

# CHAMBERS OF TAX CONSULTANTS

## Clause by Clause Analysis and Reporting Requirements in Tax Audit Report

*Presentation by*  
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**CLAUSE 30A – PARTICULARS REGARDING 'PRIMARY  
ADJUSTMENTS TO TRANSFER PRICE AS PER SEC. 92CE(1)**

## Clause 30A – PROVISIONS – 92CE(1)...

| Sub-section           | Particulars  | Provision   |
|-----------------------|--|---|
| (1)                   | Secondary adjustment to be made in case of specified primary adjustments | Primary adjustment to transfer price -<br>i. Suo moto adjustment in the return of income;<br>ii. Acceptance of adjustment made by AO<br>iii. Determination in an APA;<br>iv. Adoption of safe harbour rules<br>v. Resolution under MAP  |
| Proviso to S. 92CE(1) | S. 92CE not applicable   | <ul style="list-style-type: none"><li>Amount of primary adjustment made in any previous year does not exceed Rs. 1 crore</li></ul> <p style="text-align: center;"><b>AND</b></p> <ul style="list-style-type: none"><li>Primary adjustment is made in respect of an AY commencing on or before the 1<sup>st</sup> day of April, 2016</li></ul> |

# Clause 30A – INTERPRETATION ISSUES – S.92CE(1)...

## ❑ Proviso to S. 92CE(1):

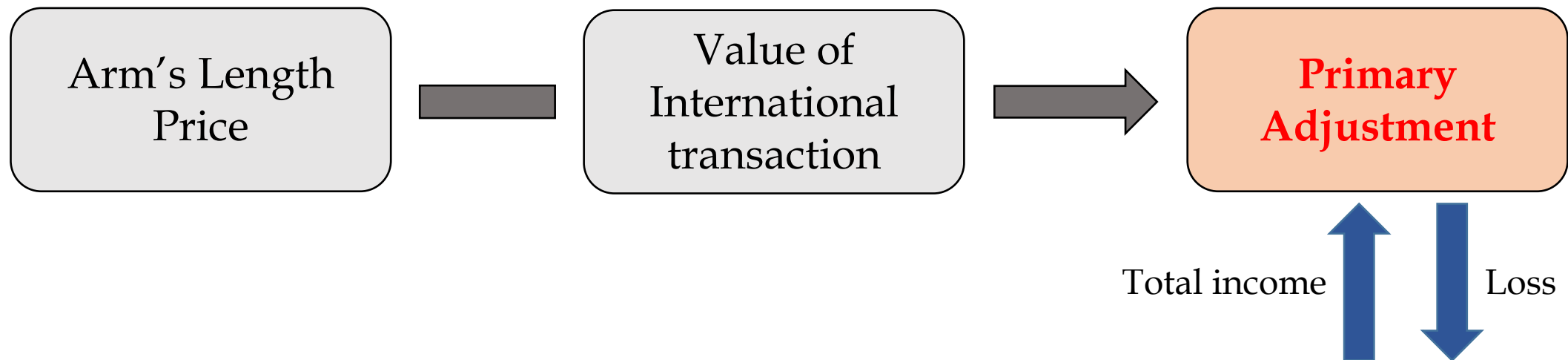
- ‘primary adjustment made in any previous year’ →
  - PY to which the adjustment relates; or
  - PY in which the event of adjustment takes place
- Threshold of Rs. 1 crore is *qua* each international transaction or aggregate of all international transactions
- ‘AND’ to be interpreted as ‘OR’

## Clause 30A – PROVISIONS– S.92CE(2)...

Where, → **as a result of primary adjustment** to the transfer price, → there is an increase in the total income or reduction in the loss, as the case may be, of the assessee, → **the excess money** which is available with its associated enterprise, → **if not repatriated to India** → within the time as may be prescribed, → **shall be deemed to be an advance** made by the assessee to such associated enterprise → and the **interest on such advance, shall be computed** in such manner as may be prescribed.

## Clause 30A – PROVISIONS– S.92CE(3)(iv)...

"**primary adjustment**" to a transfer price, means the determination of transfer price in accordance with the arm's length principle resulting in an increase in the total income or reduction in the loss, as the case may be, of the assessee;



## Clause 30A – PROVISIONS– S.92CE(3)(v)...

"secondary adjustment" means an adjustment

in the books of account of the assessee

and its associated enterprise

to reflect that the actual allocation of profits between the assessee and its associated enterprise are consistent with the transfer price determined as a result of primary adjustment,

thereby removing the imbalance between cash account and actual profit of the assessee.



## Clause 30A – EXCESS MONEY– S.92CE(3)(iii)...

"**excess money**" means the difference between the arm's length price determined in primary adjustment and the price at which the international transaction has actually been undertaken;



## Clause 30A – TIME FOR REPATRIATION...

As per Rules 10CB(1), due dates for various types of primary adjustments are as under:

| <b>Type of Primary Adjustment</b>    | <b>On or before 90 days from</b>           |
|--------------------------------------|--|
| Made Suo Moto                        | Due date of filing return u/s 139(1)       |
| Made by AO and accepted by $\bar{A}$ | Date of order of AO or appellate authority |
| Determined under APA                 | Due date of filing return u/s 139(1)       |
| Made as per Safe Harbour Rules       | Due date of filing return u/s 139(1)       |
| Made under MAP                       | Due date of filing return u/s 139(1)       |

## Clause 30A – INTEREST RATE...

- ❑ Rule 10CB(2) prescribes rate of interest to be levied on failure to repatriate excess money within the time limit prescribed in Rule 10CB(1)

| Transaction Currency | Interest Rate  |
|----------------------|--|
| Indian Currency      | One year marginal cost of fund lending rate (MCLR) of State Bank of India as on 1 <sup>st</sup> of April of the relevant previous year plus 325 basis points |
| Foreign Currency     | Six month London Interbank Offered Rate (LIBOR) as on 30 <sup>th</sup> September of the relevant previous year plus 300 basis points                         |

- ❑ Relevant previous year for the purpose of Rule 10CB(2) would be the year for which interest is to be computed.

## Clause 30A – ILLUSTRATION...

| Particulars   | Amount |
|---|--------|
| Sale consideration for international transaction with AE                        | 10000  |
| Arm's length consideration (i.e. ALP)   | 12000  |
| Primary adjustment (suo moto adjustment in return of income) made in FY 2017-18 | 2000   |

- A to make secondary adjustment of Rs. 2000 lakhs in books of account
  - AE A/c.....Dr. 2000
  - To Profit & Loss A/c (Income) 2000
- Rs. 2000 to be repatriated from AE within 90 days from due date of filing return u/s 139(1) (i.e. November 30, 2018)
- If repatriation not made within 90 days, Rs.2000 lakhs shall be deemed to be an 'advance' to the AE which would be liable to interest as per Rule 10CB

## Clause 30A – REPORTING...

30A. (a) Whether primary adjustment to transfer price, as referred to in sub-section 1) of section 92Ce, has been made during the previous year? (Yes/No)

(b) If yes, please furnish the following details:—

- (i) Under which clause of sub-section (1) of section 92CE primary adjustment is made?
- (ii) Amount (in Rs.) of primary adjustment:
- (iii) Whether the excess money available with the associated enterprise is required to be repatriated to India as per the provisions of sub-section (2) of section 92CE? (Yes/No)
- (iv) If yes, whether the excess money has been repatriated within the prescribed time (Yes/No)
- (v) If no, the amount (in Rs.) of imputed interest income on such excess money which has not been repatriated within the prescribed time:

## Clause 30A – REPORTING...

30A. (a) Whether **primary adjustment** to transfer price, as referred to in sub-section (1) of section 92Ce, has been **made during the previous year?** (Yes/No)

- PY in which event of adjustment takes place
- Adjustments for FY 2015-16 and preceding years not covered

(b) If yes, please furnish the following details:—

(i) Under which clause of sub-section (1) of section 92CE primary adjustment is made?

(ii) Amount (in Rs.) of primary adjustment:

Plausible view – report all primary adjustment irrespective of whether threshold of Rs. 1 crore *qua* each transaction exceeded or not

(iii) Whether the excess money available with the associated enterprise is **required to be repatriated** to India as per the provisions of sub-section (2) of section 92CE? (Yes/No)

(iv) If yes, whether the excess money has been repatriated within the prescribed time (Yes/No)

(v) If no, the amount (in Rs.) of imputed interest income on such excess money which has not been repatriated within the prescribed time:

# Clause 30A – REPORTING - ILLUSTRATION

## ILLUSTRATION

Assessment Year : 2020 – 21

Previous year: 2019 – 20

- In the previous year 2019-20
  - Assessee – files return for AY 2019-20
  - Might receive order for AY 2018-19
  - enter into APA w.e.f. AY 2017-18 or likeway

*Reporting under this clause (as per ILLUSTRATION):*

| <b>Particulars</b>                       | <b>Yes / No</b> | <b>Remarks</b>  |
|--|-----------------|---|
| Primary adjustment made in previous year | Yes             | Will include all adjustments (i.e. events happening in previous year) viz. suo-motu, AO's and APA |

*Reporting under this clause (For AY 2018-19)*

| <b>Particulars</b>                       | <b>Yes / No</b> | <b>Remarks</b>   |
|--|-----------------|--|
| Primary adjustment made in previous year | Yes             | Will be to the extent of primary adjustment made by AO for AY 2017-18 (if the order is received) |



## Clause 30A – REPORTING...

- ❑ Identification of primary adjustments
  - Form 3CEB & Study Report
  - Verify that Assessment order for AY 2017-18 has not been most passed (if yes, check whether appeal has been preferred against the said order) – Most likely order for AY 2017-18 would not have been passed
  
- ❑ Prepare data covering following details:
  - the transactions for which primary adjustment has been made
  - amount of primary adjustment
  - whether the transaction is excluded under proviso to S. 92CE (i.e. threshold)
  - due date for repatriation from AE
  - whether such excess income received from AE within permissible time limit
  - If not compute interest on excess income

