ANSWERS OF MODEL TEST PAPER 5

FINAL COURSE: GROUP - II

PAPER – 4: DIRECT TAX LAWS & INTERNATIONAL TAXATION

Division A – Multiple Choice Questions

MCQ No.	Most Appropriate Answer	MCQ No.	Most Appropriate Answer
1.	(b)	9.	(d)
2.	(b)	10.	(d)
3.	(b)	11.	(c)
4.	(b)	12.	(b)
5.	(d)	13.	(a)
6.	(a)	14.	(c)
7.	(a)	15.	(a)
8.	(a)		

Division B – Descriptive Questions

1. Computation of Total Income of Orient Pharmaceutical Pvt. Ltd. for the A.Y. 2025-26

	Particulars	Amount (in ₹)	
I	**Profits and gains of business or profession**		
	Net profit as per statement of profit and loss		95,00,000
	Add: **Items debited but to be considered separately or to be disallowed**		
	(1) Depreciation as per Companies Act, 2013	11,90,000	
	(2) Bonus transferred to the trust for making payment to the employees after settlement of the dispute	Nil	
	[The bonus would be allowable as deduction u/s 36(1)(ii), even though the amount of bonus payable was initially remitted to the trust created for		

		the purpose of avoiding late payment of bonus, since the actual payment of bonus made to the employees is 31st August, 2025 i.e., on or before due date of filing return of income. Since the same has been already debited to the statement of profit and loss, no further adjustment is required]		
	(3)	**Regularization fee for violating a law** [Regularization fee paid for violating a law as prescribed by Medical Council of India is a payment to compound an offence. Such expenditure is considered to be the expenses prohibited by the law. Hence, it does not qualify for deduction u/s 37. As the same has been debited to the statement of profit and loss, it has to be added back]	9,50,000	
	(4)	**Late fees to Government for failure in performance of a contract** [Late fees of ₹ 45,000 paid for non-fulfilment of a contract within the stipulated time is not for the breach of law but was paid for breach of contractual obligations and therefore, is an allowable expense. Since it is already debited in statement of profit and loss, no further adjustment is required]	Nil	
	(7)	**Payment of Interest to a company incorporated in USA** [Since the tax has been deducted in March, 2025 and deposited by the company on 14.7.2025 i.e., on or before due date of filing return of income, no disallowance would be attracted under section 40(a)(i). Since the interest has been already debited to the statement of profit and loss, no further adjustment is required]	Nil	
	(8)	**Contribution to electoral trust** [Contribution to electoral trust is not allowable as deduction while computing business income of the company. Since	65,000	

	the contribution has been debited to statement of profit and loss, the same has to be added back while computing business income]		22,05,000
			1,17,05,000
	***Less:* Items credited but not taxable or chargeable to tax under another head**		
	(5) Profit on sale of plot of land to 100% subsidiary [Capital Gain arising on sale of plot of land is taxable under the head "Capital Gains". Since the profit on sale of plot of land has been credited to the statement of profit and loss, the same has to be deducted while computing business income]	7,50,000	
	(6) Profit on sale of shares of M/s Stadel Ltd. [Capital Gain arising on sale of shares of M/s Stadel Ltd. is taxable under the head "Capital Gains". Since the profit on sale of shares has been credited to the statement of profit and loss, the same has to be deducted while computing business income]	4,50,000	
			12,00,000
			1,05,05,000
	***Less:* Depreciation as per Income-tax Act, 1961**		
	Normal depreciation		
	- On fire-fighting equipments [Eligible for depreciation even though such equipments were not used during the previous year.]	95,000	
	- On new machinery [₹ 75,00,000 x 15% since it is put to use for more than 180 days]	11,25,000	
	- On machinery sold and reacquired [15% of actual cost of ₹ 35,00,000, being lower of WDV at the time of sale (i.e., ₹ 35 lakhs) or price paid for re-acquisition (i.e., ₹ 65 lakhs)	5,25,000	

