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CA Final 2022 Suggested Answers · Paper 7 Direct Tax Laws and International Taxation (Old Scheme)

EXAM
CA Final

YEAR
2022

TYPE
Suggested Answers

SUBJECT
Paper 7 Direct Tax Laws and International Taxation (Old Scheme)

DATE
November 2022

PAPER – 7: DIRECT TAX LAWS & INTERNATIONAL TAXATION

Part - II

*Question No.**1** is compulsory.*

*Answer any **four** questions from the remaining **five** questions.*

Working notes should form part of the answer

All questions relate to Assessment Year 2022-23, unless stated otherwise in the question.

Question 1

M/s MPK Pharma Ltd, a company resident in India, in which the public are not substantially interested, is engaged in the manufacture of pharmaceutical products. The Statement of Profit & Loss for the year ended 31st March, 2022 shows a net profit of ₹ 50,75,000 after debiting or crediting the following items:

(i) One-time license fee of ₹ 12 lakhs paid to a foreign company for obtaining a franchise on 28th July, 2021.

(ii) Convertible debentures were issued by the company on which expenditure of issue and collection of ₹ 3,15,000 was incurred.

(iii) The company has paid ₹ 2,25,000 to share brokers for transactions in relation to equity shares listed in stock exchange and ₹ 1,20,000 to commodity broker for transactions in relation to commodities at MCX. Tax was not deducted at source on such transactions.

(iv) Contributed 15% of basic salary in National Pension Scheme referred in section 80CCD towards salary paid to an employee Mr. Gaurav whose basic salary was ₹ 6,00,000 p.a. and Dearness allowance of 30% of basic salary was considered. 50% of Dearness allowance formed part of the salary.

(v) Expense of ₹ 7,00,000 has been incurred for providing freebies to medical practitioners.

(vi) Expenditure of ₹ 5,20,000 incurred on feasibility study conducted for examining proposals for technological advancement for existing business. The project was abandoned without creating a new asset.

(vii) Depreciation of ₹ 13,00,000 on the basis of useful life of assets has been charged.

(viii) Employees Provident Fund (EPF) for the month of March, 2022 amounting to ₹ 5,20,000 was remitted on 17th May, 2022 which includes ₹ 2,60,000 of employer's contribution and ₹ 2,60,000 of employee's contribution.

(ix) Donation to Swachh Bharat Kosh ₹ 2,00,000.

(x) Industrial power tariff concession of ₹ 4,50,000 is received from Central Government.

The Suggested Answers for Paper 7: Direct Tax Laws and International Taxation are based on the provisions of direct tax laws as amended by the Finance Act, 2021, which are relevant for November, 2022 examination. The relevant assessment year is A.Y.2022-23.

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(xi) Interest and borrowing costs amounting to ₹ 6,85,000 and ₹ 5,65,000 though not meeting the criteria for recognition as a component of cost, is included in the cost of opening and closing inventory, respectively.

(xii) The profit from setting of warehouse in rural area for storage of sugar (before claiming deduction under section 35AD) is ₹ 10,00,000. The warehouse commenced operations on 24th October, 2021.

The Company has furnished the following additional information:

(i) The company has collected ₹ 14,00,000 as GST from its customers and remitted to the Government before due the dates. Consequent to an appeal filed, the Honourable High Court ordered the GST department to refund ₹ 5,00,000 to the Company. The Company in tum refunded ₹ 3,00,000 to its customers from whom GST was collected. Balance amount is shown under "current liabilities".

(ii) On 14.01.2022, the company has issued 2,00,000 equity shares of ₹ 10 each at ₹ 22 per share. The fair market value of the shares determined as per Income-tax Rules, 1962 was ₹ 19 per share.

(iii) The company has brought forward losses of ₹ 13,00,000 relating to assessment year 2019-20. Mr. X who continuously held 55% shares carrying voting power since incorporation of the company, had sold his entire shareholding to Mr. Y on 25.11.2021.

(iv) Depreciation allowable as per Income-tax Rules ₹ 14,50,000.

(v) The company has invested ₹ 35 lakhs in the construction of warehouse in a rural area for storage of sugar as an additional line of business. The investment includes land value of ₹ 20 lakhs.

You are required to compute the Total Income of M/s MPK Pharma Ltd. for the Assessment Year 2022-23. The company has not opted for tax u/s 115BAA of the Income-tax Act, 1961.

(14 Marks)

Answer

Computation of Total Income of M/s MPK Pharma Ltd. for the A.Y. 2022-23

	Particulars	Amount (in ₹)	
I	**Profits and gains of business and profession**		
	Net profit as per Statement of profit and loss		50,75,000
	Add: **Items debited but to be considered separately or to be disallowed**		
	(i) One time license fee [Franchise is in the nature of an intangible asset eligible for depreciation @ 25%. Since one-time license fees of ₹ 12 lakh paid to a foreign	12,00,000	

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	company for obtaining franchise has been debited to statement of profit and loss, the same has to be added back.]			
	(ii) Expenditure of issue of convertible debenture [The expenditure incurred on the issue and collection of debentures would be treated as revenue expenditure even in case of convertible debentures, i.e., the debentures which had to be converted into shares at a later date.[1] Since the said expenditure has been debited to statement of profit and loss, no further adjustment is required.]	Nil		
	(iiia) Payment to share brokers for transaction in relation to equity shares [Since the company is engaged in the manufacture of pharmaceutical products, investment in equity shares is not related to the business and the payment to share broker is not wholly and exclusively for the purpose of assessee's business. Since the said payment has been debited to statement of profit and loss, the same has to be added back] ***Note** – If it is assumed that the company also carries on share trading business and the profits of such business are included in the figure of ₹ 50,75,000, then, the payment to share brokers would be allowable as deduction. There would be no disallowance under section 40(a)(ia) since section 194H is not attracted in respect of payment for transaction in relation to equity shares. The figures of business income, gross total income and total income would, accordingly, change]*	2,25,000		
	(iiib) Payment to commodity broker without deducting tax at source [Assuming that the commodity transactions at MCX are in relation to the business of the company, the payment of ₹ 1,20,000 to commodity broker on which tax is deductible	36,000		