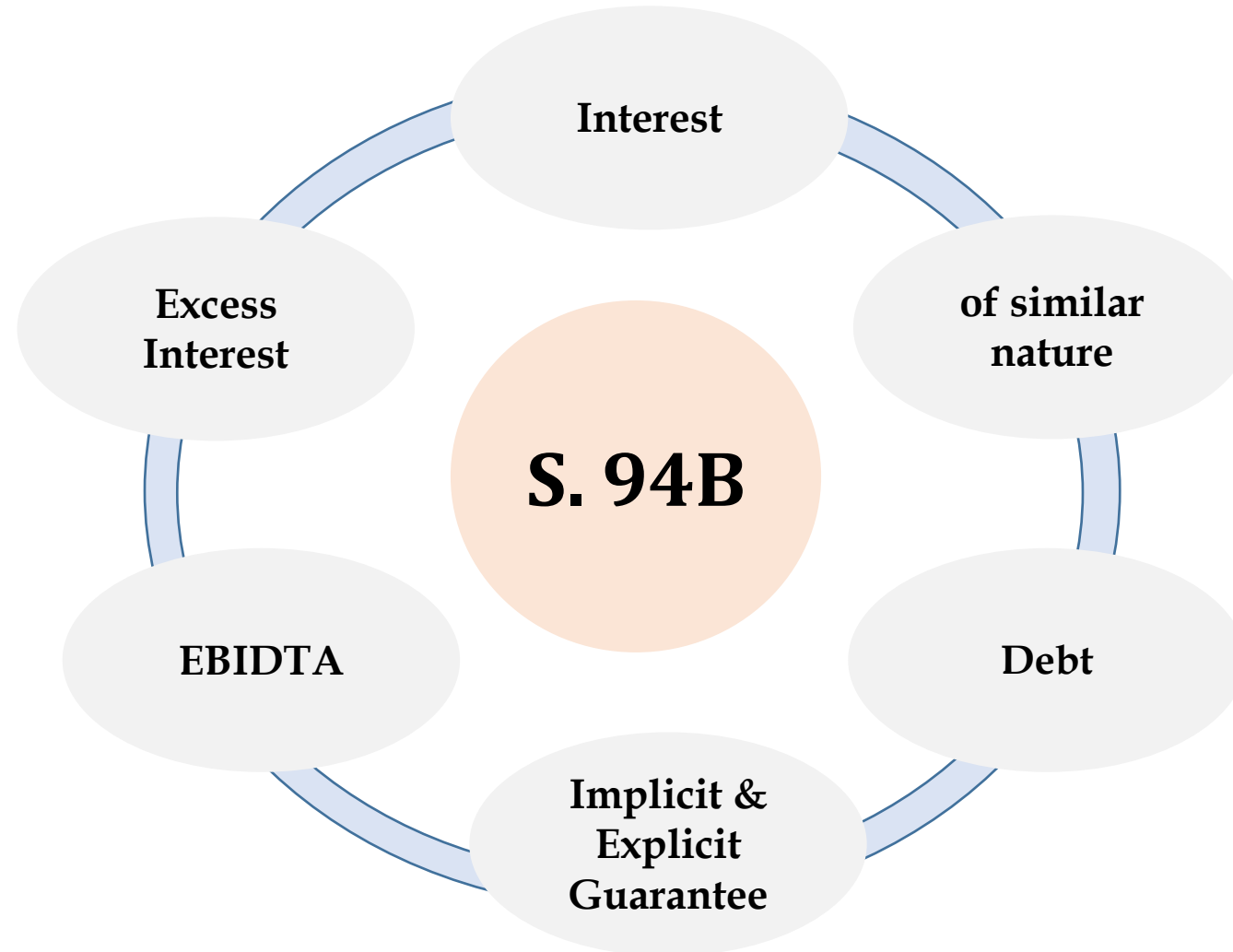


# CLAUSE 30B – THIN CAPITALIZATION

# SUB SEC. 1 & 3 of S. 94B – PROVISION



# KEY TERMS



# INTEREST

## ❑ Section 2(28A):

"interest" means → interest payable in any manner → in respect of any **moneys borrowed** → or **debt incurred** (including a deposit, claim or other similar right or obligation) → and includes any **service fee or other charge** → in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised.

## ❑ Action 4:

38. Throughout this report, references to **interest should also be taken to include amounts economically equivalent to interest**, unless the context clearly requires otherwise.

## OF SIMILAR NATURE – P. 36 Of ACTION PLAN-4

36. A best practice rule to address base erosion and profit shifting using interest expense should therefore apply to: (i) **interest on all forms of debt**; (ii) **payments economically equivalent to interest**; and (iii) **expenses incurred in connection with the raising of finance**.

These should include, but not be restricted to, the following:

- payments under profit participating loans
- **imputed interest** on instruments such as **convertible bonds and zero coupon bonds**
- amounts under alternative financing arrangements, such as Islamic finance
- the **finance cost element of finance lease** payments
- **capitalised interest** included in the balance sheet value of a **related asset, or the amortisation of capitalised interest**
- amounts measured by reference to a funding return under transfer pricing rules, where applicable
- **notional interest** amounts under **derivative instruments or hedging arrangements** related to an entity's borrowings
- certain foreign exchange gains and losses on borrowings and instruments connected with the raising of finance
- **guarantee fees** with respect to **financing arrangements**
- arrangement fees and similar costs related to the borrowing of funds.

## OF SIMILAR NATURE (Contd...)

Following are 'interest' u/s 2(28A) as per various tribunals & courts:

- ❑ **Commitment charges** are included in definition of section 2(28A)
- ❑ **Processing Fees**
  - *DCIT(TDS) v. Laqshya Media (P.) Ltd [(2016) 160 ITD 35 (Mumbai Tribunal)]*
- ❑ **Discount on Treasury bills**
  - *British Bank of Middle East v. CIT [(1998) 233 ITR 251 (Bombay HC)]*
- ❑ **Interest on loan borrowed from non-resident converted from bonds to equity**
  - *LMN India Ltd. In Re [(2008) 307 ITR 40 (AAR)]*
- ❑ **Interest on Income-tax Refund**
  - *Ansaldo Energia SPA v. DDIT(IT [(2016) 384 ITR 312 (Madras HC)] – in context of India-Italy Treaty*

## OF SIMILAR NATURE (Contd...)

Following are **not 'interest'** u/s 2(28A) as per various tribunals & courts:

**Corporate guarantee fee**

- *Johnson Matthey Public Ltd. vs. DCIT (88 taxmann.com 127)(Delhi Tribunal);*

**Upfront appraisal fee/front end fee**

- *DIT vs. Commonwealth Development (24 taxmann.com 154)(Bom)*

**Arrangers fee paid for availing loan**

- *Idea Cellular vs. ADIT (58 taxmann.com 101)(Mumbai Tribunal)]*

**Bill Discounting charges**

- *CIT vs. Cargill Global Trading Pvt. Ltd. 335 ITR 94 (Del); SLP dismissed in 21 taxmann.com 496 (SC)*

Will these expenses be covered within the scope of 'of similar nature'



## OF SIMILAR NATURE (Contd...)

- ❑ S. 94B is not the only provision disallowing interest income
  - SAARs – S. 14A, S. 36(1) (iii), S. 40(a)(i), Transfer Pricing provisions, etc.
  
- ❑ S. 94B covers only such ‘interest or similar charges’ which are deductible under the head PGBP
  - Interest or similar charges’ after considering the said disallowances/adjustments should be analysed for disallowance u/s 94B

| Particulars                                     | Amount     |
|---|------------|
| Interest expense                                | xxx        |
| Add: Disallowance u/s 14A, 36(1)(iii); 40(a)(i) | xxx        |
| Add: TP Adjustment                              | xxx        |
| <b>Net Interest to be considered for S. 94B</b> | <b>xxx</b> |

## Debt – S. 94B(5)(iii)

"debt" means any

- **loan,**
- **financial instrument,**
- **finance lease,**
- **financial derivative,**
- **or any arrangement that gives rise to interest, discounts or other finance charges**

that are deductible in the computation of income chargeable under the head "Profits and gains of business or profession";

## Debt – S. 94B(5)(iii)

- ❑ Terms 'Implicit'; 'Explicit' & 'Guarantee' not defined in the Act

### Guarantee - S. 126 of Indian Contract Act

"A 'contract of guarantee' is a contract to perform the promises, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the 'surety'. the person in respect of whose default the guarantee is given is called the 'principal debtor', and the person to whom the guarantee is given is called the 'creditor'. A guarantee may be either oral or written"

### Implicit

- capable of being recognized though unexpressed: implied – *Advance Law Lexicon* by P. Ramanatha Aiyar, 4th Edn
- Implied, rather than expressly stated; implicit agreement – *Random House Compact Unabridged Dictionary*, 2nd Edn.

### Explicit

- In a clear and detailed manner, leaving no room for confusion or doubt - <https://en.oxforddictionaries.com/definition/explicitly>
- in a clear and detailed manner, leaving no room for confusion or doubt.

Unless there is a 'guarantee', the question of it being implicit or explicit does not arise

# EBITDA

- ❑ No guidance provided in the Act;
- ❑ Therefore, EBITDA has to be considered in normal parlance which would be EBITDA as per the Books of Accounts;
- ❑ However, the Action Plan 4 of BEPS – suggest that it ought to be Tax EBITDA – there are complications/issues in relation to same.
- ❑ Issue may also arise in computation of EBITDA as per IndAS and Accounting Standard;
- ❑ For instance, under IndAS one has to account for effective interest and therefore, the EBITDA as per IndAS would be higher since it would have notional income (like notional interest on loan given to employee) whereas that would not be the case in person following accounting standard

# EXCESS INTEREST

Excess Interest = Total interest paid/payable to NR AE *minus* 30% of EBITDA  
OR  
Actual interest paid or payable to the NR AE,  
**whichever is LOWER**

The interest to the extent that it arises from excess interest would be disallowed u/s 94B.

## EXAMPLE

(Rs. In crores)

| Particulars                             | Amount |
|---|--------|
| EBITDA                                  | 100    |
| Interest expenditure on debt from NR AE | 40     |
| Other interest expenditure              | 10     |

# EXCESS INTEREST

| Views  | (a)                                    |               |   | (b)                      | Excess interest      |
|--|--|---------------|---|--------------------------|----------------------|
|  | Total interest exceeding 30% of EBITDA |               |   | Actual interest to NR AE | Lower of (a) and (b) |
|  | Total interest                         | 30% of EBITDA | Total interest in excess of 30% of EBITDA |                          |                      |
| View 1   | 50<br>(40 + 10)                        | 30            | 20  | 40                       | 20                   |
| View 2   | 40                                     | 30            | 10  | 40                       | 10                   |
| <i>In our opinion, View 2 is arguably the correct approach</i> |  |               |   |                          |                      |
| In case the EBITDA is negative                                 |  |               |   |                          |                      |
|  | 40                                     | - 30          | 70<br>[40 (-) (-30)]                      | 40                       | 40                   |

# REPORTING

30B (a) Whether the assessee has incurred expenditure during the previous year by way of interest or of similar nature exceeding one crore rupees as referred to in sub-section (1) of section 94B? (Yes/No.)

(b) If yes, please furnish the following details:—

- (i) Amount (in Rs.) of expenditure by way of interest or of similar nature incurred:
- (ii) Earnings before interest, tax, depreciation and amortization (EBITDA) during the previous year (in Rs.):
- (iii) Amount (in Rs.) of expenditure by way interest or of similar nature as per (i) above which exceeds 30% of EBITDA as per (ii) above :
- (iv) Details of interest expenditure brought forward as per sub-section (4) of section 94B:

---

A.Y.

Amount (in Rs.)

---

- (v) Details of interest expenditure carried forward as per sub-section (4) of section 94B:

---

A.Y.

Amount (in Rs.)

---

# REPORTING

30B (a) Whether the assessee has incurred expenditure during the previous year by way of interest or of similar nature exceeding one crore rupees as referred to in sub-section (1) of section 94B? (Yes/No.)

(b) If yes, please furnish the following details:—

Report only interest expense → not expense by way of similar nature (Refer S.94(2) Excess Interest defn)

(i) Amount (in Rs.) of expenditure by way of interest or of similar nature incurred:

(ii) Earnings before interest, tax, depreciation and amortization (EBITDA) during the previous year (in Rs.):

Book EBITDA

(iii) Amount (in Rs.) of expenditure by way interest or of similar nature as per (i) above which exceeds 30% of EBITDA as per (ii) above :

B/f interest expense will be NIL in AY 2018-19

(iv) Details of interest expenditure brought forward as per sub-section (4) of section 94B:

A.Y.

Amount (in Rs.)

C/f interest expense for AY 2018-19 = excess interest

(v) Details of interest expenditure carried forward as per sub-section (4) of section 94B:

A.Y.

Amount (in Rs.)



