Answers

Case Study 1.

1.1 B

1.2 C

1.3 D

1.4 C

1.5 C

1.6 The above question is based on ITAT Mumbai ruling in the case of Volkswagen Finance Private Limited vs. ITO. It was held that Mango Phone facelift launch event was India-centric and the entire expenses of the launch event were treated as expenses of Indian entities, namely this assessee and Parimal India Limited. The event has physically taken place in Dubai, UAE, but, beyond any dispute or controversy, the benefits of this event were to accrue to the assessee in India. To put a question to ourselves, what were the benefits of this event, held in Dubai, to the Indian assesses. In our humble understanding, and as the MoU with celebrity's agent unambiguously indicates in so many words- as noted earlier in this order, the predominant benefit of this event was "below the line publicity on internet, in press releases, news reports, social media" for Mango Phone facelift in India. The target audience was in India, the potential customers were in India, the intended benefits were in India, and yet the event was in Dubai UAE. The question then arises whether the income on account of this launch event in Dubai can be said to accrue or arise in India. Let us not forget the fact that the celebrity was to make an appearance in UAE event but admittedly the event was for publicity in India. It was thus a unique

situation in the sense that while the event, in which appearance was made by the celebrity, was held outside India, all the benefits accrued to the assessee in India, and it was on account of these benefits to the assessee that the international celebrity was paid for his participation in the Dubai Mango Phone facelift event. The income thus cleared accrue and arises, on the facts of this case, by the reason of business connection in India.

[Marking scheme: 5 Marks for identifying correct answer]

1.7 The scheme of Section 115 BBA provides for taxation "an entertainer, who is not a citizen of India and is a non- resident, includes any income received or receivable from his performance in India". Thus this section refers to the "performance in India" implying thereby that performance outside India is outside the ambit of taxation in India. However, Section 115 BBA deals with the mode and rate of taxation in the hands of non-resident sportsmen, non-resident sports associations and institutions, and non-resident entertainers. These modalities of taxation, cannot be treated restrictions on chargeability to tax under section 5(2)(b). In case an income is not eligible to specified treatment under section 115BBA, on account of not fulfilling the criterion set out therein, such an income is at best taxable in the normal course in the hands of the non-resident entertainer in India.

[Marking scheme: 2 1/2 marks for 115BBA, 2 ½ marks for balance answer]

1.8 As observed in above 2 answers, although income of Nicolas Cage does have a business connection in India but the same cannot be taxed under section 115BBA since the performance is not done in India. Accordingly, the tax has to be deducted under section 195 instead of section 194E. Failure to withhold tax at source under section 195 will result in Rocks & Logs being treated as assessee in default. However, in case Nicolas Cage pays tax on such income in India and files a return in India considering such income, then Rocks & Logs will not be treated as assessee in default under section 201(1).

[Marking scheme: 2 ½ marks for identifying that assessee is in default, balance for identifying the proviso to section 201(1) and its conditions]

Case Study 2.

2.1 B

2.2 C

2.3 C

2.4 B

2.5 D

2.6 As per well settled rules of Interpretation with regard to taxing statutes, the substitution of a provision results in repeal of earlier provision and its replacement by new provision. [See: **U.P.SUGAR MILLS ASSN. VS. STATE OF U.P.', (2002) 2 SCC 645].** The aforesaid principle of law was reiterated by the Supreme Court in WEST UP SUGAR MILS ASSOCIATION V. STATE OF UP (2012) 2 SCC 773 and by Karntaka High Court in

GOVARDHAN M V. STATE OF KARNATAKA (2013) 1 KarLJ 497. When a new rule in place of an old rule is substituted, the old one is never intended to keep alive and the substitution has the effect of deleting the old rule and making the new rule operative. Thus, in the instant case, it is evident that paragraph 2 of Article 12, which provided for levy of tax on royalties or fees for technical services at the rate not exceeding 12% has been deleted and in its place, the provision which provides for levy of tax on the royalties or fees for technical services at the rate not exceeding 10% has been substituted. Thus, the substitution has the effect of deleting the old rule and making the new rule operative. Therefore, the income by way of royalty and fees for technical services is liable for taxation @ 10% for the entire year.

