CA FINAL (May 2026)

GROUP II – PAPER 4

DIRECT TAX LAWS & INTERNATIONAL TAXATION

SUGGESTED ANSWERS

(Series 4)

PART – I (MCQs)

MCQ – 2 marks each														
1.	**2.**	**3.**	**4.**	**5.**	**6.**	**7.**	**8.**	**9.**	**10.**	**11.**	**12.**	**13.**	**14.**	**15.**
D	C	B	C	A	C	C	D	C	D	B	C	D	D	C

PART – II (Descriptive Answers)

Answer 1

Computation of total income of Rainbow Ltd. for A.Y.2026-27

	Particulars	₹	₹
I	**Profits & Gains of Business of Profession**		
	Net Profit as per Statement of Profit & Loss		27,22,000
	Add: Items debited but to be considered separately or to be disallowed		
	- **Interest on money borrowed for purchase of land**	2,00,000	
	[As per section 36(1)(iii), interest on borrowed capital till the asset is put to use has to be capitalized. Hence, interest on moneys borrowed is not allowable under section 36(1)(iii). Since it is already debited to statement of profit and loss, the same has to be reduced.]		
	- **Commission paid in February, 2026**	Nil	
	[Commission paid in February, 2026 after deduction of tax is allowable as deduction during the P.Y. 2025-26 since TDS has been deposited before the due date of filing return of income. Since commission is already debited to statement of profit and loss, no adjustment is required.]		
	- **Commission paid in March, 2026**	37,500	
	[30% of commission paid in March 2026 on which TDS was deducted and paid in subsequent year would be disallowed during the P.Y. 2025-26 and would be allowed as deduction in the year in which such tax has been paid. Hence, 30% of commission debited to statement of profit and loss would be added back.]		

	- **Travelling expenses on foreign tour in connection with new line of business** [Travelling expenses incurred on foreign tour of a director for initiating a new line of business is a capital expenditure. The same is, therefore, not deductible under section 37(1). Since it is already debited to statement of profit and loss, the same has to be reduced.]	90,000	
	- **Interest on term loan converted into new term loan** [Under section 43B, interest on loan due to any scheduled bank, etc. is allowed as deduction, if such interest is actually paid irrespective of the method of accounting followed by the assessee. Conversion of arrear interest into a fresh loan by a bank cannot be considered as actual payment of interest. However, the amount of funded interest (i.e., converted loan) actually paid is allowable as deduction. Hence, out of ₹ 3 lakhs, only ₹ 50,000, being the funded interest was actually paid which is allowable as deduction while computing business income of P.Y.2025-26. The balance of ₹ 2,50,000 has to be added back.]	2,50,000	
	- **Excess depreciation provided on EPABX & Mobile phones not allowable as deduction** [EPABX and mobile phones are not computers and therefore, are not entitled to depreciation @ 40%. It was so held by the Kerala High Court in Federal Bank Ltd. v. ACIT (2011) 332 ITR 319. Therefore, EPABX and mobile phones would be entitled to depreciation of ₹ 6,75,000, calculated by applying the rate of 15%, being the general rate applicable to plant and machinery, on the cost of ₹ 45,00,000 (₹ 18,00,000 × 100/40). The excess depreciation of ₹ 11,25,000 (being ₹ 18,00,000 – ₹ 6,75,000), debited to statement of profit and loss, has to be added back.]	11,25,000	
	- **Contribution to S Ltd. (wholly owned subsidiary company)** [Contribution to a wholly owned subsidiary company for construction of a school for the benefit of its employees is allowable under section 37(1).]	-	
	- **Provision for gratuity ₹ 6,00,000** **Less: Gratuity paid ₹ 1,50,000** [Under section 40A(7), no deduction is allowed in respect of any provision made for the payment of gratuity to the employees on retirement or termination of employment for any reason. However, gratuity actually paid is admissible as deduction. Therefore, provision for gratuity of ₹ 6,00,000 is to be disallowed. Actual gratuity paid ₹ 1,50,000 debited to provision for gratuity account is allowable. Hence, only the net sum of ₹ 4,50,000 has to be added back.]	4,50,000	
	- **Depreciation on commercial vehicle** [Depreciation on commercial vehicle has been calculated @15% and, consequently, ₹ 1,20,000 has been debited to	60,000	22,12,500

