BUSINESS TRUST

[AS AMENDED BY FINANCE ACT, 2016]

Relevant for May 2017/Nov 2017 Exam

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ASSESSMENT YEAR 2017-18

Special Thanks to CA Chetan V Chaudhary

Law stated in this book is as amended by the Finance Act, 2016

DAY 2 - BUSINESS TRUST

SCHEME OF TAXATION OF VCC/VCF REGISTERED BEFORE 21ST DAY OF MAY, 2012 UNDER SEBI REGULATIONS/ VENTURES CAPITAL SCHEME OF UTI AND THEIR STAKEHOLDERS

Section:- 10(23FB) & 115U

(A) Tax Treatment in the hands of

(a) Venture Capital Company / Venture Capital Fund registered before 21st day of May, 2012 under SEBI Regulations

(b) Venture Capital Scheme of UTI

- Tax treatment is governed by section 10(23FB).
- As per this section, any income derived by VCC/VCF (before 21st day of May, 2012) / Venture Capital Scheme of UTI from investment in a venture capital undertaking is exempt from tax.
- The provisions of Chapter XII-D or Chapter XII-E or Chapter XVII-B shall not apply to the income paid by a venture capital company or venture capital fund. (That means, VCC/VCF/ Venture Capital Scheme of UTI are not subject to dividend distribution tax or tax on distributed income as well as not required to deduct TDS while making payment to unitholders / shareholders)

(B) Tax Treatment in the hands of Unit-holders / Shareholders of VCC/VCF/Venture Scheme of UTI mentioned above

- Under section 115U, any income received by a person out of investments made in a VCC / VCF / Venture capital scheme of UTI shall be chargeable to income-tax in the same manner as if it were the income received by such person had he made investments directly.
- The income paid by the VCC/ VCF / Venture capital scheme of UTI shall be deemed to be of the same nature and in the same proportion in the hands of the person receiving such income as it had been received by, or had accrued to, the venture capital company or the venture capital fund, as the case may be, during the previous year.
- The income accruing or arising to the VCC / VCF/ Venture capital scheme of UTI during a previous year, if not paid or credited to the person, shall be deemed to have been credited to the account of the person on the last day of the previous year in the same proportion in which such person would have been entitled to receive the income had it been paid in the previous year.
- However, where income has been so included on accrual basis in the total income of the person in the previous year, then it shall not be included again at the time such income is actually paid to him by the VCC / VCF/ UTI Scheme.

Practical 1

A Venture Capital Fund registered before 21-05-2012 derived income of Rs.17 lakh comprising dividend of Rs.4 lakh from shares from a Venture Capital Undertaking and interest of Rs.13 lakh on loan granted to such undertaking. G receives income of Rs.2 lakh from such fund. Examine the taxability of the sum of Rs.2 lakh received by G.

Solution

Tax Treatment in the hands of G

Taxable portion pertaining to Dividend: Rs.47,059 (i.e., Rs. 2 lakh x Rs.4 lakh ÷ Rs. 17 lakh).

Taxable portion pertaining to Interest: Rs.1,52,941 (i.e., Rs. 2 lakh x Rs.13 lakh ÷ Rs. 17 lakh).

Readers Note:

SCHEME OF TAXATION OF INVESTMENT FUNDS AND ITS STAKEHOLDERS

Section:- 10(23FBA), 10(23FBB), 115UB, 139 & 194LBB

(A) Tax Treatment in the hands of Investment Fund (in the form of trust or company or LLP) registered as a Category I or a Category II Alternative Investment Fund under the SEBI (AIF) regulations, 2012 [Effective from A.Y. 2016-17]

- As per section 10(23FBA) any income of Investment Fund other than PGBP income is exempt from tax.
- As per section 115UB(4), the total income of the investment fund is chargeable to tax as under:

Investment Fund	Tax Rate
A company or a firm	30%
Other than a company or a firm	34.50% (Maximum Marginal Rate) plus E.C. = 35.535%

- If in any year there is a loss at the fund level, either current loss or the loss which remained to be set off, such loss shall not be allowed to be passed through to the investors but has to be carried over at fund level to be set off against income of the next year in accordance with the provisions of Chapter VI [Section 115UB(2)].
- Income paid by an investment fund to its unit holders would not be subject to dividend distribution tax under Chapter XII-D or tax on distributed income under Chapter XII-E [Section 115UB(5)].
- With effect from 1st June, 2015, tax has to be deducted@10% on any income (other than the proportion of income which is of the same nature as income chargeable under the head "Profits and gains of business or profession" which is taxable at investment fund level) payable by the investment fund to a unit holder. Such tax has to be deducted at the time of credit of such income to the account of the payee or at the time of payment, whichever is earlier [Section 194LBB].

