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A quandary of claim of foreign tax credit

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Background

The rapid infusion of digitisation into the business has made world one global market. In today' era, the business transactions extend beyond national boundaries and the businesses are tailored to meet the needs of consumers over wider geographic areas. Tax treaties play a crucial role in these times to ensure that the taxes on income are distributed between the sovereigns while minimising double taxation in the hands of person earning the income.

The tax treaties provide that wherever the source country exercises a right to tax the income of the resident of another country, the latter country should provide a credit of tax paid in the source country while exercising its sovereign right to tax its resident. For example, an Indian resident receives certain fees in lieu of providing technical services from Japan which is subject to tax in Japan. In such a case, the Indian resident shall be allowed a credit of tax paid in Japan against the income tax liability in India. In this regard, appropriate provisions have been provided not only in the tax treaties but also in the Income-tax Act, 1961 ('**IT Act**').

Provisions pertaining to avoidance of double taxation and foreign tax credit in the IT Act

Section 90(1) of the IT Act, *inter alia*, empowers the Central Government to enter into a Double Taxation Avoidance Agreement ('**DTAA**') with other countries for avoidance of double taxation and for granting relief in respect of income on which tax has been paid or income tax is chargeable both in India and the foreign country

Further, Section 295(2)(ha) of the IT Act empowers the Central Board of Direct taxes ('**CBDT**') to make rules and prescribe the procedure for granting of relief or deduction under Section 90 for income-tax paid in any foreign country against the income-tax payable in India. Accordingly, *vide* Notification No. 54/2016 dated 27 June 2016, CBDT notified Rule 128 in the Income tax Rules, 1962 ('**IT Rules**') on Foreign Tax Credit ('**FTC**').

Rule 128 of the IT Rules, *inter alia,* provides that FTC shall be lower of the tax payable on a foreign income in India and in the foreign country.

Further, there are specific provisions relating to FTC in the DTAAs entered by India with various countries and as per Section 90 of the IT Act, the DTAA will override the provision(s) of the IT Act in case they are more beneficial to the assessee[1].

Provisions relating to relief from double taxation in various DTAAs

On a plain reading, the Article relating to India's obligation to provide credit of taxes seems to be worded on similar lines in most treaties entered by it. However, on a closer look, one may observe some changes in the language. As illustration, the extracts of article relating to FTC in India-USA and India-UK are reproduced as under:

- India-USA DTAA [Article 25(2)(a)]:

[1] SC in *Azadi Bachao Andolan*: [2002] 125 Taxman 826 (SC)[18 November 2002]

'Where a resident of India derives income which, in accordance with the provisions of this Convention, may be taxed in the United States, India shall allow as a deduction from the tax on the income of that resident an amount equal to the income-tax paid in the United States, whether directly or by deduction. ***Such deduction shall not, however, exceed <u>that part of the income-tax</u> (as computed before the deduction is given) which is attributable to the income which may be taxed in the United States****.'*

- India-UK DTAA [Article 24(2)]:

'2. Subject to the provisions of the law of India regarding the allowance as a credit against Indian tax of tax paid in a territory outside India (which shall not affect the general principle hereof), the amount of the United Kingdom tax paid, under the laws of the United Kingdom and in accordance with the provisions of this Convention, whether directly or by deduction, by a resident of India, in respect of income from sources within the United Kingdom which has been subjected to tax both in India and the United Kingdom shall be allowed as a credit against the Indian tax payable in respect of such ***income but in an amount not exceeding <u>that proportion of Indian tax</u> which such income bears to the <u>entire income chargeable to Indian tax.</u>****'*

Juxtaposing the aforesaid Articles reveals that India-UK tax treaty explicitly states that the FTC to be allowed in India will be equivalent to a portion of the total income tax liability in India in the same ratio which the income generated in UK is to the total income of such assessee. Meaning thereby, that the FTC in India shall be restricted to the extent of the Indian tax liability on the income received from UK which is similar to that of Rule 128 of the IT Rules. However, the India-USA DTAA simply states that the claim of FTC in India will not exceed that income tax which is attributable to the income which is generated and taxed in USA. Thus, unlike India-UK tax treaty, India-USA tax treaty does not make a specific reference to **<u>Indian income-tax</u>** while providing for restriction on the quantum of credit.

Now, due to the difference in the language of the abovementioned Articles of the DTAA, the taxpayers have contended that where the Article relating to foreign tax credit is worded like that in India-USA tax treaty, the quantum of credit allowed in India should not be restricted to income-tax payable in India but restricted to income-tax paid in USA. The judicial forums have rendered divergent views on this issue. Various judgements in this regard have been discussed below.

Entire tax paid in the foreign country will be allowed as FTC

In the case of *Wipro Ltd.*[2]**,** the Karnataka High Court discussed the issue of availability of FTC for an income which is eligible for exemption under section 10A of the IT Act. The Hon'ble High Court held that the income derived by an Indian resident, which is taxable in USA (directly or by deductions), would get FTC in India for the entire amount of income tax paid in USA. The Court held that the India-USA DTAA does not make the payment of income tax in India as a condition precedent to claim FTC and that the only embargo prescribed under the IT Act is that

[2] *Wipro Ltd*. v. *DCIT*: [2016] 382 ITR 179 (Kar)

the FTC will be available to an assessee only in respect of that income, which is taxed in USA. The reading of the Hon'ble High Court had the effect of allowing FTC even in a case where the income of the Indian resident is not taxable in India and only taxable in USA.