	statement of profit and loss. Since it was acquired in March 2026 only, 50% of normal depreciation is allowable. The excess depreciation of ₹ 60,000 is, hence, disallowed.]		
			49,34,500
	Less: Items credited but to be considered separately and those not charged but to be allowed		
	- **Long term capital gain on sale of equity shares** [Taxable under the head "Capital gains"]	3,00,000	
	- **Bonus paid on 15.11.2025 in respect of P.Y. 2024-25 disallowed last year but allowable in P.Y. 2025-26** [Provision for bonus for the previous year 2024-25 would have been disallowed under section 43B for non- payment by due date for filing of return of income for assessment year 2025-26. Payment of bonus made after the said date is allowed in the year of actual payment. However, such deduction allowable in the year of payment is subject to the provisions of section 40A(3). Hence, the sum of ₹ 34,000, being bonus paid by bearer cheque shall not be allowed as deduction in the year of payment.]	64,000	
	- **Dividend from P Ltd.** [Dividend is taxable under the head "Income from Other Sources"]	1,00,000	4,64,000
			44,70,500
II	**Capital Gains**		
	Long term capital gain on sale of equity shares [Taxable @12.5% on sum exceeding ₹ 1,25,000]		
	Sale consideration [10,000 x ₹ 130]	13,00,000	
	Less: Cost of acquisition	11,00,000	2,00,000
	Higher of - Actual cost of ₹ 10 lakhs [10,000 x 100] - Lower of fair market value as on 31.1.2018 of ₹ 11 lakhs or sale consideration of ₹ 13 lakhs		
III	**Income from Other Sources**		
	Dividend from P Ltd. [Dividend is taxable under the head "Income from Other Sources"]		1,00,000
	Total Income		**47,70,500**

Answer 2A

Computation of MAT payable by Alpha and Beta Tyres Limited under section 115JB

Particulars	₹	₹
Net profit as per statement of profit and loss		20,00,00,000
Add: Net profit to be increased by the following amounts as per Explanation 1 to section 115JB(2):		

Depreciation	18,00,00,000	
Interest charged for delay in remittance of TDS	20,00,000	
[As per Explanation 2 to section 115JB, income-tax shall include, any interest charged under the Act. Therefore, interest on delay in remittance of TDS has to be added back]		18,20,00,000
		38,20,00,000
Less: Net profit to be decreased by the following amounts as per Explanation 1 to section 115JB(2):		
Depreciation other than depreciation on revaluation of assets [₹ 18 crore – ₹ 3 crore]	15,00,00,000	
Share income from Association of Persons	50,00,000	
[Share income of company in AOP has to be reduced while computing the book profit, since no income-tax is payable by the company on share income in AOP, as the AOP is chargeable to tax at Maximum Marginal Rate]		
Amount withdrawn from revaluation reserve [₹ 6 crore] to the extent it does not does not exceed depreciation on revaluation of assets [₹ 3 crore]	3,00,00,000	
Brought forward business loss of ₹ 8 crore [₹ 3 crore + ₹ 5 crore] and unabsorbed depreciation of ₹ 3 crore [₹ 1 crore + ₹ 2 crore]	11,00,00,000	
[Since Alpha and Beta Tyres Limited is a company against which an application for corporate insolvency resolution process has been admitted by NCLT under section 7 of the Insolvency and Bankruptcy Code, 2016, the amount of total loss brought forward (including unabsorbed depreciation) is allowed to be reduced from the book profit for the purposes of levy of MAT under section 115JB].		29,50,00,000
Book profit computed in accordance with Explanation 1 to section 115JB(2)		8,70,00,000
Add: Items credited to OCI that will not be reclassified to profit or loss:		
Re-measurement of defined employee benefit plan	50,00,000	
Revaluation surplus of property, plant and equipment ₹ 1 crore [Book profit not to be increased by revaluation surplus for assets]	Nil	50,00,000
		9,20,00,000
Add: One-fifth of Transition amount [Credit Balance]		
Transition amount	5,00,00,000	
Less: Amounts to be excluded from transition amount		
Capital Reserve	50,00,000	
	4,50,00,000	
One-fifth of ₹ 4,50,00,000		90,00,000
Book Profit for levy of MAT		**10,10,00,000**
Computation of MAT		**₹**
MAT on book profit under section 115JB = 15% of ₹ 10,10,00,000		1,51,50,000