[Marking scheme: 2 Marks for identifying rule of interpretation, 3 marks for correct answer]

2.7 19,71,61,400/- **[Marking scheme: 2 Marks for correct answer]**

2.8 Mobilisation advance is treated as part of gross receipts. 10 per cent of the same is regarded as presumptive income. The actual expenses for mobilisation is irrelevant

[Marking scheme: 1 Mark for each statement]

2.9 Finance Act 2010 has inserted a proviso below section 44DA which specifically provides that in case income is in the nature of royalty or

fees for technical services, then the assessee is not entitled for availing benefit of section 44BB. This has fundamentally restricted the applicability of section 44BB. This proviso has to be given due consideration and a meaning, recognizing the legislative intent. A plain reading of section 44BB (1) shows that it applies to an assessee who is engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire use, or to be used, in the prospecting for, or extraction or production of mineral oils. However, the proviso thereto carves out an exception that the sub-section shall not apply in a case where the provisions of section 44DA apply for the purpose of computing profits or gains or any other income referred to in those sections. Further, a reading of section 44DA makes it clear that it applies to the character of income which is in the nature of royalty or fees for technical services. The legislative intent behind the amendment is also evident from the memorandum to the Finance Bill 2010 which reads as under:

> "*Under the existing provisions contained in section 44BB(1) of the Income-tax Act, income of a non-resident taxpayer who is engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils is computed at ten per cent of the aggregate of the amounts paid.*
>
> *Section 44DA provides the procedure for computing income of a non-resident, including a foreign company, by way of royalty or fee for technical services, in case the*

right, property or contract giving rise to such income are effectively connected with the permanent establishment of the said non-resident. This income is computed as per the books of account maintained by the assessee.

Section 115A provides the rate of taxation in respect of income of a non-resident, including a foreign company, in the nature of royalty or fee for technical services, other than the income referred to in section 44DA i.e., income in the nature of royalty and fee for technical services which is not connected with the permanent establishment of the non-resident.

Combined effect of the provisions of sections 44BB, 44DA and 115A is that *if* the income of a non-resident is in the nature of fee for technical services, it shall be taxable under the provisions of either section 44DA or section 115A irrespective 'of the business to which it relates. **Section 44BB applies only in a case where consideration is for services and other facilities relating to exploration activity which are not in the nature of technical services. However, owing to judicial pronouncements, doubts have been raised regarding the scope of section 44BB vis-a-vis section 44DA as to whether fee for technical services. relating to the exploration sector would also be covered under the presumptive taxation provisions of section44BB.**

In order to remove *doubts and clarify the distinct scheme of taxation of income by way of fee for technical services,*

it is proposed to amend the proviso to section 44BB so as to exclude the applicability of section 44BB to the income which is covered under section 44DA. Similarly, section 44DA is also proposed to be amended to provide that provisions of section 44BB shall not apply to the income covered under section44DA.

This proviso reinforces the legislative intent to carve out an exception to the character of the income referred to in this section i.e. royalty and fees for technical services. The principles relating to interpretation of statute, emphatically lay down that statute should be interpreted to preserve the legislative intent. A reading of the overall scheme of section 44BB and 44DA leaves no manner of doubt that section 44BB applies if the assessee is engaged in the business of providing services or facilities in the prospecting for, or extraction or production of minerals oils. However, if income earned by such assessee takes the colour of royalty or FTS, then the computation for the purposes of determining "*profits and gains of business or profession*" is to be done as per the provisions of section 44DA of the Act. Therefore, in the current scenario if the income of the assessee is Royalty or FTS, then the same would be taxed under Section 9(1)(vi)/(vii) read with Section 115A or 44DA, as the case may be and section 44BB would have no application in the said scenario.

[Marking scheme: 2 Marks for identifying correct proviso from the provisions, balance 3 marks for correct answer]

Case Study 3.

3.1 A

3.2 B

3.3 D

3.4 D

3.5 D

3.6 As far as countries with which there is no DTAA, the foreign tax credits are granted unilaterally under section 91(1) of the Income Tax Act, 1961. A plain reading of this statutory provision shows that double taxation of an income is a condition precedent for this relief because the relief is granted only with respect to "such doubly taxed income", and when there is no income which has been taxed doubly, there is no question relief being granted under section 91(1). The word 'such' in the phrase 'such doubly taxed income' has reference to the foreign income which is again being subjected to tax by its inclusion in the computation of the income under the Act. Thus, it is clear that the relief under section 91 of the Act is limited only to the amount of tax paid on such doubly taxed income at the Indian rate of tax or the rate of tax of the foreign country, whichever is the lower, or at the Indian rate of tax, if both the rates are equal. As no part of the income earned abroad had actually suffered tax in India, relief under section 91 is not admissible in respect of the same.