# GUIDANCE POINTS

- ❑ Peruse the Balance Sheet to verify whether the Company has debt funds;
- ❑ Identify non-resident AEs (if any) and transactions thereof;
- ❑ Check whether Non-resident AE has issued any debt resulting into expenditure by way of interest or similar nature;
  - Loan Agreement, finance lease agreement, etc.
- ❑ Check whether Non-resident AE has guaranteed debt issued by third party non-resident lender;
  - Loan Agreement, finance lease agreement, letter of comfort, etc.
- ❑ Arrive at the interest expense or equivalents thereof (i.e. similar nature) for the purpose of S. 94B
  - Collect data of disallowances of such expenses under other sections



# CLAUSE 43 – COUNTRY BY COUNTRY REPORTING

# BACKGROUND

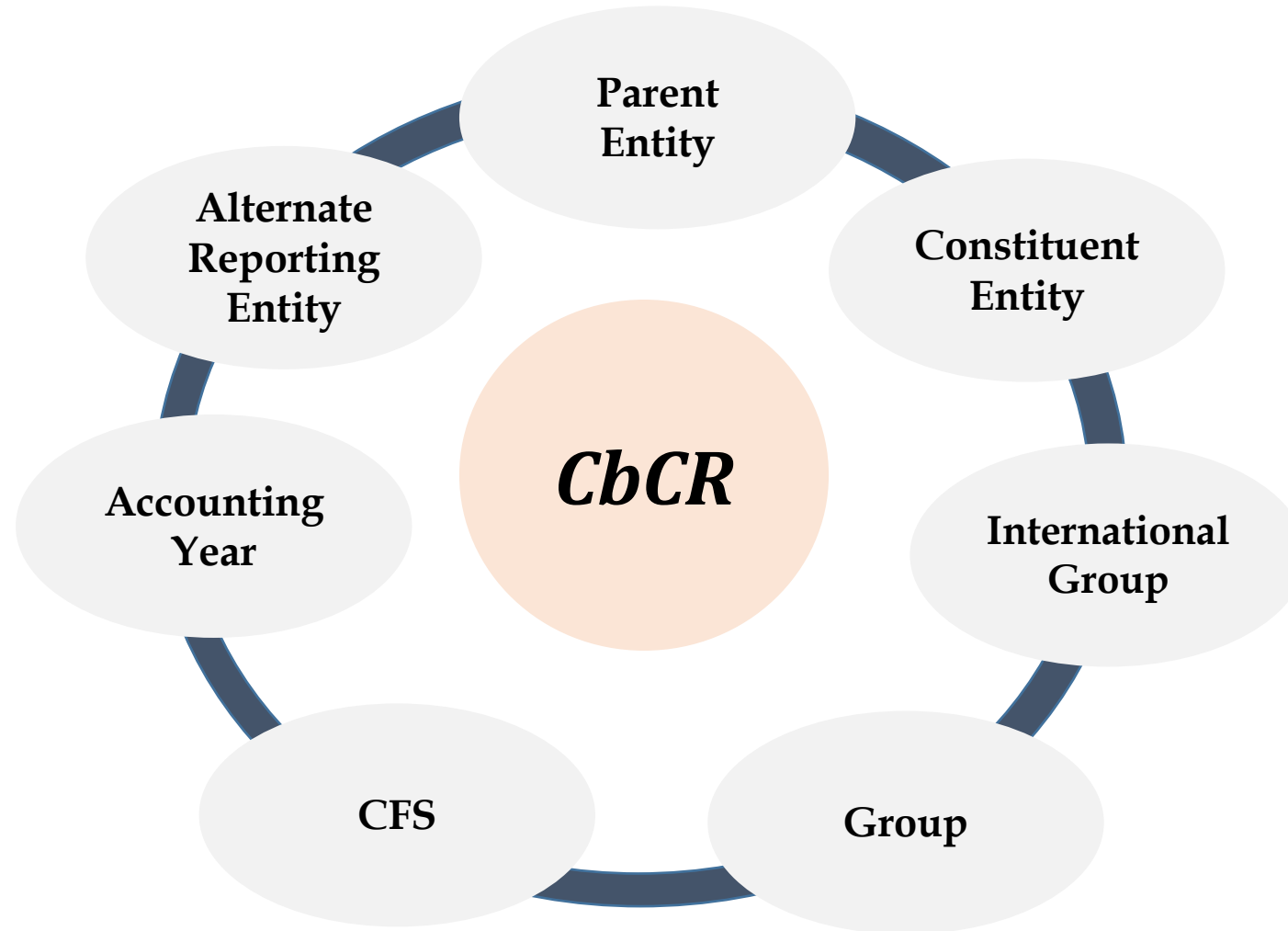
## What is CbCR?

High-level tax jurisdiction-wide information relating to the global allocation of the income, the taxes paid, number of employees, capital, and tangible assets

## Relevant Provisions

- **Sec. 286** – Furnishing of CbC Report
- **Rule 10DB** – Furnishing of Report in respect of an International Group
- **Form 3CEAC** – Intimation by CE providing details of Parent Entity/ ARE
- **Form 3CEAD** – CbC Report;
- **Form 3CEAE** – Intimation designating CE which would furnish the CbC Report

# IMPORTANT DEFINITIONS - SUB-SEC (9) to SEC 286

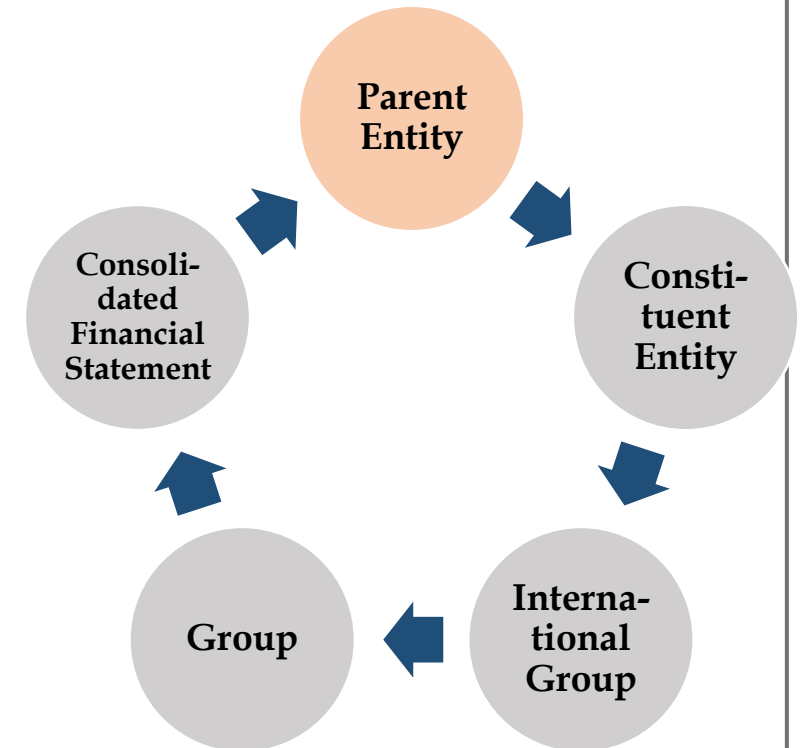


# PARENT ENTITY

- (h) "parent entity" means a **constituent entity**, of an **international group** holding, directly or indirectly, an **interest** in one or more of the other constituent entities of the international group, such that, —
- (i) it is required to prepare a CFS under any law for the time being in force or the accounting standards of the country or territory of which the entity is resident; or
  - (ii) it would have been required to prepare a CFS had the equity shares of any of the enterprises were **listed on a stock exchange**,

and, there is no other constituent entity of such group which, due to ownership of any interest, directly or indirectly, in the first mentioned constituent entity, is required to prepare a CFS, under the circumstances referred to in clause (i) or clause (ii), that includes the separate financial statement of the first mentioned constituent entity;

**ULTIMATE PARENT ENTITY**



# CONSTITUENT ENTITY

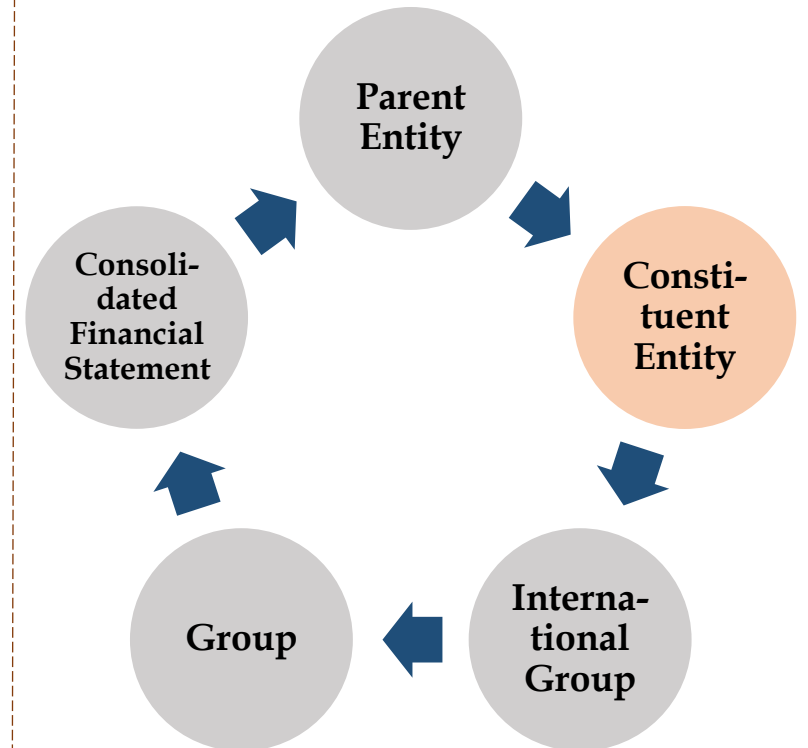
(d) "**constituent entity**" means, –

(i) any separate entity of an international group that is included in the CFS of the said group for financial reporting purposes, or

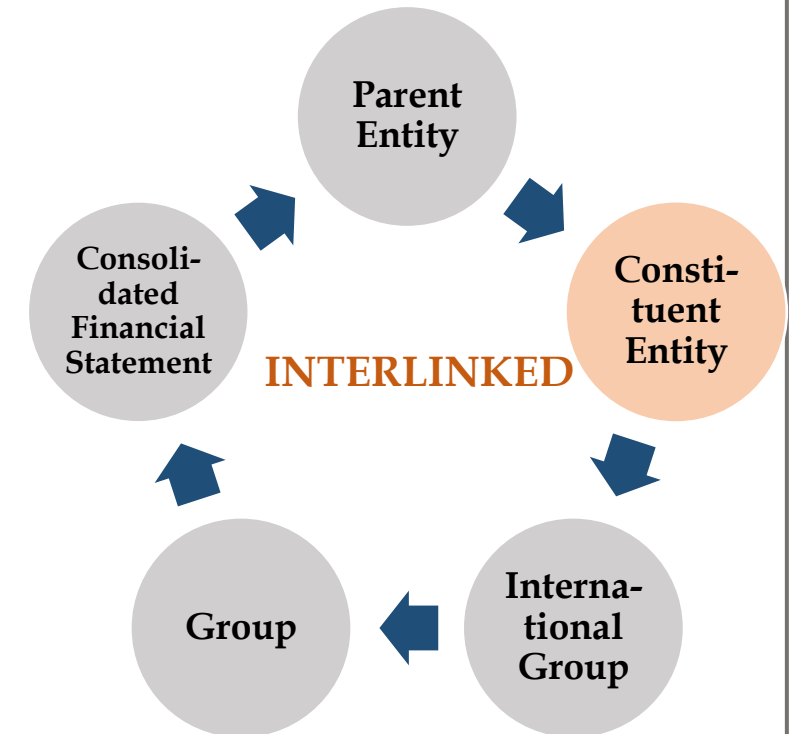
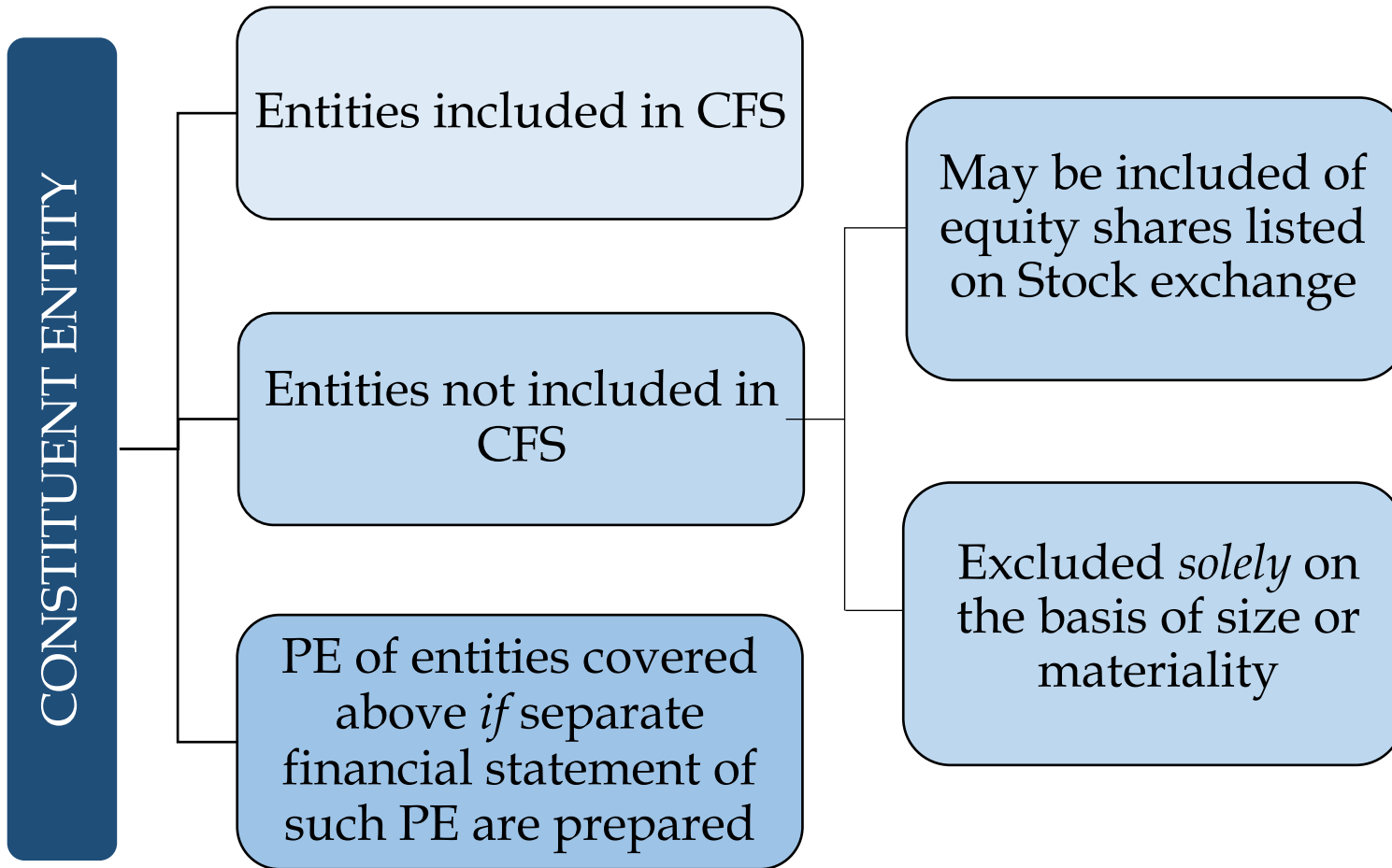
may be so included for the said purpose, if the equity share of any entity of the international group were to be listed on a stock exchange;