With effect from 1st June, 2016, following changes have been made in rates of TDS:

Payee	Rate of TDS
Resident	10%
Non-resident, not being foreign company	30% Plus SC and EC
Foreign Company	40% Plus SC and EC

This section has been further amended w.e.f. 1st June, 2016 to provide that where payee is a non-resident or foreign company, then no tds shall be made under this section if such income is not chargeable to tax in their hands in India.

- The person responsible for crediting or making payment of the income on behalf of an investment fund and the investment fund are required to furnish, within the prescribed time, to the person who is liable to tax in respect of such income and to the prescribed income-tax authority a statement in the prescribed form and verified in the prescribed manner. Such statement should give details of the nature of the income paid or credited during the previous year and such other relevant details as may be prescribed [Section 115UB(7)].
- TDS provisions would not be attracted in respect of the income received by the investment fund. This would be provided by issue of appropriate notification under section 197A(1F) subsequently.
- Every investment fund has to compulsorily file its return of income or loss under section 139(4F), if it is not required to do so under any other provision of section 139. The provisions of the Act would apply as if such return of income or loss were a return required to be furnished under section 139(1).

(B) Tax Treatment in the hands of Unitholders / Shareholders/Partners of Investment Fund mentioned above

- Any income accruing or arising to, or received by, a person, being a unit holder of an investment fund, out of investments made in the investment fund shall be chargeable to income-tax in the same manner as if it were the income accruing or arising to, or received by, such person had the investments, made by the investment fund, been made directly by him.
- The income paid or credited by the investment fund shall be deemed to be of the same nature and in the same proportion in the hands of the unit holder as if it had been received by, or had accrued or arisen to, the investment fund [Section 115UB(3)].
- Income accruing or arising to, or received by, a unit holder of an investment fund, being that proportion of income which is of the same nature as income chargeable under the head “Profits and gains of business and profession” at investment fund level, shall be exempt under section 10(23FBB).
- If the income accruing or arising to, or received by, an investment fund, during a previous year is not paid or credited to the unit-holders, it shall be deemed to have been credited to the account of the unit-holder on the last day of the previous year in the same proportion in which such person would have been entitled to receive the income had it been paid in the previous year [Section 115UB(6)].

Practical 2

PQR Private Limited is an Investment Fund as per explanation to section 115UB. There are 50 shareholders each having equal share. For previous year **2016-17**, PQR Private Limited reports following incomes.

Particulars	Company (Rs.)
Business Income	60,00,000
Capital Gains	1,00,00,000
Income from other sources	20,00,000
Total	**1,80,00,000**

Compute the total income and tax liability of the PQR Private Limited.

Also compute income of each shareholders from the said investment fund.

Solution

Computation of Total Income and Tax Liability in the hands of PQR Private Limited

Particulars	Company (Rs.)
Business Income	60,00,000
Capital Gains	Exempt u/s 10(23FBA)
Income from other sources	Exempt u/s 10(23FBA)
Total Income	**60,00,000**
Tax Liability (30.90%)	**18,54,000**

Computation of Income of each shareholder from PQR Private Limited

Particulars	Company (Rs.)
Business Income	Exempt u/s 10(23FBB)
Capital Gains [1,00,00,000 ÷ 50]	2,00,000
Income from other sources [20,00,000 ÷ 50]	40,000
Income	**2,40,000**

Readers Note:

Practical 3

ABC Trust is an Investment Fund as per explanation to section 115UB. There are 20 unit holders each having equal share. ABC Trust reports following incomes.

Particulars	P.Y. 2016-17	P.Y. 2017-18
Business Income	(20,00,000)	8,00,000
Long Term Capital Gain	(25,00,000)	35,00,000
Income from other sources	60,00,000	30,00,000

Compute the total income of the ABC Trust. What is the applicable tax rate to ABC Trust?

Also compute income of each unit holders from the said investment fund.

