MOCK TEST PAPER 1

FINAL (NEW) COURSE: GROUP – II

PAPER – 7: DIRECT TAX LAWS & INTERNATIONAL TAXATION

SOLUTIONS

Division A – Multiple Choice Questions

1. (c)
2. (d)
3. (c)
4. (c)
5. (a)
6. (c)
7. (d)
8. (c)
9. (c)
10. (d)
11. (b)
12. (c)
13. (b)
14. (a)
15. (d)
16. (c)
17. (d)
18. (d)
19. (d)
20. (a)

Division B – Descriptive Choice Questions

1. Computation of Total Income of TrustMe Private Ltd. for the A.Y.2019-20

	Particulars	Amount (Rs.)	
I	**Income from house property**		
	[Rental income from commercial property]		
	Gross Annual Value[1]/Net Annual Value[2]	4,30,000	
	Less: Deduction under section 24(a)		
	30% of Net Annual Value	1,29,000	
			3,01,000

[1] Rent received has been taken as the Gross Annual Value (GAV) in the absence of information relating to Municipal Value, Fair Rent and Standard rent.
[2] Since the question does not contain information about municipal taxes paid, the net annual value is the same as the GAV.

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II	**Profits and gains of business and profession**		
	Profits from manufacturing business **[See Working Note below]**	70,88,000	
	Less: Set-off of losses from trading in derivatives in shares in a recognized stock exchange [allowed to be set-off against profits from the business of manufacturing as per section 70(1) since it is not speculative in nature **[See Note below]**	1,80,000	
			69,08,000
III	**Capital Gains**		
	Sale consideration	52,00,000	
	Less: Indexed Cost of Acquisition [Rs. 50,00,000 × 280/264]	53,03,030	
	Long-term capital loss to be carried forward to A.Y.2020-21 for set-off against long-term capital gains, if any, in that year	(1,03,030)	
IV	**Income from Other Sources**		
	Rent received from vacant land	2,05,000	
	Interest received on income-tax refund	42,000	
	Excess of issue price of shares over the fair market value of shares is taxable as per section 56(2)(viib) in the case of TrustMe Private Ltd., not being a company in which public are substantially interested [Rs. 40 (i.e., Rs. 100 – Rs. 60) × 1,00,000 shares]	40,00,000 – –	42,47,000
	Gross Total Income		**1,14,56,000**
	***Less:* Deductions under Chapter VI-A**		
	Deduction under section 80G		
	Donation to Swachh Bharat Kosh [qualifies for 100% deduction – assuming that the same has not been spent in pursuance of corporate social responsibility under section 135(5) of the Companies Act, 2013]	70,000	
	Deduction under section 80GGB		
	Contribution to Political Party [Not allowable as deduction since the contribution is made in cash]	Nil	70,000
	Total Income		**1,13,86,000**

Working Note:

Computation of profits and gains from the business of manufacturing

Particulars	Amount (Rs.)	
Net profit as per statement of profit and loss		77,00,000
***Add:* Items debited but to be considered separately or to be disallowed**		
B(ii) Donation paid to Swachh Bharat Kosh, considered separately	70,000	
[Not an expenditure incurred wholly and exclusively for the manufacturing business. Hence, not allowable under section 37]		
B(iii) Contribution to political party	1,50,000	
[Not an expenditure incurred wholly and exclusively for the manufacturing business. Hence, not allowable u/s 37]		

