➤ Double Taxation & Connecting Factors which lead to Double Taxation

The taxability of a foreign entity in any country depends upon whether it is doing business **with** that country or in **that** country. There are two types of connecting factors to determine the jurisdiction, namely, "Residence" and "Source". It means a company can be subject to tax either on its residence link or its source link with a country. If a company is doing business with another country (i.e. host/source country), then it would be subject to tax in its home country only, based on its residence link. However, if a company is doing business in a host/source country, then, besides being taxed in the home country on the basis of its residence link, it will also be taxed in the host country on the basis of its source link.

- **Jurisdictional double taxation:** When source rules overlap, double taxation may arise i.e. tax is imposed by two or more countries as per their domestic laws in respect of the same transaction, income arises or is deemed to arise in their respective jurisdictions. This is known as "jurisdictional double taxation". In order to avoid such double taxation, a company can invoke provisions of DTAA with the host/source country, or in the absence of such an agreement, invoke provisions of sec. 91 of the IT, 1961, providing unilateral relief in the event of double taxation.
- **Economic double taxation:** 'Economic double taxation' happens when the same transaction, item of income or capital is taxed in two or more states but in hands of different person (because of lack of subject identity).

Example: Suppose Sam Inc. (USA Co.) distribute dividend and paid DDT in USA & same dividend is received by Indian Resident is taxed in India. In this case, same Income is taxed in hands of Sam Inc. as well as Indian Resident.

➤ Types of DTAA:

- **Limited DTAA** - Limited to certain types of Income only. Ex: DTAA between India and Pakistan is limited to aircraft profits only
- **Comprehensive DTAA** - They cover almost all types of incomes covered by any model convention. Ex: Sometimes, a treaty covers wealth tax, gift tax, etc.



- Directives Principle set out by Article 51 of Indian Constitution to be followed by the State in the context of International Agreements; - The State shall endeavor to
- Promote international peace and security;
 - Maintain just and honorable relations amongst nations;
 - Foster respect for international law and treaty obligations in the dealings of organized people with one another; and
 - Encourage settlements of international disputes by arbitration.
- Need of Tax Treaty
- Allocating the taxing rights
 - Elimination of double taxation
 - Ensuring non-discrimination between residents and non-residents
 - Resolution of disputes arising on account of different interpretations of tax treaty
 - Providing assistance in the collection of the fair and legitimate share of tax.
- Further, in addition to above, there are some other principles which must be considered by countries in their tax system -
- (i) Equity and fairness: Same income earned by different taxpayers must be taxed at the same rate regardless of the source of income.
- (ii) Neutrality and efficiency: Neutrality factor provides that economic processes should not be affected by external factors such as taxation. Neutrality is two-fold:
- a. Capital export neutrality (CEN) provides that business decision must not be affected by tax factors between the country of residence and the target country
Example: Mr Devam Resident of India wants to invest in Business of Country X then his business decision must not be affected due to taxation.
 - b. Capital import neutrality (CIN) provides that the level of tax imposed on non residents as well as the residents must be similar
Example: Mr Sam resident of country X doing business in India then Tax imposed on Mr Sam and Indian resident person must be similar.
- (iii) Promotion of mutual economic relations, trade and investment.
- Interpretation of Tax Treaties
- Basic Principles of Interpretation of a Treaty derived by customary international law
- (i) Golden Rule - Objective Interpretation: Ideally any term or word should be interpreted keeping its **objective or ordinary or literal meaning** in mind and the term has to be interpreted contextually. However, if grammatical interpretation would result in absurdity or inconsistency, it should not be adopted.



- (ii) Subjective Interpretation: Terms of Treaty are to be interpreted according to the **common intention of the Contracting parties at the time treaty was concluded**.
- (iii) Purposive Interpretation (Objects and Purpose method): Treaty is to be interpreted so as to facilitate the attainment of the **aims and objectives** of the Treaty.
- (iv) The Principle of Effectiveness: A treaty should be interpreted in a manner to have **effect rather than make it void**.
- (v) Principle of Contemporanea Expositio: A treaty's terms are normally to be interpreted on the basis of their **meaning at the time the treaty was concluded**. However, this is not a Universal Principle.
- (vi) Liberal Construction It is a general principle of construction with respect to treaties that they shall be **liberally construed** so as to carry out the apparent intention of the parties.
- (vii) Treated as a whole - Integrated Approach A treaty should be construed as a **whole** and effect should be given to each word which would be construed in the same manner wherever it occurs. Any provision should **not be interpreted in isolation**; rather the entire treaty should be read as a whole to arrive at its object and purpose.
- (viii) Reasonableness and Consistency Treaties should be given an interpretation in which the **reasonable** meaning of words and phrases is preferred, and in which a consistent meaning is given to different portions of the instrument. In accordance with the principles of consistency, treaties should be interpreted in the **light of existing international law**.
- Extrinsic Aids to interpretation of a tax treaty
A wide range of extrinsic material is permitted to be used in interpretation of tax treaties
 - (i) Interpretative Protocols, Resolutions and Committee Reports, setting out agreed interpretations;
 - (ii) A subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
 - (iii) Subsequent conduct of the state parties, as evidence of the intention of the parties and their conception of the treaty;
 - (iv) Parallel Treaty, in pari materia (i.e., relating to the same subject matter), in case of doubt;
 - (v) International Articles/Essays/Reports/ Cahiers published by International Fiscal Association (IFA), Netherlands
 - (vi) Preamble
 - (vii) Mutual Agreement Procedure



- (viii) Commentaries on OECD/UN Models and their importance
- (ix) Foreign Courts' Decisions

- **Protocol:** It is like a supplement to the treaty. In many treaties, in order to put certain matters beyond doubt, there is a protocol annexed at the end of the treaty, which clarifies borderline issues. A protocol is an integral part of a tax treaty and has the same binding force as the main clauses there in.

Protocol to India France treaty contains the Most Favoured Nation Clause. Thus, one must refer to protocol before arriving at any final conclusion in respect of any tax treaty provision.

Under MFN clause a country agrees to extend the benefits to the residents of the other country, which it had (first country) promised to the residents of third country. It tries to avoid discrimination between residents of different countries.

Example: Suppose as per India-UK treaty resident of UK liable to pay tax in India on royalty derived from India @10%. After some time India entered into DTAA with Sri Lanka & as per India-Sri Lanka DTAA, resident of Sri Lanka liable to pay tax in India on royalty derived from India @5%. Now in this example suppose India-UK treaty contain MFN clause then Resident of UK liable to pay tax in India only @5%.

CBDT clarifies that the applicability of the MFN clause and benefit of the lower rate or restricted scope of source taxation rights in relation to certain items of income (such as dividends, interest income, royalties, Fees for Technical Services, etc.) provided in India's DTAA's with the third States will be available to the first (OECD) State **only when all the following conditions are met:**

- (i) The second treaty (with the third State) is entered into after the signature/ Entry into Force (depending upon the language of the MFN clause) of the treaty between India and the first State;
- (ii) The second treaty is entered into between India and a State which is a member of the OECD **at the time of signing the treaty with it;**
- (iii) India limits its taxing rights in the second treaty in relation to rate or scope of taxation in respect of the relevant items of income; and
- (iv) **A separate notification has been issued by India, importing the benefits of the second treaty into the treaty with the first State,** as required by the provisions of sec. 90(1) of the IT Act, 1961.

If all the conditions enumerated in (i) to (iv) are satisfied, then, the lower rate or restricted scope in the treaty with the third State is imported into the treaty with an OECD State having MFN clause from the date as per the provisions of the MFN clause in the DTAA, after following the due procedure under the Indian tax law.



➤ Difference between Ambulatory and Static Approach

To decide what meaning is to be assigned to the said term, 2 views can be taken:

- ✓ **Static** - It looks at the meaning at the time when the Treaty was signed.
- ✓ **Ambulatory** - It provides that one looks to the meaning of the term at the time of application of Treaty Provisions. All Model Commentaries favor this Approach, however with one caution that this approach cannot be applied when there is a radical amendment in the domestic law thereby changing the sum and substance of the said term.