[1] *CIT v. ITC Hotels Ltd. (2011) 334 ITR 109 (Kar.)*

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	under section 194H would attract disallowance@30% u/s 40(a)(ia), due to non-deduction of tax at source u/s 194H.] ***Note*** *– If the transactions are not related to the business, the entire amount of ₹ 1,20,000 would be disallowed. The figures of business income, gross total income and total income would accordingly change.*		
	(iv) Contribution towards NPS in excess of 10% of salary disallowed [Contribution to the extent of 10% of salary (basic salary + dearness allowance, if it forms part of pay for retirement benefits) is allowable as deduction under section 36(1)(iva). In this case, ₹ 90,000 (15% of ₹ 6,00,000) – ₹ 69,000 [10% of (₹ 6,00,000 + 50% of 30% x ₹ 6,00,000)], would be disallowed]	21,000	
	(v) Expense on freebies to medical practitioners [Any expense incurred in providing freebies to medical practitioners is an expense prohibited by the law. Any expenditure incurred by an assessee for any purpose which is prohibited by law is not deemed to have been incurred for the purpose of business or profession and hence, has to be disallowed from business income.[2]	7,00,000	
	(vi) Expenditure on feasibility study [If there is no creation of a new asset, then the expenditure incurred on feasibility study would be of revenue nature. In this case, since the feasibility study was conducted for the existing business and the project was abandoned without creating a new asset, the expenses were of revenue nature[3]. Since the expenditure of ₹ 5,20,000 has already been debited to statement of profit and loss, no further adjustment is required.	Nil	

[2] *Circular No. 5/2012 dated 01.08.2012 and Confederation of Indian Pharmaceutical Industry (SSI) v. CBDT (2013) 353 ITR 388 (H.P.)*
[3] *CIT v. Priya Village Roadshows Ltd. (2011) 332 ITR 594 (Delhi)*

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	(vii) Depreciation on the basis of useful life of asset	13,00,000	
	(viiia) Employees' contribution to EPF	2,60,000	
	[Since employees' contribution to EPF has not been deposited on or before the due date under the PF Act, the same is not allowable as deduction as per *Explanation 2* below to section 36(1)(va). Since the same has been debited to Statement of profit and loss, it has to be added back for computing business income].		
	(viiib) Employer's contribution to EPF	Nil	
	[As per section 43B, employers' contribution to EPF is allowable as deduction since the same has been deposited on or before the due date of filing of return of income u/s 139(1). Since the same has been debited to statement of profit and loss, no further adjustment is necessary]		
	(ix) Donation to Swachh Bharat Kosh	2,00,000	
	[Donation to Swachh Bharat Kosh is not an allowable expenditure under section 37 since it is not laid out wholly or exclusively for the purposes of business or profession. Hence, the same has to be added back while computing business income.]		
	(xi) Difference on account of interest and borrowing costs	1,20,000	
	[As per ICDS II, Interest and borrowing costs not meeting the criteria for recognition as component of cost shall not be included in the cost of opening and closing stock. ₹ 1,20,000 [₹ 6,85,000 – ₹ 5,65,000] being the difference between closing and opening stock, has to be adjusted to remove the effect of interest and borrowing costs included in the value of stock.		40,62,000
			91,37,000

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	***Add:* Income taxable but not credited to statement of profit and loss**		
	AI(i) GST not refunded to customers out of GST refund received from Government [The amount of GST refunded to the company by the Government is a revenue receipt chargeable to tax. Out of the refunded amount of ₹ 5 lakhs, the amount of ₹ 3 lakh stands refunded to customers and hence, would not be chargeable to tax. The balance amount of ₹ 2,00,000 lying with the company would be chargeable to tax]		2,00,000
			93,37,000
	***Less:* Items credited but chargeable to tax under another head/expenses allowed but not debited**		
	(x) Industrial power tariff concession received from Central Government [Any assistance in the form of, *inter alia*, concession received from the Central or State Government would be treated as income as per section 2(24)(xviii). Since the same has been credited to Statement of Profit and Loss, no adjustment is required]	Nil	
	(xii) Profits from setting of warehouse in rural area for storage of sugar [Since it is a specified business, its profits would be computed separately]	10,00,000	
	AI(iv)Depreciation as per Income-tax Rules [As depreciation is as per Income-tax Rules is stated as ₹14,50,000, it has been considered that it includes depreciation on Franchise. ***Note -*** *If it is assumed that the figure does not include depreciation on franchise, then, depreciation of ₹ 17,50,000 (₹ 14,50,000 + ₹ 3,00,000, being depreciation@25% on franchise) has to be reduced*]	14,50,000	24,50,000
			68,87,000

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	Less: Brought forward business loss relating to A.Y. 2019-20 [Brought forward loss relating to A.Y. 2019-20 not allowed to be set off from the profits of A.Y. 2022-23 as 51% or more of the shares of MPK Pharma Ltd., which is a company in which public are not substantially interested, on 31.3.2022 are not held by the same persons who held not less than 51% shares of the company on 31.3.2019]		Nil
	Profits and gains from manufacture of pharmaceutical products		68,87,000
	Profits and gains from setting of warehouse in rural area for storage of sugar		
	Net profit before deduction under section 35AD	10,00,000	
	Less: Deduction under section 35AD 100% deduction u/s 35AD in respect of cost of warehouse [₹ 35 lakhs – ₹ 20 lakhs, being cost of land, not allowable]	15,00,000	
	Loss from the specified business of setting up a warehousing facility to be carried forward as per section 73A for set-off against profits of any specified business in the subsequent year	(5,00,000)	
II	**Income from Other Sources**		
	Consideration received in excess of FMV of shares issued [The shares of the company are issued at a premium (i.e., issue price exceeds the face value of shares); The excess of the issue price of the shares over the FMV would be taxable u/s 56(2)(viib). ₹ 6,00,000 [2,00,000 × ₹ 3 (₹ 22 – ₹ 19)] shall be treated as income in the hands of MPK Pharma Ltd., which is not a company in which public are substantially interested]		6,00,000
	Gross Total Income		**74,87,000**

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	***Less:* Deduction under Chapter VI-A**		
	Deduction u/s 80G in respect of donation to Swachh Bharat Kosh, assuming that the donation is otherwise than by way of cash		2,00,000
	Total Income		**72,87,000**

Question 2

(a) M/s PRK LLP, a limited liability partnership, set up a unit in Special Economic Zone (SEZ) on 1st April, 2019 to develop and export computer software. The unit complied with all the conditions of section 10AA. The net profit of the unit as per Statement of Profit & Loss for the year ended 31st March, 2022 was ₹ 65 lakhs after debiting/crediting the following items:

(i) Profit on sale of import entitlement ₹ 9 lakhs.

(ii) Remuneration to its working partners ₹ 58 lakhs.

(iii) Interest at the rate of 16% per annum on partners' capital ₹ 20 lakhs.