Solution

Computation of Total Income of ABC Trust

Particulars	P.Y.2016-17	
	Rs.	Rs.
Business Income (Adjusted against Income from other sources)		Nil
Long Term Capital Loss (Rs. 25 lakhs carried forward)		Nil
Income from other sources	60,00,000	
Less: Business Loss to be set-off	(20,00,000)	
	40,00,000	Exempt u/s 23(FBA)
Total Income		Nil

Particulars	P.Y.2017-18	
	Rs.	Rs.
Business Income		8,00,000
Long Term Capital Gain	35,00,000	Nil
Less: Brought forward Long Term Capital Loss	(25,00,000)	
	10,00,000	Exempt u/s 23(FBA)
Income from other sources	30,00,000	Exempt u/s 23(FBA)
Total Income		8,00,000

Computation of Income of each Unit Holder from ABC Trust

Particulars	P.Y.2016-17	P.Y.2017-18
Business Income (If any)	Exempt u/s 10(23FBB)	Exempt u/s 10(23FBB)
Long Term Capital Gains	Nil	50,000 [10,00,000 ÷ 20]
Income from other sources	2,00,000 [40,00,000 ÷ 20]	1,50,000 [30,00,000 ÷ 20]
Income	**2,00,000**	**2,00,000**

Readers Note:

SPECIAL TAXATION REGIME FOR BUSINESS TRUSTS

Section:- 115UA, 10(23FCA), 10(38), 111A, 194LBA(3) & 194-I

(A) Tax Treatment in the hands of REIT

(a) Under section 10(23FC), following incomes are exempt in the hands of REIT.

- Interest income from SPV.
- Dividend income from SPV in which Business Trust has become the holder of the whole of the nominal value of equity share capital of such SPV. (In Short, dividend from SPV in which Business trust holds 100% equity) even if SPV had not paid corporate dividend tax due to section 115-O (7). (Amendment by Finance Act, 2016)

(b) Any income of a business trust, being a REIT, by way of renting or leasing or letting out any real estate asset owned directly by such business trust is exempt under section 10(23FCA).