While interpreting the India-Canada DTAA (similar to the India-UK DTAA as reproduced above), the court differentiated it from the India-USA DTAA and observed that if the income tax paid in India is less than the income tax paid in Canada, then the assessee would be entitled to relief only to the extent of tax paid in India and not to the extent of tax paid in Canada.

Further, the India-Japan DTAA (similar to the India-USA DTAA) was analysed in a recent judgement of *Canon India Private Limited*[3]**,** wherein, the Income Tax Appellate Tribunal (**'ITAT'**) Delhi relied upon *Wipro (supra)* and gave a similar decision.

In *Ittiam Systems Private Limited*[4]*,* ITAT Bangalore has held that the DTAAs of India with USA, Germany and Japan have similar double taxation avoidance Articles. Accordingly, relying on *Wipro (supra)* the ITAT held that the assessee is eligible for FTC in India on full amount of taxes paid in USA, Japan and Germany. However, while interpreting the India-Korea DTAA (similar to the India-UK DTAA as reproduced above), the ITAT held that FTC is limited to taxes paid in Korea or India, whichever is less.

Further relying on the judgement of *Wipro (supra)*, similar view has been taken while analysing India – USA DTAA by ITAT Delhi in *HCL Comnet Systems and Services Ltd.*[5] and by ITAT Mumbai in *Tata Consultancy Services Ltd.*[6]*.*

FTC allowed to the extent of tax payable on the foreign income in India

In the case of *Digital Equipments India Ltd.*[7]*,* the Assessing Officer did not allow the credit on account of taxes paid on income generated in USA. The Hon'ble ITAT Mumbai analysed the India-USA DTAA and held that the India-USA DTAA in the last sentence of Article 25(2)(a) states unambiguously and beyond any controversy that the deduction on account of income tax paid in USA, from income tax payable in India, cannot exceed Indian income tax liability in respect of such an income. The ITAT further held that the India-USA DTAA, and other DTAAs as well, does stipulate that the FTC cannot exceed the income tax leviable in respect of that income in the country of which the assessee is resident.

Similarly, while considering the India-Singapore DTAA (which is similarly phrased as that of India-Japan DTAA with respect to the Article on FTC) ITAT Ahmedabad in the case of *Elitecore Technologies (P.) Ltd.*[8] has held that FTC shall be available to the extent of income tax payable in India on such foreign income.

Conclusion

The intent behind formulating the article on FTC in the DTAA can be understood by referring to Paragraph 14 on Article 23 of the UN Model Commentary 2021, wherein it states that *'the credit for tax imposed by the other State is limited to the tax attributable to items of income which the other State is entitled to tax under the provisions of the treaty.'*

[3] *Canon India Private Limited* v. *ACIT* [ITA No. 468/DEL/2021]
[4] *Ittiam Systems Private Limited* v. *ITO* [2021] 86 ITR(T) 611 (Bangalore - Trib.)
[5] *DCIT* v. *HCL Comnet Systems and Services Ltd.* [ITA No. 5555 / DEL / 2014]
[6] *Tata Consultancy Services Ltd*. v. *ACIT* [ITA No. 1650/Mum.
[7] *JCIT* v. *Digital Equipments India Ltd*. [2005] 94 ITD 340 (MUM.)
[8] *Elitecore Technologies (P.) Ltd.* v. *DCIT, Ahmedabad* [2017] 184 TTJ 166 (Ahmedabad - Trib.)

Further, OECD Model Commentary 2017, while discussing Article 23B (which is identical to Article 25 of India-USA DTAA) states in paragraph 57 that the state of residence (in our case India) will allow deduction of FTC against its own tax, but such deduction will be restricted to the appropriate proportion of its own tax. The commentary further states that the deduction which India has to allow is restricted to that part of the Indian income tax which is appropriate to the income derived from the other foreign state (in our case USA). Accordingly, as per OECD commentary, the FTC allowed in India is intended to be restricted to tax payable in India.

However, it should be noted that Supreme Court in the case of *P.V.A.L. Kulandagan Chettiar*[9] and High Court of Madhya Pradesh in the case of *Turquoise Investment & Finance Ltd.*[10] have held that the commentaries on the articles of the model convention will not have any applicability when the terms of the DTAAs have provided for the manner in which tax is to be levied on the assessee. Therefore, the OECD commentaries are not binding on Indian Courts.

Further, Revenue's appeal against the ruling of High Court of Karnataka in *Wipro (Supra)* has been granted a Special Leave for Appeal[11], leaving the decision of the High Court to be adjudicated upon by the Supreme Court. Accordingly, it would be interesting to see as to how the Apex Court interprets India-USA DTAA especially in the light of newly introduced Rule 128 of the IT Rules. In the meanwhile, the taxpayers claiming the entire amount of foreign taxes paid as a credit are likely to face resistance from the income-tax department in India which may seek to restrict credit to limits provided in Rule 128 of the IT Rules.