(iv) Donation to a political party ₹ 3 lakhs.

(v) Depreciation ₹ 17 lakhs.

Additional Information:

(i) Payment of remuneration to working partners and interest on capital are authorized by the partnership deed.

(ii) Brought forward business loss from assessment year 2017-18 was ₹ 4 lakhs.

(iii) Unabsorbed depreciation brought forward from assessment year 2016-17 was ₹ 35 lakhs.

(iv) Total export turnover was ₹ 45 crores and the sale proceeds in convertible foreign exchange received in India by 30th September, 2022 was 38 crores. Total export turnover of ₹ 45 crores include telecommunication charges of ₹ 5 crores attributable to delivery of software. Sale proceeds realization of ₹ 38 crores also include such telecommunication charges of ₹ 2 crores.

(v) Depreciation allowable as per Income-tax Rules is ₹ 26 lakhs.

You are required to compute:

(i) Income-tax (including AMT under section 115JC) payable by Mis PRK LLP for the Assessment Year 2022-23.

(ii) Amount of tax credit allowed to be carried forward.

Necessary working notes should form part of your answer. ***(8 Marks)***

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(b) *Mr. Robert, a non-resident and German citizen, is employed in a German company. The German company has a PE in India and accordingly the income of the PE is chargeable to tax in India. Robert visited India during the FY 2021-22 on official work and stayed for 85 days. His salary for that period was ₹ 28,00,000 which is borne by the Indian PE.*

Robert held 1200 shares of Nalapir Pvt. Ltd. (NP), an Indian company since 28.11.2015 which he acquired for ₹ 15 per share. For acquiring the shares, he remitted USD 50,000 to India on 1.11.2015. He sold these shares on 23.6.2021 for ₹ 43 per share.

Robert also held 2000 equity shares of Aribitz GmbH (AG), a German company, which he had acquired for ₹ 145 per share in 2018. AG follows April to March as its financial year. He sold all these shares for ₹ 615 per share to David, another non-resident, on 26.08.2021. The relevant information of AG as on 31.3.2021 is given below:

(i) Total value of assets ₹ 15 crores.

(ii) Total value of immovable properties worldwide= ₹ 12 crores.

(iii) Immovable properties held in India (included in (ii) above) - ₹ 8 crores.

Dividend from Aribitz GmbH received in India on 28.06.2021 was - ₹ 1,11,000.

You are required to compute the total income taxable in India of Mr. Robert ignoring the provisions of DTAA between India and Germany, if any.

Exchange rates for 1 USD on the relevant dates is given as hereunder:

Date	*Buying Rate (1 US $)*	*Selling Rate (1 US$)*
28.11.2015	*₹ 59*	*₹ 61*
1.11.2015	*₹ 61*	*₹ 64*
23.6.2021	*₹ 74*	*₹ 76*

(6 Marks)

Answer

(a) Computation of total income and tax liability of M/s PRK LLP for A.Y.2022-23

(under the regular provisions of the Income-tax Act, 1961)

Particulars	Amount (in ₹)	Amount (in ₹)
Net profit as per Statement of Profit & Loss		65,00,000
***Add:* Items debited but to be considered separately or to be disallowed**		
- Remuneration to its working partners	58,00,000	
- Interest@16% p.a. on partners' capital (Interest on capital account would be fully	5,00,000	

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allowed to the extent of 12%, since the same is authorized by the partnership deed. Thus, interest in excess of 12% i.e., ₹ 20 lakhs/16% x 4% would be disallowed)		
- Donation to a political party [not allowed as deduction as per section 37(1) while computing business income, since it is not incurred wholly and exclusively for the business]	3,00,000	
- Depreciation	17,00,000	
		83,00,000
		1,48,00,000
***Less:* Permissible expenditure and allowances**		
- Depreciation allowable as per Income-tax Rules, 1962	26,00,000	
- Unabsorbed depreciation under section 32(2) [allowable as deduction while computing book profit as per *Explanation 3* to section 40(b)]	35,00,000	61,00,000
Profit on sale of import entitlement [taxable as profits and gains from business as per section 28, since the same has already credited in Statement of profit and loss, no further adjustment is required]		Nil
Book Profit		**87,00,000**
On first ₹ 3 lakh of book profit [₹ 3,00,000 × 90%]	2,70,000	
On balance ₹ 84 lakh of book profit [₹ 84,00,000 × 60%]	50,40,000	
	53,10,000	
Remuneration actually paid of ₹ 58,00,000 is allowable to the extent of		53,10,000
Business Income		**33,90,000**
***Less*:** Brought forward business loss for A.Y. 2017-18		4,00,000
Gross Total Income		**29,90,000**
***Less:* Deduction under section 10AA**		
Profit from SEZ unit x Export Turnover/ Total Turnover x 100% [₹ 24,90,000 x 36 crores /40 crores x 100% (since it is the third year of operation)]		22,41,000
Profit derived from SEZ unit	33,90,000	

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Less: Profits from sale of import entitlement [business income which are in the nature of ancillary profits, do not constitute profit 'derived from' business for the purpose of exemption under section 10AA]	9,00,000	
	24,90,000	
Export Turnover [₹ 38 crores – ₹ 2 crores, being telecommunication charges included therein. Telecommunication charges[4] not includible in export turnover]	36 crores	
Total Turnover [₹ 45 crores – ₹ 5 crores, being telecommunication charges included therein. Since telecommunication charges has been excluded from export turnover, the same has to be excluded from total turnover also]	40 crores	
***Less:* Deduction under section 80GGC** [Donation to political party [allowable as deduction under section 80GGC, assuming the donation made otherwise than by way of cash]		3,00,000
Total Income		**4,49,000**
Tax liability		
Tax@30%		1,34,700
Add: Health and education cess@ 4%		5,388
Tax Liability		**1,40,088**
Tax Liability (rounded off)		1,40,090

Computation of adjusted total income of M/s PRK LLP and Alternate Minimum Tax

Particulars	Amount (in ₹)
Total Income (as computed above)	4,49,000
Add: Deduction under section 10AA	22,41,000
Adjusted Total Income	**26,90,000**
Alternate Minimum Tax@18.5%	4,97,650
Add: Health and Education cess@4%	19,906
Tax liability under section 115JC	**5,17,556**
Since the regular income-tax payable is less than the alternate minimum tax payable, the adjusted total income shall be deemed to be the total income and tax is leviable @18.5% thereof *plus* cess@4%. Therefore, the tax liability is ₹ 5,17,560 (rounded off).	