	Additional depreciation			
	- On new machinery [₹ 75,00,000 x 20%]		15,00,000	
				32,45,000
				72,60,000
II	**Capital Gains**			
	Profit on sale of plot of land to 100% subsidiary		Nil	
	[Short-term capital gains arise on sale of plot of land held for less than 24 months. However, in this case, since the transfer is to a 100% subsidiary company and the subsidiary company is an Indian company, the same would not constitute a transfer for levy of capital gains tax]			
	Long term capital gain on sale of shares of M/s. Stadel Ltd. [Since shares were held for more than 12 months]			
	[Full value of consideration (2,500 x ₹ 280)]	7,00,000		
	Less: Cost of acquisition - Higher of (i) and (ii)	4,37,500		
			2,62,500	2,62,500
	(i) Actual cost of acquisition (2,500 x ₹100) ₹ 2,50,000			
	(ii) ₹ 4,37,500, being lower of fair market value as on 31.1.2018 (i.e., ₹ 4,37,500, being 2,500 x 175) and sale consideration (i.e., ₹ 7,00,000)			
	Gross Total Income			**75,22,500**
	Less: **Deduction under Chapter VI-A**			65,000
	Under section 80GGB [Contribution by a company to an electoral trust is allowable as deduction, since payment is made otherwise than by cash]			
	Total Income			**74,57,500**

2. (a) (i) Computation of taxable Capital gain in the hands of Mrs. Seema Aggarwal for A.Y.2025-26

Particulars	₹
Full value of consideration	15,50,00,000
As per section 50C, the full value of consideration would be actual sales consideration since the stamp duty value as on 15.10.2024 of ₹ 17,00,00,000 does not exceed 110% of actual consideration of ₹ 15,50,00,000.	
Less: **Cost of acquisition**	1,02,00,000
[₹ 1,02,00,000 (Higher of actual cost of ₹ 45,00,000 and Fair market value as on 1.4.2001 of ₹ 1,20,00,000, but restricted to stamp duty value as on 1.4.2001 of ₹ 1,02,00,000)	
[Indexation benefit would not available while computing capital gains since the property is transferred on or after 23.7.2024]	
	14,48,00,000
Less: **Exemption under section 54**	**10,00,00,000**
[Purchase of one residential plot of ₹ 8 crores on 18.2.2025 and deposit of ₹ 3 crores in Capital Gain Account Scheme on 31.3.2025 (before the date of filing of return of income) provided that the construction thereon is completed within the stipulated time of three years, but restricted to maximum of ₹ 10 crores]	
Taxable long term capital gains	**4,48,00,000**

(ii) The words “by way of advance or loan" in section 2(22)(e) must be construed to mean those advances or loans which a shareholder enjoys simply on account of being a person who is the beneficial owner of shares holding not less than 10% of the voting power.

In case such loan or advance is given to such shareholder as a consequence of any further consideration received from such a shareholder which is beneficial to the company, such advance or loan cannot be a deemed dividend within the meaning of the Act.

Gratuitous loan or advance given by a company to a shareholder, who is the beneficial owner of shares holding not less than 10% of the voting power, would come within the purview of section 2(22)(e) to the extent of accumulated profits of the company but not the cases where the loan or advance is given in return for an advantage conferred upon the company by such shareholder.

In the present case, advance of ₹ 15 lakh was given by Aurelia Exports (P) Ltd. to Mr. Manjoo Menon holding 20% shareholding as advance rent for the property let out by him to the company and out of which ₹ 7 lakhs was adjusted against rent payable of F.Y. 2024-25. The advance was given by the company since Mr. Menon mortgaged his personal property thereby enabling the company to obtain the loan from bank in 2013.

Therefore, such advance of ₹ 8 lakhs outstanding as on 31.3.2025 cannot be brought within the purview of section 2(22)(e)[15], since it was not in the nature of gratuitous advance but was given as advance rent and to protect the interest of the company.

(b) Miles Inc., a foreign company, would be resident in India in P.Y. 2024-25 if its POEM, in that year, is in India. Since the meeting of Board of Directors are held outside India i.e., in Chicago, USA where management and commercial decisions necessary for conduct of company's business are taken, its POEM during the A.Y. 2025-26 would be outside India. Hence, Miles Inc. is a non-resident during the P.Y. 2024-25.

