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RECENT UPDATE: DIRECT TAXATION DATE: 28-JUNE-2018

1. TAXATION

I. Summary:

Tax benefit claimed by taxpayers in the revised return can't be denied by taxmen simply on the ground that the revised ITR has been filed after the issue of notice by the Income Tax department.

In landmark judgement by the Mumbai ITAT on 20th June,2018 in the case of **Mahesh H. Hinduja Vs Income Tax Officer** now a taxpayer can claim deduction by filing a revised IT return even after the issue of notice by the Tax Department, provided the revised return is filed within the time limit prescribed under Section 139(5) of the IT Act.

Currently, the time limit for filing a revised return is earlier of the two dates:

- Before the expiry of 12 months from the last day of the financial year or
- Before the completion of I-T assessment.

II. Details of the case:

In this case before the ITAT, Mahesh Hinduja had declared a total income of Rs 4.91 lakh in his original return for the financial year 2010-11. He later filed a revised return declaring a total income of Rs 6.24 lakh. In this revised return he also disclosed long-term capital gains (LTCG) of nearly Rs 50 lakh. However, as he had invested 1.15 crore in a new residential house, he claimed a deduction under Section 54 of the I-T Act. Thus, capital gains were not offered for tax.

Under the Act, if an investment is made in another house in India, within the stipulated period of time, then the 'cost of the new house' is deducted and only the balance component of the LTCG is taxable. Thus, if the amount of capital gains is equal to or less than the cost of the new house, the entire sum of LTCG is not taxable.

To ensure that the taxpayer has not underreported his income or paid less tax, the I-T Act empowers I-T officials to issue a notice asking for further evidence. As the revised return was filedby Hinduja after he had received a notice under section 143(2), the I-T official rejected his claim fordeduction. The litigation finally reached to the ITAT.

The ITAT noted that the I-T official had rejected the revised return of income as invalid but at the same time had accepted the higher income offered in the revised return, including the LTCGs. Only the claim of deduction under Section 54 had been rejected.

III. Conclusion:

The ITAT held that the I-T Act does not bar a taxpayer from filing a revised I-T return after issue of notice under Section 143 (2). Hinduja's case was remanded(sent) back to the I-T official for examining and allowing the deduction claimed, subject to the fulfilment of conditions prescribed for such claim

2. FEMA

2.1. Introduction of Single Master Form (SMF)

Presently, the reporting of total foreign investment in India (made by Person resident outside India) are made through various forms and modes (online and offline) which leads to disintegrated reporting. Investment is made in eligible capital instruments or capital contribution in LLP or investment in other investment vehicles. However, with the objective of integrating the reporting structure of various types of investment, the Reserve Bank of India had in April 2018 **proposed to introduce an online reporting facility**. This is planned to be done through **Single Master Form (SMF)** which would subsume all current reporting requirements in FDI.

In view of the above, RBI has issued AP (DIR series) dated June 07, 2018 to lay down the roadmap for implementation of reporting of foreign investments through SMF.

The highlights of the said circular are mentioned below for your quick reference:

1. It provides a facility for reporting total foreign investment by Non resident in Indian entity (Company, LLP and Investment Vehicle).
2. Prior to the implementation of SMF, Reserve Bank would provide an interface to the Indian companies to input complete data on total foreign investment received by the companies in a specified format.
3. The interface will be **available for 15 days only**, on RBI website www.rbi.org.in, from **June 28, 2018 to July 12, 2018**.
4. Post implementation of SMF, the various reporting on the e-Biz portal will be discontinued by Reserve Bank in a phased manner.
5. Indian entities not complying with this pre-requisite will not be able to receive foreign investment (including indirect foreign investment) and will be considered non-compliant with FEMA and regulations made thereunder.

6. Indian entities are mandated to access the website and file their total foreign investment data on the interface in the specified format.
7. SMF would subsume the following forms for reporting foreign investment in Indian entities/LLP/Investment Vehicle: Form FC-GPR, Form FC-TRS, Form LLP-I, Form LLP-II, Form ESOP, Form CN, Form DRR, Form DI, Form InVi.

2.2. Amendment in Liberalised Remittance Scheme (LRS)

RBI has vide AP (DIR series) Circular No. 32 dated 19.06.2018 has amended Liberalised Remittance Scheme (LRS). The amendments as covered in the said circular are as under:

a) **Furnishing of Permanent Account Number** (PAN), which was earlier not to be insisted for permissible current account transactions of up to USD 25,000, **shall now be mandatory** for making all remittances under Liberalised Remittance Scheme (LRS).

b) In the context of remittances allowed under LRS for maintenance of **close relatives**, it has been decided, in consultation with Government, **to align the definition of 'relative'** with the definition given in Companies Act, 2013 instead of Companies Act, 1956.