➤ Principles under Vienna Convention of Law of Treaties

- **Article 26 - Pacta Sunt Servanda (in good faith):** Every treaty in force is binding upon the parties and must be followed by them in good faith.
- **Article 27 - Internal law and observance of treaties:** A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty. For instance, the parties to the treaty should not dishonour their international commitments with each other by retrospectively amending their domestic tax laws or by not abiding by the treaty terms.
- **Article 28 - Non-retroactivity of treaties:** Treaty provisions are not binding on a party for any act which ceased to exist before the date of the entry into force of the treaty with the respect to that party. In other words, unless otherwise provided, treaties cannot have retrospective application.
- **Article 29 - Territorial scope of treaties:** A treaty is binding upon each party in respect of its entire territory, unless a different intention appears from the treaty.
- **Article 31 - General Rule of Interpretation**

A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms thereof in the context and in the light of its object and purpose. The context for the purpose of interpretation of a treaty shall comprise its text, preamble and annexure.

(a) Any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;

(b) Any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related there to.

The following shall be taken into account, together with the context in that:

(a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;

(b) Any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;

(c) Any relevant rules of international law applicable to relation between the parties. A special meaning shall be given to a term if it is established that the parties so intended.



- Article 32 - Supplementary means of Interpretation

When interpretation according to Article 31

- Leaves meaning ambiguous
- Leads to an unreasonable result

- Article 33 - Interpretation of Treaties authenticated in 2 or more languages

- Text shall be equally authoritative in each language
- A version of treaty in another language shall be considered authentic if treaty so provides
- Terms of the Treaty shall be presumed to have the same meaning in each text
- Except where a particular text prevails in accordance with paragraph 1, when a comparison of the authentic texts discloses a difference in meaning which the application of Articles 31 and 32 does not remove, the meaning which best reconciles the texts, having regard to the object and purpose of the treaty, shall be adopted.

- Article 34 - General rule regarding third states: A treaty creates neither obligations nor rights for a third State without its consent

- Article 42 - Validity and continuance in force of treaties

The validity of a treaty or of the consent of a State to be bound by a treaty may be impeached only through the application of the Convention.

The termination of a treaty, its denunciation or the withdrawal of a party, may take place only as a result of the application of the provisions of the treaty or of the Convention. The same rule applies to suspension of the operation of a treaty.

- Article 60 - Termination or Suspension of the operation of a treaty as a consequence

of a breach: A material breach of a bilateral treaty by one party entitles the other to invoke the breach as a ground for terminating the treaty or suspending its operation wholly or partly

- Material breach of a multilateral party,

(i) Other parties may unanimously agree to suspend the operation of the treaty wholly or partly or terminate it.

(ii) A party specially affected by the breach to invoke it as a ground for suspending the operation wholly or partly in relation between itself and Contracting State

(iii) Any party other than the Defaulting State to invoke the breach as a ground for suspending the operation of the Treaty wholly or partly with respect to itself if the treaty is of such nature that a material breach of its provisions by one party radically changes the position of every other party with respect to further performance of its obligations under the treaty.

- Material breach means

(i) Repudiation (rejection) of the treaty not sanctioned by the Convention

(ii) Violation of an essential provision



- **Article 61 - Supervening impossibility of performance:** In case of permanent disappearance or destruction of an object indispensable for the execution of the Treaty, a party may terminate or withdraw from the Treaty. If the impossibility is temporary, it may be invoked only as a ground for suspending its operation. But impossibility of performance shall not be invoked if impossibility is a result of a breach of an obligation by that party.

- **Article 62 - Fundamental change of circumstances**
 A fundamental change of circumstances which has occurred with regard to those existing at the time of conclusion of a treaty, and which was not foreseen by the parties, may not be invoked as a ground for terminating or withdrawing from the treaty unless-
 - (i) The existence of those circumstances constituted an essential basis of the consent of the parties bound by the Treaty, and
 - (ii) The effect of the change is radically to transform the extent of obligations still to be performed under the Treaty.
 A fundamental change of circumstances may not be invoked as a ground for terminating or withdrawing from a Treaty
 - (i) If the treaty establishes a boundary, or
 - (ii) If the fundamental change is the result of a breach by the party invoking it either of an obligation owed to any other party to the treaty
 If a party invokes fundamental change of circumstances as a ground for terminating or withdrawing from a treaty, it may also invoke the change as a ground for suspending its operation.

- **Article 64 - Emergence of new peremptory norm of general international law**
 If a new peremptory norm (new international laws) emerges, any existing treaty which is in conflict with that norm becomes void and stands terminated.



Notes



- **Base Erosion and Profit Shifting (BEPS) & its adverse effects:** It refers to tax planning strategies that exploit gaps and mismatches in tax rules to make profits 'disappear' for tax purposes or to shift profits to locations where there is little or no real activity but the taxes are low, resulting in little or no overall corporate tax being paid.

Adverse Effects of BEPS:

- (i) Governments have to cope with less revenue and a higher cost to ensure compliance.
- (ii) In developing countries, the lack of tax revenue leads to significant under-funding of public investment that could help foster economic growth.
- (iii) BEPS undermines the integrity of the tax system, as reporting of low corporate taxes is considered to be unfair. When tax laws permit businesses to reduce their tax burden by shifting their income away from jurisdictions where income producing activities are conducted, other taxpayers, especially individual taxpayers in that jurisdiction bear a greater share of the burden. This gives rise to tax fairness issues on account of individuals having to bear a higher tax burden.
- (iv) Enterprises that operate only in domestic markets, including family-owned businesses or new innovative businesses, may have difficulty competing with MNEs that have the ability to shift their profits across borders to avoid or reduce tax. Fair competition is harmed by the distortions induced by BEPS.

- **Need for international collaboration between countries**

Interaction of domestic tax laws with other countries laws may either lead to gaps (no taxation in either country or taxed at a nominal rate) or double taxation. Since there is no principle of matching (payment deductible by the payer is generally taxable in the hands of the recipient, unless specifically exempted) at the international level, it leaves considerable scope of arbitrage by taxpayers. BEPS relates to instances where the interaction of tax rules of different countries leads to double non-taxation and arrangements that achieve low or no taxation by shifting profits away from the jurisdictions where the activities creating those profits take place. International standards have tried to reduce these frictions; however, gaps still remain. Therefore, there is a need for countries to collaborate on tax matters so that they are able to get their due share of taxes.

- **The Action Plans were structured around three fundamental pillars viz.:**

- (i) Introducing coherence in the domestic rules that affect cross-border activities.
- (ii) Reinforcing of 'substance' requirements in existing international standards; Alignment of taxation with location of value creation and economic activity; and
- (iii) Improving transparency and tax certainty.



➤ Action Plan 1 - Addressing the Challenges of The Digital Economy

Taxation issues in E-Commerce: New business models have created new tax challenges. The typical taxation issues relating to e-commerce are:

- (i) the difficulty in characterizing the nature of payment and establishing a nexus or link between a taxable transaction, activity and a taxing jurisdiction,
- (ii) the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes.

The digital business, thus, challenges physical presence-based permanent establishment rules. If 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.

☞ OECD Recommendation

- (i) Modifying existing PE rule to provide whether an enterprise engaged in fully dematerialised digital activities would constitute a PE if it maintained significant digital presence in another country's economy.
- (ii) A virtual fixed place of business PE when the enterprise maintains a website on a server of another enterprise located in a jurisdiction & carries on business through that website.
- (iii) Imposition of a final withholding tax on certain payments for digital goods or services provided by a foreign e-commerce provider.
- (iv) Imposition of a equalisation levy on consideration for certain digital transactions received by a NR from a resident or NR having PE in the other country.

☞ Provision incorporated in Indian Tax Laws

- 1. Significant economic presence (Already Covered in topic 2)
- 2. Equalisation Levy (Already Covered in topic 5)

➤ Action Plan 2 - Neutralise the Effects of Hybrid Mismatch Arrangements

HMA means exploits a difference in the tax treatment of an entity or an instrument under the law of two or more countries to achieve double non-taxation.

E.g.

- 1. Creation of two deductions for single borrowers.
- 2. Taking deductions without corresponding Income Inclusion.
- 3. Misuse of foreign Tax Credit.
- 4. Participation exemption regime (showing activity in low tax jurisdiction)

☞ OECD Recommendation

1. Change in the domestic law & make rules to neutralise the effect of HMA.
2. Change in tax treaty to deal with dual resident companies, transparent entity, Hybrid entity etc.