The decisions made by shareholders in India on modification of the rights attaching to various classes of shares and sale of company's assets situated in India are not relevant for determination of Miles Inc.'s place of effective management.

[15] *Pradip Kumar Malhotra v. CIT (2011) 338 ITR 538*

Computation of total income of Miles Inc. for the A.Y. 2025-26

Particulars	Amount (₹)
Dividend received on GDR of an Indian company [Taxable, since income is from any asset or source of income is in India. Tax @10.4% would have been deducted on dividend of GDR] [₹ 5,50,000 / 89.6%]	6,13,839
Fees for technical services received from Government of India [Taxable, since it is deemed to accrue or arise in India on account of being received from Government of India even though services are utilised for development project carried out outside India. Tax @20.8% would have been deducted on FTS received from Government] [5,55,000/79.2%]	7,00,758
Total Income	**13,14,597**

3. (a) (i) "Specified income" under section 115BBI includes the following:

- income which has been applied for the benefit of prohibited persons u/s 13(3)
- deemed income under section 11(3) on account of violation of certain conditions stipulated for accumulation of income.

Specified income of Devyani Trust liable to tax@30% under section 115BBI for A.Y. 2025-26

Particulars	Amount (₹)
Amount applied for the benefit of the trustee [Trustee of the trust is one of the persons specified u/s 13(3)]	4,50,000
Amount applied for the benefit of Mr. Sujan Dave [Since Mr. Sujan Dave's total contribution to the trust upto 31.3.2025 is more than ₹ 50,000, he is a person specified u/s 13(3)]	2,50,000
Donation made to another trust out of accumulated income of P.Y. 2022-23 [Donation to another charitable trust out of accumulated income is one of the violations of condition specified for	2,50,000

accumulation of income – Section 11(3)]	
Specified income liable to tax @30% under section 115BBI	**9,50,000**

(ii) Since Parivartan trust has already commenced its activities and has not availed exemption under section 11 for any P.Y. ending on or before 1.11.2024, (being the date of application), it need not first apply for provisional registration.

It can at any time after the commencement of such activities directly apply for final registration under section 12AB[16].

Thus, the action of trust for applying for the final registration as per section 12AB before applying for provisional registration for exemption under section 11 is valid.

The Principal Commissioner or Commissioner has to pass the order granting or rejecting the registration before expiry of 6 months from the end of the quarter in which application is received i.e., by 30.6.2025.

Exemption under section 11 and 12 would be applicable from the assessment year immediately following the financial year in which such application is made i.e., from A.Y. 2025-26 (P.Y. 2024-25).

(b) Computation of total income and net tax liability of Mr. Kumar Saurav for A.Y.2025-26 under the default tax regime

Particulars	₹	₹
Income from house property		
Gross Annual Value[17] of property in Country 'P'	1,92,000	
Less: Municipal taxes paid in Country 'P'	9,500	
Net Annual Value	**1,82,500**	
Less: Deduction under section 24 – 30% of NAV	54,750	
		1,27,750

[16] Read with section 12A(1)(vi)(B), w.e.f. 1.10.2023.
[17] Rental income has been taken as GAV in the absence of other information relating to fair rent, municipal value etc.

Profits and Gains of Business or Profession		
Income from profession in India	10,75,000	
Royalty income from literary book from Country 'P' (after deducting expenses of ₹ 35,000)	4,15,000	
		14,90,000
Income from Other Sources		
Interest on Fixed deposit with XYZ Bank	95,000	
Interest on savings bank account	47,000	
Agriculture income in Country 'P'	65,000	
Dividend from a company incorporated in Country 'P'	1,59,000	
		3,66,000
Gross Total Income		**19,83,750**
Less: Deductions under Chapter VI-A [Not available under default tax regime]		Nil
Total Income		**19,83,750**
Tax liability on ₹ 19,83,750		
Tax on total income [30% of ₹ 4,83,750 + ₹ 1,40,000]		2,85,125
Add: Health and Education cess@4%		11,405
		2,96,530
Less: Deduction u/s 91 (See Working Note below)		1,14,614
Net Tax Liability		**1,81,916**
Net Tax Liability (Rounded off)		**1,81,920**