[4] *It is assumed that telecommunication charges are incurred in foreign currency outside India.*

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AMT Credit to be carried forward under section 115JEE	
Tax liability under section 115JC (rounded off)	5,17,560
Less: Tax liability under the regular provisions of the Income-tax Act, 1961	1,40,090
Amount of Credit	**3,77,470**

Note *– In the above solution, while computing deduction under section 10AA, the brought froward business loss of ₹ 4,00,000 from A.Y. 2017-18 is not deducted from profits derived from SEZ, considering the view that such profits have to be computed as per Chapter IV-D and hence, effect of carry forward and set-off of losses is not given.*

However, alternate view is also possible based on Circular No. 7/DV/2013 [FILE NO.279/MISC./M-116/2012-ITJ], dated 16-7-2013 that provisions contained in Chapter VI relating to set-off and carry forward and set-off of losses shall also apply while determining the income for the purpose of computing deduction under section 10AA. If this view is considered, the deduction under section 10AA has to be computed after deducting brought forward business losses of ₹ 4,00,000 from the profits of SEZ. In such case, the deduction under section 10AA would be ₹ 18,81,000 [(₹ 20,90,000 x ₹ 36 crores/₹ 40 crores) x 100%], total income would be ₹ 8,09,000, tax liability as per normal provisions would be ₹ 2,52,410. Alternate minimum tax liability would remain same. However, AMT credit to be carried forward would be ₹ 2,65,150]

(b) Computation of Total income of Mr. Robert for the A.Y. 2022-23

Particulars	₹	₹
Salary	28,00,000	
[Salary deemed to accrue or arise in India, since it is paid for services rendered in India as per section 9(1)(ii). Hence, it is taxable in the hands of Mr. Robert.		
Exemption u/s 10(6)(vi) would not be available to him, though he stayed in India for a period of not exceeding 90 days during the previous year since he is receiving salary from a German company which is engaged in business and trade in India through a PE in India and such salary is borne by Indian PE]		
Less: Standard deduction u/s 16(ia)	50,000	
		27,50,000
Capital Gains		
Transfer of 1200 equity shares of Nalapir Pvt. Ltd. [Taxable in India, since shares are situated in India]		
Sale Consideration (1200 x ₹ 43 per share/75, being average of ₹ 74 (TTBR) + ₹ 76 (TTSR)/2 on 23.6.2021)	$ 688	

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Less: Cost of acquisition (1200 x ₹ 15 per share/60, being average of ₹ 59 (TTBR) + ₹ 61 (TTSR)/2 on 28.11.2015)	$ 300	
	$ 388	
Long-term capital gain [$ 388 x ₹ 74, being TTBR on 23.06.2021]		28,712
Transfer of 2000 Equity shares of Aribitz GmbH (AG)		Nil
[Not taxable in India, since shares of foreign company do not derive its value substantially from assets located in India as value of Indian assets do not exceed ₹ 10 crores]		
Income from Other Sources		
Dividend received in India from Aribitz Gmbh [taxable in India, since dividend is received in India]		1,11,000
Gross Total Income/total income		**28,89,712**
Total income (rounded off)		**28,89,710**

Question 3

(a) *The Head of Accounts of Fit Me Foundation, a trust, established for the purpose of promotion of Yoga has approached you to guide him about the tax implications of the following:*

(i) *During the financial year 2021-22, it received a voluntary contribution of ₹ 125 lakhs with a specific direction that it should form part of the corpus of the trust. The trust invested such amount in the shares of M/s. Bend and Blend Private Ltd., a private sector company.*

(ii) *Apart from the above-mentioned ₹ 125 lakhs, during the financial year 2021-22, it received ₹ 95 lakhs from other voluntary contributions and ₹ 60 lakhs of fees towards providing Yoga classes.* ***(4 Marks)***

(b) *Mr. Nagaraj is the founder of SSVB Trust, a public charitable trust registered u/s 12A of the Income-tax Act, 1961. The trust runs a hospital for the treatment of various diseases. Mr. Ram, son of Mr. Nagaraj, was admitted in May 2021 in the hospital due to COVID for treatment. He was charged a total fee of ₹ 3 lakhs as against the amount of ₹ 5 lakhs charged by the hospital for similar treatment to the general public.*

The Board of trustees were served with a notice by the income tax authorities for cancellation of registration u/s 12A.

Discuss whether registration can be denied to the trust. What are the further tax implications? ***(4 Marks)***

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(c) Mr. Ritesh, a resident individual, aged 42 years, received the following sums during the previous year 2021-22:

Income from a business in India ₹ 4,85,000

Royalty from Country N ₹ 7,80,000 (Rate of Tax in Country N 10%, Tax deducted ₹ 78,000)

Interest from Country Y US $ 9,500 (interest became due on 01.04.2021) Tax deducted (on 21.02.2022) : US $ 950 (Rate of Tax 10%)

Agriculture income in Country M: ₹ 1,09,000

Additional Information:

(i) As per the DTAA between India and Country N, the royalty will only be taxable in the Source State.

(ii) As per the DTAA between India and Country Y, interest can be taxed in both the states and tax credit will be available in respect of tax payable in resident state.

(iii) Agriculture income is exempt in country M. India does not have a DTAA with Country M.

Telegraphic transfer buying rate on different dates of US $:

Date	Rate (₹)
31.03.2021	75
31.01.2022	78
21.02.2022	79
31.03.2022	80
01.01.2022	80

You are required to calculate the total income and tax payable by Mr. Ritesh assuming that he did not opt to be governed by provisions of Section 115BAC. ***(6 Marks)***

Answer

(a) (i) Voluntary contribution of ₹ 125 lakhs received with a specific direction that it will form part of corpus of the trust would be exempt from tax only if it is invested in any of the modes specified under section 11(5) specifically maintained for such corpus. If the same is not so invested, then, it would not be exempt under section 11(1)(d) for P.Y.2021-22.

Investment in shares of private company is not a specified mode under section 11(5). Hence, ₹ 125 lakhs received by Fit Me Foundation would not be exempt under section 11.

(ii) Yoga is included in the definition of "charitable purpose" under section 2(15).

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Accordingly, voluntary contributions of ₹ 95 lakhs and fees towards providing Yoga classes of ₹ 60 lakhs would be income from property held for charitable purposes and eligible for unconditional exemption of 15% under section 11.

Exemption will be available under section 11 subject to the fulfilment of the necessary conditions.