[Marking scheme: 1 mark for conditions under section, 3 Marks for the answer]

3.7 The foreign tax credit claim in respect of countries with which India has a DTAA is concerned, the OECD Model states that:

ARTICLE 24- METHODS FOR ELIMINATION OF DOUBLE TAXATION

1. The laws in force in either of the Contracting States will continue to govern the taxation of income in the respective Contracting States except where provisions to the contrary are made in this Agreement.
2. Double taxation shall be eliminated in India as follows:
   (a) Where a resident of India derives income which, in accordance with the provisions of this Agreement, may be taxed in one contracting state, India shall allow as a deduction from the tax on the income of that resident, an amount equal to the tax paid in one contracting state. Such deduction shall not, however, exceed that portion of the tax as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in other contracting state.
   (b) Where in accordance with any provision of the Agreement income derived by a resident of India is exempt from tax in India, India may nevertheless, in calculating the amount of tax on the remaining income of such resident, take into account the exempted income.

It is clear that in this case also the foreign tax credit is restricted to the Indian tax attributable to the income which has been taxed in other contracting state. No part of the said income has been taxed in India inasmuch the total income of the assessee was a negative figure. There is no question of any admissible foreign tax credit in this year. In any event, any such foreign tax credit, on the facts of this case, will result in a refund of taxes paid to the other contracting state by the Indian

exchequer- something clearly impermissible. Hence, such foreign tax credit is not admissible.

[Marking scheme: 4 Marks for complete correct answer]

3.8 As per ruling in PILCOM Limited, even when there is DTAA, the payer is required to withhold tax as per provisions of section 194E in respect of payments covered under section 115BBA. However, as per Finance (No.2) Act, 2019, in case any payer fails to withhold tax at source but the resident payee has furnished return in India, considered such income and paid due taxes thereon, in such case, the payer shall not be considered as assessee in default. Therefore, suppose a company say ABC Limited does not withhold appropriate taxes at source, it may still take a stand that when payee furnishes return in India, considers the amount paid as his income and pays due taxes thereon, then ABC Limited ceases to be assessee in default in respect of the tax. However, naturally, interest under section 201(1A) @ 1% will be attracted till such return is furnished in India.

[Marking scheme: 1 Marks for identifying correct amendments, balance 2 marks for critical examination of provisions]

3.9 Separate payments made towards drawings and designs (described as "engineering fee") are in the nature of fees for technical services [Aeg Aktiengesllschaft v. CIT (2004) 267 ITR 209 (Kar.)]. Fees for technical services payable by a resident (Super Thermal Power Ltd., an Indian company, in this case) would be deemed to accrue or arise in India

under section 9(1)(vii) in the hands of the non-resident recipient (Techno Engineering GMBH, the German company).

The payment made is not in respect of services utilized for a business or profession outside India or for the purpose of making or earning income from any source outside India and, therefore, is deemed to accrue or arise in India as per section 9(1).

Further, as per Explanation to section 9, where income is deemed to accrue or arise in India under section 9(1)(vii), such income shall be included in the total income of the non-resident German company, regardless of whether it has a residence or place of business or business connection in India, and even if such services are rendered from outside India.

Accordingly, in this case, payments towards drawings and designs would taxable in India in the hands of Techno Engineering GMBH, the German company.

[Marking scheme: 4 Marks for correct discussion and answer]

Case Study 4.