Working Note: Calculation of deduction under section 91

Particulars	₹
Doubly Taxed Income – Country P	
Income from house property	1,27,750
Royalty Income [₹ 4,50,000 – ₹ 35,000 (Expenses)]	4,15,000
Agricultural income	65,000

Dividend	1,59,000
	7,66,750
Rate of tax in Country P = 16%	
Indian rate of tax = 2,96,530/19,83,750 x 100 = 14.948%	
Lower of the above = 14.948%	
Deduction u/s 91 [14.948% x ₹ 7,66,750]	**1,14,614**

4. (a) (i) In respect of tips collected by the company from the guests and distributed to the employees, the person responsible for paying the employee was not the employer at all, but a third person, namely the guest.

The payments of collected tips included and paid by way of a credit cards, UPI or Net Banking in the bills by guest, would not be payments made "by or on behalf of" an employer.

The contract of employment not being the proximate cause for the receipt of tips by the employee from a guest, such payments would be outside the scope of sections 15 and 17.

There is no employer-employee relationship between customers and the employees of Raj Keshri Hotels and Resorts Ltd. and therefore such payments do not fall in the nature of salary.

On account of such tips being received from guests and not from the employer, section 192 would not get attracted at all in the hands of Raj Keshri Hotels and Resorts Ltd.[18] Thus, the company is not responsible for deducting tax at source from disbursement of tips to its employees.

(ii) Lalit is required to deduct TDS under section 194C for contract payments and under section 194-I for rent paid for office premises during the previous year 2024-25 since Lalit's turnover for the previous year 2023-24 exceeded ₹ 1 crore.

[18] *ITC Ltd v. CIT (2016) 384 ITR 14 (SC)*

Thus, tax deduction under section 194C would be ₹ 5,000, being 1% of ₹ 5 lakhs.

Mr. Lalit is also required to deduct tax at source @10% u/s 194-I on the rent paid for office premises and for furniture, fixtures and vacant land appurtenant to office to Mr. Hemant, since aggregate of rent i.e., ₹ 2,58,000 [(16,000 + ₹ 5,500) x 12] paid during the P.Y. 2024-25 exceeds the threshold limit of ₹ 2,40,000.

The tax deduction under section 194-I would be ₹ 25,800, being 10% of ₹ 2,58,000.

(iii) As per section 194-O, ABC Limited, an e-commerce operator is required to deduct tax at source @0.1% on ₹ 4,90,000, being the gross amount of sale of products 'R' of XY and Co., a partnership firm, an e-commerce participant, since such sale of goods is facilitated by ABC Limited through its digital facility.

ABC Ltd. is also required to deduct tax @0.1% on the payment of ₹ 60,000 directly made to XY and Co., since such amount is deemed to be amount credited or paid by ABC Ltd. to XY and Co.

Thus, ABC Ltd. is required to deduct tax of ₹ 550**,** being 0.1% of ₹ 5,50,000.

(b) Since Armo Ltd. entered into a transaction with Yalin Ltd., in Country X which is located in a notified jurisdictional area (NJA), Armo Ltd. and Yalin Ltd. would be deemed as associated enterprises and the transactions between them would be deemed to be international transactions. Accordingly, all the provisions of transfer pricing would be attracted in case of such a transaction.

The transactions of Armo Ltd. with KB Inc., U.K. for sale of identical goods are comparable uncontrolled international transactions, since it is neither associated enterprises of Armo Ltd. nor situated in NJA.

Hence, Comparable Uncontrolled Price (CUP) method can be used to determine ALP.

Computation of ALP using CUP method

Particulars	₹ in crores
Price charged by KB Inc. (on CIF basis)	13.00
Less: Ocean freight and insurance, has to be reduced since the price charged to Yalin Ltd. is on FOB basis	0.25
Less: Cost of after-sales support service (has to be reduced, since such services are being provided to KB Inc. but not to Yalin Ltd.)	0.19
Arm's Length Price	**12.56**
Less: Price at which goods were sold to Yalin Ltd.	11.75
Arm's length adjustment [Increase in profit of Armo Ltd.]	**0.81**

5. (a) (i) **Issue Involved:** The issue under consideration is whether the provisions of section 206AA, which prescribe a higher rate of tax deduction at source in case of non-furnishing of PAN by a foreign company, override the Double Taxation Avoidance Agreement (DTAA) that specify a lower rate of tax.