(b) As per section 13(6), SSVB Trust shall not be denied the benefit of exemption under section 11 in respect of its entire income merely due to the reason that the benefit of medical facilities have been provided to Mr. Ram, son of Mr. Nagaraj, being the specified person. Accordingly, the registration of SSVB Trust cannot be cancelled by the Income-tax authorities on this basis.

As per section 12(2), the value of medical facilities provided to Mr. Ram, being the specified person, at a concessional rate would be deemed to be the income of the trust and such income would not be eligible for exemption under section 11. Hence, ₹ 2,00,000, being the concessional value of medical services would be deemed to be the income of SSVB Trust.

The remaining income would be eligible for benefit of section 11.

(c) Computation of total income and tax payable by Mr. Ritesh for A.Y.2022-23

Particulars	₹	₹
Profits and Gains of Business or Profession		
Income from business in India		4,85,000
Income from Other Sources		
Royalty from Country N [As per India-Country N DTAA, royalty is taxable in Country N only]	Nil	
Interest from Country Y [US $ 9,500 x 80 (being conversion rate as on 31.3.2022 i.e., last day of the previous year – Rule 115]	7,60,000	
Agricultural Income in Country M [Not exempt in India]	1,09,000	
		8,69,000
Gross Total Income/ Total Income		**13,54,000**
Tax liability on ₹ 13,54,000		
Tax on total income [30% of ₹ 3,54,000 + ₹ 1,12,500]		2,18,700
Add: Health and Education cess@4%		8,748
		2,27,448
Less: **Deduction under section 91**		Nil
[Since agricultural income is exempt in Country M, there is no doubly taxed income. Hence, no deduction under section 91 is allowable]		

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Less: Deduction u/s 90 **(See Working Note below)**		74,100
Tax payable		**1,53,348**
Tax payable (Rounded off)		**1,53,350**

Working Note: Calculation of deduction under section 90

Particulars	₹
Average rate of tax in India [i.e., ₹ 2,27,448 / ₹ 13,54,000 x 100]	16.798%
Tax payable in India on interest from Country Y [₹ 7,60,000 x 16.798%]	1,27,665
Tax paid in Country Y [US $ 950 x 78, being conversion rate as on 31.1.2022 i.e., the last day of the month immediately preceding the month in which tax has been deducted – Rule 128]	74,100
Deduction u/s 90 [being the lower of tax paid on interest income in Country Y and tax payable in India]	**74,100**

Note – *Interest from Country Y represents interest other than interest on securities, in the absence of specific information that the same represents interest on securities. Accordingly, the same has been converted applying the TTBR as on 31.3.2022, being the last day of the P.Y.2021-22. If it is specifically assumed that the same represents interest on securities, then, the TTBR as on 31.3.2021, being the last date of the month immediately preceding the month in which interest became due (April, 2021) has to be considered.*

Question 4

(a) In respect of the following independent case scenarios, you are required to discuss the provisions related to tax deducted at source for the year ended 31st March, 2022:

(i) Tam Electronics Ltd., an Indian company, imports certain computer software from Jam Electronics Inc., a non-resident company based in USA for reselling it to the end users in India. During the F.Y. 2021-22, Tam Electronics Ltd. paid a sum of ₹ 85 crores to Jam Electronics Inc.

(ii) DEHP Ltd., a public sector bank in India, paid ₹ 20 crores to M/s NFGS Ltd., an organisation that provides ATM networks to the banks as commission for facilitating ATM credit/debit cards. NGFS Ltd. also facilitates online convenience banking. It links together the country's ATM in a single network.

(iii) Mr. A received an order from PQR Ltd. to stich T-shirts. To complete such order, he purchased cloth of ₹ 35 lakhs from Fashion Ltd. on 24th May 2021. He stitched T-shirts as per given specifications and supplied to PQR Ltd. He raised a consolidated invoice in the following manner:

Sale of 8000 T-shirts @ ₹ 500 each = ₹ 40,00,000

Fashion Ltd. is closely related to PQR Ltd. as specified under section 40A(2)(b).

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(iv) Mr. David, a Canadian citizen and a non-resident sportsman, received the following sums during the F.Y. 2021-22 from India:

(i) Income from participation in matches ₹ 4,58,000

(ii) Honorarium from writing an article related to sports for a sports magazine ₹ 1,25,000. ***(4 x 2 = 8 Marks)***

(b) MNO Ltd., Mumbai, is engaged in providing IT and communication services. It is a subsidiary company of MNO Inc., USA. During the previous year 2021-22, MNO Ltd. has provided such services to MNO Inc. and similar type of services were also provided to HTY Ltd., Hong Kong. Billing details and other information are given below:

(i) Billing per month to MNO Inc.: USD 85,000

(ii) Billing per month to HTY Ltd.: USD 92,000

(iii) MNO Inc. has given a loan of USD 1,20,000 to MNO Ltd. to purchase hardware for execution of its project. Rate of interest is 4%p.a.

(iv) Direct and indirect cost incurred are USD 120 and USD 210 per hour respectively.

(v) MNO Ltd. works 9 hours per day for 18 days to execute the projects for MNO Inc. and 8 hours per day for 18 days to execute projects for HTY Ltd. MNO Ltd. has provided such services throughout the year to both the customers.

(vi) Warranty was provided to HTY Ltd. for a period of 2 years. Cost of warranty is calculated at the rate of 1.5% of direct cost incurred. The cost of warranty is neither included in the direct nor indirect cost.

Assume all the cost and billing are even throughout the year.

Compute Arm's Length Price as per the cost-plus method and the amount to be added, if any, to the income of MNO Ltd. Assume conversion rate 1 USD = ₹ 75. ***(6 Marks)***

Answer

(a) (i) For the payment in question, since the payment has been made to a non-resident, applicability of TDS will have to be considered as per the provisions of section 195. The obligation to deduct tax at source u/s 195 arises only in respect of any sum chargeable to tax in India.

As per *Explanation 4* to section 9(1)(vi) of the Income-tax Act, 1961, "royalty" includes transfer of all or any right for use or right to use a computer software. Hence, royalty payable by a resident in India to a non-resident company based in USA for the purposes of importing computer software for reselling to end users in India would be deemed to accrue or arise in India in the hands of the non-resident company, and hence, would be chargeable to tax in India in its hands. There being income chargeable to tax in India, TEL is required to deduct tax at source under section 195 at the rates in force as per the provisions of the Income-tax Act, 1961.

