

Black Money Compliance Window

The Undisclosed Foreign Income And Assets (Imposition Of Tax) Bill, 2015
{UFIA Act, 2015}

Surprises continued..

CA. Ashwani Rastogi

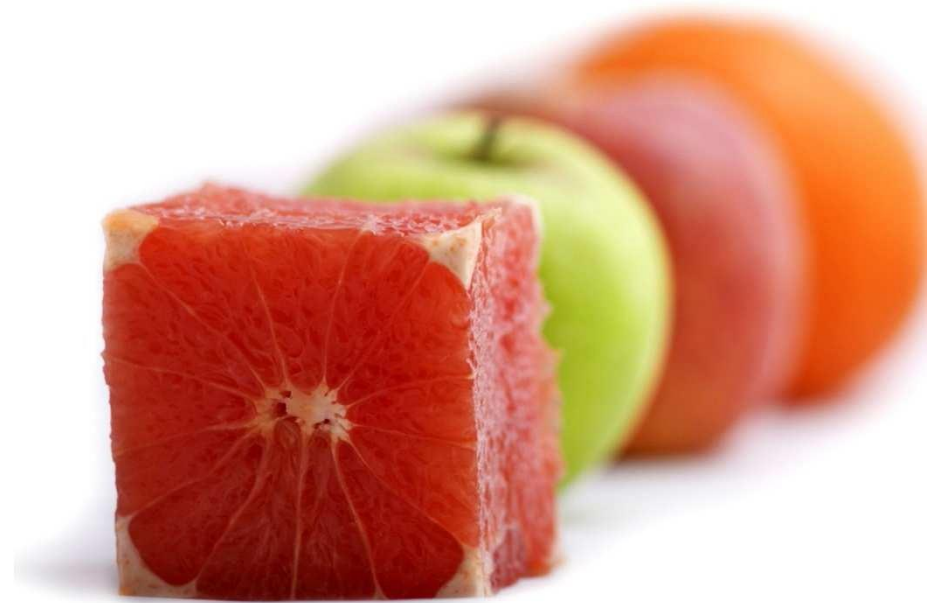
ashwani.rastogi.ca@gmail.com

+91 9990999281

+91 9810999281

New Delhi

2nd July 2015



C O N T E N T S

| Matter Covered | Page No. |
|--|----------|
| One time compliance procedure | 3 |
| One time compliance NOT OPEN FOR | 4 |
| Highlights of the UFIA Act | 5 |
| Analysis of the UFIA Act | |
| • Applicability of the UFIA Act | 6-7 |
| • Undisclosed foreign income and assets | 8-10 |
| • Computation of tax on UFIA | 11-15 |
| • Assessment procedures & Treaty protection | 16 |
| • FEMA and UFIA – Issues | 17 |
| • Mandatory filing of IT Return & disclosure requirement | 18 |

One time compliance procedure

- Positioned as not being an amnesty scheme – there is no immunity from penalty
- Merely an opportunity for persons to come clean and become compliant before the stringent provisions of the new Act come into force
- One time compliance scheme window (with a time limit to be notified) for disclosing any UFA acquired from income chargeable to tax under ITA for any assessment year prior to AY 2016-17*
- Any person can make declaration (format and the due date to be notified) in respect of UFAs and pay tax on it @ 30% plus penalty (equal to tax) i.e. total 60%
- Tax will be on value of UFA as on the date of enactment of this new legislation
- No exemption, deduction or set-off of any carried forward losses
- Amount of UFA so declared shall not be included in the total income of any assessment year in ITA
- No reopening of assessment due to disclosure under this scheme - Declaration will not affect finality of completed assessment
- Contents of declaration cannot be used as evidence for imposing penalties under any other law or for prosecution under ITA, Wealth tax, FEMA, Companies Act 2013, or Customs Act 1962
- No Wealth Tax on UFA declared. Assets declared by firm shall not be considered in computing net wealth of individual partner or value of interest of any partner

*Central Government indicated that Declaration has to be filled by 30th September 2015 and Tax need to be discharged by 31st December 2015 – Source Aaj Tak Media dt. 1st July 2015

One time window NOT OPEN for the following persons:

- Any person who has been issued an order of detention under the Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974 (subject to certain conditions)
- Any person who is subject to prosecution for any offence punishable under Chapter IX or Chapter XVII of the Indian Penal Code, the Narcotic Drugs and Psychotropic Substances Act, 1985, the Unlawful Activities (Prevention) Act, 1967, the Prevention of Corruption Act, 1988
- Any person notified under section 3 of the Special Court (Trial of Offences Relating to Transactions in Securities) Act, 1992
- Any person against whom notice of assessment has been issued under ITA
- Any person against whom time limit for furnishing of notice of assessment has not expired due to search, survey under the ITA
- Any person against whom information has been received in respect of UFA from competent authority under a formal pact (cases like account holders of HSBC Geneva which has not been disclosed, whether or not having any balance)

Highlights of the UFIA Act

- Act is effective from 1 April 2016 onwards (Assessment Year 2016-17) and extends to whole of India
- Applicable to all persons resident in India. In case of Individuals, it applies to ordinary resident under ITA
- Flat 30% tax rate (without surcharge and cess) on the value of total undisclosed foreign income and asset
- No exemption, deduction, set-off and carry forward of losses under ITA, no set off of foreign tax credit will be allowed on UFIA
- Additional 300% penalty for non-disclosure of foreign income or an asset. Rs.10 Lakhs penalty for non-filing of return / not furnishing complete details of foreign assets
- Rs.10 Lakhs penalty for non-filing of return / not furnishing complete details of foreign assets
- Prosecution for various violations (including abetment) including rigorous imprisonment from 3 to 10 years.
- Tax and penalty proposed to be calculated at current value of assets instead of original purchase price
- One time compliance opportunity before commencement of the UFIA Act (just notified) : 30% tax and equal penalty, no interest and prosecution
- Imposition of personal liability on the Manager (including MD) of a company if any amount due under UFIA Act is not recoverable from the company

Applicability of the UFIA Act

Applicable to all persons resident in India. In case of Individuals, it applies to ordinary resident under ITA

Who is an RNOR?

To understand who an RNOR is, we first need to understand the definitions of resident and non-resident Indian.

A person is a resident Indian in a particular year if he fulfills either of these two conditions: - He/she has been in India in that year for 182 days or more or -He/she has been in India for 60 days or more in that year and 365 days or more in the 4 years preceding that year

A person who does not fulfill the above conditions is considered to be a non-resident.

Now, if you have recently moved back to India after spending many years overseas, you must check for the status of RNOR.

A person is an RNOR if he meets either of these two conditions: -He/she has been non-resident in India, that is, an NRI, in nine out of the ten previous years preceding that year, or -He/she has, during the seven previous years preceding that year, been in India for a period of 729 days or less

Now depending on the date of return, a person can take the benefit of the RNOR status for up to 3 tax years in India. (Note than a tax year in India is a fiscal year, that is, from April to March)

Illustration: Rakesh Verma returns to India on 15th January 2011 after spending more than 20 years abroad. The first tax year for him in India would be 2010-2011. Does he qualify as RNOR in

2010-2011? Yes, because: -He has been an NRI for all the years preceding 2010-2011.

Will he qualify as RNOR in 2011-2012? Yes, because -He will have been an NRI for nine out of the ten previous years. That is, except for 2010-2011, he will have been NRI in all other years

Will he qualify as RNOR in 2012-2013? -He will not have been NRI for nine out of the ten previous years because he would have been RNOR for 2010-2011 and 2011-2012. -During the seven previous years, that is for the seven tax years from 2005-2006 to 2011-2012, he would have been in India for the entire 2011-2012 (366 days) and for 75 days in 2010-2011. That's 441 days in total which is less than 729 days. Because he will fulfill this second condition, he will qualify as an RNOR in 2012-2013 as well.

Will he qualify for RNOR in 2013-2014? -He will not have been NRI for nine out of the ten previous years because he would have been RNOR from 2010-11 to 2012-13 -During the seven previous tax years, that is from 2006-2007 to 2012-2013, he would have been in India for 365 days in 2012-2013, 366 days in 2011-2012 and 75 days in 2010-2011. That's 806 days in total. Since he will not fulfill either condition, he will be considered as Resident Indian in 2013-2014.

Accordingly UFIA applicable only to those person who are ROR, not to RNOR & NRI.