Provisions Applicable: As per section 206AA, in case of non-furnishing of PAN by the deductee to the deductor, the tax is required to be deducted at higher of the rate specified in the relevant provision or at the rates in force or at the rate of 20%.

Analysis and Conclusion: Section 90(2) provides that the provisions of the DTAAs would override the provisions of the Act in cases where the provisions of DTAAs are more beneficial to the assessee.

Even the charging sections 4 and 5 of the Act, which deal with the principle of ascertainment of total income under the Act, are also subordinate to the principle enshrined in section 90(2).

Thus, in so far as the applicability of the scope/rate of taxation with respect to the impugned payments made to the non-residents is concerned, no fault can be found with the rate of

taxation invoked by the assessee based on the DTAAs, which prescribed for a beneficial rate of taxation.

The provisions of tax withholding, i.e., section 195 of the Act, would apply only to sums that are otherwise chargeable to tax under the Act. The provisions of DTAAs, along with sections 4, 5, 9, 90 & 91 of the Act, are relevant while applying the provisions of tax deduction at source. Therefore, section 206AA of the Act cannot be understood to override charging sections 4 and 5 of the Act.

Accordingly, the contention of the revenue that in the absence of furnishing of PAN, the assessee was under an obligation to deduct tax at a higher rate of 20% is not correct.

The above answer is based on the rationale of the Supreme Court in *CIT (International Taxation) v. Air India Ltd. [2023] 456 ITR 139*.

(ii) **Issue Involved:** The issue under consideration is whether the Assessing Officer is bound to allow the set-off of brought forward losses under section 72 even if the assessee, Mr. X, in this case, has not claimed the same in the return filed by him and the time limit for filing revised return has expired.

Provisions Applicable: Under section 72, business losses shall be carried forward and shall be set-off against the profits and gains of any business in the next assessment year. It is assumed that the assessee has filed the return of income within the time stipulated u/s 139(1) and hence is eligible for set off of the unabsorbed loss in the subsequent year.

The wording used in section 72 is “shall”, indicating that the provisions relating to set off of brought forward business loss are mandatory provided the loss was determined in pursuance of a return filed under section 139(3) in any earlier previous year.

Analysis and Conclusion: As per *CBDT Circular No.14 (XL-35) of 1955 dated 11.04.1955,* it is the duty of the Assessing Officer to assist a taxpayer in every reasonable way, particularly in the matter of claiming and securing reliefs and in this regard, they should take the initiative in guiding a

taxpayer where proceedings or other particulars before them indicate that some refund or relief is due to him.

Thus, it is the duty of the Assessing Officer to apply the relevant provisions of the Act for the purpose of determining the true figure of Mr. X's total income and consequential tax liability. Merely because Mr. X has not claimed the set-off of brought forward losses of ₹ 3 lakh in the original return filed and the time limit for filing revised return has expired, it cannot relieve the Assessing Officer of his duty to apply section 72 in the appropriate case.

The Assessing Officer is bound to accept the request of Mr. X and allow the set-off of brought forward losses of ₹ 3 lakh under section 72, even if Mr. X has not claimed the same in the return filed, and the time limit for filing the revised return has expired.

The above answer is based on the rationale of the Supreme Court in *CIT v. Mahalakshmi Sugar Mills Co. Ltd. (1986) 160 ITR 920, taking note of the CBDT Circular No.14 (XL-35) of 1955 dated 11.04.1955.*

(iii) **Issue Involved:** The issue under consideration is whether penalty u/s 271C and interest u/s 201(1A) both are leviable on late deposit of TDS.

Provisions applicable: Section 271C(1)(a) provides that if any person fails to deduct the whole or any part of the tax as required by or under the provisions of Chapter XVII-B, then, such person is liable to pay, by way of penalty, a sum equal to the amount of tax which such person failed to deduct.

Section 201(1A) provides that in case a tax has been deducted at source but is subsequently remitted belatedly, such a person is liable to pay interest as provided under section 201(1A).