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B(iv) Payment to transport contractor [As per section 194C(6), no tax is required to be deducted at source since the payment is to a transport contractor not having more than 10 goods carriages at any time during the previous year and he has given a declaration to that effect along with his PAN. Hence, disallowance under section 40(a)(ia) for non-deduction of tax at source is not attracted. Also, since payment is made by account payee cheque, no disallowance under section 40A(3) is attracted].	-	
B(v) Bonus to employees [Since the payment is made after the due date of filing return of income, disallowance under section 43B is attracted]	3,20,000	
B(vi) Provision for income-tax (including interest of Rs. 70,000 thereon) [Not allowable as deduction. Disallowance under section 40(a)(ii) is attracted]	4,20,000	
B(viii) Loss from trading in derivatives in shares in a recognized stock exchange [See Note below] [Since loss from trading in derivatives in shares is not related to the business of manufacturing, the same is not incurred wholly and exclusively for this business, and hence, is not allowable as deduction under section 37 while computing profits from the business of manufacturing]	1,80,000	
		11,40,000
		88,40,000
Add: **Cash Payment for purchase of raw material deemed as income** AI(1) [Since the provision for outstanding bill for purchase of raw material has been allowed as deduction during the P.Y.2017-18, cash payment in excess of Rs. 10,000 against such bill in the P.Y.2018-19 would be deemed as income of P.Y.2018-19 as per section 40A(3A)]		45,000
		88,85,000
Less: **Expenditure to be allowed** B(i) & AI(4) Depreciation [Difference between the normal depreciation of Rs. 16.75 lakhs as per Income-tax Act, 1961 **[See Note below]** and depreciation charged to the statement of profit and loss of Rs. 11.75 lakhs]. ***Note*** – [3]*Printers and scanners form an integral part of the computer system and they cannot be used without the computer. Hence, they are part of the computer system, they would be eligible for depreciation at the higher rate of 40% applicable to computers including computer software. However, EPABX is not a computer and is, hence, not entitled to higher depreciation@40%*[4]	5,00,000	

Particulars	Rs.
Depreciation computed as per Income-tax Act, 1961	18,00,000

[3] *CIT v. BSES Yamuna Powers Ltd (2013) 358 ITR 47 (Delhi)*

[4] *Federal Bank Ltd. v. ACIT (2011) 332 ITR 319 (Kerala)*

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Less: Depreciation@40% wrongly provided in respect of EPABX = 40% of Rs. 5,00,000	2,00,000		
	16,00,000		
Add: Depreciation@15% on EPABX = 15% of Rs. 5,00,000	75,000		
Correct Depreciation as per Income-tax Act, 1961	**16,75,000**		
AI(5) **Additional depreciation on new plant and machinery** Since plant and machinery was purchased only on 18.11.2018, it was put to use for less than 180 days during the year. Hence additional depreciation is to be restricted to 10% (i.e., 50% of 20%) of Rs. 34 lakhs.[5]		3,40,000	
AI(6) **Audit Fees relating to P.Y.2017-18** [Rs. 30,000, being 30% of audit fees of Rs. 1,00,000 provided for in the books of account of F.Y.2017-18 would have been disallowed due to non-deduction of tax at source. Since tax has been deducted in September, 2018 and paid on 6.10.2018, the amount of Rs. 30,000 is deductible while computing business income of P.Y.2018-19].		30,000	
B(vii) **Contribution to University** [Contribution to a University approved and notified under section 35(1)(ii) would qualify for weighted deduction@150%. Since Rs. 1,00,000 has already been debited to the statement of profit and loss, the balance Rs. 50,000 has to be deducted while computing business income]		50,000	9,20,000
			79,65,000
***Less:* Items credited to statement of profit and loss, but not includible in business income.**			
A(i) Rent received from vacant land [Chargeable to tax under the head "Income from other sources"]		2,05,000	
A(ii) Rent received from commercial property owned by the company [Chargeable to tax under the head "Income from house property"]		4,30,000	
A(iii) Interest received on income tax refund **[**Chargeable to tax under the head "Income from other sources"]		42,000	
A(iv) Profit on sale of unused land [Chargeable to tax under the head "Capital Gains"]		2,00,000	
			8,77,000
Profits and gains from the business of manufacturing			**70,88,000**

Note: *As per section 43(5), an eligible transaction of trading in derivatives in shares in a recognized stock exchange is not a speculative transaction.*

In this case, the company is engaged in the business of manufacturing and hence, the loss on account of trading in derivatives is not incurred wholly and exclusively in relation to such business and hence, has to be disallowed while computing profits from the business of manufacturing. Trading in derivatives in shares is also not incidental to the business of manufacturing. Therefore, it has to be

[5] *Balance additional depreciation of Rs. 3.40 lakhs can be claimed in the next year i.e., A.Y.2020-21*

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assumed that the company is also carrying on the business of trading in derivatives in shares in addition to its manufacturing business.

In this case, the loss has to be disallowed at the first instance while computing income from the business of manufacturing since it is not wholly and exclusively incurred for the said business and thereafter, loss from trading in derivatives has to be set-off against the profits from manufacturing business applying the provisions of section 70(1) permitting inter-source set-off of losses.