3. CASE LAW ON INTERNATIONAL TAXATION-DTAA & TAXABILITY

Assessee (Plaintiff)	**Clearwater Capital Partners (Cyprus) Ltd.**
Department (Respondent)	Deputy Commissioner of Income-tax
Journal of Publication	94 taxmann.com 118
Date of Publication:	2nd May ,2018
Ruling authority	**Mumbai-Tribunal (Mum - ITAT)**

I. Key take-away from the Judgement:

Where non-resident assessee earned interest income on FCCBs issued by an Indian company abroad,

- it was not liable to tax in India as per exception carved out in section 9(1)(v)(b).

Where non-resident assessee earned interest on fully convertible debentures issued by an Indian company,

- it would be liable to tax at rate of 10 per cent in terms of article 11 of India-Cyprus DTAA.

Where non-resident assessee earned consultancy fee from an Indian company,

- same was liable to be taxed at rate of 10 per cent in terms of article 12 of India-Cyprus DTAA.

II. Detailed analysis:

Facts:

- S. Ltd. an Indian company had issued Foreign Currency Convertible Bond (FCCB) to repay its borrowing from ABN Amro Bank NV for the purpose of its business outside India.
- The assessee, a tax resident of Cyprus had received from S Ltd.:
  a) Interest income on FCCB and
  b) Incentive fees as a difference in conversion price of the FCCB's
- The assessee claimed non taxability of:
  1) Interest income- due to the exception carved out in section 9(1)(v) *
  2) Incentive fee - because money was raised and utilized by S Ltd. outside India.

- However, the AO rejected the assessee's contention holding that the FCCB was raised by an Indian company and hence it was incurred in India.
- The AO taxed the total income of the assessee at 42.23% including surcharge and cess whereas the assessee pleaded for taxability at 10% on the consultancy services citing the India Cyprus tax treaty.
- The DRP after making necessary verifications, accepted the assessee's standpoint.

Issue:

- Whether interest on FCCB were taxable in India in view of exception to Section 9(1)(v)(b)?
- Whether provisions of act would apply to the extent they are more beneficial to the assessee?

Held:

- Money borrowed by the Indian Co. Was wholly utilized for repayment outside India. Where interest is paid by resident for debt incurred outside India used for business carried on outside India, it shall not be deemed to accrue or arise in India as per the exception to 9(1)(v)(b)

- Incentive fees was received for revision in conversion price of FCCBs issued outside India. As money was raised and utilized outside India, it could not be deemed to accrue or arise in India in view of section 9(1)(i) of the Act.

- As per article 11 and 12 of the India-Cyprus DTAA, interest and FTS may be taxed at maximum of 10% in the contracting state in which they arise, provided the beneficial owner of interest/FTS is a resident of that contracting state. As the Treaty is more favorable to the assessee the 10% rate will be applicable on the consultancy fees received by it.

Cases referred to:

Suzlon Energy Ltd. vs. *Asst. CIT [2015]*

DIT (International Taxation) vs. *NGC Networks Asia LLC [2009]*

III. Did you know?

***Section 9**

(1) The following incomes shall be deemed to accrue or arise in India:

(v) income by way of interest payable by -

(b) a person who is a resident, except where the interest is payable in respect of any debt incurred, or moneys borrowed and used, for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India.

What is an FCCB?

A foreign currency convertible bond (FCCB) is a type of convertible bond issued in a currency (Eg. $) different than the issuer's domestic currency (INR). In other words, the money being raised by the issuing (Indian) company is in the form of a foreign currency ($). A convertible bond is a mix between a debt and equity instrument.

It acts like a bond by making regular coupon and principal payments, but these bonds also give the bondholder the option to convert the bond into stock.

Relevant extract from the India-Cyprus DTAA:

In this case law, Interest is paid by Indian Co. (S Ltd.) to Cyprus company (assessee)

Article 11 - Interest

- Interest arising in a Contracting State (India) and paid to a resident of the other Contracting State (Cyprus Co.) may be taxed in that other State (Cyprus). Meaning-Generally, it will be taxed in Cyprus as it is paid there.

- However, such interest may also be taxed in the Contracting State in which it arises (India) and according to the laws of that State, but if the beneficial owner of

the interest is a resident of the other Contracting State(Cyprus), the tax so charged shall not exceed 10 percent of the gross amount of the interest.

Meaning-Tax may be charged in India but not exceeding the rate of 10%

Article 12 - Royalties and Fees for Technical Services

- Royalties or fees for technical services arising in a Contracting State(India) and paid to a resident of the other Contracting State (Cyprus Co.) may be taxed in that other State(Cyprus).

Meaning-Generally, it will be taxed in Cyprus as it is paid there.

- However, such royalties or fees for technical services may also be taxed in the Contracting State in which they arise (India), and according to the laws of that State, but if the beneficial owner of the royalties or fees for technical services is a resident of the other Contracting State(Cyprus), the tax so charged shall not exceed 10 percent of the gross amount of the royalties or fees for technical services.

Meaning-Tax may be charged in India but not exceeding the rate of 10%