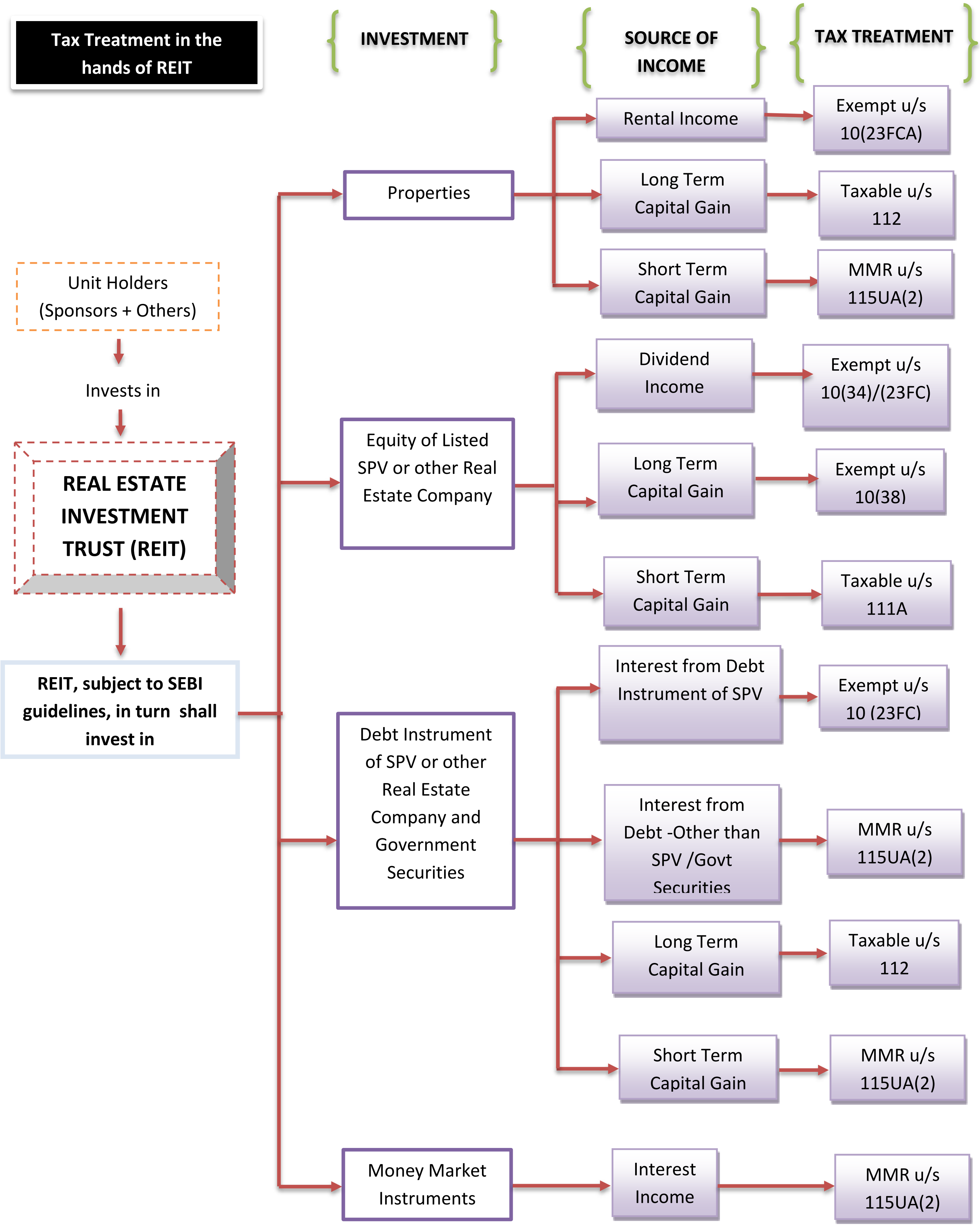
(c) As per section 115UA(2),

- capital gain derived by REIT shall be taxed under section 111A or 112, as the case may be.
- while other incomes of REIT shall be taxed at Maximum Marginal Rate

(d) As per section 115UA(4), any person responsible for making payment of the income distributed on behalf of a business trust to a unit holder shall furnish a statement to the unit holder [Form No. 64B – 30th June of every financial year] and the Principal Commissioner or Commissioner of Income Tax [Form No. 64A- 30th November of every financial year], giving the details of the nature of the income paid during the previous year and such other details as may be prescribed.

(e) Further, REIT is required to furnish its return of income under section 139(4D).

Readers are advised to go through following diagram covering possible sources of income in the hands of REIT and its tax treatment.


Tax Treatment in the hands of REIT
INVESTMENT
SOURCE OF INCOME
TAX TREATMENT
Unit Holders (Sponsors + Others)
Invests in
REAL ESTATE INVESTMENT TRUST (REIT)
REIT, subject to SEBI guidelines, in turn shall invest in
Properties
Rental Income
Exempt u/s 10(23FCA)
Long Term Capital Gain
Taxable u/s 112
Short Term Capital Gain
MMR u/s 115UA(2)
Equity of Listed SPV or other Real Estate Company
Dividend Income
Exempt u/s 10(34)/(23FC)
Long Term Capital Gain
Exempt u/s 10(38)
Short Term Capital Gain
Taxable u/s 111A
Debt Instrument of SPV or other Real Estate Company and Government Securities
Interest from Debt Instrument of SPV
Exempt u/s 10 (23FC)
Interest from Debt -Other than SPV /Govt Securities
MMR u/s 115UA(2)
Long Term Capital Gain
Taxable u/s 112
Short Term Capital Gain
MMR u/s 115UA(2)
Money Market Instruments
Interest Income
MMR u/s 115UA(2)

