DIRECT TAX LAWS AND INTERNATIONAL TAXATION

Time Allowed: 3 Hours **Full Marks: 100**

The figures in the margin on the right side indicate full marks.
Where considered necessary, suitable assumptions may be made and clearly indicated in the answer.
Answer to Question No. 1 and 8 are compulsory; Answer any four from Question No. 2, 3, 4, 5, 6 & 7

SECTION - A

1. (a)

Sl. No.	Answer	Justification
(i)	(a)	**Justification**: As per Rule 10U, the provisions of Chapter X-A (i.e., GAAR Provisions) shall not apply to an arrangement where the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed a sum of ₹ 3 crore.
(ii)	(a)	**Justification:** Uncontrolled transaction means a transaction between enterprises other than associated enterprises, whether resident or non-resident.
(iii)	(d)	**Justification:** The provisions of section 92 will apply only if the aggregate value of specified domestic transactions entered into by the taxpayer during the year exceeds a sum of ₹ 20 crore.
(iv)	(a)	**Justification:** UN Model gives more weight to the source principle as against the residence principle of the OECD Model. UN Model is designed to encourage flow of investments from the developed countries to developing countries. It takes into account sharing of tax-revenue with the country providing capital. Most of India's tax treaties are based on the UN Model.
(v)	(a)	**Justification:** The standards are required to be followed: • by all assessee (other than an individual or a Hindu undivided family who is not required to get his accounts of the previous year audited u/s 44AB) • who follows the mercantile system of accounting, • for the purposes of computation of income chargeable to income-tax under the head "Profits and gains of business or profession" or "Income from other sources".

(vi)	(a)	**Justification:** Where tax structure of any country deliberately is made to take advantage of, and exploit, a worldwide demand for opportunities to engage in tax avoidance, then this country is identified as tax havens.
(vii)	(a)	**Justification:** Additional depreciation is available only in respect of eligible plant and machinery to a manufacturer and not in respect of factory building. Hence the amount is Nil.
(viii)	(a)	**Justification:** Since the company has entered into international transactions with its Subsidiary Company in USA for purchase of raw materials having aggregate value of ₹ 7 crores is required to comply with the provisions of sec. 92D. This information and documents shall be kept and maintained for a period of 8 years from the end of the relevant assessment year.
(ix)	(a)	**Justification:** As per sec. 115BBG, where the total income of an assessee includes any income by way of transfer of carbon credits, tax @ 10% [plus surcharge and cess] shall be payable on the income by way of transfer of carbon credits. Hence, ₹ 15,00,000 x 10% x 104% = ₹ 1,56,000/-
(x)	(a)	**Justification:** As per sec. 115BBE, unexplained cash credit is taxable @ 60% + surcharge @ 25% + cess @ 4%. Further, such income shall not be reduced by way of set off of losses against any other income or head of income. Thus, his tax liability would be ₹ 15,60,000 [(₹ 20,00,000 x 60%) x 125% x 104%]
(xi)	(d)	**Justification:** Since during the financial year annual payment to Facebook did not exceed ₹ 1,00,000, he is not liable to deduct equalisation levy.
(xii)	(a)	**Justification:** The amount of subsidy received from the State Government or any other authority shall go to reduce the actual cost of asset computed u/s 43(1) and hence the applicable depreciation would be computed on the resultant value. Depreciation at 15% on ₹ 9 lakhs being ₹ 1,35,000 and 50% thereon being ₹ 67,500 would be the eligible amount.

SECTION – B

2. (a) Computation of Total Income of Mr. Crown, a non-resident, for the A.Y.2023-24

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

Note: Computation of Deduction u/s 80G

Computation of Adjusted GTI:

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

= ₹ 71,000 – ₹ 2,000 = ₹ 69,000

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

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

(b) Computation of total income and tax liability of Mr. Ramesh for the A.Y. 2023-24

Particulars	Amount
Income from profession in India	2,44,000
Income from profession in Country A	4,50,000
Gross Total Income	6,94,000
Less: Deduction u/ch. VIA	Nil
Total income	6,94,000
Tax on above	51,300
Add: Health & Education cess	2,052
Tax and cess payable	53,352
Less: Relief u/s 90 [₹ 4,50,000 x 5%]	22,500
Tax payable in India (Rounded off u/s 288B)	**30,850**

3. (a) The assessee is entitled to raise additional claims before the appellate authorities.

The Supreme Court in Goetze (India) Ltd -vs.- CIT (2006) 284 ITR 323 has held that an assessee cannot make a claim before the Assessing Officer otherwise than by filing a revised return.