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Notifications and Circulars

TDS on benefits and perquisites – Second set of guidelines to clarify application of Section 194R

With a mandate to deduct tax on benefit or perquisite arising from the business or profession of the recipient, section 194R was introduced in the Income Tax Act, 1961. The CBDT, to clarify the position and application of the said section, had issued the first set of guidelines *vide* Circular no. 12 of 2022 dated 16 June 2022. Now it has issued a second set of guidelines *vide* Circular No. 18 of 2022, dated 13 September 2022 providing for the following clarifications:

[9] CIT vs. P.V.A.L. Kulandagan Chettiar [(2004) 137 taxman 460(SC)]
[10] DCIT vs. Turquoise Investment & Finance Ltd. [(2006) 154 taxman 80 (MP)]
[11] Special Leave to Appeal (C) CC No(s). 15932/2016 / Diary No. 25267/2016

i. Application of Section 194R where banks and other specified institutions have settled/waived of a loan:

One-time loan settlement with borrowers or waiver of loan granted on reaching settlement with the borrowers by banks and other institutions (including Scheduled bank, public financial institutions, Cooperative banks, asset reconstruction companies, etc.) would not be subjected to tax deduction at source under Section 194R of the Act.

It has been further provided that this clarification is only for the purposes of Section 194R of the Act. The treatment of such settlement/waiver in the hands of the person who had got benefitted by such waiver would not be impacted by this clarification. Taxability of such settlement/waiver in the hands of the beneficiary will be governed by the relevant provisions of the Act.

ii. Applicability of Section 194R where the service provider received reimbursement for the expenses incurred during the course of service and the invoice of the expense is in the name of the service provider:

Vide Circular 12 of 2022 it was clarified that if a service provider incurred some expense in the course of rendering service to a service recipient and the invoice is in the name of the service provider, then the expense is the liability of the service provider and any reimbursement of such expense from the services recipient will be treated as a benefit in the hands of the service provider and liability to deduct TDS under Section 194R will arise in the hands of the service recipient. The rationale for such clarification was given to be that on such invoice the input credit of GST on such expenses is available to the service provider.

However, if the service provider incurs expense as 'Pure Agent', then GST input credit is allowed to the service recipient and not to the service provider. In such a case, the amount incurred by such Pure Agent which is reimbursed by the recipient would not be treated as benefit/perquisite in the hands of the Pure Agent for the purpose of section 194R of the IT Act.

iii. Applicability of Section 194R where deductions have been made under Section 194C or 194J of the IT Act for reimbursement made against an invoice which already includes out-of-pocket expenses:

Out-of-pocket expenses is part of consideration in the bill for professional fee that is charged to the company and the tax is deducted under Section 194C or 194J of IT Act. In such a case the out-of-pocket expense is already part of professional fee, hence no further tax is to be deducted under Section 194R of the Act.

iv. Clarification w.r.t. dealer conference:

a) **Requirement to invite all dealers to business conference is not necessary for exemption under Section 194R:** The expenditure incurred on a dealer / business conference will not be considered as a benefit / perquisite being provided to the attendee irrespective of the fact that whether **all dealers / business associates** are invited to such conference or not. This is subject to satisfaction of other conditions specified under Question 8 to the earlier Circular 12 of 2022.

b) **Overstay of a dealer defined:** Expenditure incurred on participants of dealer/business conference for a day immediately prior to actual start of the conference and one day immediately following the actual end date of conference would be not considered as overstay, meaning thereby TDS will not be required to be deducted.

c) **Identification of benefit arising to a dealer in a group activity during such conference:** If benefit/perquisite is provided in a group activity in a manner that it is difficult to match such benefit/perquisite to each participant using a reasonable allocation key, the benefit/perquisite provider may at its option not claim the expense incurred on such benefit/perquisite, as a deductible expenditure for calculating its total income. If it decides to opt so, it will not be required to deduct tax under Section 194R on such benefit/perquisite and therefore it will not be treated as assessee in default under Section 201 of the IT Act. Thus, in such a case if the expenditure incurred on such benefit/perquisite is debited in the books of account then it should be added back to calculate the total income.

v. **Claim of depreciation on a benefit / perquisite on which TDS under Section 194R was deducted:**

Once TDS under Section 194R is deducted on the benefit (e.g., gift of car), the recipient of the benefit will include the value of the benefit (value of the car) as income in the return of income. Accordingly, the 'actual cost' for the purpose of Section 32 of the IT Act will be deemed to be the amount of benefit (value of the car) included by the assessee as income in his income-tax return.

vi. **Embassy/High Commissions:**

Section 194R is not applicable on benefit/perquisite provided by an organization in scope of The United Nations (Privileges and Immunity Act) 1947, an international organization whose income is exempt under specific act of Parliament (such as the Asian Development Bank Act, 1966), an embassy, a High Commission, legation, commission, consulate, and the trade representation of a foreign state.

vii. **Applicability of Section 194R where bonus/right shares are issued by a company in which there is substantial public interest as defined under Section 2(18) of the IT Act.**

The tax under Section 194R of the IT Act is not required to be deducted on issuance of bonus or right shares by a company in which the public are substantially interested as defined in clause (18) of Section 2 of the IT Act, where ***bonus shares are issued to all shareholders*** by such a company or ***right shares are offered to all shareholders*** by such a company, as the case may be.

Time for furnishing modified returns under Section 170A extended till 31 March 2023

Vide Finance Act 2022, w.e.f. 1 April 2022, a new Section 170A was inserted in the IT Act to effect order of tribunal or court in respect of business reorganization. Entities going through business reorganization, may furnish modified return of income for any assessment year to which such order of business reorganization is applicable. Such modified returns shall be furnished within a period of six months from the end of the month in which such order of business reorganization was issued by the competent authority.