(ii) any such entity that is excluded from the CFS of the international group solely on the basis of size or materiality; or

(iii) any permanent establishment of any separate business entity of the international group included in clause (i) or clause (ii), if such business unit prepares a separate financial statement for such permanent establishment for financial reporting, regulatory, tax reporting or internal management control purposes;

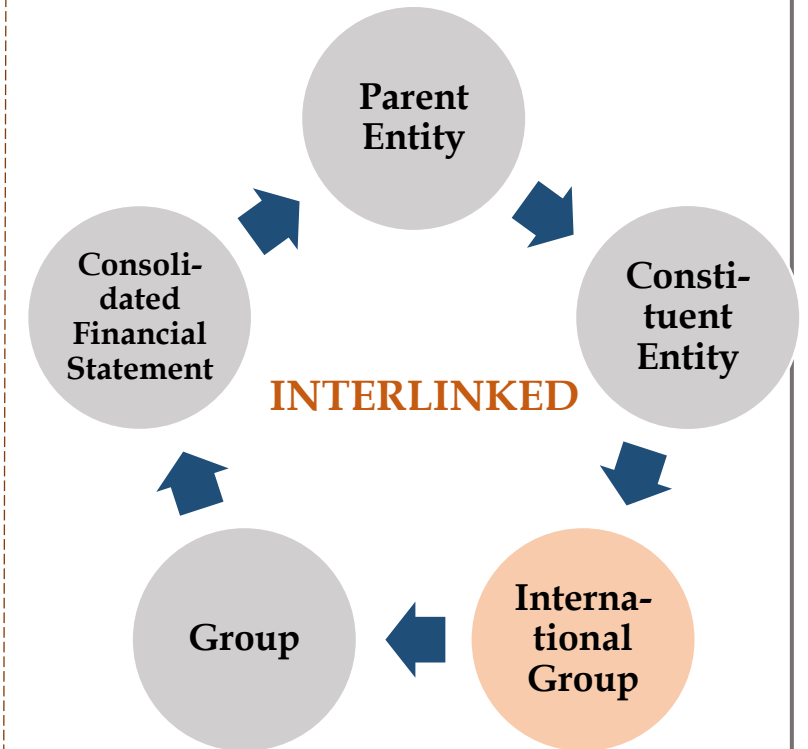


# CONSTITUENT ENTITY (contd...)



# INTERNATIONAL GROUP

- (g) "international group" means any **group** that includes, –
- (i) two or more enterprises which are resident of different countries or territories; or
  - (ii) an enterprise, being a resident of one country or territory, which carries on any business through a permanent establishment in other countries or territories;

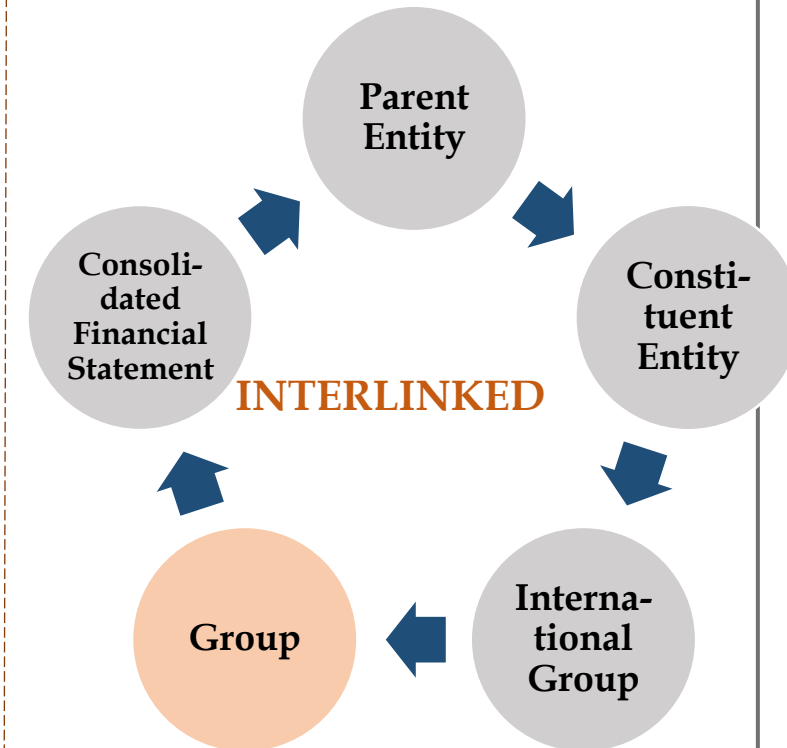




# GROUP

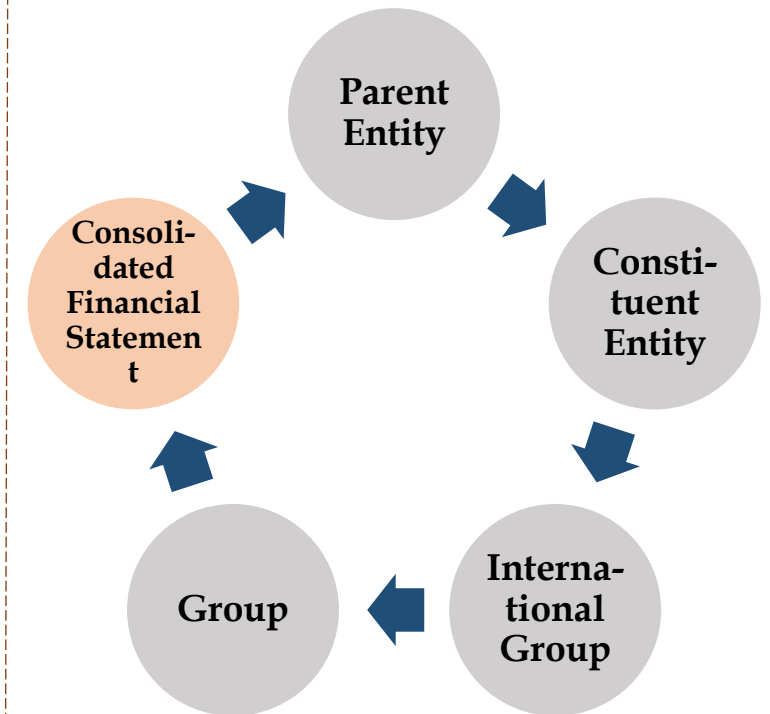
- (e) "group" includes a **parent entity** and all the entities in respect of which, for the reason of ownership or control, a CFS for financial reporting purposes, –
- (i) is required to be prepared under any law for the time being in force or the accounting standards of the country or territory of which the parent entity is resident; **or**
  - (ii) would have been required to be prepared had the equity shares of any of the enterprises were *listed on a stock exchange in the country or territory of which the parent entity is resident*;

Definitions of the terms 'constituent entity' and 'parent entity' merely state '*listed on a stock exchange*'



# CONSOLIDATED FINANCIAL STATEMENTS

(f) "consolidated financial statement" means the financial statement of an **international group** in which the assets, liabilities, income, expenses and cash flows of the **parent entity** and the **constituent entities** are presented as those of a single economic entity;



## CONSOLIDATED FINANCIAL STATEMENTS (Contd....)

- Applicability of Master File & CbCR to –
  - a) Individuals;
  - b) Persons other than Company and Individual (eg. LLP, Partnership firm)

- **FAQ on preparation of CFS - ICAI**

*“It is noted that relevant Indian Accounting Standard i.e., Ind AS 110, Consolidated Financial Statements provides that where an **entity has control** on one or more other entities, the controlling entity is required to consolidate all the controlled entities. Since, the word ‘**entity**’ includes a company as well as any other form of entity, therefore, LLPs and partnership firms are required to be consolidated. Similarly, under Accounting Standard (AS) 21, as per the definition of subsidiary, an enterprise controlled by the parent is required to be consolidated. The term ‘enterprise’ includes a company and any enterprise other than a company. Therefore, under AS also, LLPs and partnership firms are required to be consolidated.”*

## ALTERNATE REPORTING ENTITY

- (k) "**reporting entity**" means the constituent entity including the parent entity or the alternate reporting entity, that is required to furnish a report of the nature referred to in sub-section (2);
  
- (c) "**alternate reporting entity**" means any constituent entity of the international group that has been designated by such group, in the place of the parent entity, to furnish the report of the nature referred to in sub-section (2) in the country or territory in which the said constituent entity is resident on behalf of such group;