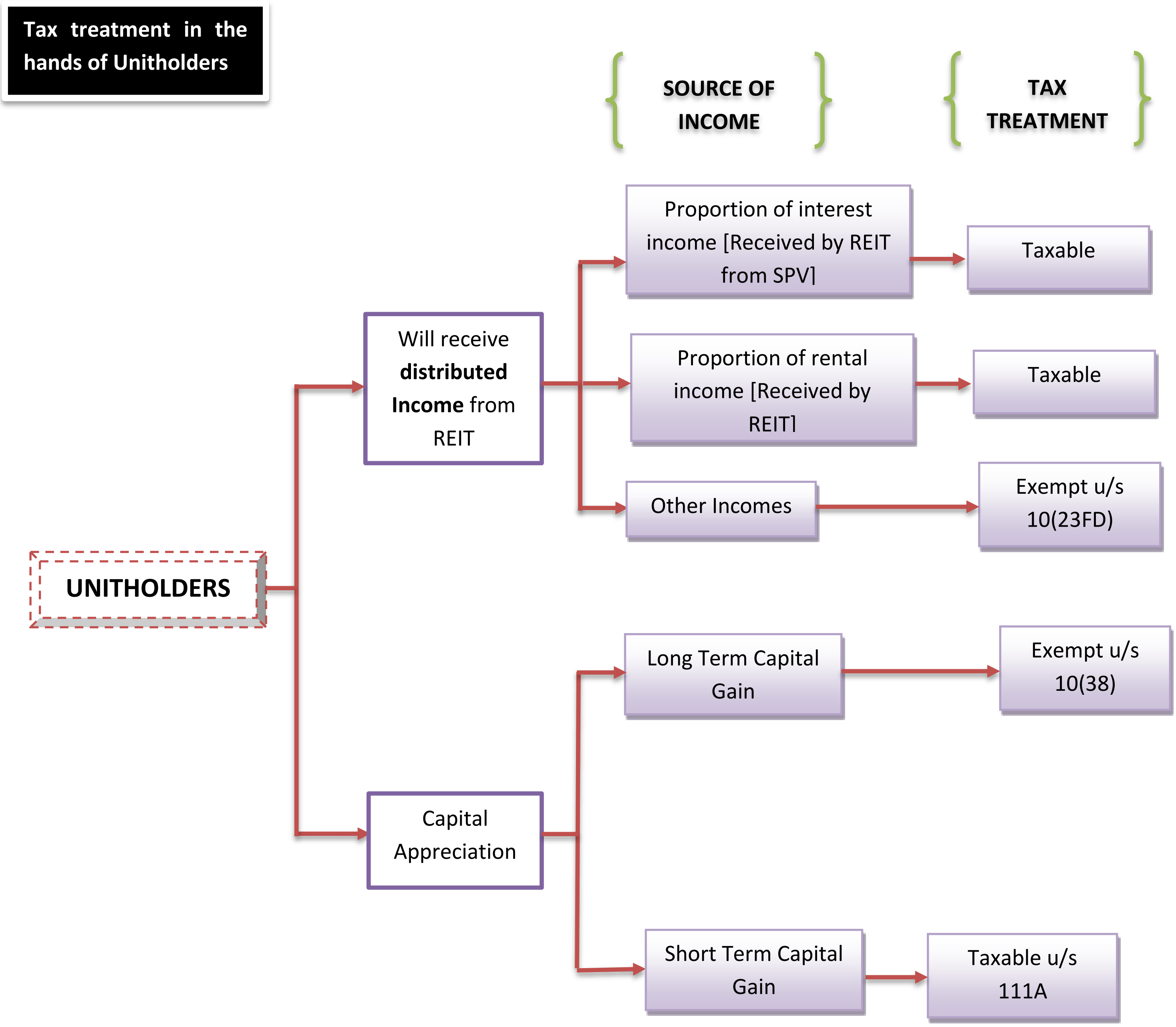
(B) Tax Treatment in the hands of Unit-holders

(i) As per section 115 UA (1), any income distributed by a business trust to its unit holders shall be deemed to be of the same nature and in the same proportion in the hands of the unit holder as it had been received by, or accrued to, the business trust.

(ii) As per section 115 UA(3), the distributed income or any part thereof, received by a unit holder from the business trust being interest from SPV or income by way of renting or leasing or letting out any real estate asset owned directly by such REIT shall be charged to tax in the hands of unit holder.

(iii) As per section 10(23FD), other distributed income received by unit holder from business trust is exempt

Readers are advised to go through following diagram covering tax treatment in the hands of Unit Holders.



TDS Mechanism

When SPV → Makes Interest Payment to → REAL ESTATE INVESTMENT TRUST (REIT)

TDS Not Applicable

When Tenant → Makes Rent Payment to → REAL ESTATE INVESTMENT TRUST (REIT)

TDS Not Applicable

When (REIT) → Distributes Interest Portion from SPV → TDS Applicable

- If Unit holder is resident then rate of TDS is 10% u/s 194A
- If Unit holder is Non-Resident/Foreign Company then rate of TDS is 5% u/s 194LBA / 194LC

When (REIT) → Distributes Rent Portion → TDS Applicable

- If Unit holder is resident then rate of TDS is 10% u/s 194LBA(1)
- If Unit holder is
  - Non-Resident (Not being Foreign Company) then rate of TDS is 30% u/s 194LBA(3)
  - Foreign Company then rate of TDS is 40%