Further, Hon'ble Bombay High Court in CIT -vs.- Pruthvi Brokers & Shareholders (2012) 349 ITR 336 has held that this restriction does not apply to an additional claim made before an appellate authority. The appellate authorities have jurisdiction to permit additional claims before them, though, the exercise of such jurisdiction is entirely the authorities' discretion.

Thus, an additional claim can be raised before the Appellate Authority even if no revised return is filed.

(b)

1. Identify the Associated Enterprise in the scenario?

Ans: ABC Inc., USA by virtue of ownership criteria.

2. Identify the International transaction?

Ans: Purchase of the laptop during the year of ₹ 4,800 (₹ 6,000 less 20%)

3. Which is the comparable uncontrolled transaction here?

Ans: Sale of computers and printers (since they are similar product to laptops), procured from, as well as sold to independent parties.

4. What is the normal gross profit margin on the comparable transactions?

Ans:

Gross profit as per trading account [8,000 + 2,000 + 800 + 250 – 500 – 200 – 5,000 – 1,300]	4,050
Less: Interest elements factored in sale price [2% of [8,000 + 2,000]	200
Less: Fright outward costs	250
Normal gross profit	3,600
Normal gross profit percentage [3,600 / 10,000 x 100]	36%

At this stage, the difference in the terms of sales transactions of computers and printers vis-a-vis the sale transactions of laptops are considered. The difference in terms of purchase will be adjusted in subsequent stage.

5. What is the price of laptop being purchased from the AE, is resold to unrelated enterprise?

Ans: ₹ 11,000

6. What is the resultant cost of sales after deducting 'Normal Gross Profit Margin'

Ans: ₹ 7,040 (i.e. ₹ 11,000 less 36% Normal Gross Profit Margin)

7. What are the expenses incurred in connection with purchase?

Ans: ₹ 1,200 (since it is mentioned that around 20% of the purchase cost reported in P&L is toward freight, customs duty and clearance charges)

8. What are the functional difference, including accounting practices, between the international transaction and the comparable uncontrolled transaction, which could materially affect the amount of gross profit margin?

Ans: ₹ 300 on account of ocean freight

9. What is the cost of sale after adjustment made as per 7 & 8 above?

Ans: ₹ 5,540 (i.e. ₹ 7,040 *less* ₹ 1,200 *less* ₹ 300)

10. How is the arm's length purchase price determined?

Ans:

Price as arrived at 9 above	₹ 5,540
Add: Amount in closing stock (80% of ₹ 1200)	₹ 960
	₹ 6,500
Less: Amount in opening stock (80% of ₹ 800)	₹ 640
Arm's length price of purchase	₹ 5,860

11. Is the purchase price at arm's length?

Ans: Yes. Since the purchase price is ₹ 4,800 is less than arm's length price determined at ₹ 5,860.

4. (a) Computation of penalty are as under

Assessee	Return Filed	Income u/s 143(1)(a)	Assessed Income	Under-reported Income	Tax payable on (a)	Tax payable on (b)	Tax payable on (c)	Penalty
		a	b	c = (b – a)	d	e	f = (e – d)	f x 50%
Individual	Yes	6,00,000	10,00,000	4,00,000	33,800	1,17,000	83,200	41,600
Firm	Yes	17,00,000	20,00,000	3,00,000	5,30,400	6,24,000	93,600	46,800
Firm	Yes	(8,00,000)	20,00,000	28,00,000	-	8,73,600	8,73,600	4,36,800
Individual	Yes	(9,00,000)	(3,00,000)	6,00,000	-	33,800	33,800	16,900
Individual	No	N.A.	7,50,000	5,00,000#	-	65,000	65,000	32,500

Assessed income as reduced by basic exemption

(b) Thin Capitalization [Sec. 94B]

Applicable to

Indian company, or a permanent establishment of a foreign company in India, being the borrower

- *Permanent establishment* includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.

Conditions

a) The borrower has debt issued by a non-resident, being an associated enterprise of such borrower.

  - *Debt* means any loan, financial instrument, finance lease, financial derivative, or any arrangement that gives rise to interest, discounts or other finance charges that are deductible in the computation of income chargeable under the head "Profits and gains of business or profession";

b) He incurs any expenditure by way of interest or of similar nature exceeding ₹ 1 crore;

c) Such expenditure is deductible in computing income chargeable under the head "Profits and gains of business or profession"

Effect

If all the aforesaid conditions are satisfied then, excess interest shall not be deductible in computation of income under the said head.