## ACCOUNTING YEAR

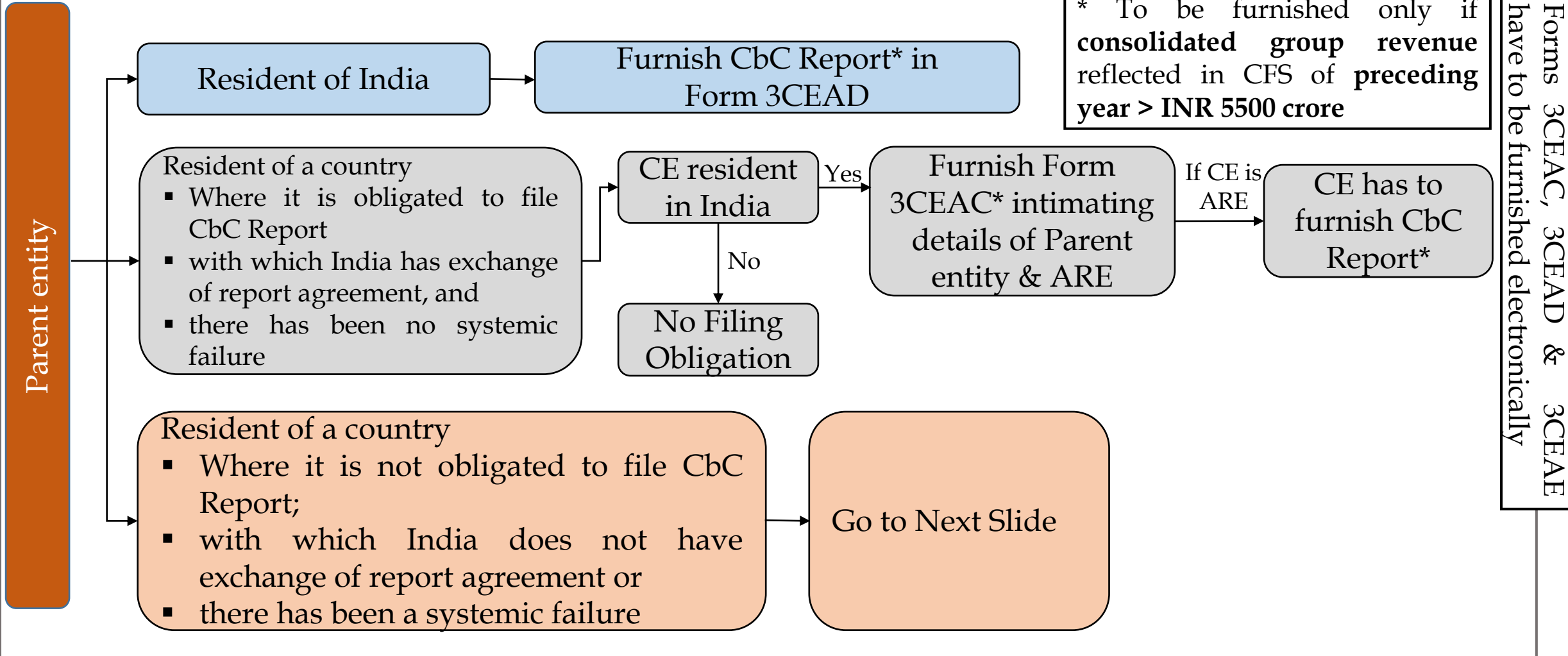
(a) "**accounting year**" means,—

(i) a previous year, in a case where the parent entity or alternate reporting entity is resident in India;

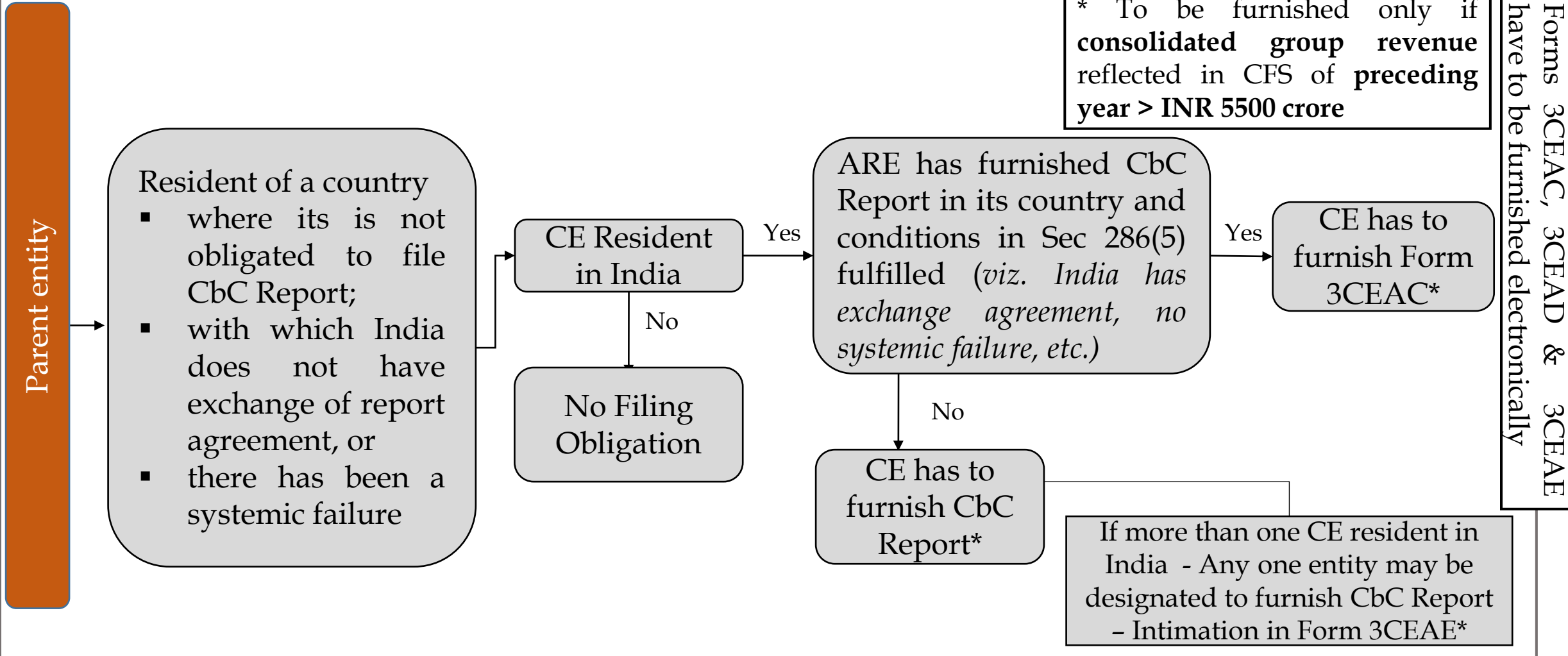
**or**

(i) an annual accounting period, with respect to which the parent entity of the international group prepares its financial statements under any law for the time being in force or the applicable accounting standards of the country or territory of which such entity is resident, in any other case;

# CbCR FLOWCHART



# CbCR FLOWCHART (Contd...)



# REPORTING

Refer sub-sections (4) & (5) of section 286

43. (a) Whether the assessee or its parent entity or alternate reporting entity is liable to furnish the report as referred to in sub-section (2) of section 286? (Yes/No)

(b) If yes, please furnish the following details :

(i) Whether report has been furnished by the assessee or its parent entity or an alternate reporting entity

(ii) Name of parent entity

(iii) Name of alternate reporting entity (if applicable)

(iv) Date of furnishing of report

Is most cases, CbC Report would not be filed before due date of TAR



## GUIDANCE POINTS

- ❑ Check whether following forms are furnished for last year i.e. AY 2017-18  
Form 3CEAC – Intimation by CE providing details of Parent Entity/ ARE)  
Form 3CEAD – CbC Report;
- ❑ Identify whether there is an international group
- ❑ Identify the UPE → if resident in India, it is liable to furnish CbC Report
- ❑ If UPE is not resident in India → Identify any ARE is designated by the group → If ARE resident in India, it is liable to furnish CbC Report
- ❑ If ARE is not resident in India → Identify whether Ā is liable to furnish CbC Report

## GUIDANCE POINTS (Contd...)

Parent Entity or ARE or Ā liable to furnish CbC Report *is resident in India*

No

Sub-clause (b) is not required to be filled

Yes

Sub-clause (b) has to be filled

Simply mention  
'NOT APPLICABLE'

### ISSUE:

#### **Date of furnishing report:**

Reporting accounting year for Parent Entity or ARE would be FY 2017-18

Due date for CbC Report → **March 31, 2019**

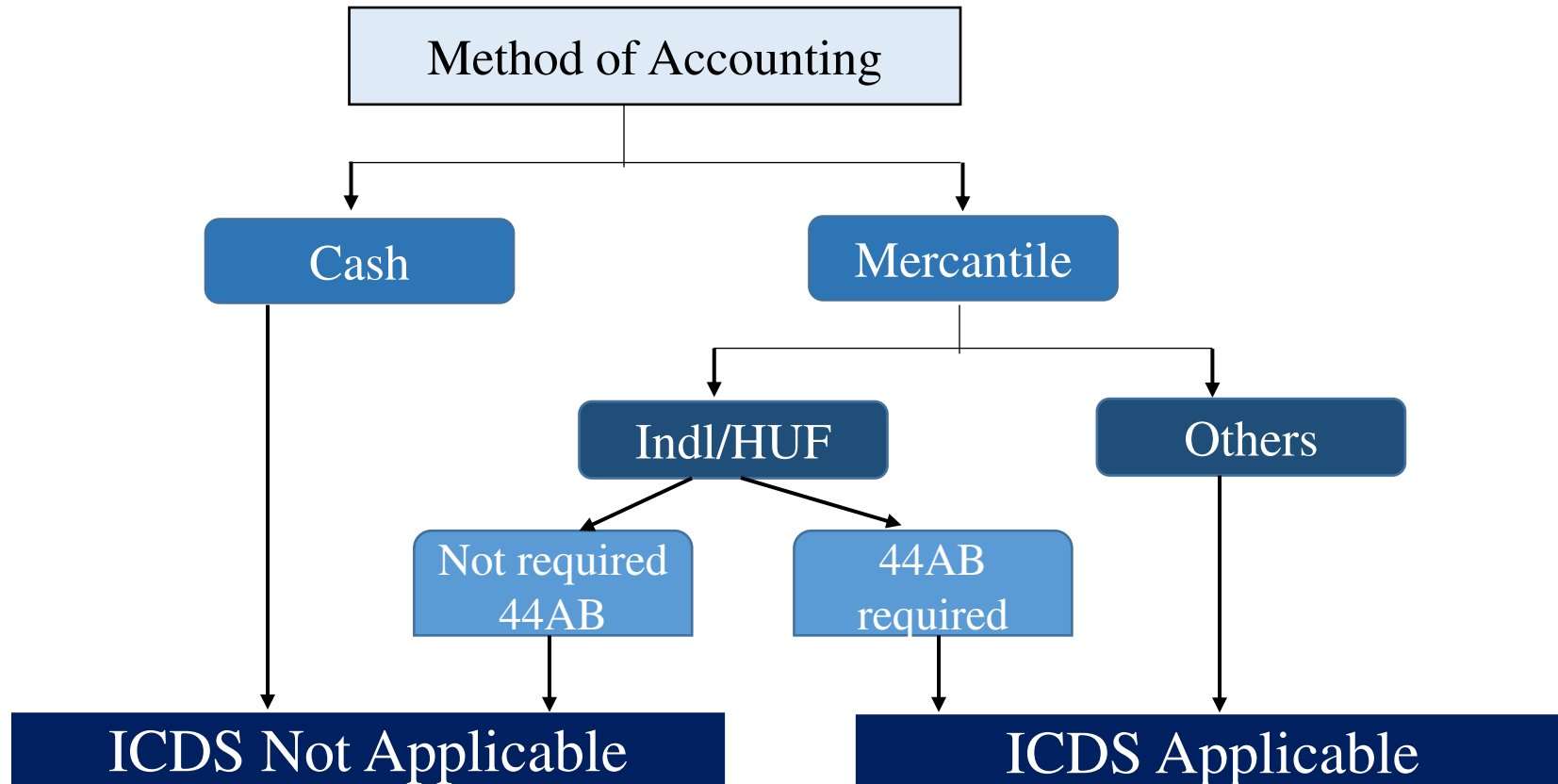
- Mostly, CbC Report would have not been filed before filing of TAR
- If CbC Report not filed, write a *Note*

# CLAUSE 13 - ICDS

## What is ICDS?

- ❑ Section 145(1) - Income chargeable under the heads “Profits and Gains from Business or Profession” or “Income from other Sources” - subject to 145(2) - as per method of accounting regularly followed
- ❑ Section 145(2) - the Central Government has power to notify “ICDS”
- ❑ CBDT vide notification dated March 31, 2015 introduced 10 ICDS to be effective from April 1, 2015 so as to apply for AY 2016-17 onwards
- ❑ However, the said notification was withdrawn by a press release and vide Notification No. S. O. 3079 (E) dated September 29, 2016, the new notification was introduced so as to apply w.e.f. AY 2017-18 and onwards

