# ELECTIVE PAPER 6C: INTERNATIONAL TXATION

## SUGGESTED SOLUTION – CASE STUDY 2

### ANSWERS TO OBJECTIVE TYPE QUESTIONS

1. (d) Non-resident for P.Y. 2017-18 and Resident and ordinarily resident for P.Y. 2013-14

2. (b) Tax rebate of INR 2,500 from tax payable on her total income of INR 3,40,000

3. (d) Neither (a) nor (b)

4. (a) Basic Salary paid outside India

5. (d) Normal tax slab rates

6. (b) if she has income exceeding the basic exemption limit but after taking into account deduction under Chapter VI-A, her income falls below the basic exemption limit

7. (c) No capital gains would arise on sale of 300 GDRs, but capital gains arising on sale of 200 GDRs shall be taxed in India @10% without indexation benefit

8. (c) Civil Construction in connection with an approved turnkey project

9. (a) taxable @10%

10. (c) A broker in India dealing with the non-resident person only through a non-resident broker, where both non-residents carry on transactions in the ordinary course of business

### ANSWERS TO DESCRIPTIVE QUESTIONS

1. (i) In accordance with the provisions of section 115A, where the total income of a non-corporate non-resident includes any income by way of royalty or fees for technical services other than the income referred to in section 44DA(1), received from an Indian concern in pursuance of an agreement made by him with the Indian concern and the agreement is approved by the Central Government, then, the special rate of tax at 10% of such fees for technical services is applicable. No deduction would be allowable under sections 28 to 44C while computing such income.

Section 90(2) makes it clear that where the Central Government has entered into a DTAA with a country outside India, then, in respect of an assessee to whom such agreement applies, the provisions of the Act shall apply to the extent they are more beneficial to the assessee. Therefore, if the DTAA provides for a rate lower than 10%, then, the provisions of DTAA would apply.

(a) In this case, since India does not have a DTAA with Country 'X', of which the Abhinav is a resident, the fees for technical services (FTS) of INR 10,00,000 from ABC Ltd. would be taxable @10%, by virtue of section 115A.

(b) In this case, the FTS from ABC Ltd. would be taxable @5%, being the rate specified in the DTAA, even though section 115A provides for a higher rate of tax, since the tax rates specified in the DTAA are more beneficial. However, since Abhinav is a non-resident, he has to furnish a tax residency certificate from the Government of Country X for claiming such benefit. Also, he has to furnish other information, namely, his nationality, his tax identification number in Country X and his address in Country X

(c) In this case, the FTS from ABC Ltd. would be taxable @10% as per section 115A, even though DTAA provides for a higher rate of tax, since the provisions of the Act (i.e. section 115A in this case) are more beneficial.

(ii) Under section 206AA, any person who is entitled to receive any sum or income or amount on which tax is deductible under Chapter XVII-B has to furnish his Permanent Account Number (PAN) to the person responsible for deducting such tax, failing which tax shall be deducted at –

- the rate mentioned in the relevant provisions of the Act or
- the rate or rates in force or
- the rate of 20%

whichever is higher.

For the purpose of reducing the compliance burden of non-corporate non-residents or foreign company, section 206AA(7) provides for non-applicability of the requirements contained in section 206AA to a non-corporate non-resident or foreign company, in respect of interest on long-term bonds as referred to in section 194LC and any other payment subject to prescribed conditions.

As per Rule 37BC, the provisions of section 206AA shall not apply to a non-corporate non-resident or foreign company not having PAN in respect of payments in the nature of interest, royalty, fees for technical services and payments on transfer of any capital asset, if the deductee furnishes the following details and documents to the deductor:

- Name, e-mail id, contact number;
- address in the country or specified territory outside India of which the deductee is a resident;

- a certificate of his being resident in any country outside India from the Government of that country, if the law of that country provides for issuance of such certificate;
- Tax Identification Number of the deductee in the country of his residence. In case no such number is available, then a unique number on the basis of which the deductee is identified by the Government of that country or the specified territory of which he claims to be a resident.

Hence, if Mr. Abhinav fails to furnish the PAN details to ABC Ltd., then the company can obtain the above information from him and deduct TDS @10% in accordance with provisions of section 115A. If he is not able to furnish the requisite details, tax has to be deducted @20% under section 206AA, being the highest of the following rates –

- rate under section 115A i.e., 10%,
- rates in force i.e., 10%,
- 20%.