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However, as per India-USA DTAA, since Tam Electronics Ltd. (TEL) resells the computer software purchased from Jam Electronics Inc. to resident Indian end-users without modification, the amount paid by Tam Electronics Ltd. to Jam Electronics Inc. for purchase of computer software is not royalty, due to absence of provision akin to *Explanation 4* to section 9(1)(vi) in the DTAA including such payment within the definition of royalty. It was so held by the Supreme Court in *Engineering Analysis Centre of Excellence P. Ltd v. CIT and Another (2021) ITR 471*.

As per section 90(2), where India has entered into a DTAA with a country outside India, the provisions of the Income-tax Act, 1961 will apply only to the extent they are more beneficial to the assessee. In this case, since the DTAA provisions are more beneficial to TEL, the same will prevail over the provisions of the Income-tax Act, 1961. Accordingly, there being no income chargeable to tax in India, TEL is not required to deduct tax at source.

(ii) The relationship between the DEHP Ltd., a public sector bank, and M/s NFGS Ltd., is not of an agency but that of two independent parties on principal-to-principal basis. Therefore, TDS provisions under section 194H would not be attracted on commission payment made by DEHP Ltd., a public sector bank to M/s NFGS Ltd. for ATM network services provided by it. It was so held in *CIT and another vs. Corporation Bank (2021) 431 ITR 554 (Kar).*

Also, section 194J will not apply is case of provision of ATM network services. since the same takes place without manual or human intervention.

(iii) Tax is required to be deducted under section 194C by PQR Ltd. on payment for stitching of T-shirts to Mr. A,

- since the supply of t-shirts is as per the specification of PQR Ltd. and the cloth is purchased from Fashion Ltd., which is an associate of PQR Ltd, specified under section 40A(2), and
- Since a consolidated invoice has been raised, tax would be deducted on the entire amount, including the cost of purchases.

Tax rate would be deducted@1% under section 194C since the contractor is an individual. Therefore, tax to be deducted = ₹ 40,00,000 x 1% = ₹ 40,000.

(iv) Tax is to be deducted under section 194E at 20% on amount payable to a non-resident sportsman who is not a citizen of India for participation in matches and honorarium for writing an article related to sport for a sports magazine.

Further, since Mr. David, a Canadian citizen, is a non-resident, health and education cess@4% on TDS should also be added. Thus the effective TDS rate will be 20.8%

Tax to be deducted = (₹ 4,58,000 + ₹ 1,25,000) x 20.80% = ₹ 95,264 + ₹ 26,000 = ₹ 1,21,264.

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(b) Computation of Arm's Length Price as per Cost Plus Method

Determination of Gross Margin of Comparable Uncontrolled transaction i.e., of HTY Ltd.

Particulars	HTY Ltd. (USD)
Direct Cost (USD 120 x 8 hours x 18 days)	17,280
Indirect Cost (USD 210 x 8 hours x 18 days)	30,240
Total Direct and Indirect cost	**47,520**
Billing per month	92,000
Gross Margin being gross profit	**44,480**
Gross Margin to cost (%) [44,480 x 100/47,520]	**93.60%**
Adjustment for functional difference on account of cost of warranty	
Total Direct and Indirect Cost	47,520.00
Add: Cost of warranty [1.5% of direct cost of USD 17,280]	259.20
Total Cost	**47,779.20**
Billing per month	92,000.00
Margin after cost of warranty being profit margin [92,000 – 47,779.20]	**44,220.80**
Profit margin to cost (%) [after considering functional difference on account of cost of warranty [44,220.80 x 100/47,779.20]	**92.55%**

Computation of Arm's Length Price by applying Cost Plus Method

	MNO Inc (USD)
Direct Cost (USD 120 x 9 hours x 18 days)	19,440.00
Indirect Cost (USD 210 x 9 hours x 18 days)	34,020.00
Total Direct and Indirect cost	53,460.00
Add: **Interest on loan of USD** 1,20,000 borrowed for purchase of hardware [USD 4,800 (i.e., USD 1,20,000@4%) / 12]	400.00
Total Cost	53,860.00
Profit margin by applying the margin of 92.55% of total cost of USD 53,860	49,847.43
Arm's length price of billing per month	**1,03,707.43**
Arm's length price (in ₹) [USD 1,03,707.43 x 75]	77,78,057
Actual Billing per month [USD 85,000 x ₹ 75]	63,75,000
Income to be added to the total income of MNO Ltd. [77,78,057 – 63,75,000] = 14,03,057 x 12 =	1,68,36,684

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Question 5

(a) Answer any two out of the following three sub-parts, viz. (i), (ii) and (iii).

Your answer should cover

(a) Issue involved

(b) Provision applicable

(c) Analysis

(d) Conclusion

(i) During the scrutiny assessment of Refresh Me Ltd., a company engaged in manufacture and distribution of packaged juices, the Assessing Officer (AO) increased the income and thus, passed an order of demand. Aggrieved by the order, the assessee filed an appeal to CIT(A), who confirmed the order of A.O. Assessee further appealed to ITAT and requested ITAT for the stay of collection of tax, which the Honourable ITAT provided initially for 180 days which was further extended till 365 days as provided in section 254(2A) of the Act. The ITAT did not dispose off the appeal before the time extended for collection of tax. The revenue served an order of demand citing the reason that the order of stay automatically gets vacated post the expiry of 365 days. The assessee seeks your opinion as to whether the contention of the revenue is justified.

(ii) On 31.12.2021, a search under section 132 of the Income-tax Act was conducted in the business and residential premises of Mr. Rajshekaran and some gold bars were seized from the locker. Mr. Rajshekaran voluntarily disclosed ₹ 12.50 crores of income during the course of search. Later on, he filed an application for sale of the gold bars worth 5 kgs for adjustment "towards the automatic tax liability", even before the completion of the assessment by the AO. However, AO rejected the application and observed that such action can be taken only after. the assessment is completed and a demand has been quantified.

Is the AO justified in rejecting the application?