2. (a) Computation of Taxable and Exempt Income of M/s Jeevan Pvt Ltd. for the A.Y. 2019-20

Particulars		Rs.
Net profit as per Profit and Loss Account		37,65,00,000
Add: **Excess depreciation as per books of account**	Rs.	
Depreciation as per books of account	30,00,00,000	
Less: Depreciation allowable as per the Income-tax Act, 1961	28,00,00,000	2,00,00,000
Net profit before allowing deduction under section 33AB		39,65,00,000
Less: Deduction under section 33AB would be the lower of:		
- **Amount deposited in Rubber Development Account** on or before 30.9.2019 [i.e., Rs. 30,00,00,000]		
- **40% of profits of such business** [i.e., Rs. 15,86,00,000, being 40% of Rs. 39,65,00,000]		15,86,00,000
Net profit after allowing deduction under section 33AB		**23,79,00,000**
Add: Amount withdrawn from special account with NABARD, which is deemed as profits and gains of business or profession		
(i) **Purchase of a new machine for use in its operation for Rs. 10 crores,** would **not** be deemed as profits and gains of business or profession, since the said amount is utilised as per the specified scheme.		Nil
(ii) **Purchase of office appliances for corporate office at Hyderabad for Rs. 10 crores,** out of the amount withdrawn from the deposit account, would be deemed as profits and gains of business or profession, since the said utilisation is not permissible.		10,00,00,000
(iii) **Rs. 5 crores utilised for purchase of computers and accessories is permissible.** Thus, such amount would **not** be deemed as profits and gains of business or profession.		Nil
(iv) **Rs. 1 crore utilised for construction of a godown near rubber estate to store raw rubber,** would **not** be deemed as profits and gains of business or profession, since the said amount is utilised as per the specified scheme.		Nil
(v) **Rs. 35 lakhs utilised for repairs to machinery** would not be deemed as profits and gains of business or profession, since the said amount is utilised as per the specified scheme. ***Note*** *- However, no deduction would be allowed in respect of such expenditure mentioned in (i), (iii), (iv) and (v) during the P.Y. 2018-19, since amount is spent out of the amount deposited in special account with NABARD, which has already been allowed as deduction in an earlier*		Nil

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assessment year.	
(vi) The **remaining amount of Rs. 13.65 crores {Rs. 40 crores *less* Rs. 26.35 crores** [utilised above in **(i) to (v)]}**, which is **not** utilised during the previous year in which such amount is withdrawn, would be deemed as profits and gains of business or profession.	13,65,00,000
Total Composite business profits	**47,44,00,000**
Less: 65% of Rs. 47,44,00,000, being agricultural income exempt	30,83,60,000
Business income	**16,60,40,000**
Less: Brought forward business loss of Rs. 6 crores pertaining to A.Y.2016-17 not allowed to be set-off against the business profits of the P.Y. 2018-19, since as on 31.3.2019, the shares of M/s Jeevan Pvt Ltd carrying 60% (i.e., not less than 51%) of the voting power is held by Mr. Bhola and not by Mr. Alok, being the person who held such shares as on 31.03.2016, being the last day of previous year 2015-16, in which such loss was incurred.	-
Business income chargeable to tax	**16,60,40,000**

(b) Computation of total income and tax payable of Madhuvan for A.Y. 2019-20

Particulars	Rs.	Rs.
Profits and gains from business and profession		
Income from sole proprietary concern in India	50,00,000	
Share of profit from a partnership firm in India of Rs. 30 lakhs, is exempt	Nil	
Business profit	50,00,000	
Less: Business Loss in Country T (USD 10,000 x Rs. 64/USD)	6,40,000	43,60,000
Income from Other Sources		
Agricultural income from rubber estate in Country T, is taxable in India (USD 70,000 x Rs. 64/USD)		44,80,000
Gross Total Income/ Total Income		**88,40,000**
Tax on total income		
Tax on Rs. 88,40,000 [(30% x Rs. 78,40,000 plus Rs. 1,10,000) applicable for an individual, resident in India who is of the age of 60 years or more]		24,62,000
Add: Surcharge@10%, since total income exceeds Rs. 50 lakhs		2,46,200
		27,08,200
Add: Health & Education cess @4%		1,08,328
		28,16,528
Average rate of tax in India [i.e., Rs. 28,16,528/Rs. 88,40,000 x 100]	31.86%	
Average rate of tax in Country T [i.e., USD 10,500/USD 70,000]	15%	
Doubly taxed income [Rs. 44,80,000 – Rs. 6,40,000]	38,40,000	
Rebate under section 91 on Rs. 38,40,000 @15% (lower of average Indian tax rate and rate of tax in Country T]		5,76,000