(iii) By virtue of section 44DA, the income by way of fees for technical services received by Mr. Abhinav from ABC Ltd., India, would be computed under the head "Profits and gains of business or profession" in accordance with the provisions of Income-tax Act, 1961, since technical services are provided from a fixed place of profession situated in India and fees for technical services is received from an Indian concern in pursuance of an agreement with the non-resident and is effectively connected with such fixed place of profession. No deduction would, however, be allowed in respect of any expenditure or allowance which is not wholly and exclusively incurred for the fixed place of profession in India.

Mr. Abhinav is required to keep and maintain books of account and other documents in accordance with the provisions contained in section 44AA and get his accounts audited by an accountant and furnish the report of such audit in the prescribed form duly signed and verified by such accountant along with the return of income.

2. (i) The statement is **incorrect**, since as per section 195(1), the obligation to deduct tax at source from interest and other payment to non-resident which are chargeable to tax in India, is on “any person responsible for paying to a non-resident or to a foreign company”. The words “any person” used in section is intended to include both residents and non-residents. Therefore, if the income of payee non-resident is chargeable to tax, then tax has to be deducted at source, whether the payment is made by a resident or non-resident.

Further, *Explanation 2* to section 195(1) also clarifies that the obligation to comply with section 195(1) and to make deduction thereunder applies and shall be deemed to have

always applied and extends to all persons, resident or non-resident, whether or not the non-resident has:

(a) a residence or place of business or business connection in India; or

(b) any other presence in any manner whatsoever in India.

(ii) Section 194A requiring deduction of tax at source on any income by way of interest, other than interest on securities credited or paid to a resident, excludes from its scope, income credited or paid by a firm to its partner. However, section 195 which requires tax deduction at source on payment to non-residents, does not provide for any exclusion in respect of payment of interest by firm to its non-resident partner. Therefore, tax has to be deducted under section 195 @ 30%, being the rate in force in respect of Interest on capital paid to Mr. Abhinav.

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

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

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

Hence, M/s Lotus & Co., India can claim tax refund of excess tax deducted at source under section 195 where tax has been deducted at source at the rate of 30% provided under the Income-tax Act, 1961 while a lower rate i.e., 10% is prescribed under the DTAA with Country 'X'.

**3. Computation of Total Income of Mr. Abhinav for A.Y. 2018-19**

| Particulars | INR | INR | INR |
|---|---|---|---|
| **Profits & Gains of Business & Profession** | | | |
| Income from partnership firm M/s Lotus & Co., India | | | |
| - Interest on Capital *[See Note (ii)]* | | 5,00,000 | |
| - Share of Profit | 4,00,000 | | |

| | | | |
|---|---|---|---|
| *Less:* Exempt under section 10(2A) | (4,00,000) | - | |
| Fees for technical services received from ABC Ltd., India | | 10,00,000 | |
| Fees for technical services received from Government of Country "Y" *[See Note (iii)]* | | | 15,00,000 |
| **Capital Gains *[See Working Note]*** | | | |
| Short-term capital gain on sale of shares of - | | | |
| - PQR Pvt. Ltd. | 1,500 | | |
| - Hello Pvt. Ltd | 1,80,000 | 1,81,500 | |
| Long- term capital gain on sale of shares of | | | |
| - PQR Pvt. Ltd. | Nil | | |
| - Prime Pvt. Ltd. | 72,500 | 72,500 | 2,54,000 |
| **Income from Other Sources** | | | |
| Interest earned on deposits: | | | |
| - Interest earned on NRO saving deposits | | 4,000 | |
| - Interest earned on fixed deposits | | 5,000 | |
| - Interest on NRE savings account [Exempt u/s 10(4)(ii)] *[See Note (v)]* | | - | 9,000 |
| **Gross Total Income** | | | 17,63,000 |
| ***Less:* Deductions under Chapter VI-A** | | | |
| **Deduction under section 80C *[See Note (viii)]*** | | | |
| Life insurance premium for self and his spouse | 50,000 | | |
| Term deposit [Five year term deposit] | 60,000 | | |
| Repayment of housing loan borrowed for construction of residential house | - | 1,10,000 | |
| **Deduction under section 80D [*See Note (ix)]*** | | | |
| Health insurance of self and spouse | 20,000 | | |
| Health insurance of mother | 25,000 | 45,000 | |
| **Deduction u/s 80TTA *[See Note (x)]*** | | 4,000 | 1,59,000 |
| **Total Income** | | | **16,04,000** |