# APPLICABILITY OF ICDS?



Applies for PGBP and IFOS

## EFFECS OF ICDS?

- ❑ A. Profits as computed in accordance with GAAP xxx
- ❑ B. ADD/LESS: Adjustments as required under the IT Act/Rules xxx
- ❑ C. Total Income as computed prior to introduction of ICDS (A±B)
- ❑ D. ADD/LESS: Adjustments as per ICDS xxx
- ❑ E. Total Income to be computed after introduction of ICDS (A±B±D)



# CLAUSE 13 – REPORTING OF ICDS

## Form 3CD - Clause 13...

- ❑ **Clause 13(d)** – “ *Whether any adjustment is required to be made to the profits or loss for complying with the provisions of income computation and disclosure standards notified under section 145(2)*”
- ❑ **Clause 13(e)...** – “ *If answer to (d) above is in affirmative, give details of such adjustments:*

| Sr No. | ICDS                     | Increase in profit (Rs) | Decrease in profit (Rs) | Net Effect (Rs) |
|--------|--------------------------|-------------------------|-------------------------|-----------------|
| I      | Accounting Policies      |                         |                         |                 |
| II     | Valuation of Inventories |                         |                         |                 |
| III    | Construction Contracts   |                         |                         |                 |
| IV     | Revenue Recognition      |                         |                         |                 |
| V      | Tangible Fixed Assets    |                         |                         |                 |



## ...Form 3CD - Clause 13

- **...Clause 13(e)** – “ *If answer to (d) above is in affirmative, give details of such adjustments:*

| Sr No. | ICDS   | Increase in profit (Rs) | Decrease in profit (Rs) | Net Effect (Rs) |
|--------|--|-------------------------|-------------------------|-----------------|
| VI     | Changes in Foreign Exchange Rates                        |                         |                         |                 |
| VII    | Government Grants  |                         |                         |                 |
| VIII   | Securities   |                         |                         |                 |
| IX     | Borrowing Costs  |                         |                         |                 |
| X      | Provisions, Contingent Liabilities and Contingent Assets |                         |                         |                 |
| XI.    | <b>Total</b>   |                         |                         |                 |

- **Clause 13(f)** – “ *Disclosures as per ICDS*”

# Circular No. 10/2017 dated March 23, 2017

## ❑ FAQ 25

*”ICDS-I requires disclosure of significant accounting policies and other ICDS requires specific disclosures. Where is the taxpayer required to make such disclosures specified in ICDS?”*

## ❑ Answer

- Net effect on the income due to application of ICDS is to be disclosed in the Return of income;
- The disclosures under ICDS shall be made in the tax audit report in Form 3CD;
- There **shall not be** any separate disclosure requirements for persons who are not liable to tax audit

## CTC v. UOI [WP. (C) 5595/2017 (Del)]

- ❑ Writ petition was filed challenging the vires of ICDS before the Hon'ble Delhi High Court
- ❑ The Delhi HC passed the order dated November 8, 2017 wherein it held certain provisions of ICDS to be ultra vires and consequently, held portions of the Notifications 87 and 88 dated September 29, 2016 (ICDS Notifications) and part of Circular No. 10 of 2017 issued by the CBDT to be ultra vires and struck down and / or read down
- ❑ The Finance Act, 2018 has carried out certain retrospective amendments in the Act, whereby certain aspects of the Delhi HC decision have been nullified. The amendments are effective from AY 2017-18.



# RECENT AMENDMENTS IN THE ACT AND THEIR RELATED ISSUES

## Finance Act, 2018...

| ICDS     | Delhi HC decision   | Whether nullified by the FA 2018              |
|----------|---|---|
| -        | ICDS cannot override the provisions of the Act, the Rules and the judicial precedents.  | No  |
| ICDS I   | The concept of prudence (which was done way with in ICDS I) would continue to be applicable   | Yes – S. 36(1)(xviii) and s. 40A(13) inserted |
| ICDS II  | Held to be ultra vires and struck down  | Yes – 145A substituted                        |
| ICDS III | Retention money is not taxable in absence of right to receive and consequently, Para 10(a) of ICDS III which states that retention money has to be considered as contract revenue, to that extent, is struck down<br><br>Para 12 of ICDS III r.w. Para 5 of ICDS IX, dealing with Borrowing costs which makes it clear that no incidental income can be reduced from borrowing cost is contrary to the SC decision of Bokaro Steel Limited and those paras are thereby, struck down | Yes – S. 43CB inserted                        |

## ...Finance Act, 2018...

| ICDS      | Delhi HC decision   | Whether nullified by the FA 2018                           |
|-----------|---|--|
| ICDS IV   | Export incentives would be continued to be recognised as per the ratio laid down in Excel Industries irrespective of the ICDS requirement   | S. 145B(2) inserted  |
|           | ICDS permits recognition of revenue only as per POCM. This is held as contrary to case laws and hence ultra vires.  | Yes. Construction and Service contracts – S. 43CB inserted |
| ICDS VI   | ICDS VI states that MTM loss or gain in case of foreign currency derivatives are not to be allowed. Since this is contrary to the SC decision of Sutlej Cotton Mills, it is struck down | Yes – 43AA inserted  |
| ICDS VII  | ICDS provides that Government grants cannot be postponed beyond the date of its actual receipt. This is held as ultra vires the concept of accrual.                                     | ?? - S. 145B(3) inserted                                   |
| ICDS VIII | Part A of ICDS VIII on securities (for those entities not governed by RBI) is held to be ultra vires to the extent contrary to AS and is thereby, struck down                           | Yes. S. 145A is substituted.                               |

## ICDS – I - Section 40A(13) & Section 36(1)(xviii)

- ❑ Section 40A(13) :-

*“No deduction or allowance shall be allowed in respect of any marked to market loss or other expected loss, except as allowable under clause (xviii) of sub-section (1) of section 36.”*

- ❑ Section 36(1)(xviii) :-

*“(xviii) marked to market loss or other expected loss as computed in accordance with the income computation and disclosure standards notified under sub-section (2) of section 145.”*

- ❑ Applies to business income and Income from other Sources ( Section 58(2)) ;

- ❑ Whether applicable to cases to which ICDS do not apply?

# ICDS-I - Section 40A(13) & Section 36(1)(xviii)

Specifically allowable marked-to-market losses/expected losses

| ICDS                           | Description   |
|--------------------------------|---|
| II: Valuation of Inventories   | Para 3: Cost or NRV- whichever is lower   |
| III: Construction Contracts    | Losses only upto the stage of completion  |
| IV: Service Contracts          | Losses only upto the stage of completion  |
| VI: Forward Exchange Contracts | <ul style="list-style-type: none"><li>• Para 4(a) : Monetary Items</li><li>• Para 8 : Forward Exchange Contracts - Not for trading/speculation, Not for hedge of firm commitment/highly probable forecast transaction</li></ul> |
|                                |   |



## Section 40A(13) & Section 36(1)(xviii)

- ❑ Examples of marked-to-market losses/expected losses not allowable
  - Expected losses in construction contracts/ service contracts ;
  - Non-monetary items in foreign currency- Allowable only on settlement [Subject to section 43A/Rule 115A];
  - Forward Exchange Contracts for trading and speculation ;
  - Forward Exchange Contracts for hedging the risk of firm commitment or highly forecast transactions;
  - Interest rate Swap transactions ;
  - Currency Swap transactions

## ...Finance Act, 2018 – ICDS I...

### ❑ Issues:

- Whether marked-to-market gain will be taxable?
  - Generally - **NO** - In absence of accrual;
  - Monetary items - **taxable** under ICDS - VI;
  
- Whether mark to market loss on interest rate swaps recognized in earlier year needs to be reversed in AY 2016-17?
  - Transitional Provision of ICDS - I states as under:  
*“All contract or transaction existing on the 1st day of April, 2016 or entered into on or after the 1st day of April, 2016 shall be dealt with in accordance with the provisions of this standard after taking into account the income, expense or loss, if any, recognised in respect of the said contract or transaction for the previous year ending on or before the 31st March, 2016.”*

## ...Finance Act, 2018 – ICDS II / VIII...

- ❑ ICDS- VIII- Securities held as S-I-T to be valued at cost or NRV- whichever is lower- To determine category-wise. ( For other than Banks) ;
- ❑ Held - Contrary to Accounting Standards ;
- ❑ Pre-amended 145A- non-obstante clause;
- ❑ Delhi HC- Held ICDS ultra vires ;
- ❑ Section 145A substituted by FA 2018.

## Section 145A

- ❑ Amendment to section 145A
  - Non-obstante clause removed ;
  - Section itself provides for valuing inventory of securities category-wise
  - Unlisted/thinly traded securities to be valued only at actual cost (lower NRV not permitted)
  - Banks to value inventory of securities as per RBI guidelines
  
- ❑ **Affected entities**
  - NBFCs ;
  - Other traders in shares and securities ;
  - All holdings of unlisted/thinly traded shares/securities

## Section 145A

- ❑ Units of mutual funds held as S-I-T
  - Securities “not listed on BSE” ;
  - Hence covered under the mischief of this amendment ;
  
- ❑ Inventory valuation on dissolution of firm :-
  - ICDS- II- para 24 ;
  - Held by Delhi HC as contrary to Sakthi Trading (250 ITR 871) (SC) ;
  - No amendment in the Act;
  - Para 24- still ineffective;

## Section 145A...

- ❑ Illustration of impact: NRV has to be done category wise not individual asset wise.

| Individual Security    | Cost       | NRV        | Lower      |
|------------------------|------------|------------|------------|
| Company P              | 150        | 20         | 20         |
| Company Q              | 150        | 45         | 45         |
| Company R              | 150        | 15         | 15         |
| Company S              | 150        | 300        | 150        |
|                        | <b>600</b> | <b>380</b> | <b>230</b> |
|                        |            |            |            |
| Valuation (A.S.)       |            |            | 230        |
| Valuation (under 145A) |            |            | 380        |

## ...Finance Act, 2018 – ICDS III AND ICDS IV...

### ❑ Delhi HC decision –

- Para 10(a) of ICDS III w.r.t. including retention money as income on receipt basis is against the settled position in law - Therefore, ultra vires
- Para 12 of ICDS III r.w. Para 5 of ICDS IX stating that no incidental income can be reduced from borrowing cost, is contrary to the decision of Bokaro Steel Limited - Therefore, struck down
- Para 6 of ICDS IV permits only one of the methods (proportionate completion method) is contrary to the decisions - Therefore, ultra vires and struck down

## Section 43CB

- ❑ Applies to Profits and Gains arising from :-
  - a construction contract ;
  - a contract for providing services ;
- ❑ Profits and Gains to be determined on percentage of completion method in accordance with ICDS ;
  - ❑ Exceptions:
    - Service Contracts
      - Duration  $\leq$  90 days- Project Completion Method ;
      - Specified Time Limit- but indeterminable number of acts involved then Straight Line Basis
- ❑ Retention money to be included in Contract Revenues (for all 3 methods)
- ❑ Contract costs- Not to be reduced by
  - Interest
  - Dividend
  - Capital Gains



# Issues

- ❑ It applies to construction contracts, not to builders ;
- ❑ Applies also to contracts for rendering services directly related to construction of assets;
- ❑ Applies also to contracts for destruction or restoration of assets ;
- ❑ Whether applicable to service providers following cash method of accounting ?
- ❑ Major points of distinction compared to AS/Ind AS :
  - Retention Money
  - Expected losses
  - Incidental Income

## ...Finance Act, 2018 – ICDS VI...

- ❑ Delhi HC decision - ICDS VI which states that marked to market loss / gain in case of foreign currency derivatives held for trading or speculation purposes are not allowable, is contrary to the SC decision in Sulej Cotton Mills Ltd - Therefore, ultra vires and struck down
  