- Excess interest means lower of the following:
  a) An amount of total interest paid or payable in excess of 30% of earnings before interest, taxes, depreciation and amortisation (EBITDA) of the borrower in the previous year; or
  b) Interest paid or payable to associated enterprises for that previous year

Taxpoint

- *Guarantee*: Where the debt is issued by a lender which is not associated but an associated enterprise either provides an implicit or explicit guarantee to such lender or deposits a corresponding and matching amount of funds with the lender, such debt shall be deemed to have been issued by an associated enterprise.
- *Exception*:

  The provision of sec. 94B is not applicable:

  a) to an Indian company or a permanent establishment of a foreign company which is engaged in the business of banking or insurance; or

b) to interest paid in respect of a debt issued by a lender which is a permanent establishment in India of a non-resident, being a person engaged in the business of banking

- *Carry forward*: Where for any assessment year, the interest expenditure is not wholly deducted against income under the head "Profits and gains of business or profession", so much of the interest expenditure as has not been so deducted, shall be carried forward to the following assessment year(s), and it shall be allowed as a deduction against the profits and gains, if any, of any business or profession carried on by it and assessable for that assessment year to the extent of maximum allowable interest expenditure.
- *Maximum carried forward*: No interest expenditure shall be carried forward for more than 8 assessment years immediately succeeding the assessment year for which the excess interest expenditure was first computed.

5. (a) (i) Following are the essentials of tax planning:

- Up-to-date Knowledge of tax laws alongwith circulars, notifications, clarifications and Administrative instructions issued by the CBDT.
- Disclosure of full and true material information
- Avoid sham transactions or make-believe transactions or colourable devices
- Foresight of future development or changes and enterprise's goal. The planning should be flexible enough to adjust statutory negation.

(ii) ***Assessment [Sec. 10]***

- The Assessing Officer may, on receipt of an information from an income-tax authority or any other authority under any law for the time being in force or on coming of any information to his notice, serve on any person, a notice requiring him, on the specified date, to produce such accounts or documents or evidence as the Assessing Officer may require for the purposes of this Act.
  - No separate return is required to be filed under this Act
  - There is no time limit for issuance of the aforesaid notice. The Assessing Officer may issue such notice any time on the basis of information.
- The Assessing Officer may, from time to time, serve further notices requiring the production of such other accounts or documents or evidence as he may require.
- The Assessing Officer may make such inquiry, as he considers necessary, for

the purpose of obtaining full information in respect of undisclosed foreign income and asset of any person for the relevant financial year or yea₹

- The Assessing Officer, after considering such accounts, documents or evidence, as he has obtained, and after taking into account any relevant material which he has gathered and any other evidence produced by the assessee, shall by an order in writing, assess the undisclosed foreign income and asset and determine the sum payable by the assessee.
- Such order shall be made within 2 years from the end of the financial year in which the notice was issued by the Assessing Officer [Sec. 11]
- *Best Judgment Assessment*: If any person fails to comply with all the terms of the notice, the Assessing Officer shall, after taking into account all the relevant material which he has gathered, make the assessment of undisclosed foreign income and asset to the best of his judgment and determine the sum payable by the assessee. [Sec. 10(4)]
  - Before making such an assessment, an opportunity of being heard is required to be given to the assessee.

(b) (A) Computation of Arms' Length Gross Profit Mark-up

Particulars	**%**
Normal Gross Profit Mark up	50.00
Less: *Adjustment for differences*	
Technical support from Brain Inc [8% of Normal GP = 8% of 50%]	(4.00)
	46.00
Add: Cost of Credit to Brain Inc 3% of Normal Bill [3% ×GP 50%]	1.50
Arm's Length Gross Profit mark-up	47.50

(B) Computation of Increase in Total Income of Brain Inc

Particulars	**Amount**
Cost of services	15,00,000
Arm's length Billed Value [Cost / [(100 – Arm's Length mark-up)] [₹ 15,00,000 / (100% - 47.50%)]	28,57,143
Less: Billed amount [2,000 hours x ₹ 1,000 per hour]	20,00,000
Therefore, Increase in Total Income	**8,57,143**

6. (a) Since the undertaking is owned by the company for more than 3 years hence the gain on transfer shall be liable to long term. Calculation of cost of acquisition (i.e. Net worth)