In pursuance of the above, exercising power under Section 170A read with Section 295 of the IT Act, CBDT *vide* Notification No. 110 of 2022 (F. No. 370142/41/2022-TPL), dated 19 September 2022 has notified Rule 12AD which will come into effect from 1 November 2022. The said rule states that the modified return of income is to be furnished by a successor entity to a business organization under Section 170A in form ITR-A. In order to provide adequate time, CBDT *vide* Order dated 26 September 2022, under Section 119 of the IT Act, has allowed successor companies whose order of business reorganization was issued between the period 1 April 2022 and 30 September 2022, to furnish said return till 31 March 2023.

Statement to be furnished under Section 285B by producers of cinematograph film or persons engaged in specified activity

Finance Act, 2022 substituted Section 285B, w.e.f. 1 April 2022 to state that producers of cinematograph films or persons engaged in specified activity need to provide a statement in a prescribed form to the prescribed income tax authority containing particulars of all payments of over INR Fifty thousand in the aggregate made by him or due from him to each such person as is engaged by him in such production or specified activity.

Now *vide* Notification No. 109 of 2022, dated 14 September 2022, the CBDT has substituted Rule 121A of the Income-tax Rules, 2022 (‘**Rules**’). The said rule has prescribed Form No. 52A for furnishing statement under Section 285B. As per the said rule, Form No. 52A shall be furnished within sixty days from the end of the previous year. The said form will be furnished electronically, either under digital signature, if the return of income is required to be furnished under digital signature, or through electronic verification code if not falling under the case of digital signature.

Application for re-computation of total income under Section 155(18) – Procedure notified

Vide Finance Act, 2022, w.e.f. 1 April 2022, sub-section (18) was inserted to Section 155 of the IT Act to provide that when any deduction in respect of any surcharge or cess, which is not allowable as deduction under Section 40, had been claimed and allowed in the case of an assessee in any previous year, then such claim shall be deemed to be under-reported income of the assessee for such previous year for the purposes of section 270A(3). Section 155(18) further empowers the Assessing Officer to recompute the total income of such assessee for such previous year and make necessary amendment as per the provisions of Section 154. Further it was provided that the period of four years specified under Section 154(7) will be calculated from the end of the previous year commencing on 1 April 2021. The section exempted such situation from being deemed to be under reported income under Section 270A(3) wherein the assessee has made an application to the concerned AO for recomputing its total income after disallowing the claim for deduction of surcharge and cess.

CBDT has *vide* Notification No. 111 of 2022, dated 28 September 2022, inserted Rule 132 to prescribe the following:

i. An application requesting the AO to recompute the total income after disallowing the claim for deduction of surcharge and cess must be made in Form No. 69 on or before 31 March 2023.

ii. Form No. 69 shall be furnished electronically to the Principal Director General of Income-tax (Systems) ('**PDGI**') or the Director General of Income-tax (Systems) ('**DGI**') or any other person authorized by PDGI or DGI.

iii. Further, PDGI or DGI shall lay down the procedure and standards for furnishing and verification of Form No. 69 and to forward the same to the AO.

iv. The Assessing Officer shall, on receipt of the application in Form No. 69, recompute the total income by amending the relevant order and issue notice under Section 156 specifying the time period within which amount of tax payable, if any, is to be paid.

v. After making the payment of the tax determined by the AO, the assessee shall furnish the details of payment of tax in Form No.70 to the AO within 30 days from date of making the payment.

Compounding of Offences under the Income Tax Act, 1961 – Guidelines issued

In supersession of all earlier guidelines on compounding of offences under the IT Act, the CBDT *vide* letter dated 16 September 2022, has issued guidelines to simplify and facilitate compounding of offences. These guidelines are issued in exercise of power conferred under Section 119 of the IT Act read with explanation below sub-section (6) of Section 279.

Section 279(2) of the IT Act provides that any offence under chapter XXII of the IT Act may either before or after the proceedings be compounded by Pr. CCIT / CCIT / Pr. DGIT / DGIT.

CBDT has stated that compounding of offences is not a matter of right, however on satisfying the conditions prescribed under the guidelines, the competent authority may compound the offences.

Applicability of these guidelines to prosecution under Indian Penal Code ('IPC')

Prosecution instituted under IPC cannot be compounded. However, in case the prosecution complaint filed under the provisions of both the IT Act and the IPC are based on the same facts and, the complaint under the IT Act is compounded, then the process of withdrawal of the complaint under the IPC may be initiated by the Competent Authority under Section 321 of the Criminal Procedure Code, 1973.

Classification of offences under Chapter XXII of the IT Act

S.No.	Category A (Offences are of technical nature caused by an act of omission)	Category B (Offences are of non-technical nature caused by an act of commission)
1.	Section 276B	Section 276
2.	Section 276BB	Section 276A
3.	Section 276CC	Section 276AA
4.	Section 276CCC	Section 276AB
5.	Section 276DD	Section 276C(1)
6.	Section 276E	Section 276Q(2)
7.	Section 277	Section 276D
8.	Section 278	Section 277
9.		Section 277A
10.		Section 278

Eligibility conditions for compounding

1. Application is made to the Pr. CCIT/ CCIT / Pr. DGIT / DGIT having jurisdiction in the prescribed format in the form of an affidavit on a stamp paper of INR 100.
2. Compounding application may be filed *suo-moto* at any time after the offence(s) is committed irrespective of whether it comes to the notice of the Department or not.
3. In case where prosecution complaint has already been filed in the court of law, compounding application must be filed within:
   a. 12 months from the end of the month in which prosecution complaint has been filed in the court of law,
   b. a period starting from the end of 12 months from end of month in which prosecution complaint is filed to 24 months, provided an increased compounding charges at the rate of 1.25 times of the normal compounding charges will be applicable.