Practical 4

A REIT provides the following particulars of its income for the **P.Y.2016-17**:

Sr. No.	Particulars	Rs. in Lakhs
1.	Interest income from SPV	200
2.	Rental/Leasing income from real estate asset owned directly by REIT	300
3.	Dividend income from SPV "A" (in which REIT holds 60% equity)	100
4.	Dividend income from SPV "B" (in which REIT holds 100% equity)	200
5.	Short-term capital gains on sale of listed shares of SPV	200
6.	Interest from Government Securities	15
7.	Interest received from investments in unlisted debentures of real estate companies	10
8.	Long Term Capital Gains on sale of property	200
9.	Long Term Capital Gains on sale of listed shares of SPV	270
10.	Short term gain on sale of unlisted debentures of real estate companies	5

(i) Discuss Tax treatment of each receipts in the hands of REIT.

(ii) Discuss the tax consequences in the hands of unit holders assuming that the REIT has distributed Rs. 1400 Lakhs to the unit holders in the **P.Y.2016-17**.

(iii) Discuss Corporate Dividend Tax (CDT) obligation under section 115-O in the hands of SPV "A" and SPV "B" in the light of amendments by finance Act, 2016.

Solution

(i) Tax Treatment in the hands of REIT

Sr. No.	Particulars	Amount Rs. in Lakhs	Section Applicable	Tax Rate applicable
1.	Interest income from SPV	200	10(23FC)	Exempt
2.	Rental/Leasing income from real estate asset owned directly by REIT	300	10(23FCA)	Exempt
3.	Dividend income from SPV "A"	100	10(34)	Exempt
4.	Dividend income from SPV "B"	200	10(23FC)	Exempt
5.	Short-term capital gains on sale of listed shares of SPV	200	111A	15%
6.	Interest from Government Securities	15	115UA(2)	34.50%
7.	Interest received from investments in unlisted debentures of real estate companies	10	115UA(2)	34.50%
8.	Long Term Capital Gains on sale of property	200	112	20%
9.	Long Term Capital Gains on sale of listed shares of SPV	270	10(38)	Exempt
10.	Short term gain on sale of unlisted debentures of real estate companies	5	115UA(2)	34.50%

(ii) Tax treatment in the hands of unit holders.

(a) Distributed income representing Interest from SPV

Out of distributed income of Rs. 1400 Lakhs, interest portion from SPV and rental income from REIT shall be taxable in the hands of unit holders. Same shall be worked out as under:

Total income derived by REIT during the year : 1500 Lakhs

Interest from SPV included in above income : Rs.200 Lakhs

Rental Income from REIT included in above income : Rs. 300 lakhs

Distributed income to Unit Holders : Rs. 1400 Lakhs

Therefore, Interest portion from SPV, distributed to Unit Holders = Rs. 186.66 Lakhs $\left[200 \times \frac{1400}{1500}\right]$

Therefore, portion of Rental Income from REIT, distributed to Unit Holders = Rs. 280.00 Lakhs $\left[300 \times \frac{1400}{1500}\right]$

(b) Other distributed income

(Rs. 1400 lakhs –Rs. 186.66 Lakhs –Rs. 280.00lakhs) = Rs. 933.34 is exempt in the hands of unit holders under section 10(23FD).

(iii) CDT obligation in the hands of SPV under section 115-O.

- SPV “A” (in which REIT holds 60% equity) is required to pay CDT on the amount of dividend distributed its shareholders under section 115-O.
- Because of amendment by Finance Act, 2016, SPV “B” (in which REIT holds 100% equity) is not required to pay CDT on the amount of dividend declared / distributed / paid to its shareholders. [Section 115-O(7)].

Readers Note:

Practical 5

Mr. Kulbharat is already holding 10,000 equity of DFF Ltd (SPV). These shares were purchased on **20-01-2016** for Rs. 3,50,000. He would like to become sponsor of REIT and therefore, he exchanged these shares for units in REIT on **10-08-2016** and he was allotted 1,00,000 units with a face value of Rs.10 per unit. Thereafter, he sold out 20,000 units on **12-01-17** for Rs. 12 per unit. Discuss tax consequences of this transaction.

Before we refer solution, let us comprehend the amendment first.