Analysis and Conclusion: On a plain reading of section 271C(1)(a), no penalty would be leviable on belated remittance of TDS after it is deducted by the assessee.

Similarly, section 276B speaks about prosecution for failure to pay the tax deducted at source to the credit of the Central Government within the prescribed time.

The words "fails to deduct" in section 271C(1)(a) cannot be read as "failure to deposit/pay the tax deducted".

Accordingly, no penalty would be leviable under section 271C on delay in remittance of the tax deducted at source after deducting it on time.

However, interest u/s 201(1A) for late deposit of TDS is leviable.

The above answer is based on the rationale of the Supreme Court in *US Technologies International Pvt. Ltd. v. CIT [2023] 453 ITR 644*.

(b) (i) In order to complete tax cases, a country may require certain information which may be available with the treaty partner.

Article 26 provides for the information which may be exchanged and the manner in which such a request has to be made.

The OECD and UN Model Conventions are similar with respect to this Article.

Importance of Article 26:

- facilitates effective exchange of information between Contracting States.
- curtails cross-border tax evasion and avoidance,
- curtails the capital flight that is often accomplished through tax evasion & avoidance. This is particularly relevant in the perspective of developing countries.

(ii) Pillar Two consists of GloBE Rules which means Global Anti-Base Erosion rules, through which 15% global minimum tax has been introduced.

The GloBE Rules apply to Constituent Entities that are members of an MNE Group that has annual revenue of EURO 750 million or more in the Consolidated Financial Statements

of the Ultimate Parent Entity (UPE) in at least two of the four Fiscal Years immediately preceding the tested Fiscal Year.

6. (a) (i) Form 15CB is a certificate of an accountant wherein he certifies that he has examined the agreement between the remitter and the beneficiary requiring such remittance. He also has to examine the relevant documents and books of account required for ascertaining the nature of remittance and for determining the rate of deduction of tax at source.

The Chartered Accountant certifying the Form 15CB undertakes to have verified the agreement between the remitter and the beneficiary as well as the relevant documents and books of account to ascertain the nature of remittance and determine the rate of TDS.

In this case, however, the Chartered Accountant mentioned that he had only verified KYC of signatory to invoice and the invoices thereof.

He had not only failed to justify as to how verification of invoices was considered as sufficient compliance for certifying the forms but also failed to bring on record the said invoices.

Thus, he failed to provide any basis on which he relied for issuing Form 15CB certificates to the company.

On account of such failure, clauses (7) and (8) of Part I of the Second Schedule to the Chartered Accountants Act, 1949 for failure to exercise due diligence in discharging his professional responsibilities and failure to obtain sufficient information may be invoked.

(ii) 1. **Tax Planning** – Gifting of fixed deposits of ₹ 50 lakhs by Mr. D to his son who attained the age of 18 years for the purpose of shifting interest income from his hands to his son so that there may be zero tax implication, is a permitted **tax planning** measure under the provisions of income-tax law.

2. **Tax Evasion** – Mr. Ram's annual income is ₹ 49.50 lakhs for the A.Y. 2025-26. He also earned commission of ₹ 6 lakhs from ABC Limited. Accordingly, his total income would be ₹ 55.50 lakhs which exceeds ₹ 50 lakhs and hence surcharge is applicable on tax on total income.

However, for the purpose of saving tax, he instructed ABC Ltd. to transfer the commission in his wife's account. This is the case of application of income and not of diversion of income by overriding title, since such transfer of commission is not under any obligation but to evade tax.

This is tax evasion.

(b) The statement is not correct. As per section 245N, advance ruling not only includes a determination by the BAR in relation to a transaction which has been undertaken or is proposed to be undertaken by a non-resident applicant, but also includes, inter alia, determination by the BAR –

(i) in relation to the tax liability of a non-resident arising out of a transaction which has been undertaken or is proposed to be undertaken by a resident applicant with such non-resident and such determination shall include the determination of any question of law or of fact specified in the application

(ii) in relation to the tax liability of a resident applicant, arising out of a transaction which has been undertaken or is proposed to be undertaken by such applicant and such determination shall include the determination of any question of law or of fact specified in the application.