☞ Recommended general amendments

- A rule denying transparency to entities where the non-resident investors' resident country treats the entity as opaque (non-transparent)

Example: Let us say, X Co., a parent company in country X indirectly holds Y Co., an operating company in country Y. Between X Co. and Y Co. is a hybrid entity that is treated as transparent or disregarded for country X tax purposes and as non-transparent for country Y tax purposes. X Co. holds all or almost all equity interest in the hybrid entity which in turn holds all or almost all equity interests in Y Co. The hybrid entity borrows money from a third party and the loan is used to invest equity into Y Co (or to buy the shares in Y Co from either another company of the same group or from an unrelated third party). The hybrid entity pays interest on the loan. Except for the interest, the hybrid entity does not claim any other significant deduction and does not have any significant income. With respect to Country Y, for tax purposes, Hybrid Entity is subject to corporate income tax. Its interest expenses can be used to offset other country Y group companies' income under the country Y group tax relief regime. On the other hand, country X treats the hybrid entity as transparent or disregarded, with the result that its interest expenses are allocated to X Co, which deducts the interest expense to offset unrelated income. The net effect is that there are two deductions for the same contractual obligation in two different countries. Therefore, by virtue of rule denying transparency to an entity which is treated as opaque in the subsidiary company's country, the double deduction can be avoided.

- A rule denying an exemption or credit for foreign underlying tax for dividends that are deductible by the payer;

Example: N Co, a company resident in country N is funded by M Co., a company resident in country M with an instrument that qualifies as equity in country M but as debt in country N. A payment made under the instrument would be deductible as interest expense for N Co under country N tax law. The corresponding receipts are treated as exempt dividends under the tax laws of country M. Consequently, deduction is available under the tax laws of country N without a corresponding income inclusion in country M. Therefore, by virtue of rule denying an exemption or credit for foreign underlying tax for dividends that are deductible by the payer, exemption of such income in country M would not be possible.

- A rule denying a foreign tax credit for withholding tax where that tax is also credited to some other entity.



- ☞ **Branch mismatches:** Branch mismatches occur where two jurisdictions take a different view as to the existence of, or the allocation of income or expenditure between, the branch in head office of the same taxpayer. Branch mismatches arise where the ordinary rules for allocating income and expenditure between the branch and head office result in a portion of the net income of the taxpayer escaping the charge to taxation in both the branch and residence jurisdiction. Unlike hybrid mismatches, which result from conflicts in the legal treatment of entities or instruments, branch mismatches are the result of differences in the way the branch and head office account for a payment made by or to the branch.

- **Action Plan 3 - Strengthen Controlled Foreign Company (CFC) Rules**
CFC are corporate entities incorporated in Tax Haven countries & controlled directly or indirectly by Resident of higher tax jurisdiction. (Parent state)
E.g.: BB Ltd is an Indian Company setup a subsidiary in Dubai (tax haven) BB Dubai Ltd. In this case BB Dubai Ltd. is treated as CFC. Normally CFC earn Passive Income & accumulated such income in tax haven countries. Such income is taxable in parent state only if CFC distribute dividend but practically CFC never distribute dividend so such income is never taxable in parent state.
To curb these practices many countries come out with CFC regulation. As per CFC rules Income earn by CFC is deemed to be income of parent entity and taxable in parent state. Normally CFC rules applicable in passive income like Interest, Royalty, Dividend, Income from transactions with related parties etc.

- **Action Plan 4 - Interest Deductions and other Financial Payments (Thin Capitalisation)**
Normally International Group taking loan or debt in High Tax Jurisdiction because interest is deductible expenses & they can reduce their overall tax liability. Many times enterprise of MNE located in tax haven gives loan to entity located in high tax jurisdiction so their over all tax burden get reduced.

- ☞ **Recommendations of OECD**
 - **Fix Ratio Rule:** Interest deduction should be allowed on the basis of level of economic activity. As per this rule interest is allowed at certain percentage of EBITDA (India @30%).
 - **Group Ratio Rule:** As per this rule entity allows to deduct more interest expenses on the basis of position of its worldwide group.
 - **Targeted Rules:** There should be certain rule to address some specific risk in case of Banking and Insurance business. If there is no risk then country can exclude banking and insurance business.
- ☞ **Provision incorporated in Indian Tax Laws:** Sec 94B incorporated in Transfer Pricing.



➤ Action Plan 5 - Counter Harmful Tax Practices

Normally every country tax royalty on Intellectual Property at lower rate. MNE's normally develop IP in high tax jurisdiction but registered that IP in tax haven or low tax rates jurisdiction. OECD recommended that low tax rate benefit should be available only if IP is developed (substantial Activity) in that country.

- ☞ Provision incorporated in Indian Tax Laws: Sec. 115BBF introduced where royalty income on patent taxable at 10% when patent developed in India.

➤ Action Plan 6 - Preventing Treaty Abuse

Protection against treaty shopping: Treaty shopping means taking the benefit of any treaty by any person which is not meant for that person. Suppose as per India Mauritius treaty if any person resident of Mauritius earning capital gain on shares of Indian Company shall not be taxable in India. Now, suppose any person resident of UK incorporates a shell company in Mauritius & takes the benefit of India-Mauritius treaty is treated as treaty shopping.

Recommendations of OECD

1. Clear statement in Preamble of treaty that such treaty is for avoidance of double taxation & not for creating opportunities for Non-taxation through treaty shopping.
2. LOB Rules: Rules based on objective criteria's such as Legal Nature, ownership, general activities etc. As per India-Mauritius treaty resident of Mauritius shall be liable to pay tax in India on shares @ 50% of Indian Tax rate but this benefit is not available Mauritius residents shell companies whose operational expenses is less than ₹ 7,00,000.
3. PPT Rules: General anti-abuse rules on the basis of principle purpose of transaction.

➤ Action Plan 7 - Prevent the Artificial Avoidance of Permanent Establishment (PE) Status

Recommendations of OECD

1. Reworking exceptions to PE definition: To define PE all activities carried on by enterprises alongwith activity by closely related shall be examined.
2. Analyzing arrangements entered through contractual agreements: Business through commissionaire also included in the definition of PE except it is performed as independent Business activity.

➤ Action Plan 8-10 - Transfer Pricing outcomes in Line with Value Creation/Intangibles/Risk and Capital and other High-Risk Transactions

Action Plan	Details
8	Addresses transfer pricing issues relating to controlled transactions involving intangibles, since intangibles are by definition mobile and they are generally difficult-to-value. Misallocation of the profits generated by valuable intangibles is a significant cause of BEPS.
9	Contractual allocations of risk are respected only when they are supported by actual decision-making and thus exercising control over these risks. Contractual allocations of risk are respected only when they are supported by actual decision-making and thus exercising control over these risks.
10	This action focuses on other high-risk areas, which include: - the scope for addressing profit allocations resulting from controlled transactions which are not commercially rational, - the scope for targeting the use of transfer pricing methods in a way which results in diverting profits from the most economically important activities of the MNE group, and - the use of certain type of payments between members of the MNE group (such as management fees and head office expenses) to erode the tax base in the absence of alignment with the value-creation.

➤ Action Plan 11 - Measuring and Monitoring BEPS

Indicators of BEPS activity: Six indicators of BEPS activity highlight BEPS behaviour using different sources of data, employing different metrics, and examining different BEPS channels. When combined and presented as a dashboard of indicators, they confirm the existence of BEPS, and its continued increase in scale in recent years.

- (i) The profit rates of MNE affiliates located in lower-tax countries are higher than their group's average worldwide profit rate. For example, the profit rates reported by MNE affiliates located in lower-tax countries are twice as high as their group's worldwide profit rate on average.
- (ii) The effective tax rates paid by large MNE entities are estimated to be lower than similar enterprises with only domestic operations - This tilts the playing-field against local businesses and non-tax aggressive MNEs, although some of this may be due to MNEs' greater utilisation of available country tax preferences.
- (iii) Foreign direct investment (FDI) is increasingly concentrated - FDI in countries with net FDI to GDP ratios of more than 200% increased from 38 times higher than all other countries in 2005 to 99 times higher in 2012.
- (iv) The separation of taxable profits from the location of the value creating activity is particularly clear with respect to intangible assets, and the phenomenon has grown rapidly - For example, the ratio of the value of royalties received to spending on research and development in a group of low-tax countries was six times higher than the average ratio for all other countries, and has increased three-fold between 2009 and 2012.