   The time limits may be relaxed with the approval of the Pr.CCIT of the region, for application filed beyond 24 months but before 36 months from the end of month in which complaint was filed in a court. However, when such relaxation is granted, the compounding charges would be @ 1.5 times of the normal compounding charges as applicable to the offence on the date of filing of the original compounding application.
4. The person has paid the outstanding tax, interest (including interest under Section 220 of the IT Act), penalty and any other sum due relating to the offence for which compounding is sought.
5. The person undertakes to pay the compounding charges determined in accordance with these guidelines.
6. The person undertakes to withdraw appeals filed by him related to the offence for which compounding is sought.
7. Application for compounding of offences under Section 276B/276BB of the IT Act by an applicant for any period for a particular TAN should cover all defaults constituting offence under Section 276B/276BB in respect of that TAN for such period.

Offences not to be compounded

a. Section 275A – (Contravention of order made under sub-section (3) of section 132)

b. Section 275B – (Failure to comply with the provisions of clause (iib) of subsection (1) of section 132)

Offences normally not to be compounded

i. Offences under Category A; On more than three occasions.

ii. Offences under Category B: Other than the first offence(s).

iii. Any offence under Direct Taxes laws for which he was convicted earlier with imprisonment for two years or more.

iv. Any offence which is directly related to an offence relation to:

- Undisclosed foreign bank account/assets in any manner;
- The black money (undisclosed foreign income and assets) and imposition of tax act, 2915; or
- Prohibition of Benami Property Transactions Act, 1988.

v. Any other offence as provided under these guidelines.

'Occasion' for these purpose of guidelines means if in one instance, the assessee files multiple applications for one or more than one assessment year (AYs).

For the purpose of these guidelines, the term '**First Offence**' has been defined to mean:

a. Offences committed prior to any of the following –

   i. The date of issue of any letter/notice in relation to the prosecution or

   ii. Any intimation relating to filing of prosecution complaint sent by the Department to the person concerned, or

   iii. Launching of prosecution, whichever is earlier, or

b. Offence(s) not detected by the department but voluntarily disclosed by a person with the filing of application for compounding of offence(s) in the case under the Act for one assessment year or more.

Compounding procedure

1. On receipt of the compounding application, the report on the same shall be obtained from the AO/ACIT/DCIT, who shall submit it to the competent authority.
2. In cases where, the compounding application is not found to be acceptable, then the competent authority shall dispose of every such application through a speaking order within six months from the end of the month of receipt of the application.
3. In cases where, the compounding application is found to be acceptable. then the Competent Authority shall intimate the same to the applicant along with the compounding charges payable and other liabilities pending within six months from the end of the month of receipt of the application.
4. Where compounding application is found to be acceptable, the Competent Authority shall intimate the amount of compounding charges to the applicant, requiring him to pay the same within one month from the **end of the month** of receipt of such intimation him.

   a. On written request of applicant for further extension of time, the time period to pay the same may be extended up to 6 months.

   b. Extension beyond 6 months and up to 12 months shall require approval from Pr. Chief Commissioner of Income tax of the Region concerned.

c. Extension beyond 12 months shall require approval of Member (Inv.), CBDT on a proposal of the competent authority concerned.

5. Whenever the compounding charges are paid beyond one month from the end of month in which it was received by the applicant, on account of extension then he shall have to pay interest at the rate of 1 % per month or part of the month on the unpaid amount of compounding charges upto three months and thereafter at the rate of 2 %.

6. The Competent Authority shall pass the compounding order within one month from the end of the month of payment of compounding charges. Where compounding charge is not deposited within the time allowed, the compounding application shall be rejected after giving the applicant an opportunity of being heard only in relation to compounding charges payable.

7. The order of acceptance/rejection of compounding application shall be brought to the notice of the Court, where the prosecution complaint was filed/or the complaint is pending, immediately through prosecution counsel in all cases where prosecution proceedings have been instituted.

8. The timelines mentioned for processing the compounding applications prescribed in these Guidelines are administrative and indicative for work management and do not prescribe a limitation period for disposal of the compounding application.

9. Wherever the facility to perform any function relating to processing of any compounding application is available on ITBA, such function should be performed on ITBA.

Compounding charges

The compounding charges shall include -

a) Compounding fee - offence wise compounding fee is prescribed under para 13 of the guidelines.

b) Prosecution establishment expenses - to be charged @ 10% of the compounding fee subject to a minimum of INR 25,000/- and

c) Litigation expenses, including Counsel's fee - paid/payable by the Department in connection with offence(s) compounded by a single order.

In case of any extension of time limit, the compounding charges will be increased, and interest will be charged at the rate as discussed above.

Further, the compounding charges are payable in addition to the outstanding tax, interest, penalty and any other sum, if any payable or imposable as per provisions of the IT Act. Such tax, interest, penalty and any other sum shall be paid before filing the compounding application as required in these Guidelines.

Ratio Decidendi

FTC claim to be allowed if Form No. 67 filed before completion of assessment, even though beyond the time limit prescribed in Rule 128

For AY 2018-19, the assessee filed her return of income (‘**ROI**’) on 22 September 2018, which was within the due date prescribed under Section 139 of the Act. During the assessment proceedings, it was found that the assessee had claimed foreign tax credit (‘**FTC**’) for taxes paid in the UK. It was also found that the Form no. 67, used for claiming FTC, was filed by the assessee belatedly on 20 January 2020, i.e., during the assessment proceedings.