Undisclosed foreign income and assets

Undisclosed Foreign Income and Asset (UFIA) [Section 2(12)]

- Total amount of undisclosed income from source located outside India [as referred in Section 4(1)], and
- Value of UFA located outside India
- UFIA shall be
 - Income from a source located outside India which has not been disclosed in the Return of Income filed under the ITA
 - Income from sources, in respect of which return is not filed under the ITA and
 - Value of undisclosed foreign asset (UFA) located outside India
(fair market value in the previous year in which AO notices UFA- method of valuation to be prescribed)
- Computation of UFIA laid down under section 5 of the Bill

Undisclosed Asset located outside India (UFA) [Section 2(11)]

- An asset (including financial interest in any entity) located outside India
- Asset can be held by the assessee in his name or in respect of which he is a beneficial owner, and
- Assessee has no explanation about the source of investment in such asset or the explanation given by him is the opinion of the Assessing Officer is unsatisfactory

Test of undisclosed foreign asset is to explain the source of investment

Asset not taxable as UFA if its source is explained (even though it is not declared in the return of income)

UFA is not defined under the Bill. It will include all assets either movable or immovable (including financial interest in an entity)

- A cue can be taken from the Instructions to the Income Tax Returns:

“Financial interest would include, but would not be limited to, any of the following:-

(1) if the resident assessee is the owner of record or holder of legal title of any financial account, irrespective of whether he is the beneficiary or not.

(2) if the owner of record or holder of title is one of the following:-

(i) an agent, nominee, attorney or a person acting in some other capacity on behalf of the resident assessee with respect to the entity.

(ii) a corporation in which the resident owns, directly or indirectly, any share or voting power.

(iii) a partnership in which the resident assessee owns, directly or indirectly, an interest in partnership profits or an interest in partnership capital.

(iv) a trust of which the resident has beneficial or ownership interest.

(v) any other entity in which the resident owns, directly or indirectly, any voting power or equity interest or assets or interest in profits.”

Computation of tax on UFIA

- UFIA will be taxed @ 30% - no surcharge and cess
- Tax will be charged on its value in the previous year in which UFIA same is noted by AO
- Value of UFA means fair market value of an asset 'including financial interest in any entity) in the previous year in which it comes to AO's notice- method of valuation to be prescribed
- Computation of total UFIA (Section 4)

| | |
|---|----|
| Computation of total UFIA | |
| Income from source located outside India (foreign income ' FI') which has not been disclosed in IT Return | XX |
| FI in respect of which no IT return has been filed | XX |
| FMV of UFA (no explanation or unsatisfactory explanation about the source of income has been provided – Section 4(3)) | XX |

- If UIFA is taxed under this new legislation, it will not be taxed under ITA
- Any variation made to the foreign sourced income as per section 29 to 43C or section 57 to 59 or section 92C of the ITA will not be included in total undisclosed foreign income
- Hardship to the assessee as tax and penalties proposed to be calculated at current value of assets instead of original purchase price

Computation of tax on UFIA

- As per Section 5,
 - No expenditure, allowance, set off of any loss shall be allowed as deduction from total UFIA – no mention about liabilities incurred against undisclosed foreign assets
 - If any income is assessed prior to AY 2016-17 under ITA or any income is assessed / assessable under UFIA Act shall be reduced from the value of UFA outside India – subject to producing evidence that the UFA was acquired from such income
 - Proportionate income which was been assessed to tax under ITA or UFIA Act shall be reduced from FMV of UFA being immovable property

Reduction Formula:

$$\text{Value of UFA as on first day of FY (in which AO notices such asset)} \times \frac{\text{Assessed / assessable foreign income}}{\text{Total cost of the asset}}$$

Computation of tax on UFIA

| | |
|---|------|
| Computation of total UFIA | |
| Income from source located outside India (foreign income or 'FI') which has not been disclosed in IT Return | XX |
| FI in respect of which no IT return has been filed | XX |
| FMV of UFA (no explanation or unsatisfactory explanation about the source of income has been provided) – manner of valuation to be provided | XX |
| <u>Less:</u> | |
| Income which has been assessed to tax for any assessment year under the ITA prior to relevant AY in which UFIA applies | (XX) |
| Income which is assessable or has been assessed to tax for any assessment year under UFIA | (XX) |
| In case of immovable properties, the deduction will be: Value of UFA as on first day of FY in the same proportion as assessed / assessable foreign income bears total cost | (XX) |
| Total value of UFIA | XX |
| Tax @ 30% | XX |

The quantum of penalty may vary between 100% to 300% of the tax amount, depending on whether voluntarily disclosures are made under one time disclosure window or UFIA is detected by AO

Computation of tax on UFIA

Illustration 1:

- Mr. Y acquired foreign asset (immovable property) in the assessment year 2010-11 for Rs.120 lacs. Out of the total investment, Rs.80 lacs was assessed to tax in an earlier year.
- In AY 2007-08, the AO identified the undisclosed asset having value of Rs.4 crore for which no explanation was provided

| Computation of total UFIA – Shares | Rs. (in crores) |
|---|-----------------|
| FMV of UFA (no explanation provided or explanation not satisfactory) | 4 |
| Less | |
| Income which has been assessed to tax for any assessment year under the ITA prior to relevant AY in which UFIA applies (Rs.4crore X 0.80 lacs / 1.20 lacs) | (2.67) |
| Amount chargeable to tax under UFIA Act | 1.33 |

Computation of tax on UFIA

Illustration 2:

- Mr. X acquired share of foreign company, in the assessment year 2011-12 for 40 lacs.
- AO identified the undisclosed asset in the assessment year 2018-19, the FMV of such asset is determined at Rs.60 lacs
- Shares were acquired from the income assessed to tax of Rs.16 lacs

| Computation of total UFIA – Shares | Rs. (in crores) |
|--|-----------------|
| FMV of UFA in respect of which no explanation or unsatisfactory explanation about the source of income has been given | 60 |
| Less: | |
| Income which has been assessed to tax for any assessment year under the ITA prior to relevant AY in which UFIA applies | (16) |
| Amount chargeable to tax under UFIA Act | 44 |

Assessment procedure Chapter III – Tax Management

- *No requirement to file a separate return under UFIA Act.*
- Assessment / reassessment by AO in respect of undisclosed foreign income or asset on the basis of information received
- Issue of notice for assessment / reassessment (no timeline provided), opportunity of being heard and furnishing of evidences / documents will be given – principles of natural justice to be followed
- Inquiry or investigation by Tax Authorities into matters of the assessee even though there are no proceedings pending before it
- Time limit for completion of assessment and reassessment shall be 2 years from the end of the financial year in which notice was issued
- It is expected that two assessment orders will be passed in respect of period covered by a single return of income: under section 143(3) of ITA and 10(3) of UFIA Act
- Remedial measures provided - appeal to CIT(A) / ITAT / High Court and Supreme Court (for substantial question of law), rectification of mistakes, revision of orders, recovery of arrears
- Under UFIA, the AO will be able to re-open the assessments beyond 16 years.

Treaty protection

Section 73

No provision granting relief against double taxation of income under UFIA Act and corresponding law in foreign jurisdiction

FEMA and UFIA – Issues

Foreign assets held in accordance with FEMA – examples

- Any resident individual (under FEMA or ITA or both) who is holding assets abroad acquired from LRS
- Any Indian resident company holding assets abroad under Overseas Direct Investments (ODI) Guidelines
- A resident person who continues to hold assets abroad which were acquired when non-resident as permitted under section 6(4) of FEMA
- Inheritance of foreign asset by Indian resident from non-resident relative and continues to hold the same as permitted under section 6(4) of FEMA
- However, Finance Bill 2015 proposes that the Enforcement Director under FEMA can directly seize equivalent value of Indian assets (without asking any questions) and merely on the reason to believe or suspicion – similar amendments are also proposed under Prevention of Money-laundering Act, 2002 (PMLA) vide Finance Bill 2015
- Black Money is different from criminal money – Harsh implications and arbitrary penalties under UFIA read with proposed PMLA amendment not justified

Mandatory filing of IT Return & disclosure requirement of foreign assets in ITR

- *Currently, ROR is mandatorily required to file the IT return even if total income does not exceed the maximum amount not chargeable to tax if he has any asset (including any financial interest in any entity) located outside India or signing authority in an account outside India*
- Finance Act 2015 has proposed that ROR, is mandatorily required to file the tax return if he:
 - holds, as a beneficial owner or otherwise, any asset (including any financial interest in any entity) located outside India or has signing authority in any account located outside India; or
 - is a beneficiary of any asset (including any financial interest in any entity) located outside India
- Filing of return will not be mandatory for a beneficiary of any asset (including any financial interest in any entity) located outside India, if income arising from such an asset is includible in the income of the beneficial owner of such an asset

Disclosure of Foreign Assets (Schedule FA) as per IT Return w.e.f. AY 2012-13 ITR Form contain Schedule FA that required for every assessee to disclose following details:-

- Details of foreign bank accounts
- Details of foreign immovable property
- Details of any other asset or assets in the nature of investment
- Details of account(s) in which there is signing authority and which has not been included above
- Details of trusts, created under the laws of a country outside India, in which you are a trustee



CA. ASHWANI RASTOGI
ashwani.rastogi.ca@gmail.com
9990999281