- (v) Royalties received by entities located in these low-tax countries accounted for 3% of total royalties
- This provides evidence of the existence of BEPS, though not a direct measurement of the scale of BEPS.
- (vi) Debt from both related and third-parties is more concentrated in MNE affiliates in higher statutory tax-rate countries - The interest-to-income ratio for affiliates of the largest global MNEs in higher-tax rate countries is almost three times higher than their MNE's worldwide third-party interest-to-income ratio.

➤ Action Plan 12 - Disclosure of Aggressive Tax Planning Arrangements

Design principles and significant objectives of a mandatory disclosure regime:

- Clarity and comprehensibility
- Ability to balance additional compliance costs to taxpayers with the benefit obtained by the tax administration
- Flexibility and dynamism: to allow the tax administration to adjust the system to respond to new risks (or carveout obsolete risks)
- Accurate identification of the schemes to be disclosed
- Effective achievement of objectives
- Ensuring effective use of information collected

➤ Action Plan 13 - Re-Examine Transfer Pricing Documentation

Three-tier structure mandated by BEPS

The BEPS report recommends that countries adopt a standardised approach to transfer pricing documentation; it mandates the following three-tier structure:-

Documents	Information
Master file	Standardised information relevant for all multinational enterprises (MNE) group members. Master file requires MNEs to provide tax administrations with high-level information regarding their global business operations and transfer pricing policies. The master file is to be delivered by MNEs directly to local tax administrations.
Local File	Local file requires maintaining of transactional information specific to each country in detail covering related-party transactions and the amounts involved in those transactions. In addition, relevant financial information regarding specific transactions, a comparability analysis and analysis of the selection and application of the most appropriate transfer pricing method should also be captured. The local file is to be delivered by MNEs directly to local tax administrations
Country-by-Country Report	Information relating to the global allocation of the MNE's income and taxes paid; and Indicators of the location of economic activity within the MNE group. CBC report requires MNEs to provide an annual report of economic indicators viz. the amount of revenue, profit before income tax, income tax paid and accrued in relation to the tax jurisdiction in which they do business. CBC reports are required to be filed in the jurisdiction of tax residence of the ultimate parent entity, being subsequently shared between other jurisdictions through automatic exchange of information mechanism.

➤ Action Plan 14 - Making Dispute Resolution more Effective

Due to implementation of BEPS action plan there may be risk of uncertainty or unintended double taxation. The above issue should be resolved through proper implementation of tax treaties & resolution of disputes through MAP.

☞ Minimum Standard: Ensure effective implementation of MAP

- that treaty obligations related to the MAP are fully implemented in good faith and
- that MAP cases are resolved in a timely manner
- the implementation of administrative processes that promote the prevention and timely resolution of treaty-related disputes
- that taxpayers can access the MAP when eligible.

➤ Action Plan 15 - Developing A Multilateral Instrument

The MLI is a flexible instrument which will modify tax treaties according to a jurisdiction's policy preferences with respect to the implementation of the tax treaty-related BEPS measures. The MLI provides for different types of flexibility:

- (i) Jurisdictions can choose amongst alternative provisions in certain MLI articles;
- (ii) Jurisdictions can choose to apply optional provisions (for instance, the provisions on mandatory binding arbitration);
- (iii) Jurisdictions may also choose to reserve the right not to apply MLI provisions (to opt out through a "reservation") with respect to all of their Covered Tax Agreements or with respect to a subset of their Covered Tax Agreements. Jurisdictions only have the possibility to opt out of provisions that do not reflect a BEPS minimum standard, with the possibility to withdraw their reservation (and opt in) later.

☞ **Need for MLI:** Amending the bilateral treaties involves cumbersome legal process as each country have their own constitutional or other legal mechanisms to invoke international treaties into their domestic laws. Further mere incorporation of BEPS solutions in domestic law will not achieve the desired objective as the tax treaties will remain a tool for tax evaders. Therefore, to ensure the BEPS solutions are transposed into the tax treaty, action plan 15 objective was to bring all these amendments under one single umbrella.

☞ **Structure of the MLI:** There are 7 parts and 39 articles in the MLI. Articles 3 to 17 are recognised as substantive provisions under the MLI convention

Part	Particulars	Article
Part I	Scope and Interpretation of terms	1 - 2
Part II	Hybrid Mismatches	3 - 5
Part III	Treaty Abuse	6 - 11
Part IV	Avoidance of PE Status	12 - 15
Part V	Improving Dispute Resolution	16 - 17

Part VI	Arbitration	18 - 26
Part VII	Final Provisions	27 - 39

Key Organs of MLI

- (a) **Covered Tax Agreements (CTA):** CTA is an "agreement for avoidance of double taxation with respect to taxes on income that is in force between two or more parties and/or jurisdictions with respect to which each party has notified to the Depository as a listed agreement under the MLI" To make MLI operational between two parties, each country has to notify the DTAA with other jurisdiction under MLI upon which DTAA will be termed as CTA. It is important that both countries under the DTAA notify the treaty as CTA for MLI to come into force.
- For example, if India notifies India-Mauritius DTAA as CTA, in its MLI deposit note to OECD but Mauritius does not do so, MLI provisions will not apply until notify by Mauritius as well.
- (b) **Compatibility Clause: Bridge between DTAA and MLI:** Once existing DTAA becomes a CTA, parties to the MLI are given flexibility to choose the relevant provisions of the MLI that needs to be transposed to their existing DTAA. The compatibility clause is to ensure that there is no conflict between the two treaties i.e. the DTAA and MLI. Further, the compatibility clause also gives options to parties to leave an existing provision of the DTAA undisturbed. if the existing provision serves the desired objective with which a particular provision of the MLI was placed to.
- (c) **Reservation Clauses - 'Opt-Out' Mechanism:** The reserved provisions of MLI shall not apply to a CTA if either of the parties makes a reservation. A reservation is defined in the VCLT as a "unilateral statement made by a State, when signing, ratifying, accepting, approving or acceding to a multilateral instrument, whereby it purports to exclude or to modify the legal effect of certain provisions of the Convention"
- Hence, reservations under treaties, introduce flexibility in treaty negotiations, so that States come forward to be a signatory to such multilateral conventions. The general rule of multilateral instrument is that its parties are bound by the entire instrument unless the parties make a reservation. The MLI enables states to opt-out of the provisions, either entirely or partially, by introducing a mechanism of reservations.
- (d) **Mandatory Minimum Standards:** While MLI gives flexibility to the parties through compatibility and reservation clause, to ensure there is some consistency, the parties have to adhere to incorporating mandatory minimum standard provisions in the MLI. The objective of the minimum standard provisions is to ensure that anti-abuse provisions help eliminating the treaty shopping mechanism and consequentially the elimination of double non taxation scenarios by tax-evaders. The minimum standards, therefore, achieve certain consistency amongst the existing tax Out of the four minimum standards prescribed under the BEPS action plan i.e.
- Action 5-Countering Harmful Tax Practices.
- Action 6-Treaty abuse prevention mechanism

Action 13-Country by Country Reporting

Action 14-Effective Dispute Resolution Mechanism

Action 6 & Action 14 solutions are specifically provided as a minimum standard provision under the MLI. With regards to Action 5 and Action 13, the solutions are to be incorporated under domestic laws.

However, in a case where the contracting states together agree to reflect the minimum standard provisions specified under the MLI into their existing DTAA then such treaty partner may opt-out of the minimum standards under the MLI.

(e) **Entry into force of MLI:** Upon deposit of the instrument of ratification, the MLI enters into force on the first day of the month following the expiry of 3 calendar months beginning on the date of such subsequent deposit.

(f) **Effective date of MLI:** Once the MLI is entered into force by both the Contracting States, the effective date of MLI shall be

(a) For withholding taxes- 1st day of next calendar year that begins on or after the dates on which this Convention enters into force for each of the Contracting jurisdictions to the CTA.

(b) For other taxes - Taxable period that begins on or after the expiration of 6 calendar months from the dates on which this Convention enters into force for each of the Contracting Jurisdictions to the CTA.

(g) **Mechanics for Applying MLI**

- Both the Contracting States to the DTAA should be signatories to the MLI and the MLI has entered into force.
- Both the Contracting States should have duly notified their DTAA as a CTA.
- The substantive provisions and choices of the Contracting States to be analysed through the compatibility clause and notification clause, regarding the provisions of the CTA that is to be modified by the MLI.
- Identify whether any reservation is made on the application of a provision of the MLI by either of the contracting parties.