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Tax payable in India [Rs. 28,16,528 – Rs. 5,76,000]		22,40,528
Tax payable (rounded off)		**22,40,530**

Note:

Since Madhuvan, is resident in India for the P.Y.2018-19, his global income would be subject to tax in India. He would be allowed deduction under section 91 provided all the following conditions are fulfilled:-

(a) He is a resident in India during the relevant previous year.

(b) Income accrues or arises to him outside India during that previous year.

(c) Such income is not deemed to accrue or arise in India during the previous year.

(d) The income in question has been subjected to income-tax in Country T in his hands and he has paid tax on such income in Country T.

(e) There is no agreement under section 90 for the relief or avoidance of double taxation between India and Country T, where the income has accrued or arisen.

Madhuvan is eligible for deduction under section 91 since all the conditions specified thereunder stand fulfilled by him during the previous year.

3. (a) (i) Section 11(1)(a) stipulates that in order to avail exemption of income derived from property held under trust wholly for charitable or religious purposes, the trust is required to apply for charitable or religious purposes, 85% of its income from such property. In this case, the trust has earned income of Rs. 4,90,000 for the year ended 31.3.2019. It has also earned short term capital gain from sale of capital asset for Rs. 10,60,000. The trust had utilized the entire amount of Rs. 15,50,000 for the purchase of a building meant for charitable purposes.

The Supreme Court, in *S.RM. M. CT. M. Tiruppani Trust v. CIT (1998) 230 ITR 636,* ruled that the assessee-trust, which applied its income for charitable purposes by purchasing a building for use as a hospital, was entitled to exemption under section 11(1) in respect of such income.

The ratio of the decision squarely applies to the case of the charitable trust in question. Therefore, the charitable trust is justified in claiming that the purchase of the building amounted to application of its income for charitable purposes.

Under section 11(1A), where the whole of the sale proceeds of a capital asset held by a charitable trust is utilised by it for acquiring another capital asset, the capital gain arising therefrom is deemed to have been applied to charitable purposes and would be exempt. Section 11(1A) does not make any distinction between a long-term capital asset and a short-term capital asset. The claim of the charitable trust to the effect that the capital gain is deemed to have been applied to charitable purposes is tenable in law.

(ii) Computation of taxable income of Mannat charitable trust

	Particulars	Rs.
(i)	Income from property held under trust (net)	10,00,000
(ii)	Income (net) from business (incidental to main objects)	4,00,000
(iii)	Voluntary contributions from public Voluntary contribution made with a specific direction towards corpus are alone to be excluded under section 11(1)(d). In this case, there is no such direction and hence, included.	7,00,000
		21,00,000

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	Less: 15% of the income eligible for retention / accumulation without any conditions	3,15,000 17,85,000
	Less: Amount applied for the objects of the trust (i) Amount spent for charitable purposes (Rs. 11,60,000 - Rs. 3,60,000) (ii) Repayment of loan for construction of orphan home	 8,00,000 3,60,000
	Taxable Income	**6,25,000**

(b) **(i)** As per section 9(1)(vii)(b), income by way of fees for technical services payable by a resident is deemed to accrue or arise in India, except where the fees is payable, *inter alia,* in respect of services utilized in a business or profession carried on by such person outside India. In this case, since Trim Ltd. utilizes the technical services for its business in Indore, the fees for technical services payable by Trim Ltd. is deemed to accrue or arise in India in the hands of Mr. Richard Grill.

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 and section 57 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.

(I) In this case, since India does not have a DTAA with Country F, of which Richard Grill is a resident, the fees for technical services (FTS) received from Trim Ltd., an Indian company, would be taxable @10%, by virtue of section 115A.

(II) In this case, the FTS from Trim 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 Richard Grill is a non-resident, he has to furnish a tax residency certificate from the Government of Country F for claiming such benefit. Also, he has to furnish other information, namely, his nationality, his tax identification number in Country F and his address in Country F.