Add: Surcharge@12% (since book profit exceeds ₹10 crore)	18,18,000
	1,69,68,000
Add: Health and education cess@4%	6,78,720
MAT liability	**1,76,46,720**

Computation of MAT credit to be carried forward

Particulars	₹
MAT liability	1,76,46,720
Income-tax computed as per the normal provisions of the Act	73,00,000
Since the income-tax liability computed as per the regular provisions of the Income-tax Act, 1961 is less than MAT payable, the book profit of ₹ 10,10,00,000 would be deemed to be the total income and tax is leviable@15%: **The total tax liability is ₹ 1,76,46,720.**	
Computation of tax credit to be carried forward:	
Tax payable on deemed total income	1,76,46,720
Less: Income-tax payable as per the normal provisions of the Act	73,00,000
Tax credit in respect of tax paid on deemed income	**1,03,46,720**

Answer 2B

AI Kuber Ltd., a company incorporated in Dubai, would be resident in India in the P.Y. 2025-26, if its place of effective management is in India in that year.

For determining the POEM of AI Kuber Ltd., the important criteria is whether the company is engaged in active business outside India or not.

A company would be said to be engaged in "Active Business Outside India" (ABOI) for POEM, if

- its passive income is not more than 50% of its total income; and
- less than 50% of its total assets are situated in India; and
- less than 50% of total number of employees are situated in India or are resident in India; and
- the payroll expenses incurred on such employees is less than 50% of its total payroll expenditure.

AI Kuber Ltd. would be regarded as a company engaged in active business outside India for POEM purpose only if it satisfies all the four conditions cumulatively.

Condition 1: The passive income of AI Kuber Ltd. should not be more than 50% of its total income.

Total income of AI Kuber Ltd. is ₹ 2,980 crores Passive income is the aggregate of, -

(i) income from the transactions where both the purchase and sale of goods is from/to its associated enterprises i.e., ₹ 125 crores; and

(ii) income by way of, inter alia, interest and dividend i.e., ₹ 880 crores;

Passive Income of AI Kuber Ltd. is ₹ 1,005 crores (i.e., ₹ 125 crores + ₹ 880 crores) Percentage of passive income to total income = ₹ 1,005 crore/ ₹ 2,980 crore x 100 = **33.72%**

Since passive income of AI Kuber Ltd. i.e., 33.72% is not more than 50% of its total income, the **first condition is satisfied.**

Condition 2: AI Kuber Ltd. should have less than 50% of its total assets situated in India

Value of total assets of AI Kuber Ltd. is ₹ 6,150 crores [₹ 1,500 crore + ₹ 225 crore + ₹ 800 crore + ₹ 650 crore + ₹ 1,075 crore + ₹ 1900 crore].

Value of total assets of AI Kuber Ltd. in India is ₹ 2,525 crores [₹ 1,500 crore + ₹ 225 crore + ₹ 800 crore]

Percentage of assets situated in India to total assets = ₹ 2,525 crores/₹ 6150 crores x 100 = **41.06%**

Since the value of assets of AI Kuber Ltd. situated in India is less than 50% of its total assets, the **second condition for ABOI test is satisfied.**

Condition 3: Less than 50% of the total number of employees of AI Kuber Ltd. should be situated in India or should be resident in India

Number of employees working in India is 70.

Total number of employees of AI Kuber Ltd. is 160 [70+90].

Percentage of employees working in India to total number of employees is 70 x 100/160 = **43.75%**

Since the number of employees of AI Kuber Ltd. working in India is less than 50% of its total number of employees, the **third condition for ABOI test is satisfied.**

Condition 4: The payroll expenses incurred on employees situated in India or resident in India should be less than 50% of its total payroll expenditure

Payroll expenditure on employees in India is ₹ 940 crores

Total payroll expenditure of AI Kuber Ltd. is ₹ 2190 crores [₹ 940 crore + ₹ 1250 crore]. Percentage of payroll expenditure on employees in India to total payroll expenditure is **42.92%**, being ₹ 940 crores x 100/₹ 2190 crores.