India's Journey

1.	7 th Jun 2017	The signing of the MLI
2.	25 th Jun 2019	Deposit of ratification instrument of 93 jurisdictions with the OECD depository.
3.	9 th Aug 2019	Notification No. 57/2019 giving effect to the provisions of MLI in Union of India
4.	1 st Oct 2019	Entry into Force of India's MLI

Latest Developments of International Taxation

Introduction of Two Pillar solution [BEPS 2.0]

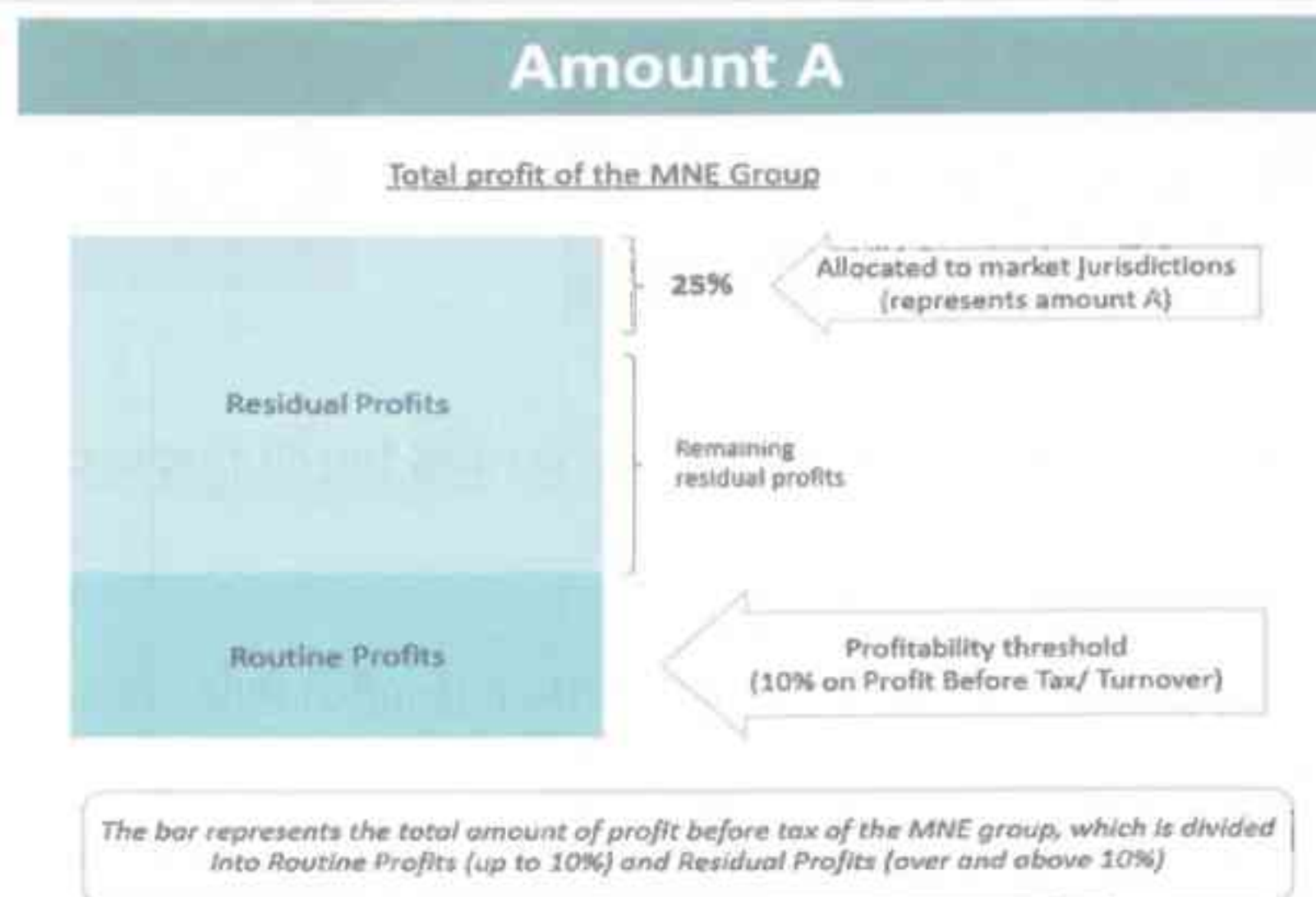
137 countries and jurisdictions have joined the landmark agreement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy on 8th Oct, 2021.

Pillar One: Profit Allocation and Nexus

Pillar One is a significant departure from the standard international tax rules of the last 100 years and moves away from the idea that taxation largely requires a physical presence in a country before that country has a right to tax.

Pillar One will apply to multinational groups (MNC) that have **more than € 20 billion of global turnover, and profitability above 10%** (measured as profits before tax, divided by revenue).

For in-scope groups, **25% of profits above a 10% profit margin** (referred to as "Amount A") will be subject to reallocation to market jurisdictions based on a formulary approach.



Allocation of Amount A is majorly based on the following two factors:

- (i) Nexus Test
- (ii) Revenue Sourcing Rules

Nexus test

Nexus rule applies solely to determine whether a jurisdiction qualifies for profit reallocation under Amount A. These rules will not alter the nexus for any other tax or non-tax purpose. Amount A is allocated to the market jurisdiction only if the nexus exists. To determine whether an MNE in-scope of Amount A satisfies the nexus test for Amount A in a jurisdiction, it will have to apply the revenue sourcing rules to identify the jurisdiction in which revenue arises for purposes of Amount A.

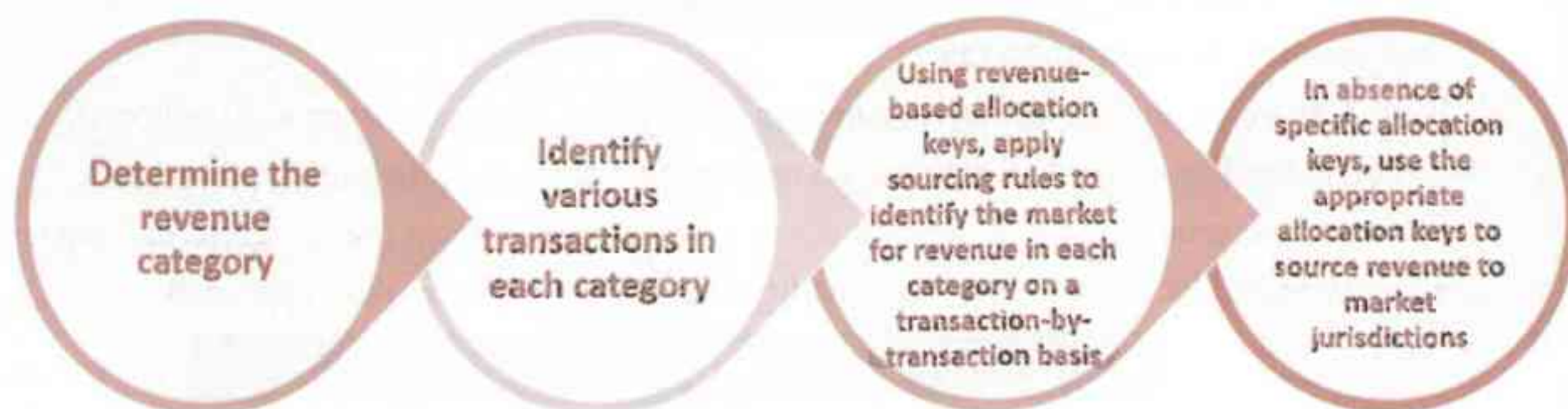
To establish nexus, the **market revenue** thresholds is:

- Greater than or equal to **€1 million** for jurisdiction with annual **GDP >= €40 billion**
- Greater than or equal to **€250,000** for jurisdiction with annual **GDP <= €40 billion**

It transfers taxing rights over residual profits to jurisdictions with business activities regardless of the physical presence.

Revenue sourcing rules

Revenue will be sourced to the end market jurisdictions where goods or services are used or consumed.



Amount B simplifies the existing transfer pricing rules for all taxpayers.

Pillar Two: Global Minimum Taxation

Pillar Two consists of the Global Anti-Base Erosion (GloBE) Rules and a treaty-based Subject to Tax Rule (STTR).