(III) In this case, the FTS from Trim 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) Where Zing Inc., a UK company, has a PE in India and rendering technical services is effectively connected with the PE in India.

Since Zing Inc. carries on business through a PE in India, in pursuance of an agreement with Swing Ltd. or other Indian companies entered into after 31.3.2003, and the income by way of fees for technical services is effectively connected with the PE in India as per section 44DA, such income shall be computed under the head “Profits and gains of business or profession” in accordance with the provisions of the Income-tax Act, 1961.

Accordingly, expenses of Rs. 22 lakhs (Rs. 10 lakhs + Rs. 12 lakhs) incurred for earning fees for technical services of Rs. 9 crore (Rs. 3.5 crore + Rs. 5.5 crore) is allowable as

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deduction therefrom. However, expenditure of Rs. 6 lakhs which is not incurred wholly and exclusively for the business of the PE and the amount of Rs. 12 lakhs paid by the PE to the Head Office is **not** allowable as deduction.

Zing Inc. is required to maintain books of account under section 44AA and get the same audited under section 44AB and furnish report along with the return of income under section 139.

4. (a) (i) Section 206C(1F) provides for collection of tax at source@1% by the seller from the buyer, at the time of receipt of consideration for sale of motor vehicle, the value of which exceeds Rs. 10 lakhs. CBDT Circular No.22/2016 dated 8.6.2016 clarifies that this section has been inserted to cover all transactions of retail sales and accordingly, it will not apply to sale of motor vehicles by manufacturers to dealers. Hence, car manufacturers are not liable to collect tax at source under section 206C(1F).

In respect of sale of premium model cars (of value ranging above Rs. 10 lakhs and upto Rs. 50 lakhs) by dealers to retail customers, tax has to be collected at source@1% under section 206C(1F), even if no part of the consideration is received in cash.

As regards small cars of value ranging from Rs. 5 lakhs upto Rs. 10 lakhs, there is no requirement to collect tax at source.

(ii) The first proviso to section 201 provides that the payer (including the principal officer of the company) who fails to deduct the whole or any part of the tax on the amount credited or payment made to a resident payee shall not be deemed to be an assessee-in-default in respect of such tax if such resident payee –

(1) has furnished his return of income under section 139;

(2) has taken into account such sum for computing income in such return of income; **and**

(3) has paid the tax due on the income declared by him in such return of income,

and the payer furnishes a certificate to this effect from an accountant in such form as may be prescribed.

The date of deduction and payment of taxes by the payer shall be deemed to be the date on which return of income has been furnished by the resident payee.

However, where the payer fails to deduct the whole or any part of the tax on the amount credited or payment made to a resident and is not deemed to be an assessee-in-default under section 201(1) as mentioned above, interest under section 201(1A)(i) i.e., @1% p.m. or part of month, shall be payable by the payer from the date on which such tax was deductible to the date of furnishing of return of income by such resident payee.

Therefore, M/s Fitband Limited shall not be required to pay the difference tax in case the above mentioned conditions are fulfilled. However, the company shall be liable to make payment of interest from the date on which such tax was deductible to the date of furnishing of return of income by Star Warehousing.

Therefore, the submission of the assessee company, in this case, is correct.

(b) (i) Clause (i) of *Explanation* to section 92B amplifies the scope of the term "international transaction". According to the said *Explanation*, international transaction includes, *inter alia*, provision of scientific research services. L Inc. is a specified foreign company in relation to X Ltd. Therefore, the condition of X Ltd. holding shares carrying not less than 26% of the voting power in L Inc. is satisfied, assuming that all shares carry equal voting rights. Hence, L Inc. and X Ltd. are deemed to be associated enterprises under section 92A(2). Since the provision of scientific research services by L Inc. to X Ltd. is an "international transaction" between associated enterprises, transfer pricing provisions are attracted in this case.

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(ii) In this case, salary payment has been made to a related person referred to in section 40A(2)(b) i.e., relative (i.e., daughter) of Mrs. Chiya, who is a director of T Ltd. However, with effect from A.Y.2018-19, section 92BA has been amended to exclude such transactions from the scope of "specified domestic transaction". Consequently, transfer pricing provisions would not be attracted in this case.