Since payroll expenditure on employees of AI Kuber Ltd. in India is less than 50% of its total payroll expenditure, the **fourth condition for ABOI test is satisfied.**

Since AI Kuber Ltd. satisfies all the above four conditions cumulatively, **AI Kuber Ltd. has passed the Active Business Outside India (ABOI) test.**

POEM of a company engaged in active business outside India shall be presumed to be outside India, if the majority of the board meetings are held outside India.

Since AI Kuber Ltd. is engaged in active business outside India in P.Y. 2025-26 & **majority of its board meetings i.e., 4 out of 7, were held outside India, POEM of AI Kuber Ltd. would be outside India.**

Therefore, AI Kuber Ltd. would be non-resident in India for the P.Y. 2025-26.

Answer 3A

As per section 115TD, the accreted income of Ramnarayan Foundation trust, a charitable trust, registered under section 12AA would be chargeable to tax at the rate of 34.944% [30% plus surcharge @12% plus cess@4%] on non-distribution of assets on dissolution to another trust registered u/s 12AB within 12 months from the end of month in which the dissolution takes place.

Computation of accreted income and tax liability in the hands of Ramnarayan Foundation trust on dissolution

Particulars	Amount (₹)
Aggregate FMV of total assets as on the specified date (date of dissolution) **[See Working Note 1]**	61,12,500
Less: Total liability computed in accordance with the prescribed method of valuation **[See Working Note 2]**	9,00,000
Accreted Income	52,12,500
Less: Value of assets distributed within a period of 12 months from the end of the month of dissolution	8,00,000

	44,12,500
Tax Liability@34.944% of ₹ 44,12,500	15,41,904
Tax Liability (rounded off)	**15,41,900**
Working Notes:	
(1) Aggregate FMV of total assets on the date of dissolution	
- **Land and building,** FMV as on specified date has to be considered and one-fourth of the value of land and building to be ignored, since acquired out of agricultural income exempt u/s 10(1) [₹ 50 lakhs x 3/4]	37,50,000
- **Equity shares - quoted [market value on the date of dissolution]**	18,00,000
- **Equity shares – unquoted in Z Ltd. [**Since the trust was registered only on 1.4.2013 and benefit of section 11 and 12 was available to the trust only from A.Y.2014-15, relevant to P.Y.2013-14, the value of 50% of the unquoted shares purchased in P.Y.2010-11, in respect of which benefit under sections 11 and 12 was not allowed, has to be ignored for computing accreted income]	4,12,500
Value of unquoted shares = ₹ 4,12,500 [50% of ₹ 8,25,000 (Book value of assets (other than bullion, jewellery) of Z Ltd. i.e., ₹ 60,00,000 + Market value of bullion and jewellery of Z Ltd. i.e., ₹ 30,00,000 – Liabilities of ₹ 35,00,000 x paid up value of shares i.e., ₹ 1,50,000/total amount of paid up equity share capital as shown in the Balance Sheet of ₹ 10,00,000)]	
- Cash	1,00,000
- Bank Balance	50,000
	61,12,500
(2) Total liability	
- Corpus Fund of ₹ 6,00,000 [not includible]	Nil
- Reserves and Surplus ₹ 3,00,000 [not includible]	Nil
- Loan taken for purchase of land and building	9,00,000
- Loan taken for purchase of unquoted shares [Since the entire loan is in relation to unquoted shares acquired during the year 2010-11, when the trust was not eligible for exemption under section 11 and 12, the same is not deductible]	Nil
	9,00,000

Answer 3B

Computation of total income of Miss Sapna

Particulars	₹	₹
Salaries [Indian Income]		
Basic Salary (₹ 45,000 x 12 months)	5,40,000	
Dearness Allowance (10% of basic salary of ₹ 5,40,000)	54,000	
Transport Allowance (₹ 8,000 x 12) [Fully taxable]	96,000	
Medical Allowance (₹ 3,500 x 12) [Fully taxable]	42,000	
Gross Salary	7,32,000	
Less: Standard deduction u/s 16		
Lower of actual salary or ₹ 50,000	50,000	
Net Salary		**6,82,000**

Income from Other Sources [Foreign Income]		
Income from lectures in foreign university [₹ 7,92,000 plus tax deducted at source of ₹ 1,08,000]		9,00,000
Gross Total Income		**15,82,000**
Less: Deduction under Chapter VIA		
Under section 80CCC – Contribution to approved Pension Fund of LIC	15,000	
Under section 80D – Medical insurance premium of her father, being a resident senior citizen, ₹ 35,000 [being 1/5th of the lumpsum premium of ₹ 1,75,000 paid for 5 years] fully allowable, even though he is not dependent on her, since the same does not exceed ₹ 50,000	35,000	50,000
Total Income		**15,32,000**