**Computation of Tax Liability of Mr. Abhinav for A.Y. 2018-19**

| Particulars | INR | INR |
|---|---|---|
| Tax@10% on fee for technical services under section 115A | | 1,00,000 |
| Tax@10% on long-term capital gain on sale of foreign exchange assets under section 115E[1] | | 7,250 |
| Tax on balance income of INR 5,31,500 (i.e., INR 6,90,500 - INR 1,59,000) | | 18,800 |
| | | 1,26,050 |
| *Add:* Education cess @2% | 2,521 | |
| Secondary higher education cess @1% | 1,261 | 3,782 |
| **Tax liability** | | **1,29,832** |
| **Tax liability (rounded off)** | | **1,29,830** |

**Woking Note:**

**Computation of Capital Gain on sale of shares purchased in convertible foreign currency**

| Particulars | INR |
|---|---|
| **LTCG on sale of shares of Prime Pvt. Ltd., since held for more than 24 months** | |
| *(As per the provisions of Chapter XII-A, long term capital gain, on sale of any specified asset in foreign currency, shall be calculated at flat rate of 10% without indexation. Shares of Prime Pvt. Ltd fall under the category of "specified assets")* | |
| Sale Consideration | 12,00,000 |
| *Less:* Cost of Acquisition | (6,20,000) |
| Long term capital gain | 5,80,000 |
| *Less:* Exemption under section 115F | |
| 5,80,000*10,50,000/12,00,000 | (5,07,500) |
| **Long-term capital gain as per Chapter XII-A** | **72,500** |
| *(**Note** - Since within a period of six months after the date of transfer of a long term foreign exchange asset, Mr. Abhinav has invested part of the net consideration in any specified asset, namely shares of Cheers Pvt. Ltd., he is eligible to claim proportionate deduction as per section 115F)* | |

[1] Since the question specifies that the Abhinav has opted for Chapter XII-A, the resultant long-term capital gains would be taxable @10%, after providing for proportional exemption under section 115F, which is available in respect of investment of net consideration in another specified asset, shares of a private company in this case. It would have been more beneficial for Abhinav to have not opted for Chapter XII-A, as he could have claimed exemption of the entire capital gain of INR 5,80,000 under section 54F, since the amount invested in construction of house at Pune exceeds the net sale consideration of INR 12 lakhs on sale of shares of Prime Pvt Ltd.

| | |
|---|---|
| **STCG on sale of shares of Hello Pvt. Ltd., since held for less than 24 months** | |
| Sale Consideration | 9,30,000 |
| *Less:* Cost of Acquisition | (7,50,000) |
| **Short term Capital Gain** | **1,80,000** |
| *(Provisions of Chapter XII-A are only applicable in respect of long term capital gain from transfer of foreign exchange assets.)* | |

**Computation of Capital Gain on sale of shares of PQR Pvt. Ltd.**

| Particulars | INR |
|---|---|
| **LTCG on sale of 1500 shares acquired on October 1, 2015** | |
| *(As per section 2(42A), share of an unlisted company, if sold after period of 24 months from the acquisition date will be considered as long-term capital asset)* | |
| Sale Consideration [1,500 x INR 15] | 22,500 |
| *Less:* Cost of Acquisition [1,500 x INR 10] | (15,000) |
| **Long term Capital Gain** | **7,500** |
| *Less:* Exemption u/s 54F [since the amount invested in construction of house at Pune exceeds the net sale consideration of INR 22,500 on sale of shares, the entire capital gain would be exempt. The construction of the house in Pune was completed within the prescribed time i.e., within three years after the date of transfer] | 7,500 |
| | Nil |
| **STCG on sale of 500 shares acquired on October 31, 2016** | |
| Sale Consideration [500 x INR 15] | 7,500 |
| *Less:* Cost of Acquisition [500 x INR 12] | (6,000) |
| **Short term Capital Gain** | **1,500** |

**Notes:**

(i) Mr. Abhinav is a person who, staying outside India, comes on a visit to India every year. Hence, the minimum period of stay in India for Mr. Abhinav to be treated as a resident is 182 days in any previous year. For A.Y.2018-19, Mr. Abhinav is a non-resident since his stay in India in the P.Y.2017-18 is less than 182 days. In case of a non-resident, only income which accrues or arises or is deemed to accrue or arise in India or is received or is deemed to be received in India is taxable in India. Income which accrues or arises outside India is not taxable in India. Rental income from property in Country 'X' received there and subsequently brought to India is not taxable in India in the hands of Mr. Abhinav, since it neither accrues to him in India nor is it received by him in India.