4.1 D

4.2 B

4.3 A

4.4 C

4.5 A

4.6 The facts of the above are based on decision in the case of Unnikrishnan VS vs. ITO (ITAT Mumbai). In the said case, it was held that in respect of ESOP benefit, while the income has arisen to the assessee in the year of exercise as per Section 17(2)(vi), admittedly the related rights were granted to the assessee in the year when he was a resident and in consideration for the services which were rendered by the assessee prior to the rights being granted - which were rendered in India all along. The character of income may be inchoate at that stage but certainly what is being sought to be taxed now, on account of the specific provision under section 17(2)(vi), is a fruit of services rendered much earlier and the benefit, which has now become a taxable income, accrued to the assessee in 2018. All that section 17(2)(vi) decides is the timing of an income, but it does not dilute or negate the fact that the benefit, in which is being sought to be taxed, had arisen much earlier i.e. at the point of time when the ESOP rights were granted. On these facts, it was held that even if it was inchoate at the point of time when the options were granted, has accrued and has arisen in India. The assessee is a nonresident in the current assessment year, but quite clearly, the benefit, in respect of which the income is bring sought to be taxed now, had arisen at an earlier point of time in India. Viewed thus, the income in respect of ESOP grant benefit accrued and had arisen at the point of time when the ESOP rights were granted, even though the taxability in respect of the same, on account of the specific legal provisions under section 17(2)(vi), has arisen in the present in this year. The same is therefore taxable in India.

[Marking scheme: 1 Mark for identifying correct stage of taxation, 4 Marks for correct answer]

4.7 Article 15 of India – UAE DTAA permits taxation of ESOP benefit, which is included in the scope of the expression "other similar remuneration" appearing immediately after the words "salaries and wages", in the jurisdiction in which the related employment is exercised. Thus, in case the assessee is to get ESOP benefits in respect of his service in U.A.E. and he exercises these options at a later point of time, say after returning to India and ceasing to be a non-resident, he will still have the treaty protection of that income under article 15(1). This principle, however, is not a one-way route. Conversely, when the assessee gets the ESOP benefit on account of rendering services in India, he cannot have the benefit of article 15 in respect of the said income. The reason is simple. Article 15(1) itself provides that "salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State" and so far as the "other similar benefits" are concerned, which include the ESOP benefits, the employment is exercised in the other contracting State, i.e., in India. As much as the nexus is required to be between salaries and wages vis-à-vis the employment, the nexus is also required between other similar benefits vis-à-vis the employment; what hold goods for the former holds good for the latter as well. In the absence of nexus of 'other similar benefits', as wages and salaries, received by the assessee vis-à-vis his employment in the U.A.E., the treaty protection of the said income in India cannot be available to a resident of the U.A.E.

[2 marks for identifying Other similar remuneration, balance marks for analysis]

4.8 Rental Income – taxable for Radhakrishan

Dividend Income from SPV – Taxable for Radhakrishnan in case SPV has opted for Section 115BAA

Capital Gains on sale of development properties – Exempt for Radhakrishnan

[2 Mark for Dividend taxation, 1 mark each for balance two points]

Case Study 5.

5.1 A

5.2 B

5.3 D

5.4 B

5.5 B

5.6 The contentions of New York Limited are not acceptable. Buy Back Distribution tax [BBDT] is an obligation cast in India on the company conducting buy back. The said responsibility cannot be shifted on the shareholders. Further, no credit of BBDT is available in USA since as per section 115QA, BBDT is a final tax for which no credit is available to the shareholder. The capital gains shall be exempt for shareholder u/s. 10(34A) of the Income-tax Act.

[Marking scheme: 2 Marks for identifying that New York Limited is wrong. 4 marks for identifying that no credit is available]

5.7 Admittedly since the BBDT is paid by company, there is no question of taxing capital gains in the hands of New York Limited. The assessee has four options:

(a) Try to convince the AO by relying on Circular 14 – XL of 1955 that this being not real income, the same should not be taxable for New York Limited

(b) File an application under section 154 to get this "mistake" rectified;

(c) File an application for revision under section 264;

(d) File an appeal to CIT(A) against order of assessment;

[Marking scheme: 1 Mark for each point]

5.8 No, the income is not taxable in the hands of New York Limited. Accordingly, no question of seeking credit for BBDT

[Full marks for correct answer]

5.9 Capital Gains on which BBDT is paid is exempt in India as per Section 10(34A). But the same is exempt in India. The same may not be true in USA. In USA, the said income may be taxable as per its domestic tax

laws. This causes Economic Double Taxation since the capital gains [or distributed income] is taxed in India in the hands of Maharashtra Limited and the same capital gains is taxable in USA in the hands of New York Limited. Hence, in principle, the credit for BBDT paid in India should be in USA as foreign tax credit. The same however, is subject to the specific provisions of DTAA between India and USA.

[Full marks for correct answer]