(i) *As per section 47(*xvii*) any transfer of a capital asset, being share of a special purpose vehicle to a business trust in exchange of units allotted by that trust to the transferor is not treated as transfer.*

(ii) *As per section 2(42A), while determining nature of capital asset being units allotted under section 47(xiii), the period of holding of shares shall be included.*

(iii) *As per section 49(2AC), where the capital asset, being a unit of a business trust, became the property of the assessee in consideration of a transfer as referred to in clause (*xvii*) of section 47, the cost of acquisition of units shall be deemed to be the cost of acquisition of the shares to the sponsor.*

Solution

As per provisions of section 47(xvii), exchange of shares in SPV by sponsor for units in REIT is not treated as transfer. Therefore, exchange will not attract capital gain in the hands of Mr. Kulbharat.

But, subsequent sale of REIT Units will attract capital gain tax in the hands of Mr. Kulbharat, computation of which is as under:-

Period of Holding: From **20-01-2016 to 12-01-2017**, hence Long Term Capital Asset.

Particulars	Amount Rs
Sale Consideration (20,000 × 12)	2,40,000
Less: COA	70,000
STCG u/s 111A	**1,70,000**

Working Note:

As per section 49(2AC),

Cost of acquisition of 1,00,000 units of REIT Ltd. = Cost of acquisition of 10,000 shares of DFF

=Rs. 3,50,000

Hence, cost of acquisition per unit of REIT is =Rs. 3,50,000/1,00,000

= Rs. 3.5 per unit

Hence, cost of acquisition of 20,000 units = Rs. 3.5 × 20,000

= 70,000

Readers Note:

Practical 6

Does you answer differ if Mr. Kulbharat had purchased shares of DFF Ltd. on **01-01-2016 instead of 20-01-2016**?

Solution

Readers Note:

SCHEME OF TAXATION OF SECURITISATION TRUST AND ITS INVESTORS

Section:- 10(23DA), 115TCA & 194LBC

(A) Process of Securitisation

- Original lender (bank or FI) selects and then sells various types of loans to another institution (which may promote a subsidiary for this purpose called Special Purpose Vehicle, which is a sort of Trust);
- The special purpose vehicle- SPV (called issuer also) makes the payment to the original lender for the loans purchased under the arrangement;
- These loans are converted into a pool of securities (generally called “Pass Through Certificates”) by SPV.
- These PTCs are then sold to individual or institutional investors, who are willing to make investments;
- The original lender may keep on getting recoveries from the original borrowers;
- He passes on these recoveries to the SPV.
- The issuer in turn passes on these recoveries to the individual/institutional investors as per the arrangement made.

(B) Tax Treatment in the hands of Securitisation Trust

Tax treatment is governed by section 10(23DA).

- As per this section, entire income of securitization trust shall be exempt.
- The person responsible for crediting or making payment of the income on behalf of securitisation trust and the securitisation trust shall furnish, within such period, as may be prescribed, to the person who is liable to tax in respect of such income and to the prescribed income-tax authority, a statement in such form and verified in such manner, giving details of the nature of the income paid or credited during the previous year and such other relevant details, as may be prescribed.

- With effect from 1st June, 2016, tax has to be deducted by securitisation trust at the time of payment or credit to the account of investor, whichever is earlier. [Section 194LBC]. Depending upon type of payees, the rates of TDS are as under:

Payee	**Rate of TDS**
Resident Individual and HUF	25%
Resident other than individual and HUF	30%
Non-resident, not being foreign company	30% Plus SC and EC
Foreign Company	40% Plus SC and EC

(C) Tax Treatment in the hands of Investors of Securitisation Trust

- Under section 115TCA, any income accruing to or received by a person, being investor of a securitization trust shall be chargeable to income-tax in the same manner as if it were the income received by such person had he made investments directly.
- The income paid or credited by the securitisation trust shall be deemed to be of the same nature and in the same proportion in the hands of the investors as it had been received by, or had accrued to, securitisation trust during the previous year.
- The income accruing or arising to the securitisation trust during a previous year, if not paid or credited to the investor, shall be deemed to have been credited to the account of the person on the last day of the previous year in the same proportion in which such investor would have been entitled to receive the income had it been paid in the previous year.
- However, where income has been so included on accrual basis in the total income of the investor in the previous year, then it shall not be included again at the time such income is actually paid to him by the securitisation trust.