(ii) Interest on capital paid by the partnership firm is includible as business income in the hands of the partner, only to the extent the interest is allowed as deduction in the hands of firm. In

this case, the entire interest of INR 5 lakhs is included in the income of Mr. Abhinav assuming that the same has been fully allowed as deduction in the hands of firm.

(iii) Fees for technical services received from ABC Ltd., an Indian company, would be chargeable to tax under the head "Profits and gains of business or profession" in the hands of Mr. Abhinav. Since Mr. Abhinav is a resident of a country 'X' with which India has no DTAA, such fees for technical services would be taxable @10% as per section 115A.

However, fees for technical services received in foreign currency by Mr. Abhinav from the Government of Country "Y" would not be taxable in India, since such income has neither accrued in India nor is the same received in India.

(iv) As per section 9(1)(v)(c), interest payable by a non-resident would be deemed to accrue or arise in India, where the interest is payable on any debt incurred, or money borrowed and used, for the purpose of a business or profession carried on by such non-resident in India. In the present case, Mr. George, a non-resident had purchased bonds of MNO Ltd., an Indian company out of the money borrowed. Consequently, the interest received by Mr. Abhinav in foreign currency equivalent to INR 1,95,000 will not be taxable in India, since such interest is neither received nor is it deemed to accrue or arise in India. Mr. George is a non-resident in India for A.Y.2018-19 since his stay in India during the P.Y.2017-18 is only 36 days.

(v) As per section 10(4)(ii), in case of an individual, any income by way of interest on moneys standing to his credit in Non-resident External Account (NRE A/c) would be exempt, provided the individual is a person resident outside India, as defined in Foreign Exchange Management Act (FEMA), 1999. Here, it is assumed that Mr. Abhinav qualifies to be person resident outside India as per FEMA, 1999 and hence, interest of INR 9,000 from NRE A/c is exempt from tax in his hands.

(vi) Transfer outside India of Rupee denominated bonds of an Indian company issued outside India and Government Securities through an intermediary dealing settlement of securities by Mr. Abhinav, a non-resident, to Mr. Thomas, another non-resident, would not be regarded as a transfer under section 47 for levy of capital gains tax. Thomas is a non-resident since he has stayed in India only for 100 days in the P.Y.2017-18. Being a citizen of India residing in Country "X", he has to come and stay in India for atleast 182 days in a year to be treated as a resident.

(vii) As per section 64(1A), all income accruing to minor child is includible in the hands of the parent, whose total income before including minor's income is higher, after providing deduction of INR 1,500 per child under section 10(32). However, if minor child has earned the income because of his skill or talent then it will not be included in the hand of parents. Hence,

income generated by Mr. Abhinav's minor son, Kapil, by winning Science Olympiad shall not be clubbed with Mr. Abhinav's income.

(viii) Under section 80C, deduction is allowed for life insurance premium paid for self or spouse or any child, even though such premium is paid outside India. It is assumed that the annual premium is not more than 10% of actual capital sum assured. However, deduction in respect of tuition fees paid by individual to any university, college, school or other educational institution for full time education of his two children would be allowed only if, such institution is situated in India. Thus, payment for life insurance premium paid by Mr. Abhinav is fully allowable as deduction but no deduction would be allowed for annual tuition fees, since it is for education abroad. Further, no deduction is allowable under section 80C for A.Y.2018-19 in respect of repayment of housing loan, since the property in Pune is under-construction and no amount is chargeable to tax as income from house property, during the previous year 2017-18.

(ix) Mr. Abhinav is eligible for deduction of INR 20,000 in respect of health insurance premium of self and spouse, since the same is less than INR 25,000. He is also eligible for deduction in respect of premium paid for insuring the health of his mother, subject to a maximum of INR 25,000. However, he would not be eligible for claiming higher deduction of upto INR 30,000 under section 80D, as applicable to senior citizen, for the insurance on the health of his mother, since she is non-resident. Further, he is not eligible for any deduction in respect of the premium paid to insure the health of his sister, Ms. Geetha, since sister is not included within the definition of "family".

(x) As per section 80TTA, deduction in respect of interest earned on savings deposits with a bank, co-operative society carrying on the business of banking or post office is allowed to the extent of INR 10,000. Mr. Abhinav can, therefore, claim deduction u/s 80TTA on account of NRO saving bank interest of INR 4,000. However, no deduction is allowed on interest earned on time deposits.

Therefore, interest earned on fixed deposits by Mr. Abhinav shall not be eligible for deduction under section 80TTA.