(iii) The scope of the term "intangible property" has been amplified to include, *inter alia*, technical knowhow, which is a technology related intangible asset. Transfer of intangible property falls within the scope of the term "international transaction". Since A Inc., a French company, guarantees not less than 10% of the borrowings of Y Ltd., an Indian company, A Inc. and Y Ltd. are deemed to be associated enterprises under section 92A(2). Therefore, since transfer of technical knowhow by Y Ltd., an Indian company, to A Inc., a French company, is an international transaction between associated enterprises, the provisions of transfer pricing are attracted in this case.

5. (a) (i) The action of the Commissioner in issuing the second notice is not justified. The term "record" has been defined in clause (b) of Explanation to section 263(1). According to this definition "record" shall include and shall be deemed always to have included all records relating to any proceeding under the Act available at the time of examination by the Commissioner. In other words, the information, material, report etc. which were not in existence at the time the assessment was made and came into existence afterwards can be taken into consideration by the Commissioner for the purpose of invoking his jurisdiction under section 263(1). However, at the same time, in view of the express provisions contained in clause (b) of the Explanation to section 263(1), such information, material, report etc. can be relied upon by the Commissioner only if the same forms part of record when the action under section 263 is taken by the Commissioner,

Issuance of a notice under section 263 succeeds the examination of record by Commissioner. In the present case, the Commissioner initially issued a notice under section 263, after the examination of the record available before him. The subsequent second notice was on the basis of material collected under section 133A, which was totally unrelated and irrelevant to the issues sought to be revised in the first notice. Accordingly, the material on the basis of which the second notice was issued could not be said to be "record" available at the time of examination as emphasized in Explanation (b) to section 263(1).

(ii) (I) It has been held by the Apex Court in the case of *Hind Wire Industries Ltd. v. CIT (1995) 212 ITR 639* that the order once amended can also be rectified subsequently provided the mistake apparent from record is rectifiable under section 154. The Apex Court enlarged the scope of the words used in that section by stating that it does not necessarily mean the original order. It could be any order including the amended or rectified order. The action of the Assessing Officer is, therefore, incorrect.

(II) The original return for A.Y.2019-20 was filed in time and the proceedings were already taken up for assessment under section 143(3). A revised return was filed by the assessee after the end of the relevant assessment year. The action of the Assessing Officer in making the assessment in disregard of the revised return filed on 20.4.2020 is correct because as per the provisions of section 139(5) the assessee can file the revised return only within the end of the relevant assessment year to which the return relates or before completion of the assessment, whichever is earlier.

(iii) The issue under consideration in this case is, whether omission to issue notice under section 143(2) is a defect not curable in spite of section 292BB

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This issue came up before the Apex Court in *Asstt. CIT v. Hotel Blue Moon (2010) 321 ITR 362,* wherein it was held that without the statutory notice under section 143(2), the Assessing Officer could not assume jurisdiction. In that case, the Assessing Officer recorded his inability to generate a notice due to certain reasons. Such defect cannot be cured subsequently, since it is not procedural but one that goes to the root of the jurisdiction. Even though the assessee had participated in the proceedings, in the absence of mandatory notice, section 292BB cannot help the Revenue officers who have no jurisdiction, to begin with. Section 292BB helps Revenue in countering claims of assessees who have participated in proceedings once a due notice has been issued.

Applying the rationale of the Supreme Court ruling to the case on hand, the failure to issue notice under section 143(2) would vitiate the assessment proceedings notwithstanding the assessee's participation in the proceedings. Section 292BB would not come to the rescue of the Revenue Authority if they omit to issue notice under section 143(2).

(b) A hybrid mismatch is an arrangement that exploits a difference in the tax treatment of an entity or an instrument under the laws of two or more tax jurisdictions to achieve double non-taxation.

Branch mismatches arise where the ordinary rules for allocating income and expenditure between the branch and head office result in a portion of the net income of the taxpayer escaping the charge to taxation in both the branch and residence jurisdiction. Unlike hybrid mismatches, which result from conflicts in the legal treatment of entities or instruments, branch mismatches are the result of differences in the way the branch and head office account for a payment made by or to the branch.

Hybrid mismatch arrangements arise due to -

(i) Creation of two deductions for a single borrowal

(ii) Generation of deductions without corresponding income inclusions

(iii) Misuse of foreign tax credit

(iv) Participation exemption regimes

Specific country laws that allow taxpayers to opt for the tax treatment of certain domestic and foreign entities may aid hybrid mismatches.