The assessing officer (**AO**) disallowed the claim of FTC stating that the assessee failed to file Form no. 67 on or before the due date of filing ROI, as required by Rule 128(9) of the Income-tax Rules, 1962 (‘**Rules**’). The CIT(A) also dismissed the assessee’s appeal.

Before the ITAT, the assessee contended that she had claimed FTC in her ROI. Further, the requirement to file Form no. 67 to claim FTC flows from the Rules and not the parent legislation, i.e., the IT Act. Thus, it was argued that the requirement to file Form no. 67 within the time limit in Rule 128 is directory and not mandatory. The assessee relied on the decision of ITAT Bangalore in *Brinda Ramakrishna* v. *ITO* [2022] 193 ITD 840 (Bangalore - Trib.) and in *42 Hertz Software India (P.) Ltd.* v. *ACIT* [2022] 139 taxmann.com 448 (Bang. - Trib.).

The Revenue contended that the requirement to file Form no. 67 within time limit prescribed under Rule 128 is mandatory, irrespective of the fact that the time limit is contained in the Rules and not the Act. Further, it was argued that the conditions prescribed for claiming FTC, which is beneficial to the assessee, are to be strictly followed, as per the Supreme Court decision in *Ramnath & Co.* v. *CIT,* [2020] 425 ITR 337 (SC). Non-filing of Form no. 67 within the prescribed time limit results in denial of FTC and hence the time limit in Rule 128 cannot be considered as directory.

The ITAT relied on ITAT Bangalore decisions in *42 Hertz (supra)*, *Brinda Rama Krishna (supra)* and *Vinodkumar Lakshmipathi* v. *CIT(A) NFAC Delhi,* ITA no. 680/Bang/2022, dated 6 September 2022. In these cases, it was held that the time limit requirement in Rule 128(9) is not mandatory but directory because, Rule 128(9) does not provide for disallowance of FTC in case of delay in filing Form No. 67. The ITAT further noted that:

a. it is a well-settled law that while laying down a particular procedure, if no negative or adverse consequences are contemplated for non-adherence to such procedure, the relevant provision is usually understood to be purely directory and not mandatory,

b. neither does Rule 128 prescribe for denial of FTC nor do Section 90 or 91 of the Act prescribe the timeline for filing of such declaration on or before due date of filing of ROI,

c. even the legislature amended Rule 128 with effect from 1 April 2022, to allow filing of Form no. 67 on or before the end of the assessment year, which is beyond the due date of filing of ROI.

The ITAT thus allowed the assessee’s appeal and held that the assessee is eligible to claim

FTC as she filed Form no. 67 before completion of assessment, even though beyond the time limit prescribed in Rule 128. [*Sonakshi Sinha* v. *Commissioner* – [2022] 142 taxmann.com 414 (Mumbai - Trib.)]

Time limit to initiate reassessment for A.Y. 2013-14 under unamended Section 149 stands extended till 30 June 2021; first proviso of amended Sec. 149 not applicable for A.Y. 2013-14

The petitioner filed a writ petition in the Delhi High Court challenging the order passed under Section 148A(d) of the IT Act and the notice issued under Section 148 of the Act for AY 2013-14 and also the CBDT Instruction No. 1/2022, dated 11 May 2022.

Initial notice under Section 148 of the IT Act as issued to the Petitioner was quashed by the Delhi High Court following its judgement in *Mon Mohan Kohli* v. *ACIT and Anr,* 2021 SCC OnLine Del 5250. Following the Supreme Court decision in *UoI* v. *Ashish Agarwal*, 2022 SCC OnLine SC 543, a notice under Section 148A(b) was issued to the Petitioner later. This notice and the information contained therein cast scrutiny on certain share sale and purchase transactions undertaken by the Petitioner. After considering Petitioner's reply to this notice, the AO passed the impugned order in which several findings were given against the Petitioner and it was concluded that the share transfer was carried out at a value which is inconsistent with Section 56 of the Act and thus the whole transaction needs to be further scrutinized. Subsequently, the impugned notice under Section 148 was issued.

The Petitioner contended that the information regarding the concerned share transfer is factually wrong since there was no sale/purchase transaction of shares in AY 2013-14. Further, the Petitioner is not connected to the concerned transactions as they are undertaken by Petitioner's shareholders. Further, the present reassessment proceedings, initiated by notice dated 29 June 2021, are time-barred as the time limit for initiating reassessment as per the first proviso to section 149 of the Act (as amended by Finance Act, 2021) expired on 30 March 2020.

The Delhi HC dismissed the writ petition for the following reasons:

a. The Petitioner hasn't proven that the reassessment proceedings are being conducted arbitrarily. Upon perusal of the impugned order and the letter of investigation wing, *prima facie* it can't be said that the Petitioner is not concerned with the transactions. The Revenue's contentions of the Petitioner being beneficiaries of accommodation entry transactions are seriously disputed questions of facts which cannot be adjudicated in writ proceedings. Further, the Petitioner cannot invoke writ jurisdiction when it can resort to the complete machinery for assessment/reassessment provided by the Act. Reliance in this regard was made on the SC decision in *Raymond Woollen Mills Ltd.* v. *ITO and Ors.*, [1999] 236 ITR 34 SC and *CIT and Ors.* v. *Chhabil Das Agarwal*, (2014) 1 SCC 603.