- ❑ S. 43AA introduced by FA 2018 to nullify HC decision
  - Any gain / loss arising on account of any change in foreign exchange rates to be treated as income or loss and to be computed in accordance with ICDS
  - Gain / loss on account of effects of changes in foreign exchange rates is in respect of “all foreign currency transactions” including some specified transactions. Transactions specifically included are:
    - Monetary and non-monetary items;
    - Translations of financial statements of foreign operations
    - Forward exchange contracts
    - Foreign currency translation reserve

# Section 43AA

## ❑ Issues:

- S. 43AA now provides for taxing / allowing gains / losses that are capital in nature – Contrary to the decision of Sulej Cotton Mills (116 ITR 1)
- However, definition of income in s. 2(24) is not amended to include such capital receipts to tax
- S. 43AA cannot override s. 4 and 5 which deal with the scope of income and accrual of income
- What is not income cannot be taxed – S. 43AA vulnerable to challenge
- Q. 16 of FAQ - What is the taxability of opening balance as on 1<sup>st</sup> day of April 2016 of Foreign Currency Translation Reserve (FCTR) relating to non-integral foreign operation, if any, recognised as per Accounting Standards (AS) 11?
  - *FCTR balance as on 1 April 2016 pertaining to exchange differences on monetary items for non-integral operations, shall be recognised in the previous year relevant for assessment year 2017-18 to the extent not recognised in the income computation in the past.*

# Section 145B

- ❑ S. 145B inserted
  - Overrides section 145
  - Interest received on any compensation or on enhanced compensation to be deemed to be income of the previous year in which it is received
  - Any escalation of price in a contract or export incentives to be deemed to be income of the previous year in which reasonable certainty of realisation is achieved
  - Subsidy / Govt. grant which is treated as income u/s. 2(24)(xviii) to be chargeable to tax in the year in which it is received, if not already charged to tax in an earlier year

# Consequences of Retrospective Amendments

- ❑ Amendment is with retrospective effect from AY 2017-18
- ❑ Amendment could not have been foreseen when ROI was filed- no need to revise ROI- **National Agricultural Co-op v JCIT ( 4 SOT 862) (Delhi)**;
- ❑ There can be no penalty (as long as the interpretation taken while filing ROI was in line with Delhi HC decision (Refer CIT v Mentha & Allied Products (304 ITR 214)) (All))
- ❑ Interest levy could be waived- based on Notification F.No. 400/234/95-IT(B) dated 23rd May 1996
  - See Emami Ltd v CIT (200 taxmann 326)( Calcutta HC)
  - CIT v. JSW Energy Ltd. (379 ITR 36) (Bombay HC) – rendered in context of s. 115JB
  - CIT v. Glenmark Pharmaceuticals Ltd. (398 ITR 439) (Bombay HC)
  - West Coast Paper Mills v ACIT (52 taxmann.com 268) (Mum ITAT)



# CLAUSE 14 – METHOD OF VALUATION OF CLOSING STOCK

# Disclosure

- a) Method of valuation of closing stock employed in the previous year
- b) Details of deviation, if any, from the method of valuation prescribed under Section 145A, and the effect thereof on the profit or loss, please furnish details-

| Serial number | Particulars | Increase in profit<br>(₹) | Decrease in profit<br>(₹) |
|---------------|-------------|---------------------------|---------------------------|
|               |             |                           |                           |

No **change** under this Clause in new Form 3CD applicable w.e.f. August 20, 2018

# Audit Procedures...

- ❑ To state the method of valuation adopted for closing stock
  - “Inventory” is defined in ICDS – Para 2(1)(a) of ICDS II
    - Held for sale in ordinary course of business
    - In the process of production for such sale
    - In the form of materials for supplies to be consumed in the production process or in the rendering of services
      - All inventories – Raw Materials, Packing Materials, Work-in-progress, Finished Goods, Stores and Spares
- ❑ Review the accounting policy adopted for valuation of closing stock as given in notes to financial statements
  - If it is verified at the time of Statutory Audit, review those working papers are appropriately filed and its cross referencing in Tax Audit File
  - Else, review, the workings from the assessee and take on file



## ...Audit Procedures...

- ❑ For 2017-18, review be in two parts
  - Pre-Goods and Service Tax (“GST”) (that is, upto June 30, 2017) - excise duty and VAT were in force and hence, purchases, sales and also the closing inventory containing items purchased during that period shall be adjusted to include Excise duty and VAT paid or incurred
  - Post-GST (From July 1, 2017) - Purchases, sales and closing inventory containing items purchased during that period to be adjusted to include GST paid or incurred
  
- ❑ Value of opening inventory to be adjusted for Excise duty and VAT

## ...Audit Procedures

- ❑ Verify the workings provided by the assessee for provision of Excise duty, VAT and GST on closing stock
- ❑ Check the relevant ledgers accounts and returns for verifying the amounts of Excise duty, VAT and GST paid or incurred and credits of the same taken under the respective law, if any

## Issues...

- ❑ Whether to account for stocks, where an assessee is following cash system of accounting?
  - The assessee should account for closing stock even if the assessee follows cash system of accounting
  - Tax Auditor to state the method of valuation adopted for closing stock

## ...Issues...

- ❑ If the assessee is not complying with the provisions of Section 145A in the books of account and the same is reported in TAR, can the AO reject the books on the ground that the books are not properly maintained?
  - Statutory adjustments under Section 145A are out of book adjustment
  - Adjustments made to determine the total income of the assessee for purpose of the Act
  - AO cannot reject the books of account because of out of books adjustments are not complied with

## ...Issues

- ❑ Valuation of securities held as stock-in-trade at lower of cost or NRV – could have an impact if NRV is lower than cost – whether to be reported under Clause 13 or 14?
  - As per AS 13, valuation prescribed for current investments is applicable to valuation of securities held as stock-in-trade
  - Hence, in accounts, inventory being securities are valued at cost or market value, whichever is lower
  - Assuming market value (as per accounts) being same as NRV (as per ICDS VIII) and if such value is lower than cost, then the securities are valued at NRV
  - Hence, there is no impact of ICDS. Also, there is no deviation from method of valuation prescribed u/s. 145A



# CLAUSE 29 – REPORTING U/s. 56(2)(viib)

## Form 3CD - Clause 29...

- ...Clause 29** – *“Whether during the previous year the assessee received any consideration for issue of shares which exceeds the fair market value of the shares as referred to in section 56(2)(viib), if yes, please furnish the details of the same.”*

### **ANALYSIS:**

- Applicable to closely-held companies issuing shares more than fair market value;
- Subsidiary of widely held company or listed company will not be covered by this provisions;
- Fair market value of shares will be value of shares as per Rule 11UA – DCF, asset based value or book value;
- Fair market value of the shares shall be as per report of the valuer (merchant banker or chartered accountant);
- The provisions would apply to preference shares;
- Provisions of section would not be applicable to Non-residents;
- Provisions will not be applicable to share application money;
- It will trigger when the consideration is received;

## Form 3CD - Clause 29...

Documents to be vouched or verified:

- Peruse the Equity capital account and share premium account and notes to account;
- Verify return of allotment and resolutions;
- Peruse the valuation report;

### **ISSUES:**

- Whether the provisions of section would be applicable to convertible debentures or bonds or preference shares;





# CLAUSE 21(h) – REPORTING FOR SECTION 14A

## Form 3CD - Clause 21(h)...

- ❑ **Clause 21** – *“Please furnish the details of amounts debited to profit and loss account, being in nature of capital, personal, advertisement expenditure etc.:*

*(h) amount of deduction inadmissible in terms of section 14A in respect of the expenditure incurred in relation to income which does not form part of total income.”*

### ANALYSIS:

- ❑ The provisions of this section will be applicable when the assessee has earned exempt income;
- ❑ Has the assessee obtained separate study report quantifying the amount of disallowance?
- ❑ If not, is Rule 8D followed? Check Rule 8D calculations;
- ❑ While computing disallowance exclude Growth funds,
- ❑ For 14A purpose also exclude foreign investments;
- ❑ In case of non-corporate assesses if dividend exceeds Rs. 10 lakhs, then arguably section is not applicable;



CLAUSE 21(i) – Disallowance in view of  
proviso to section 36(1)(iii)

## Form 3CD - Clause 21(i)...

### Legal Provisions

- ❑ Section 36(1)(iii) provides that interest on borrowed capital would be deductible only if :
  - a) The assessee has borrowed money.
  - b) It is used for the purpose of business and profession.
  - c) Interest is paid/ payable on such money
  
- ❑ The proviso to the above section requires that interest paid on the capital borrowed for acquisition of asset for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use shall not be allowed as a deduction.

## Form 3CD - Clause 21(i)...


| Clause | Disclosure  | Remarks  |
|--------|---|--|
| 21(i)  | Amount inadmissible under proviso to Section 36(1)(iii) | <ul style="list-style-type: none"><li>▪ In past, inadmissible amount was computed by applying the principles of AS 16</li><li>▪ After removal of the expression “for extension of existing .....”, from the proviso, the scope of disallowance has widened</li><li>▪ AS 16 uses the term “qualifying asset” but 36(1)(iii) refers to capital borrowed for acquisition of an asset. Hence, latter is stringent</li><li>▪ Check loan document or term sheet to determine whether the loan taken is for the purpose of business</li><li>▪ In case of specific borrowings, interest is covered by the proviso. In case of general borrowings , give adequate disclosure if MRL is given by the client that no borrowed funds were used for acquiring any asset</li></ul> |

## Form 3CD - Clause 21(i)...

| Clause | Disclosure  | Remarks  |
|--------|---|--|
| 21(i)  | Amount inadmissible under proviso to Section 36(1)(iii) | <ul style="list-style-type: none"><li>▪ Check MoA &amp; AoA to verify whether loan taken is in line with the object clause of the business</li><li>▪ Verify when the asset was actually put to use .Eg Check transfer from CWIP to Capital Asset Schedule, Review installation / Asset Valuer's Certificate etc.</li></ul> |

### ISSUES:

- Whether the proviso to section 36(1)(iii) will apply to stock-in-trade?



# CLAUSE 32(b) – CHANGE IN SHAREHOLDING – SECTION 79

## Clause 32(b) :Impact of Section 79 on Losses

| Section | Applicability of section to types of Co.'s in which public are not substantially interested     | Conditions when business loss can be allowed to be c/f and set off   |
|---------|---|--|
| 79(a)   | Co.'s other than those referred to u/s 80-IAC   | If on the last day of the PY in which the change in shareholding took place & on the last day of the PY in which loss was incurred , the shares of the company carrying not less than 51% of the voting power were beneficially held by the same person  |
| 79(b)   | Eligible start-up referred to u/s 80-IAC<br>(Amendment vide Finance Act, 2017 w.e.f 01.04.2018) | Business loss would not lapse even if there is dilution of more than 51% in the shareholding of the company by way of new issue of shares to other new investors<br><br>Such loss has been incurred during the period of 7 years beginning form the year in which the Company was incorporated |



## Clause 32(b) :Impact of Section 79 on Losses

- Provision shall **not apply** if change in voting power is on account of :
  - Death** of shareholder
  - Transfer of shares by way of **gift** to any relative of shareholder making such gift
  - Change in shareholding pursuant to resolution plan under **IBC**
  - Change in shareholding of Indian Co. which is subsidiary of Foreign Co. as a result of **amalgamation / demerger** of Foreign Co .51% of shareholders of Old Co remain shareholders of New Co.

| Clause | Disclosure Required   | Remarks  |
|--------|---|--|
| 32(b)  | Whether a change in shareholding of the company has taken place in the previous year due to which the losses incurred prior to the previous year cannot be allowed to be carried forward in terms of section 79 | <ul style="list-style-type: none"><li>Auditor to fill in the response as under:<ol style="list-style-type: none"><li>Yes: If change in shareholding results in losses not being allowed to be c/f</li><li>No:If change in shareholding does not violate condition specified u/s 79 and losses are allowed to be c/f</li><li>NA:If there is no change in shareholding</li></ol></li></ul> |