Computation of tax liability of Miss. Sapna		
Particulars		**₹**
Tax on total income [₹ 1,59,600 (i.e., 30% of ₹ 5,32,000) plus ₹ 1,12,500 (Tax on income of ₹ 10 lakh)]		2,72,100
Add: Health and education cess @4%		10,884
Tax Liability		2,82,984
Average rate of tax in India [i.e., ₹ 2,82,984/₹ 15,32,000 x 100]	18.472%	
Tax rate in foreign country [1,08,000/9,00,000] x 100	12%	
Deduction under section 91 on ₹ 9,00,000, being the doubly taxed income@ 12% [being the lower of Indian rate of tax (18.472%) and foreign tax rate (12%)]		1,08,000
Tax Payable		**1,74,984**
Tax Payable (rounded off)		1,74,980

Answer 4A

(i) Section 194A requiring deduction of tax at source on any income by way of interest, other than interest on securities credited or paid to a resident, excludes from its scope, income credited or paid by a firm to its partner. However, **section 195 which requires tax deduction at source on payment to non-residents,** does not provide for any exclusion in respect of payment of interest by firm to its non-resident partner. Further, since FTS is deemed to accrue or arise in India on account utilisation of services for a project in India and chargeable to tax in the hands of Mr. Vikas, TDS is also required to be deducted on FTS payment. Accordingly, **tax has to be deducted under section 195 @30% plus HEC@4% being rate in force on both interest on capital and FTS (assuming it is not in pursuance of Central Government agreement).**

As per section 10(2A), share of profit received by partner from the total income of firm is exempt from tax. Therefore, the **share of profit paid to non-resident Indian is not liable for tax deduction at source.**

However, section 195(6) provides that the person responsible for paying any sum, whether or not chargeable to tax, to a non- corporate non-resident or to a foreign company shall be required to furnish the information relating to payment of such sum in the form and manner prescribed under Rule 37BB.

(ii) As per section 239A, where under a DTAA, the tax deductible on any income, other than interest, under section 195 is to be borne by the person by whom the income is payable, and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, such person can file an application before the Assessing Officer for refund of such tax within 30 days from the date of payment of such tax.

In this case, Pal & Co. has to file an application before the Assessing Officer for refund of such tax within 30 days from the date of payment of such tax.

The CBDT has, vide Circular No.7/2007 dated 23.10.2007, which laid down the procedure for refund of tax deducted at source under section 195 of the Income-tax Act, 1961 to the person deducting tax at source from the payment to a non-resident. The said Circular allowed refund to the person making payment under section 195, inter alia, when there occurs payment of tax at a higher rate under the Income-tax Act, 1961 while a lower rate is prescribed in the relevant double taxation avoidance treaty entered into by India.

Hence, M/s Pal & Co., India can claim tax refund of excess tax deducted at source under section 195 where tax has been deducted at source at the rate of 30% provided under the Income-tax Act, 1961 while a lower rate i.e., 10% is prescribed under the DTAA with Country 'X', only if Pal & Co. has borne the tax. Otherwise, refund can be claimed by the non-resident, Mr. Vikas.

Answer 4B

Rollback year means any previous year, falling within the period **not exceeding four previous years, preceding first of five consecutive previous years for which advance pricing agreement is valid.**

The application for advance pricing agreement may be filed at any time before the first day of the previous year relevant to the first assessment year for which the application is made, in respect of transactions which are of a continuing nature from dealings that are already occurring; or before undertaking the transaction in respect of remaining transactions.

Accordingly, the **APA application filed on 15th March 2025 would be in respect of five previous years beginning with P.Y. 2025-26** relevant to the A.Y. 2026-27.

Consequently, APA entered by ABC (P) Ltd. can provide for determining ALP in relation to international transaction entered during **rollback years i.e., from A.Y. 2022-23 to A.Y. 2025-26** subject to satisfaction of certain conditions.