b. The time limit for issuing reassessment notice under unamended Section 149, which was falling from 20 March 2020 till 31 March 2021 was extended till 30 June 2021 ('**extended time limit**') by Taxation and Other Laws (Relaxation and Amendment of Certain Provisions) Act, 2020 ('**TOLA**') and subsequent notifications issued thereunder. The Delhi HC in *Mon Mohan Kohli (supra)* held that reassessment power that existed prior to 31 March 2021 stood extended till 30 June 2021.

c. The time period for issuing reassessment notice for AY 2013-14 was thus extended till 30 June 2021. Due to this the first proviso of Section 149 (as amended by Finance Act, 2021) doesn't apply to the Petitioner's case. Thus, the initial notice issued to Petitioner on 29 June 2021, within the extended time limit is not time barred. This initial notice was deemed to be a notice issued under Section 148A of the Act, by virtue of Supreme Court decision in *Ashish Agarwal (supra)*. Further, the income alleged to have escaped assessment in the present case is more than INR 50 lakh. Thus, the requirements of Section 149(1)(b) of the Act (as amended by Finance Act, 2021) are fulfilled.

The AO was directed to decide the Petitioner's matter in its own merits without being influenced made in the present order of the High Court except on the point of limitation. [*Touchstone Holdings Pvt. Ltd.* v. *ITO and Ors.* – [2022] 142 taxmann.com 336 (Delhi)]

Service tax collected from customers and deposited with Government is not a part of the gross receipts for calculating income on presumptive basis under Section 44BBA

The assessee is a non-resident company engaged in the business of airline service for passengers and cargo and pays tax in India on presumptive basis asp er Section 44BBA of the IT Act. As per Section 44BBA, 5% of the gross receipts earned by a non-resident airlines operator is deemed to be business income taxable in India. For AY 2015-16, while computing such gross receipts, the assessee factored in the receipts from sale of tickets but excluded the amount of service tax collected from customers and paid to the Central Government. The assessee claimed that the amount of service tax is to be excluded from the gross receipts because the service tax is a statutory levy, collected in a fiduciary capacity, on behalf of the Central Government. There is no profit element contained in the service tax amount which the assessee collects and deposits as a collection agent. Further, the service amount is not at the assessee's disposal and is instead a liability discharged by depositing the amount with the Government. However, the AO held that the amount of service tax paid as service provider is a part of the turnover.

On appeal, the CIT(A) relied on the decision of the Delhi High Court in the case of *DIT* v. *Mitchell Drilling International Pvt. Ltd.* (2016) 380 ITR 130 (Del.) and accepted the assessee's contentions. Further, it directed the AO to delete the addition made on this account. Aggrieved, the Revenue appealed before the ITAT Kolkata.

On appeal by the revenue, it was contended that Section 44BBA of the Act opens with a non-obstante clause which overrides the general computation mechanism, thus denying the deductions otherwise available to the assessee. Thus, the term 'Receipts' in Section 44BBA means receipts before allowing any expense incidental to earning of such income. Further, Section 44BBA(2) contains the words 'amounts paid and payable on account of carriage of passenger etc.' and 'amount received and deemed to be received on account of carriage of passenger etc.' The word 'amount' is absolute, is not subject to any qualification or arithmetic calculation. Further, the terms 'amounts paid' or 'amounts received' refers to the total sum paid/payable to the assessee as opposed to 'income' or 'deemed income' or 'accrued income' referred to in Sections 2(24), 5 and 9 of the IT Act.

The ITAT dismissed the appeal and upheld the CIT(A)'s decision, for the following reasons:

a. The phrase '*amount paid or payable*' in Section 44BBA(2)(a) and the phrase '*amount received or deemed to be received*' in Section 44BBA(2)(b) are qualified by the words '*on account of the carriage of passengers, livestock material or goods from any place in India/outside India*'. Thus, only those amounts which are paid/payable or received/deemed to be received by the assessee for the service provided by it can be considered while computing gross receipts u/s. 44BBA (1).

b. There is no income element in the service tax amount, a statutory levy, collected by the assessee from its customers, in the capacity of a collection agent for and on behalf of the Central Government.

c. Delhi HC in *Mitchell Drilling (supra)* had held that service tax collected by an assessee on the amounts paid for rendering services is not included in the gross receipts for calculating presumptive income under Section 44BB. The Delhi HC had considered various judicial precedents and CBDT Circular No. 4/2008, dated 28 April 2008 and Circular No. 01/2014 dated 13 January 2014 to arrive at this conclusion. Section 44BB is in *pari materia* to Section 44BBA.

[*ACIT* v. *Cathay Pacific Airways Limited* – [2022] 142 taxmann.com 196 (Kolkata - Trib.)]

Section 269SS applicable to advances received in relation to transfer of immoveable property only on or after 1 June 2015

Based on a search conducted in the assessee's case, a sum of INR 5.30 crore was treated as its undisclosed income under Section 68 of the Act and added to its income for AY 2013-14. Subsequently, the AO imposed penalty under Section 271D of the Act, holding that the assessee had accepted cash advances of INR 5.30 crore in contravention of Section 269SS of the Act The CIT(A) deleted this penalty and held that since this amount has already been treated as the assessee's undisclosed income, no further penalty under Section 271D can be imposed. The CIT(A) also observed that:

a. amount received can be given a singular nomenclature only and cannot be taxed twice,

b. penalty under section 271D, before the amendment made in Section 269SS w.e.f. 1 June 2015, can be imposed only if the assessee receives cash in the form of loan/deposit. In the present case, the assessee's position is that the concerned amount was customer advances against property received in cash. This position was also upheld with respect to quantum addition under Section 68 of the Act. As a result, penalty under section 271D cannot be imposed since it will change the basic classification of the amount.