Pillar Two rules subject thousands of multinational groups around the world to a **global minimum tax of 15% (GloBE)**. Critically, every jurisdiction in which the group has operations will need to be looked at separately to see if its effective tax rate falls under 15 %. If so, then a top-up tax will need to be calculated and paid. Additionally, specified payments made to related parties **and taxed below 9%** may be subject to new withholding taxes (STTR). Pillar Two will apply to multinational groups with revenues of at least €750 million.

Subject to Tax Rules (STTR)

Works in priority to GloBE rules, STTR is a treaty-based rule that enables developing countries (source jurisdictions) to tax certain inter-company payments at source which are subject to nominal corporate income tax (at rates below the STTR minimum rate, i.e., 9%)

Applicability – Applicable only to covered payments, by an entity in a developing country, made to a group entity in another country, i.e., connected persons.

(i)



- Applies only if the total sum of covered income arising in the source country exceeds threshold of €250,000 or €1 mn per year (depending on the GDP of source country is above or below €40 bn).

Covered payments constitute Interest, Royalties, Payments for distribution rights for a product or Service, Insurance or reinsurance premiums, Payments of guarantee or financing fees, Rental payments for industrial, commercial, or scientific equipment, Payments for services, etc.

Connected persons are defined to have legal (direct or indirect ownership of more than 50% of the interests) or de facto control relationship.

Specified rate

The STTR specified rate is equal to the difference between 9% and the nominal rate applied in the resident State, further reduced by any source taxation already allocated to the source jurisdiction in accordance with other articles of the treaty.

Country A
(Developing country)



Grant of license to
use Trademark

Royalty payment

Country B
(Nominal tax
rate=1%)



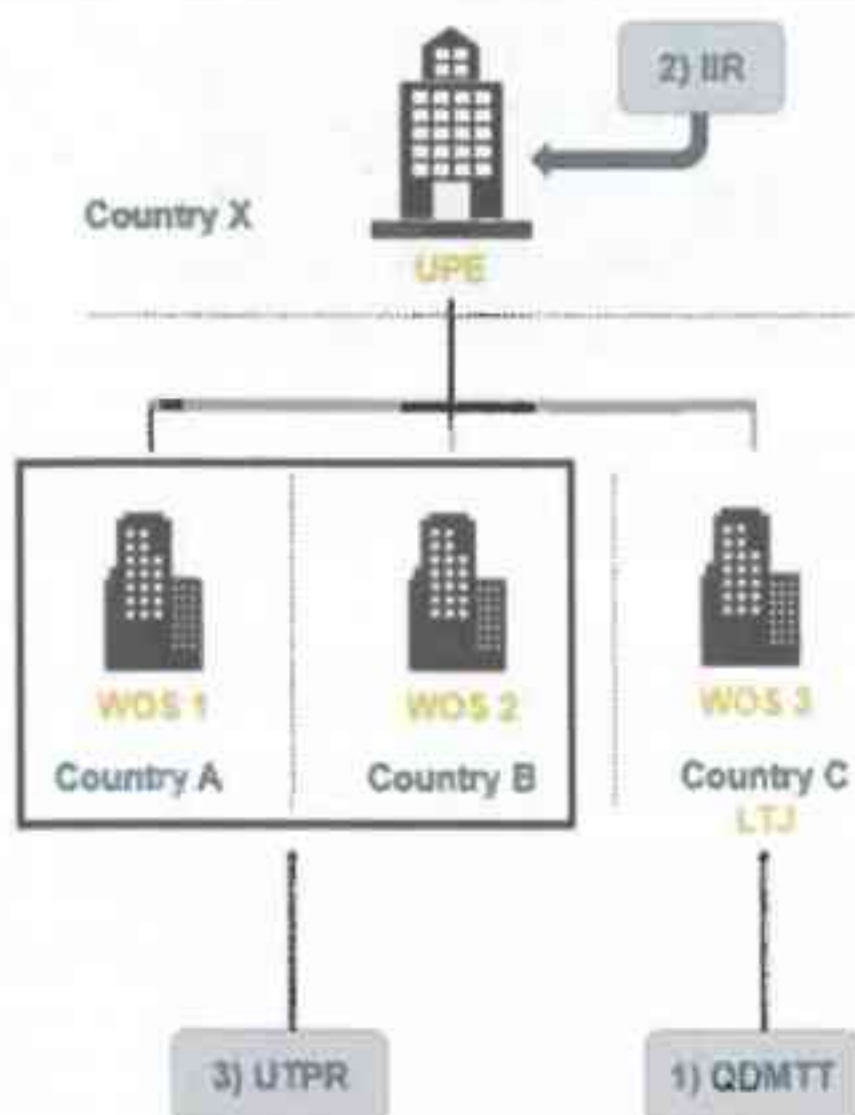
Country A and Country B incorporated STTR provisions under their Tax Treaty		Rate
STTR rate		9%
Nominal tax rate applied in the resident jurisdiction [Country B]		1%
The payor jurisdiction [Country A] retains the 5% withholding tax right under the tax treaty		5%
STTR Specified rate [Country A to tax under STTR]		3%

Pillar Two consists of the following rules (together the GloBE rules):

- (i) **Qualified Domestic Minimum Top-up Tax (QDMTT):** QDMTT imposes a jurisdictional top-up tax on the constituent entity located in a low-taxed jurisdiction (LTJ). It allows the LTJ to collect the top-up tax computed in accordance with the GloBE rules.

QDMTT provides the right to the LTJ to collect the jurisdictional top-up tax by way of the introduction of QDMTT in its domestic tax laws. This would preserve a jurisdiction's primary right of taxation over its own income.

- (ii) **Income Inclusion Rule (IIR):** IIR imposes a top-up tax on a parent entity in respect of the constituent entity located in low-taxed jurisdiction. A Constituent Entity, that is the ultimate parent entity (UPE) of an MNE Group, located in a GloBE implementing jurisdiction that owns (directly or indirectly) an Ownership Interest in a Low-Taxed Constituent Entity at any time during the Fiscal Year shall pay a tax in an amount equal to its Allocable Share of the Top-Up Tax of that Low-Taxed Constituent Entity for the Fiscal Year.
- (iii) **Undertaxed Payment Rule (UTPR):** UTPR imposes deductions or requires an equivalent adjustment to the extent the low tax income of a constituent entity is not subject to tax under an IIR. UTPR is triggered where the UPE jurisdiction does not implement IIR or does not adopt GloBE rules. Thus, UTPR serves as a backstop to IIR. UTPR transfers the levy of top-up tax to other constituent entities of the MNE group located in the jurisdiction where the GloBE rules are implemented.



UPE of an MNE group located in Country X has three wholly owned subsidiaries ("WOS") in Country A, B, and C. Let's say, Country C is a low-taxed jurisdiction ("LTJ"). The priority ranking as per the model GloBE rules prescribes that:

Priority 1 - Where Country C imposes QDMTT in its jurisdiction, the jurisdictional top-up tax shall be imposed on WOS 3 (refer to the diagram above).

Priority 2 - Where Country C does not impose QDMTT in its jurisdiction, the UPE of an MNE Group located in Country X which has implemented IIR under GloBE rules shall be liable to pay a tax in an amount equal to its Allocable Share of the Top-Up Tax of WOS 3 in Country C

Priority 3 - At last where neither Country C nor Country X implements QDMTT or IIR respectively, and Country A and Country B has implemented UTPR under GloBE rules, WOS 1 and WOS 2 shall be liable to pay jurisdictional top-up (pertaining to WOS 3) tax under UTPR in their jurisdictions, i.e., Country A and B respectively.

Other Important Topics under GloBE Rules

- A. **Effective Tax Rate (ETR):** The GloBE rules will operate to impose a top-up tax using an ETR test that is calculated on a jurisdictional basis. If the jurisdictional ETR is below the 15% minimum rate, the jurisdiction is treated as a LTJ and the constituent entities are treated as low-taxed constituent entities (LTCE).

$$\text{ETR} = \frac{\text{Total of Adjusted Covered Taxes of each Constituent Entity located in the jurisdiction}}{\text{Net GloBE Income of the jurisdiction}}$$

Net GloBE Income = GloBE Income of all Constituent Entities - GloBE Losses of all Constituent Entities



B. Jurisdictional Blending: The ETR computation is determined on a jurisdictional blending basis. Jurisdictional blending allows all the profits, losses, and taxes of the Constituent Entities of the MNE Group located in the same jurisdiction to be blended for purposes of the effective tax rate calculation.