In present case, **since A.Y. 2020-21 and A.Y. 2021-22 fall beyond said four year period, ABC (P) Ltd. cannot avail roll back benefit in respect of these years.** From A.Y. 2022-23 - A.Y. 2025-26, the applicability of rollback provisions would be as follows:

Rollback year	Applicability of rollback provisions
A.Y. 2022-23	**Yes, rollback provisions are applicable**.
A.Y. 2023-24	**Yes, rollback provisions are applicable** even if ALP adjustment was reduced to addition of ₹ 300 lakhs as against addition of ₹ 500 lakhs originally determined by the TPO on account of APA, since such reduction in the amount of ALP adjustment **does not result in reducing the total income** or increasing the total loss, as **declared in the return of income** of the said year by ABC (P) Ltd.
A.Y. 2024-25	**Yes, roll back provisions are applicable**, since ITAT has only set aside the order for fresh consideration and the matter has not reached finality.
A.Y. 2025-26	**No, rollback provisions are not applicable**, since the **return was filed belatedly** u/s 139(4) on 29.12.2025.

Answer 5A

(i) As per section 54EC, where the **capital gain arising from the transfer of a long-term capital asset, being land or building or both, is invested in the long-term specified asset, being the bonds issued by the National Highways Authority of India (NHAI) or the Rural Electrification Corporation Limited (RECL)** or any other bond notified by the Central Government in this behalf, at any time **within a period of six months after the date of such transfer, the amount of such capital gain shall not be charged to tax, to the extent of ₹ 50 lakhs.**

Section 50 is a special provision for computation of capital gains in the case of depreciable asset, and has limited application in the context of computation of capital gains to the extent that the provisions of sections 48 and 49 would apply with the modifications stated thereunder. It does not deal with exemption which is provided in a totally different provision i.e., section 54EC.

Section 54EC does not make any distinction between depreciable and non-depreciable asset for the purpose of re-investment of capital gains in long term specified assets for availing the exemption thereunder. Further, section 54EC specifically provides that when the capital gain arising on the transfer of a long-term capital asset, being land or building or both, is invested or deposited in bonds issued by NHAI or RECL, the assessee shall not be subject to capital gains to that extent [i.e., lower of capital gains or ₹ 50 lakhs]. Therefore, the exemption under section 54EC cannot be denied to the assessee on account of the fiction created in section 50.

Thus, in the present case, the **action of the Assessing Officer disallowing the claim for exemption under section 54EC** on the reasoning that capital gain on transfer of depreciable asset (building) is a short-term capital gain in respect of which the provisions of section 50 apply, even if held for more than 24 months, **is not valid.**

Note – The facts of the case are similar to the facts in CIT v. V.S. Dempo Company Ltd (2016) 387 ITR 354, wherein the above issue came up before the Apex Court. The above answer is based on the rationale of the Supreme Court in the said case.

(ii) The issue of whether the amount paid by a resident Indian end-user to a non-resident computer software supplier for use of computer software can be treated as royalty came up before the Apex Court in Engineering Analysis Centre of Excellence P. Ltd v. CIT and Another (2021) ITR 471.

The Apex Court observed that as per the definition given in Explanation 2(v) to section 9(1)(vi) of the Income-tax Act, 1961, "royalty" means consideration for, inter alia, the transfer of all or any rights (including the granting of a licence), in respect of any copyright, literary, artistic or scientific work. Further, as per Explanation 4 thereto, such transfer of all or any rights includes transfer of all or any right for use or right to use a computer software (including the granting of a licence).

As per the meaning assigned in the DTAA with Singapore, however, "royalty" means payment of any kind received as consideration for "**the use of, or the right to use, any copyright**" of a literary, artistic or scientific work. The Apex Court observed that where computer software is purchased directly by an end-user, resident in India, from a foreign, non-resident supplier or manufacturer, the end-user licence agreement (EULA) does not create any interest or right to such end-user, which would amount to the use of or right to use any copyright. The "licence" that is granted vide the EULA, is not a licence in terms of the Copyright Act, but is a "licence" which imposes restrictions or conditions for the use of computer software.

There is an important difference between the right to reproduce and the right to use computer software. Whereas the former would amount to parting with a copyright by the owner thereof,

the latter would not. Under the non-exclusive licence, the end-user only receives a right to use the software and nothing more.