## Clause 32(b) :Impact of Section 79 on Losses

### Analysis:

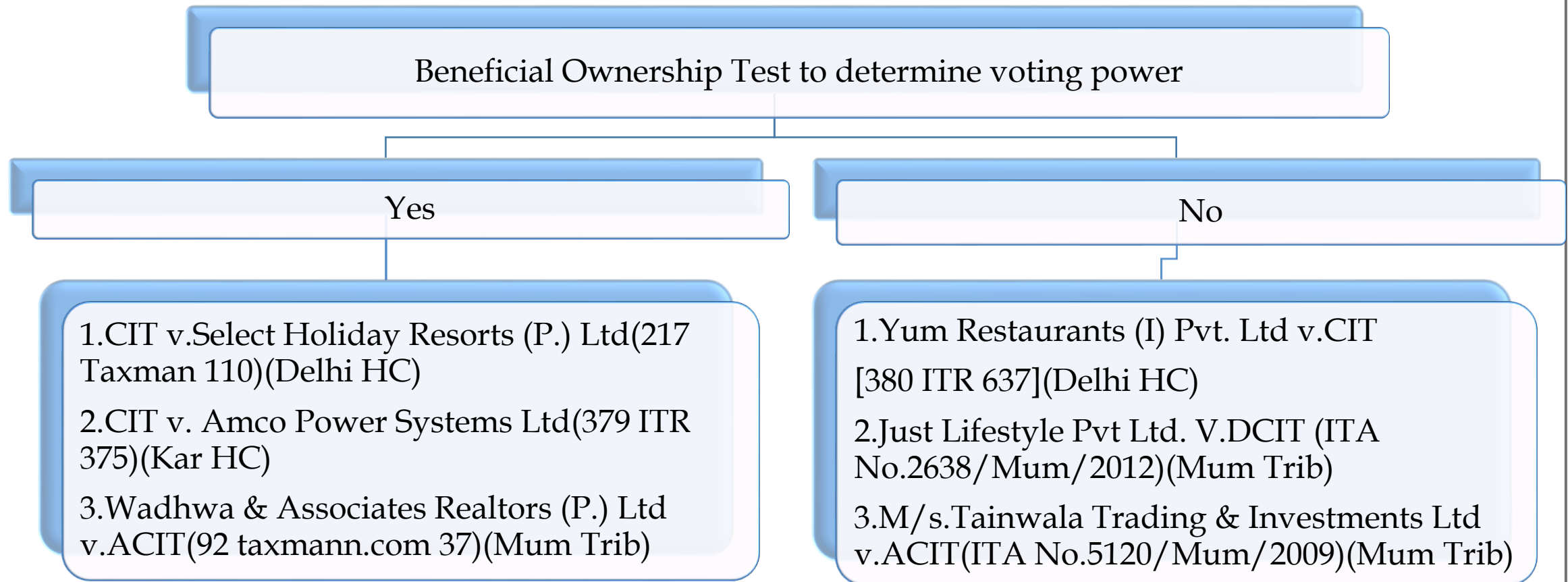
The Tax Auditor has to enquire with the management and review the statutory records of the entity to ascertain whether there is a change in the shareholding of the Co. and report accordingly

- Comparison of shareholding to be done with reference to last day of the current PY .and last day of every PY in which loss is incurred
  
- Records to be examined for change in shareholding:
  - 1) Disclosure in FS with respect to business reorganization
  - 2) Disclosure in FS with respect to Change in Equity and details of shareholding more than 5%
  - 3) ROC filing
  - 4) Register of Members
  
- Relevant Judgements**

## Clause 32(b) :Impact of Section 79 on Losses

| Judgement  | Summary   |
|--|---|
| CIT v. Select Holiday Resorts (P.) Ltd(217 Taxman 110)(Delhi HC)             | Since the shareholders of the parent company had always beneficially held the shares of the taxpayer, a reverse merger of the holding company into the taxpayer does not result in any prohibition on the carry forward and setting off of loss against the future profits of the amalgamated company   |
| CIT v. Amco Power Systems Ltd (379 ITR 375)(Karnataka HC)                    | The language employed under Section 79(a) states that 51% of the voting power should be beneficially owned by the same person (before and after change in shareholding), and that the section does not require that 51% of shares should be held by the same person. A transfer of shares of the loss-making company by the shareholder-company to its subsidiary is not hit by Section 79 of the Act.  |
| Yum Restaurants (I) Pvt. Ltd v. CIT [380 ITR 637](Delhi HC)                  | Transfer of shares of an Indian company by a holding company (i.e. Yum Asia) to another holding company (i.e. Yum Singapore) results in change of 'beneficial ownership' of shares and results in disallowance of brought forward losses even though the ultimate beneficial owner remains the same (i.e. Yum USA). A company is a separate legal entity, the parent company and its shareholders should be viewed as distinct and separate persons |
| Wadhwa & Associates Realtors (P.) Ltd v.ACIT(92 taxmann.com 37)(Mumbai Trib) | Relies on Vegetable Products (88 ITR 192)(SC) to follow the decision rendered in Amco Power Systems & Sterling Holiday Resorts instead of Yum Restaurants   |

# Clause 32(b) :Impact of Section 79 on Losses



## Clause 32(b) :Impact of Section 79 on Losses

### ISSUES:

- ❑ Whether provisions of section 79 of the Act applicable to unabsorbed depreciation? - **NO**  
*The section only deals with the set-off of carry forward and brought forward of business losses, it does not deal with the unabsorbed depreciation.*

Further, reliance is also drawn to the following judicial pronouncements:

- **CIT v. Shri Subhulaxmi Mills Ltd (249 ITR 795) (SC)**
  - **Swiss Re-health Services P. Ltd. v. PCIT [ITA No.635 of 2015 (Bangalore Tribunal)]**
  - **DCIT v. Credila Financial Services Private Ltd. [ITA No. 1491 of 2016 (Mumbai Tribunal)]**
- ❑ Whether the provisions of section 79 would trigger in respect of carry forward of interest as provided under section 94B(4) [relating to Thin Capitalisation] of the Act?



# CLAUSE 33 - DEDUCTIONS

# REPORTING

- ❑ Section-wise details of deductions, if any, admissible under Chapter VIA or Chapter III (Section 10A, Section 10AA)

**Section under which deduction is claimed**

**Amounts admissible as per the provision of the Income Tax Act, 1961 and fulfils the conditions, if any, specified under the relevant provisions of Income Tax Act, 1961 or Income Tax Rules, 1962 or any other guidelines, circular, etc. issued in this behalf**

## ANALYSIS...

- ❑ In context of Chapter III, reporting to be done only u/s. 10A (Special provisions in respect of newly established undertakings in free trade zone, etc.) and 10AA (Special provisions in respect of newly established units in Special Economic Zones)
  
- ❑ Issue
  - Sole proprietor has paid mediclaim premium from his personal saving account. No details appear in the books of account of the business. Will the deduction admissible be reported?
  - Particulars of deduction to be given with reference to the items appearing in the books of account of business / profession which is subject to audit u/s. 44AB



## ...ANALYSIS...

- ❑ While working out the admissible deduction, tax auditor to ascertain that the conditions are fulfilled or not
  - To obtain all necessary evidence to enable him to express an opinion
  - Eg., U/s. 80IA, one condition is that the new industrial undertaking should not be formed by splitting up or by reconstruction of business already in existence or by transfer to new business of machinery previously used for any purpose
  - For this, tax auditor to obtain evidence that the machinery is new and has not been used previously for any other purpose
  
- ❑ If assessee has relied on judicial pronouncements w.r.t. a claim, then tax auditor may accept it but he has to record in working papers that admissible amount has been reported on the basis of such judicial pronouncement

## ...ANALYSIS...

- ❑ In case if separate audit report / certificate is issued (eg. s. 80-IA, 80-IB, etc.), tax auditor to refer to these reports / certificates
- ❑ S. 10AA provides for deduction in respect of profits and gains of a unit operating in Special Economic Zone and falls under Chapter III and not Chapter VIA
- ❑ Past Issue – Whether deduction u/s. 10AA has to be computed before setting off losses of other units
  - CIT v. Yokogawa India Ltd. (2017) (77 taxmann.com 41) (SC) – While dealing with s. 10A, it was held that the benefit of deduction is allowable before giving effect to the provisions for set-off and carry forward contained in s. 70, 72 and 74

## ...ANALYSIS...


- ❑ FA 2017 - Insertion of Explanation to s. 10AA(1) - Deduction under this section will be allowed from the total income before giving effect to this section
- ❑ Maximum deduction to be restricted to total income
- ❑ Seeks to nullify decision of the SC in Yokogawa
- ❑ Eligible amount of deduction not affected but quantum of loss that can be carried forward affected

## ...ANALYSIS

| Particulars                               | Pre-amendment | Post Amendment |
|---|---------------|----------------|
| Business Profit                           | 100           | 100            |
| Less: Deduction u/s. 10AA                 | 80            | -              |
| Balance                                   | 20            | 100            |
| Less: Brought forward losses              | 20            | 50             |
| Carry forward of business loss            | 30            | -              |
| Business Income                           | -             | 50             |
| Gross Total Income                        | -             | 50             |
| Less: Deduction under Chapter VI-A        | -             | -              |
| Total Income (before deduction u/s. 10AA) | -             | 50             |
| Less: Deduction u/s. 10AA                 | -             | 50             |
| Total Income                              | -             | -              |

# VERIFICATION

- ❑ Make a list of all the deductions available to a particular assessee, i.e., company, individuals, etc.
- ❑ Go through the entire trial balance to see if there is any item with respect to which benefit of deduction can be claimed
- ❑ Refer the past returns of income to ascertain that the deductions claimed in the earlier years have also been claimed in the current year. If not, then the reasons for non-deduction
- ❑ Go through the assessment orders to ascertain whether the claim for any deduction is under dispute and whether the claim made by assessee in the current year can also be disputed



**CLAUSE 36 – TAX ON DISTRIBUTED PROFITS  
&  
CLAUSE 36A – DEEMED DIVIDEND U/S.  
2(22)(e)**

## Form 3CD - Clause 36...

- ❑ **...Clause 36**– “(a) *incase of domestic company, details of tax on distributed profits under section 115O in following form:*
  - a) *Total amount of distributed profits;*
  - b) *Amount of reduction as referred to in section 115-O(1A)(i);*
  - c) *Amount of reduction as referred to in section 115-O(1A)(ii);*
  - d) *Total tax paid thereon;*
  - e) *Date of payment with amounts.*”

# TAX AUDITOR'S RESPONSIBILITIES...

- ❑ Tax auditor to report:
  - Gross amount distributed during the financial year in sub-clause (a)
  - Reductions referred in s. 115-O(1A)(i) and 115-O(1A)(ii) in sub-clause (b) and (c) respectively
  - Tax worked and paid out at the prescribed rate plus applicable surcharge and education cess
  
- ❑ Tax auditor should keep working papers to reveal how the net amount is arrived at. Tax auditor not to go into the question of how the total amount of distributed profits has been arrived at
  
- ❑ Ascertain the date of payment from the duly received challan and books of account, etc.
  
- ❑ Information about the date of declaration/distribution/payment of dividend is not required to be given



## ...TAX AUDITOR'S RESPONSIBILITIES

- ❑ Ascertain the gross amount of dividend paid from the notes to balance sheet
  
- ❑ To ascertain:
  - Whether there is any distribution of debentures to shareholders or distribution of bonus to preference shareholders?
  - Whether there has been any reduction in capital?
  
- ❑ Ascertain the amount of dividend received from the subsidiary, if any, from the note on "Related Party Transactions" in the financial statements

# ISSUES

- ❑ Whether the benefit of rate of tax as provided in the Article of Dividend of Double-taxation Avoidance Agreement ('DTAA') would be available to the Assessee if it declares dividend to its foreign holding company or foreign company having substantial interest?



**THANK YOU!!!**