Note - For the purpose of determining the applicability of the GloBE Rules, global revenue is considered. However, for determining ETR, the calculation is done on jurisdictional basis.

C. Substance-based Income exclusion (SBIE) or Substance-based carve-outs: The Net GloBE Income for the jurisdiction shall be reduced by the Substance-based Income Exclusion for the jurisdiction to determine the Excess Profit for purposes of computing the Top-up Tax. A substance carve-out based on assets and payroll costs allows a jurisdiction to continue to offer tax incentives that reduce taxes on routine returns from investment in substantive activities, without triggering additional GloBE top-up tax.

D. Top-up Tax: The Jurisdictional Top-up Tax for a jurisdiction for a Fiscal Year is equal to the positive amount, if any, computed in accordance with the following formula:

$$\text{Jurisdictional Top-up Tax} = \text{Excess Profit} \times \text{Top-up Tax Percentage}$$

$$\text{Top up Tax Percentage} = \text{Minimum Rate} - \text{Effective Tax Rate [ETR]}$$

- the Excess Profit for the jurisdiction is the positive amount, if any, computed in accordance with the following formula:

$$\text{Excess Profit} = \text{Net GloBE Income} - \text{Substance Based Income Exclusion}$$

Note: The Top-up tax percentage is calculated based on the aggregate profits, i.e., Net GloBE income. However, it is applied to the excess income, i.e., Net GloBE income - substance based income inclusion in order to provide the benefits of incentives to MNEs.

E. De-minimis Exclusion: The GloBE rules, at the election of the Filing Constituent Entity, provides a jurisdictional exclusion for LTCEs of an MNE Group on meeting the following criterion:

- the Average GloBE Revenue of such jurisdiction is **less than € 10 million**; and
- the Average GloBE Income or Loss of such jurisdiction is a loss or **is less than € 1 million**

The policy intent underlying the above exclusion is to avoid the complexities of a full ETR computation in cases where the amount of any Top Up Tax would not seem to justify the associated compliance and administrative costs.



Notes



➤ What is Foreign Tax Credit (FTC)?

FTC is tax paid in foreign country on income derived in foreign country by an assessee. It can also be tax deducted at source in the foreign country on the source of income generated by a resident in foreign country. Such amount of tax which is paid/deducted in foreign country can be claimed as credit against the tax liability in the country of resident. (Sec 90, 90A, 91)

➤ In which year the credit is available?

The credit of FTC is available in the year in which the income corresponding to such tax has been offered to tax in India. In case the income corresponding to such tax is offered to tax in India in multiple years, the FTC shall be claimed across those years in the same proportion in which the income is offered to tax.

➤ Against which liability credit can be claimed?

The FTC can be claimed against amount of Income Tax, surcharge and cess liability. It, however, cannot be claimed against any liability on account of interest, fee or penalty payable under the Income Tax Act.

If Foreign tax paid is disputed in any manner, the same will be allowed in the year of offering income only if the assessee within **6 months** from the end of month in which dispute is settled, furnishes evidence of settlement of dispute, payment of the disputed tax.

➤ What is the mechanism to compute the amount of FTC available?

The FTC shall be computed for each source of income arising from each country. The credit allowable shall be lower of tax payable under the Income Tax Act on such income and actual foreign tax paid on such income. In case where the foreign tax paid exceeds the amount of tax payable according to the DTAA, such excess shall be ignored.

➤ What documents are required to claim FTC?

A Statement of computation of Income of that country outside India and foreign tax deducted or paid on such income in **Form No. 67**;

A certificate or statement specifying the Nature of Income and the manner of tax deducted therefrom or paid by the assessee from -

- The tax authority of that country or
- The person responsible for deduction of such tax or
- The assessee.

In such case, the assessee also need to provide Acknowledgement of online payment of tax or challan for payment of tax where the payment has been made by the assessee.

Proof of deduction of tax where the tax has been deducted.



- Whether the FTC can be claimed if tax is payable under Minimum Alternative Tax (MAT)/AMT?
Yes, FTC shall be allowed against tax payable under MAT/AMT in the same manner as it is allowable under normal provisions of the Income Tax Act.

However, where the FTC available against tax payable under MAT/AMT exceeds the tax credit available under normal provisions of the Act, the excess shall be ignored.

- What conversion rate should be adopted?

For the purpose of converting foreign currency into Indian rupee, **TTBR of SBI** on the **last day** of the **previous month** in which the tax has been paid or deducted shall be adopted.

- What is the timeline to submit the claim of FTC?

Form No. 67 and a certificate or statement as referred above shall be furnished online upto due date of u/s 139(1).

Provided that where the return has been furnished u/s 139(8A), the statement in Form No. 67 and the certificate or the statement to the extent it relates to the income included in the updated return, shall be furnished on or before the date on which such return is furnished.

Duraiswamy Kumaraswamy [2024] (Madras)

Can the claim for the foreign tax credit be accepted, if a taxpayer inadvertently fails to file Form 67 along with return of income though such form is filed before receipt of intimation u/s 143(1)? Rule 128(9) provides that the statement in Form No. 67 is required to be furnished on or before the due date specified for furnishing the return of income u/s 139(1), in the manner specified for furnishing such return of income.

the High Court held that the return was filed without Form 67, however the same was filed before intimation u/s 143(1) was issued. The filing of Form 67 for foreign tax credit in terms of Rule 128 is only directory in nature. The rule is only for the implementation of the provisions of the Act and it will always be directory in nature. Therefore, in the present case, the claim of foreign tax credit cannot be denied.

Note: Rule 128(9) was amended w.e.f. 1.4.2022 to provide that the statement in Form No. 67 is required to be furnished on or before the end of the assessment year relevant to the previous year in which the income has been offered to tax or assessed to tax in India and the return for such assessment year has been furnished within the time specified u/s 139(1) or 139(4).



- Rule 115: Rate of exchange for conversion into rupees of income earned in foreign currency shall be the TTBR as on the specified date.

"Specified date" means—

- (a) Salary Income - last day of the month immediately preceding the month in which the salary is due, or is paid in advance or in arrears.
- (b) Interest on securities- last day of the month immediately preceding the month in which the income is due.
- (c) IFHP, PGBP [other than point (d)] and IFOS (not being income by way of dividends and Interest on securities)- last day of the previous year of the assessee.
- (d) "PGBP" in the case of a NR engaged in the business of operation of ships- last day of the month immediately preceding the month in which such income is deemed to accrue or arise in India.
- (e) Dividends- last day of the month immediately preceding the month in which the dividend is declared, distributed or paid by the company.
- (f) Capital gains- the last day of the month immediately preceding the month in which the capital asset is transferred.

Note: Provided that the specified date, in respect of income referred to in (a) to (f) payable in foreign currency and from which tax has been deducted at source under rule 26, shall be the date on which the tax was required to be deducted under TDS chapter.

- Rule 26 - Rate of exchange for the purpose of TDS at source on income payable in foreign currency
- For the purpose of deduction of tax at source on any income payable in foreign currency, the rate of exchange for the calculation of the value in rupees of such income payable—
- (i) To an assessee outside India;
 - (ii) To a Unit of IFSC;
 - (iii) By a Unit of IFSC to an assessee in India,
- shall be the TTBR of such currency as on the date on which the tax is required to be deducted at source under the TDS Chapter by the person responsible for paying such income.





Some Remaining Case Laws

Honda Siel Cars India Ltd. [2017] (SC):

Whether technical fee paid under a technical collaboration agreement (TCA) for setting up a joint venture company in India is to be treated as revenue or capital expenditure, where, upon termination of the agreement, the joint venture would come to an end?

SC observed that if a limited right to use technical know-how is obtained for a limited period for improvising existing business, the expenditure is revenue in nature. However, if technical know-how is obtained for setting up a new business, the position may be different. There is no single principle or test for determining the nature of expenditure; it is a question to be answered based on the circumstances in each case. In the given facts, the very purpose of the TCA was to set up the JV. The collaboration included not only transfer of technical information, but, complete assistance, actual, factual and on the spot, for establishment of plant, machinery, etc. so as to set up a manufacturing unit. Upon termination of TCA, the joint venture itself would come to an end.