Accordingly, the Apex Court held that the **amount paid by a resident Indian end-user to a non-resident computer software manufacturer or supplier, as consideration for the use of the computer software through EULA, is not royalty for the use of copyright in the computer software.**

As per section 90(2), the provisions of the Income-tax Act, 1961 will **apply only to the extent they are more beneficial to the assessee,** in a case where India has entered into a DTAA with the other country. In this case, since the provisions under the DTAA are more beneficial, the taxability of the payment would be determined as per the meaning of royalty assigned under the DTAA between India and Singapore. The Apex Court, accordingly, held that the provisions contained in the Income-tax Act, 1961 [namely, section 9(1)(vi) read along with Explanations 2 and 4 thereof], which deal with royalty, not being more beneficial to the assessee, would not be applicable.

Applying the rationale of the above decision to the facts of this case, the **consideration paid by SCEL to KAL for use of SWCS as per the terms of EULA is not "royalty" as per the meaning assigned in the DTAA, since it does not create any interest or right to SCEL which would amount to the use of or right to use any copyright. Accordingly, the same does not give rise to any income chargeable to tax in India. Since the provisions of the DTAA are more beneficial, the same would apply in the case on hand. Hence, the tax deduction at source provisions u/s 195 would not be attracted in this case.**

Answer 5B

(i) **Incorrect –** Country by Country (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.

(ii) The Action Plans were structured around three fundamental pillars viz.:

(a) Introducing **coherence** in the domestic rules that affect cross-border activities.

(b) Reinforcing of **'substance'** requirements in existing international standards; Alignment of taxation with location of value creation and economic activity; and

(c) Improving **transparency and tax certainty**.

(iii) There is a need for countries to collaborate on tax matters so that they are able to get their due share of taxes due to following reasons:

- The interaction of **separate sets of domestic laws** enforced by sovereign countries **causes frictions,** including potential double taxation for corporations operating in many countries.
- It also causes gaps, in cases where **corporate income is untaxed,** both in the country of source and in the country of residence, **or is taxed only at nominal rates.**
- BEPS relates primarily to instances where the interaction of different tax rules & tax systems leads to **double non-taxation.**
- It also relates to arrangements that achieve no or low taxation by shifting profits away from the jurisdictions where the activities creating those profits take place.

Answer 6A

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

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

The Guidance Note on Tax Audit issued by ICAI states that there may be practical difficulties in verifying whether each payment is made through account payee cheque or bank draft or ECS or other prescribed electronic modes. Where the reporting has been done on the basis of the certificate of the assessee, the fact has to be reported as an observation in para 3 of Form 3CA.

The tax auditor is required to point out in tax audit report, the violation of the provisions of section 40A(3) thereof involving expenditure to a person in a day exceeding ₹ 10,000 otherwise than by way of account payee cheque/bank draft, ECS and other prescribed electronic modes. However, in this case, the tax auditor has certified that there was no such instance, though such instances aggregate to a large quantum of ₹ 20 crores.

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

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

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

Answer 6B

Particulars	Option 1	Option 2
	Own manufacture	**Buy and Sell**
	₹ in lakhs	**₹ in lakhs**
Profit on sale of ₹ 2500 lakhs @ 15% and 5%	375.00	125.00
Interest on bank deposit ₹ 200 lakhs @ 9%	-	18.00
EBT	**375.00**	**143.00**
Tax thereon @ 30%	112.50	42.90
Profit after tax	**262.50**	**100.10**
Add: Depreciation being non-cash charge	175.00	-
Depreciation @15% on ₹ 500 lakhs = ₹ 75 lakhs		

Additional depreciation @20% on ₹ 500 lakhs = ₹ 100 lakhs		
Cash/liquid profit	**437.50**	**100.10**

Conclusion: Based on the cash/liquid profit, it is advisable to replace machinery and manufacture than buy finished goods from open market and sell in its brand name.

Answer 6C

(a) The statement is **not correct**.

The binding provision will not apply to an advance ruling pronounced by the Board of Advance Ruling. Therefore, order passed by the Board for Advance Ruling is **not binding** on Mr. Rikky.

He **may appeal to the High Court** against such order **within sixty days** from the date of the communication of that order.

(b) The statement is **not correct**.

A resident falling within any class or category of persons as notified by the Central Government i.e., **a public sector undertaking can seek advance ruling even if question raised is pending before the Appellate Tribunal**.