BEPS Action Plan 2 gives recommendations to neutralise the effects of hybrid mismatch arrangements, which include general changes to domestic law followed by a set of dedicated anti-hybrid rules. Treaty changes are also recommended. The 2017 report includes specific recommendations for improvements to domestic law intended to reduce the frequency of branch mismatches as well as targeted branch mismatch rules which adjust the tax consequences in either the residence or branch jurisdiction in order to neutralise the hybrid mismatch without disturbing any of the other tax, commercial or regulatory outcomes.

6. (a) (i) (I) Penalty under section 271C is attracted for failure to deduct tax at source. The penalty would be a sum equal to the amount of tax which such person has failed to deduct. Such penalty can be imposed only by the Joint Commissioner. Therefore, Harish & Associates shall be liable for penalty under section 271C equal to the amount of tax which they have failed to deduct under section 194C from the payments made to the contractors. The penalty would be in addition to the disallowance of 30% of expenditure/payment under section 40(a)(ia).

(II) Section 133(6) empowers the Income-tax authority to require any person to furnish information in relation to such points or matters which will be useful for or relevant to any enquiry or proceeding under the Act. Failure on the part of an assessee to furnish the information in relation to such points or matters as required makes him liable for

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penalty under section 272A(2) of Rs. 100 for every day during which the failure continues.

***Note** – In a case where no proceeding is pending, the Income-tax authority can exercise this power only after obtaining the approval of the Principal Director/Director or Principal Commissioner/Commissioner as the case may be. In this case, it is presumed that the Income-tax authority has obtained the approval of the Principal Director/Director or Principal Commissioner/ Commissioner before exercising this power.*

(ii) (I) As regards setting off of losses, the provisions relating to merger and amalgamation already contain specific anti-avoidance safeguards. Therefore, GAAR need not be invoked when SAAR is applicable, though as per *CBDT Circular No. 7/2017 dated 27.01.2017,* GAAR and SAAR can co-exist.

(II) In case of merger of a profit-making company with loss making company, there is no specific anti-avoidance safeguards. However, since such merger would be under the order of High Court, GAAR would not be invoked if the High Court has explicitly and adequately considered the tax implication while sanctioning the merger scheme.

(b) **(i)** Chapter VIII of the Finance Act, 2016, "Equalisation Levy", provides for an equalisation levy of 6% of the amount of consideration for specified services received or receivable by a non-resident not having permanent establishment in India, from a resident in India who carries out business or profession, or from a non-resident having permanent establishment in India.

"Specified Service" means

(1) online advertisement;

(2) any provision for digital advertising space or any other facility or service for the purpose of online advertisement and

(3) any other service as may be notified by the Central Government.

However, equalisation levy shall not be levied-

- where the non-resident providing the specified services has a permanent establishment in India and the specified service is effectively connected with such permanent establishment.
- the aggregate amount of consideration for specified service received or receivable during the previous year does not exceed Rs. 1 lakh.
- where the payment for specified service is not for the purposes of carrying out business or profession

In the present case, equalisation levy @6% is chargeable on the amount of Rs. 15,00,000 received by Xylo Inc., a non-resident not having a PE in India from LMN Ltd., an Indian company. Accordingly, LMN Ltd. is required to deduct equalisation levy of Rs. 90,000 i.e., @6% of Rs. 15 lakhs, being the amount paid towards online advertisement services provided by Xylo Inc., a non-resident having no permanent establishment in India. Non-deduction of equalisation levy would attract disallowance under section 40(a)(ib) of 100% of the amount paid while computing business income.

(ii) Section 245Q(3) of the Income-tax Act, 1961 provides that an applicant, who has sought for an advance ruling, may withdraw the application within 30 days from the date of the application. Since more than 30 days have elapsed from the date of application by Mr. Sarthak to the Authority for Advance Rulings, he cannot withdraw the application.

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However, the Authority for Advance Rulings (AAR*),* in *M.K. Jain AAR No.644 of 2004*, has observed that though section 245Q(3) provides that an application may be withdrawn by the applicant within 30 days from the date of the application, this, however, does not preclude the AAR from permitting withdrawal of the application after the said period with its permission, if the circumstances of the case so justify.

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