Particulars	**Workings**	**Details**	**Amount**
Value of asset taken over			
Land	Book value of non-depreciable assets	₹ 50 lacs	
Stock	Book value of non-depreciable assets	₹ 30 lacs	
Debtors	Book value of non-depreciable assets	₹ 40 lacs	
Machinery	WDV as per I.T. Act	₹ 60 lacs	
Furniture	WDV as per I.T. Act	₹ 90 lacs	₹ 270 lacs
Less: Value of liabilities taken over			
Creditors	Book Value		₹ 50 lacs
Net worth (cost of acquisition)			**₹ 220 lacs**

Computation of capital gains in the hands of X Ltd. for the A.Y. 2023-24

Particulars	**Details**	**Amount**	**Amount**
Sale Consideration			300 lacs
Less: Expenses on transfer	5% of ₹ 300 lacs		15 lacs
Net Sale Consideration			285 lacs
Less: Cost of Acquisition	Calculated above	220 lacs	
Less: Cost of improvement		Nil	220 lacs
Long Term Capital Gain			**65 lacs**

(b) Following disclosure shall be made in respect of ICDS VII - Government grants:

a. nature and extent of Government grants recognised during the previous year by way of deduction from the actual cost of the asset or assets or from the written down value of block of assets during the previous year;

b. nature and extent of Government grants recognised during the previous year as income;

c. nature and extent of Government grants not recognised during the previous year by way of deduction from the actual cost of the asset or assets or from the written down value of block of assets and reasons thereof; and

d. nature and extent of Government grants not recognised during the previous year as income and reasons thereof.

7. (a) Computation of Arm's Length Price of Products sold to J Inc. Korea by CD Ltd

Particulars	₹	₹
Price per Unit in a Comparable Uncontrolled Transaction		5,800
Less: Adjustment for Differences -		
(a) Freight and Insurance Charges	700	
(b) Estimated Warranty Costs	500	
(c) Discount for Voluminous Purchase	200	(1,400)
Arms's Length Price for Cellular Phone sold to J Inc. Korea		**4,400**

Computation of Increase in Total Income of CD Ltd

Particulars	₹
Arm's Length Price per Unit	4,400
Less: Price at which actually sold to J Inc. Korea	(3,000)
Increase in Price per Unit	1,400
No. of Units sold to J Inc. Korea	2,50,000
Increase in Total Income of CD Ltd (2,50,000 x ₹ 1,400)	₹ 35 Crores

(b) Computation of Total Income and Tax Liability

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

(c) Computation of income of the branch for the A.Y. 2023-24

Particulars	Amount	Amount
Net Income for the year ended on 31-03-2023		(50,00,000)
Add: Head office expenses (to be considered separately)		1,00,00,000
Adjusted Total Income		50,00,000
Less: Head office expenses allowable u/s 44C being lower of the following:		
- 5% of ₹ 50,00,000	2,50,000	
- Actual Expenses	1,00,00,000	2,50,000
Total Income		**47,50,000**

SECTION - C

8. **(a)** Computation of total income and tax liability for the A.Y. 2023-24

Particulars	Amount
Income from business in India	27,00,000
Income from business in Country A	15,00,000
Income from business in Country B	(-) 4,00,000
Gross Total Income	38,00,000
Less: Deduction u/s 80C	1,50,000
Total income	36,50,000
Tax on above	9,07,500
Add: Health & Education cess	36,300
Tax and cess payable	9,43,800
Average rate of tax [₹ 9,43,800 / ₹ 36,50,000 x 100]	25.86%
Rate of tax in country A	33.33%
Relief u/s 91 [25.86%[1] of ₹ 15,00,000]	3,87,900
Tax payable (Rounded off u/s 288B)	**5,55,900**

[1] Indian average tax rate: 25.86% Foreign average tax rate: 33.33%
Relief u/s 91 is available at lower of aforesaid rate. i.e., 25.86%

(b) Computation of total income of Z Ltd. for the A.Y.2023-24 (as per other provisions of the Act)

Particulars	Details	Amount
Net profit as per books of accounts		45,80,000
Add: Expenditure disallowed but debited in P/L A/c		
Excess Depreciation	1,00,000	
Provisions for Contingencies	75,000	
Wealth Tax	50,000	
Loss of subsidiary company	50,000	
Proposed Dividend	1,00,000	
Provision for income tax	1,05,000	
Unpaid customs duty	40,000	5,20,000
		51,00,000
Less: Expenditure allowed but not debited in P/L A/c		
Interest on bank loan of earlier years		1,00,000
		50,00,000
Less: Brought forward business loss		42,50,000

Gross Total Income		7,50,000
Less: Deduction u/s 80G		1,00,000
Total Income		**6,50,000**

Computation of Book Profit of Z Ltd. for the A.Y.2023-24

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

Computation of tax liability of Z Ltd.

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