(iii) On 31.3.2021, Pastro Ltd. (the assessee) had an outstanding interest liability of ₹ 2 crores towards loan payable to financial institutions. It issued debentures to the financial institutions in lieu of the outstanding interest on 1.5.2021 and deducted the same from the taxable income as payment thereof. The Assessing Officer, however, rejected the deduction claimed by the assessee, by invoking Explanation 3C of section 43B of the Income-tax Act. You are required to discuss the validity of the Assessing Officer's claim. ***(4 x 2 = 8 Marks)***

(b) (i) Explain the correctness or otherwise of the following statements giving proper reasons thereof:

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(A) *Mr. Rikky, a resident individual, is aggrieved by an order passed by the Board for Advance Ruling on 1.10.2021. Since the decision of the Board is binding on the applicant, he has no other option but to accept the ruling of the Board.*

(B) *M/s Aritri Ltd., an Indian public sector company, wants to seek advance ruling from the Board for Advance Ruling (BOAR) in respect of a matter relating to computation of its total income involving a question of law relating to such computation. However, the matter is already pending before the Income-tax Appellate Tribunal (ITAT) as on the date of application for advance ruling i.e., 12.12.2021. It cannot seek the BOAR ruling till the matter is pending before the ITAT.* ***(3 Marks)***

(ii) *M/s Boggle LLC., an entity resident in the USA, owns and operates an online shopping app, Flipzone. On this platform, it facilitates the sale of various kinds of goods owned by different entities. M/s Boggle LLC does not have a permanent establishment in India. During the F.Y. 2021-22, it gives you the following details:*

Particulars	***Amount In ₹***
Receipts from sale of good to persons resident in India using internet from India	*1,96,00,000*
Sale proceeds received from persons resident in India, while visiting some other neighboring countries.	*7,00,000*

You are required to discuss the tax implications of these transactions in respect of M/s Boggle LLC. ***(3 Marks)***

Answer

(a) (i) **Issue Involved:** The issue under consideration is whether the stay order can be automatically vacated upon expiry of extended period of stay of 365 days, where the delay in disposing of the appeal is not attributable to the assessee.

Provision Applicable: The third proviso to section 254(2A) provides that where the appeal filed before the Appellate Tribunal is not disposed of within the period of stay or extended period of stay granted by the Tribunal, the order of stay shall stand vacated after the expiry of 365 days, even if the delay in disposing of the appeal is not attributable to the assessee.

Analysis: This provision would result in the automatic vacation of a stay upon the expiry of 365 days, even if the Appellate Tribunal could not take up the appeal in time for no fault of the assessee. Thus, the vacation of stay in favour of the Department would ensue even if the Department is itself responsible for the delay in hearing the appeal. This will cause undue hardship to the assessee, even where he is not at fault. In this sense, the provision is arbitrary and disproportionate so far as the assessee is concerned.

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Conclusion: The contention of the revenue is **not** justified. Any order of stay shall stand vacated after the expiry of the period or periods mentioned in the section, only if the delay in disposing of the appeal is attributable to the assessee.

Note – *The facts given in the question are similar to the facts in DCIT v. Pepsi Foods Ltd (2021) 433 ITR 295, wherein the above issue came up before the Supreme Court. The above answer is based on the rationale of the Supreme Court ruling in that case.*

(ii) **Issue Involved:** The issue involved in this case is whether Mr. Rajshekaran's application, for adjustment of tax liability on income surrendered during search by sale of seized gold bars, can be entertained where assessment has not been completed.

Provision applicable: The provision contained in section 132B(1) lays down the manner in which the assets seized under section 132 may be dealt with. An assessee is entitled to make an application to the Assessing Officer for adjustment of seized assets towards existing tax liability.

Analysis: Here, the application by the assessee is not for adjustment of any existing liability, but "towards the automatic tax liability". In the said provision, the expression used is "the amount of the liability determined". "A liability is determined" only on completion of the assessment. Until the assessment is complete, it cannot be postulated that a liability has been crystallized.

Conclusion: Accordingly, the action of the Assessing Officer rejecting the application on the ground that such action can be taken only after the assessment is completed and a demand has been quantified, is justified.

Note - *The facts given in the question are similar to the facts in Hemant Kumar Sindhi & Another v. CIT (2014) 364 ITR 555 wherein the issue came up before the Allahabad High Court. The above answer is based on the rationale of the Allahabad High Court in the said case.*

(iii) **Issue Involved:** The issue under consideration is whether issue of debentures in lieu of outstanding interest payable to Financial Institution can be treated as "actual payment" as contemplated under section 43B for allowability as deduction while computing business income.

Provision Applicable: *Explanation 3C* to section 43B clarifies that interest that remained unpaid and converted into a loan or borrowing shall not be deemed to have been actually paid. Hence, such interest would not be deductible while computing profits and gains of business or profession.

Analysis: Interest to bank can be claimed as deduction only when the same if actually paid within the stipulated time. Where it is paid in any subsequent period, it can be claimed in the year of actual payment.

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Explanation 3C to section 43B was enacted to plug the loophole and to overcome the argument of the taxpayer that conversion of outstanding interest into loan would tantamount to actual payment and thus claim deduction under section 43B.

The issue of debentures by the assessee was to extinguish the liability of bank interest altogether. The interest was "actually paid" by the assessee by issuance of debentures, which extinguished its liability to pay interest.

Conclusion: *Explanation 3C* to section 43B, which was meant to plug a loophole, could not be invoked in this case, where debentures were issued in lieu of interest. The interest is, therefore, deductible. The Assessing Officer's claim rejecting the deduction claimed by the assessee is **not** valid.

Note - *The facts given in the question are similar to the facts in M.M. Aqua Technologies Ltd. v. CIT (2021) 436 ITR 582, wherein the issue came up before the Supreme Court. The above answer is based on the rationale of the Supreme Court in the said case.*

It may be noted that this position has undergone a change subsequently consequent to amendment of Explanation 3C to section 43B by the Finance Act, 2022 to provide that conversion of interest into debentures or any other instrument, by which liability to pay is deferred to a future date, would not be deemed as actual payment.

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

The binding provision will not apply to an advance ruling pronounced on or after 1.9.2021 by the Board of Advance Ruling. Therefore, the order passed by the Board for Advance Ruling on 1.10.2021 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.

(ii) M/s. Boggle LLC is an e-commerce operator since it is a non-resident owning and operating an online shopping app for facilitating sale of goods. Equalisation levy is attracted since it does not have a permanent establishment in India. Equalisation levy@2% is leviable on the amount of consideration received or receivable by M/s. Boggle LLC from online sale of goods facilitated by it to persons resident in India, since the aggregate consideration from such sale exceeds ₹ 2 crore in the F.Y.2021-22.

	Particulars	Amount in ₹
(a)	Receipts from sale of goods to persons resident in India using internet from India	196 lakhs

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(b)	Receipts from persons resident in India, even if it is while visiting neighbouring countries	7 lakhs
Amount of consideration		**203 lakhs**

Equalisation levy = 2% of ₹ 203 lakhs = ₹ 4.06 lakhs.