Technical fee paid under a TCA for setting up a JV company in India is to be treated as capital expenditure, since upon termination of TCA, the JV itself would come to an end.

Saurashtra Cement Ltd. (2010)(SC)

What is the nature of liquidated damages received by a company from the supplier of plant for failure to supply machinery to the company within the stipulated time a capital receipt or a revenue receipt?

- » The damages were directly and intimately linked with the procurement of a capital asset i.e., the cement plant, which lead to delay in coming into existence of the profit-making apparatus.
- » It was not a receipt in the course of profit earning process.

Therefore, the amount received by the assessee towards compensation for sterilization of the profit earning source, is not in the ordinary course of business, hence it is a capital receipt in the hands of the assessee.

Venkatesh Premises Co-operative Society Ltd. [2018] (SC)

The doctrine of mutuality is based on the common law principle that a person cannot make a profit from himself. Accordingly, the transfer charges, non-occupancy charges common amenity fund charges and other charges are exempt owing to application of the doctrine of mutuality. As these charges are collected from members and applied for the benefit of members only so its exempt due to mutuality.

Madras Gymkhana Club (2010)(Mad.)

Interest earned from investment of surplus funds in the form of fixed deposits with institutional members does not satisfy the principle of mutuality and hence cannot be claimed as exempt on this ground.

Secunderabad Club [2023](SC)

Does the principle of mutuality apply to interest income derived from fixed deposits made with the banks by the clubs if such banks are members of the club?

The deposit of surplus funds earned by the club, in banks which are members of the club, the principle of mutuality applies till the stage of deposit of funds and would lose its application, once the funds are deposited as fixed deposit in the banks. This is because the funds would be exposed to commercial banking operations, which means that the deposits could be used for lending to third parties and earning a higher interest thereon by paying a lower interest rate on the fixed deposits to the club.

The bank utilising the funds of the club deposited in FD receipts for their banking business would completely rupture the "privity of mutuality", and as a result, the element of complete identity between the contributors and participators would be lost.

Conversely, when a club provides its facilities to members who contribute to its income, the principle of mutuality applies due to the identity between contributors and participants. However, where the same facilities are offered to non-members or the public to generate additional income, it transforms into a commercial transaction, and the principle of mutuality no longer applies. Accordingly, SC held that the interest income earned on FD made with the banks by club has to be treated like any other income from other sources within the meaning of section 2(24). It would be liable to be taxed under the provisions of the Income-tax Act.

Trans Asian Shipping Services (P) Ltd (2016) (SC)

Income generated from the qualifying ship is eligible to tax as per Tonnage Tax scheme. Since it has exercised the requisite option in this behalf and submitted valid certificate in respect of such qualifying ship. In addition to the income from qualifying ship, it has also earned income from "slot charter" arrangement in other ships. SC noted that a company would regard as operating a ship "if it operates any ship whether owned or chartered by it in an arrangement such as slot charter, space charter or joint charter". Thus, even an arrangement such as slot charter would be regarded as operating a ship.

Section 115VG(4) also talks about "deemed tonnage" and explanation mentions that purchase of such slot charter shall be treated as deemed tonnage. SC held that the requirement of producing a certificate would not apply when entire ship is not chartered and the arrangement pertains only to purchase of slots. Accordingly, income from slot charter arrangement in other ships can be computed applying the special provisions as per Tonnage Tax scheme.

KBD Sugars and Distilleries Ltd. [2023](SC)

Can a resulting entity set off and carry forward the losses of the dysfunctional unit of demerged entity? ITAT opined that the words used 'on a going concern basis' in sec. 2(19AA)(vi) only means that the transfer should be based on a 'going concern', and it does not mean that the undertaking being transferred should be a 'going concern' as on the date of transfer.

'Scheme of demerger', which approved by Court, clearly establishes the fact that the transfer of the undertaking is indeed on a 'going concern basis'. The assets, liabilities, employees, debts, obligations, rights, etc., of the undertaking, immediately prior to the demerger, stand entirely vested with the assessee upon 'demerger'. This amounts to 'transfer of the undertaking on a going concern basis'.

A simple reading of the same makes it very clear that the assessee is eligible for the benefits under section 72A(4). The Act does not state that the undertaking being demerged ought to be a going concern at the time of demerger. It only states that the undertaking being demerged should stand transferred in a manner similar to the manner in which a 'going concern' is transferred. Accordingly, the HC held that if a unit were running and profitable, the same would not be available for demerger. It would be incongruous to construe section 2(19AA)(vi) to mean a running unit. The scheme of demerger had been approved by the HC's. Therefore, the assessee was entitled to set off the brought forward losses u/s 72A(4). The SC affirmed the decision of the High Court.

➤ Sec 170A: Effect of order of tribunal or court in respect of business reorganisation

In a case of business reorganisation, where prior to the date of order of a HC or tribunal or an Adjudicating Authority in IBC 2016, as the case may be, any return of income has been furnished by the successor u/s 139 for any AY relevant to the PY to which such order applies, such successor shall furnish, within a period of **6 months from the end of the month in which the said order was issued**, a modified return in **Form ITR-A electronically**, as per order.

Assessment on the basis of Modified Return

Completed Assessment	A.O. has to pass an order modifying the assessment or reassessment proceedings as per modified return
Pending Assessments	A.O. has to proceed to complete the assessment or reassessment proceedings as per modified return.



"Business reorganisation" means amalgamation or demerger or merger of business of one or more persons.

E.g.: If A Ltd. merges with B Ltd. with effect from 1.4.22 vide order of the HC dated 1.11.2023, and B Ltd. has already filed its return of income for the A.Y.23-24 on 30th October, 23, then, B Ltd. has to file a modified return for A.Y.23-24 in accordance with and limited to the Order of the HC on or before 31st May, 24.

➤ **Sec. 89A: Relief from Taxation in Income from retirement benefit a/c maintained in a notified country**

Where a specified person has income accrued in a specified account, such income shall be taxed in such manner and in such year as may be prescribed.

Explanation:

- (i) **Notified country:** Canada, USA and UK
- (ii) **Specified account:** An account maintained in a notified country by the specified person in respect of his retirement benefits and the income from such account is not taxable on accrual basis but is taxed by such country at the time of withdrawal or redemption.
- (iii) **Specified person:** A person resident in India who opened a specified account in a notified country while being non-resident in India and resident in that country.

Option to be exercised by specified person - Where a specified person has income accrued in a specified account(s) during P.Y.21-22 or thereafter, then, at the option of the specified person, such income would be included in the total income of the PY in which income from the said specified account(s) is taxed at the time of withdrawal or redemption, as the case may be, in the notified country. The option has to be exercised for all the specified accounts maintained by the specified person.

Exclusions from total income of specified person - Where the option has been exercised by a specified person, the total income of the specified person for the PY in which income is taxable would not include the income which:

- has already been included in the total income of such specified person in any of the earlier PY's during which such income accrued and tax thereon has been paid under the Act; or
- was not taxable in India, in the PY during which such income accrued, on account of,
 - ☞ such specified person being a NR, or R but NOR, during that PY; or
 - ☞ application of the DTAA, if any.

Foreign tax, if any, paid on such income would be ignored for the purposes of computation of the foreign tax credit under Rule 128.



Option once exercised cannot be withdrawn - The option has to be exercised in Form 10-EE electronically on or before the due date u/s 139(1). The option once exercised for a specified account(s) in respect of a PY would apply to all subsequent PY's and cannot be subsequently withdrawn (except in case where the specified person becomes a NR in any subsequent PY).

Consequences when specified person becomes NR in a subsequent PY - In case the specified person, after exercising option for any PY, say, P.Y. 22-23, becomes a NR during any subsequent PY, say, P.Y. 25-26, (referred to as the relevant PY) then, the option exercised above would be deemed to have never been exercised with effect from the relevant PY, i.e., from P.Y.25-26. The income which has accrued in the specified account(s) during the PY, beginning with the PY in which option was exercised (P.Y.2022-23) till the PY immediately preceding the relevant PY (i.e., upto P.Y.2024-25) would be taxable during the PY immediately preceding the relevant PY (i.e., in the P.Y.2024-25). The tax on such income has to be paid on or before the due date for furnishing the return of income for the relevant PY (due date for P.Y. 2025-26).