On appeal before the ITAT Delhi, the Revenue contended that proceedings under Section 68 and proceedings under Section 271D are totally different. Section 68 with respect to undisclosed income and Section 269SS read with Section 271D of the IT Act will operate concurrently. The assessee argued that Section 269SS, as it applies to AY 2013-14, applies only to loans and deposits received otherwise an account payee cheque or account payee bank draft and not on any advances received by the assessee.

The ITAT referred to Section 269SS as it applied to AY 2013-14 and as it existed after the amendment made by Finance Act, 2015. It observed that the word 'advance' was notably absent in Section 269SS as it applied to AY 2013-14. Further, the ITAT referred to Webster Dictionary and provisions of the Companies Act, 2013 to understand the meaning of the terms 'loan' and 'deposit'. A 'loan' is taken at the instance/for the benefit of the borrower and is payable only when the obligation to repay arises. 'Deposit' is taken at the instance and for the benefit of the depositor and is also payable on the demand of the depositor. On the other hand, the term 'advance' refers to amounts given for specified purchases for immediate/subsequent transfer of goods & services and are settled fully after the transactions are consummated. While a 'loan' is a debt instrument for the recipient, an 'advance' is a credit instrument.

The ITAT also noted that before the amendment made by Finance Act, 2015, Section 269SS applied to loans & deposits only. Post-amendment, w.e.f. 1 June 2015, Section 269SS became applicable to 'any specified sum' which means any sum receivable, whether as advance or otherwise, in relation to transfer of immovable property, whether or not the transfer takes place. The ITAT held that since the amendment to the Section 269SS is not retrospective in operation, and came into effect from 1 June 2015 only, it won't apply to the assessee's case. However, similar transactions undertaken by the assessee w.e.f. 1 June 2015 would fall foul of Section 269SS and Section 271D. Thus, the ITAT dismissed Revenue's appeal. [*ACIT* v. *Ruhil Developers Pvt. Ltd*. – Order dated 30 August 2022 in ITA No. 7128/Del/2018, ITAT Delhi]

Payment for clinical testing/trials services is not taxable as FTS under India-USA DTAA and India-Canada DTAA, however, is taxable as FTS under India-Mexico DTAA

Assessee, a global pharmaceutical company, having its principal place of business in India. It made remittances to parties of USA, Canada, and Mexico for clinical trials, for AY 2013-14, without deducting TDS. The AO held that the assessee was liable to deduct TDS under Section 195 of the Income-tax Act, 1961 ('**IT Act**') on these remittances and made necessary additions to the assessee's income.

Payments made for clinical trials to foreign parties in USA and Canada

The CIT(A) noted that these payments were made in consideration of receiving study reports by the assessee from the overseas entities. The CIT(A) held that these payments are not Fee for Technical Services ('**FTS**'), under the India-USA DTAA and India-Canada DTAA since they do not satisfy the 'make available' clause provided in these tax treaties. There was no transfer of any skill or knowledge to the assessee by the foreign parties. Further, this issue has been earlier decided in the assessee's favor in its own case for AY 2010-11 by ITAT Ahmedabad. Thus, it was held that the assessee was not obligated to deduct tax on these payments.

The CIT(A) also rejected the alternative argument of the Revenue that these payments qualify as 'royalties.' The CIT(A) held that the payments are made for clinical trials and testing services, which by very nature, do not fall within the meaning of 'royalty' and can only be FTS.

On Revenue's appeal on this issue, the ITAT upheld the CIT(A)'s decision. The ITAT also rejected another alternative argument of the Revenue that the above payments are FTS as per the second part of FTS clause of applicable tax treaties since they are in considered for development and transfer of a technical plan or a technical design. The ITAT noted that the agreements between the assessee and the foreign parties were for provision of clinical testing services and were not agreements for developing or transferring a technical plan or design.

Payments made for clinical trials to foreign parties in Mexico

The assessee was an exporter and all its business activities were conducted in India. It had entered into a supply and distribution agreement with foreign parties based in Mexico to promote its business in Mexico. The CIT(A) rejected the assessee's argument that since the payments were made to Mexican parties for services rendered and utilised outside India, they fell under the exception provided in Section 9(1)(vii)(b) of the Act and were thus not FTS taxable in India.

The CIT(A) held that there is a difference between having a 'source of income' outside India and having a 'source of receipt of the money' outside India. To fall within the exception provided in Section 9(1)(vii)(b), the source of income should be outside India and not the source of receipt. Merely doing export business from India doesn't mean that the business itself is carried outside India. The assessee received payments against export sales and all its business-related activities are carried out in India. Hence, only a source of receipt was outside India and not the source of income. Rather, the source of income is in India and hence the assessee doesn't fall under the exception in Section 9(1)(vii)(b). The CIT(A) relied on Delhi HC decision in *CIT v. Havells India Ltd. [2013] 352 ITR 376 (Delhi)* in this regard.

The CIT(A) further held that under the India-Mexico DTAA, mere rendering of technical services is enough to trigger taxability as FTS, since there is no 'make-available' clause in this tax treaty. Hence, it was held that the payments made to Mexican parties was taxable as FTS in India and the assessee should have withheld taxes on these payments. The ITAT rejected the assessee's appeal on this issue and upheld the CIT(A)'s decision. [*Cadila Healthcare Ltd.* v. *DCIT* – [2022] 142 taxmann.com 211 (Ahmedabad - Trib.)]

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