Question 6

(a) In the following independent circumstances, discuss whether the provisions of GAAR would be applicable:

(i) Milo Ltd., an Indian company, is making losses for the past several years. Tilo Ltd., another Indian company, having huge profits acquired Ms. Milo Ltd.

(ii) DAMP Inc., a company incorporated in Country A, holds 1000 equity shares in MAP Ltd., an Indian listed entity since 1.4.2016. On 1.5.2021, MAP Ltd. issued 1000 bonus shares to DAMP Inc. As per the treaty between India and Country A, the capital gain is taxable in the country where the transferor of shares is a resident. The tax laws of Country A, exempt capital gains. DAMP Inc. sells all the shareholding in MAP Ltd. on 1.1.2022 and earned a capital gain of ₹ 5 crores.

(iii) A Ltd., an Indian company, incorporates a wholly owned subsidiary Company B, in Country B which is a Low Tax Jurisdiction with equity share capital of ₹ 1 crore. Out of the equity capital, company B gives loan to C Ltd., an Indian company at the rate of 5%. There is no other activity in Company B.

(iv) Bee Ltd., an Indian company sets up a unit in SEZ in FY 2018-19 for manufacturing of chemicals. It claims 100% deduction of profits of ₹ 100 crores earned from that unit in FY 2021-22, u/s 10AA of the Act. ***(4 Marks)***

(b) The jurisdictional Assessing Officer of Mr. Albert, a non-resident, wants to treat the following persons as his agent in India for AY 2022-23 as per the provisions of section 163 of the Income-tax Act, 1961. You are required to discuss the validity of the Assessing Officer's claims.

(i) Mr. Albert owned a residential house in Goa, India. During the financial year 2021-22, he sold the house to Mr. D'Souza, another non-resident. AO wants to treat Mr. D'Souza as an agent of Mr. Albert.

(ii) Mr. Albert employed Mr. Rakesh, a resident of India, to work for him on 1.4.2020. Mr. Rakesh left India to be employed by Mr. Albert on 1.4.2021. ***(4 Marks)***

(c) Explain the action plan for taxation of income arising from intellectual property rights in India on the basis of OECD recommendations for BEPS action plan-5. ***(2 Marks)***

(d) Significant economic presence of a non-resident in India shall also constitute business connection in India. Explain. ***(2 Marks)***

(e) What is Static approach and Ambulatory approach in interpreting tax treaties? ***(2 Marks)***

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Answer

(a) Applicability of GAAR

(i) In the present case, Tilo Ltd. having huge profits acquired Milo Ltd. a loss-making company. Due to provisions relating to merger and acquisition in the Act and considering that the scheme would have been sanctioned by the High Court/National Company Law Tribunal considering tax implications, GAAR need not be invoked.

(ii) In case of investment made prior to 1.4.2017, income arising from transfer thereof would not be subject to GAAR. Accordingly, income from transfer of shares acquired on 1.4.2016 by DAMP Inc. would not attract GAAR.

If the original shares are acquired before 1.4.2017, but bonus shares are issued after that date, GAAR provisions would not be attracted on transfer of such bonus shares also.

(iii) An impermissible avoidance arrangement means an arrangement, the main purpose or one of the main purposes of which is to obtain a tax benefit and also, *inter alia*, lacks commercial substance or is deemed to lack commercial substance. An arrangement is deemed to lack commercial substance if it involves*, inter alia,* round tripping of funds.

In this case, the arrangement of routing money through wholly owned subsidiary Company B in Country B, a low tax jurisdiction, to an Indian company (C Ltd.) involves round tripping of funds even though funds emanating from A Ltd. are not traced back to A Ltd. The alternate course available in this case is direct advance to C Ltd. an Indian company, in which case the interest income would have been chargeable to tax in the hands of A Ltd.

Therefore, the agreement is deemed to lack commercial substance as it involves round tripping of funds. Also, its main purpose is to obtain tax benefit and there is no other activity in Company B.

However, if the tax benefit in the relevant assessment year arising, in aggregate, to all the parties to the arrangement does not exceed ₹ 3 crore, then, GAAR provisions would not be invoked.

(iv) Bee Ltd. set up a SEZ unit and claiming 100% deduction under section 10AA resulting in tax benefit. However, setting up of SEZ is for the purpose of taking benefit of a fiscal incentive offered for promoting SEZs. In such a case, GAAR provisions would **not** be applicable.

(b) As per section 163, an agent, in relation to a non-resident person, *inter alia* includes

- any person in India who is employed by or on behalf of the non-resident or
- any person (whether resident or non-resident) who has acquired a capital asset in

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India by means of a transfer from the non-resident.

(i) Since Mr. D'Souza acquired residential house in Goa from Mr. Albert, the jurisdictional Assessing Officer can treat Mr. D'Souza as an agent of Mr. Albert even though Mr. D'Souza is a non-resident.

(ii) Mr. Rakesh was employed by Mr. Albert on 1.4.2020. He left India on 1.4.2021 to be employed by Mr. Albert. Since he is not in India during the P.Y. 2021-22, the jurisdictional Assessing Officer cannot treat him as an agent of Mr. Albert for the P.Y. 2021-22.

(c) Approach recommended by the OECD under BEPS Action Plan 5

The nexus approach has been recommended by the OECD under BEPS Action Plan 5 Counter Harmful Tax Practices. This approach requires attribution and taxation of income arising from exploitation of Intellectual property (IP) in the jurisdiction where substantial research and development (R & D) activities are undertaken instead of the jurisdiction of legal ownership.

Accordingly, section 115BBF has been inserted in the Income-tax Act, 1961 line with BEPS Action Plan 5 to provide that where the total income of the eligible assessee includes any income by way of royalty in respect of a patent developed and registered in India, then such royalty shall be taxable at the rate of 10% (plus applicable surcharge and cess).

For this purpose**,** "developed" means atleast 75% of the expenditure should be incurred in India by the eligible assessee for any invention in respect of which patent is granted under the Patents Act.

(d) Significant economic presence of a non-resident in India shall also constitute business connection in India. Significant economic presence means

– Transaction in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India, if aggregate of payments arising from such transaction or transactions during the previous year exceed ₹ 2 crores; or

– systematic and continuous soliciting of business activities or engaging in interaction with atleast 3 lakhs users in India.

(e) Static Approach – under static approach, a term not defined in the treaty to be assigned the meaning which prevailed on the date of signing the tax treaty.

Ambulatory Approach – under Ambulatory approach, a term not defined in the treaty to be assigned the meaning which is prevailing on the date of application of the tax treaty.

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