Monthly Newsletter Volume No. 11/2007

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DIRECT TAXES

Judicial Pronouncements

ACIT V. Rogini Garments 108 ITD 49 (Chennai)

The question before the Hon'ble Tribunal was whether in view of restriction placed on claim of repetitive deduction in section 80-IA(9), which is made applicable in respect of all deductions under Chapter VI-A, relief under section 80-IA should be deducted. It was held that section 80HHC is part of Chapter VI-A. Section 80HHC is not a self-contained provision. The deduction under said section cannot be allowed ignoring the restrictive clause contained in section 80-IA(9). The restrictive clause in section 80-IA makes it abundantly clear that wherever deduction under any other section of Chapter VI-A(C) is claimed, the computation will be subject to the restrictions laid down in section 80-IA(9). It precludes pro tanto, all the deductions of such profits and gains claimed under Chapter VI-A(C). Section 80HHC is part of Chapter VI-A(C). It is not a self-contained provision. There is absolutely no ambiguity on this aspect. Therefore, relief under section 80-IA should be deducted from the profits and gains of the business before computing relief under section 80HHC.

AAR V. Timken France 164 Taxman 354 (AAR)

Section 112, read with section 48, of the Income-tax Act, 1961 - Capital gains - Tax on long-term capital gains – It was held that benefit of proviso to section 112(1) cannot be denied to non-residents/foreign companies who are also entitled to a different relief in terms of first proviso to section 48. it was further held that eligibility to avail benefit of indexed cost of acquisition under second proviso to section 48 is not a sine qua non for applying reduced rate of 10 per cent prescribed by proviso to section 112(1). The court also stated that proviso to section 112(1) does not make any distinction between original and bonus shares. Once it is held that under proviso to section 112(1), benefit of lower rate of tax is not to be denied to non-residents in respect of long-term capital gains arising from transfer of original shares, it follows that same interpretation will hold good in case of bonus shares as well.

Moser Baer India Ltd. V. DCIT 17 SOT 510 (2007)

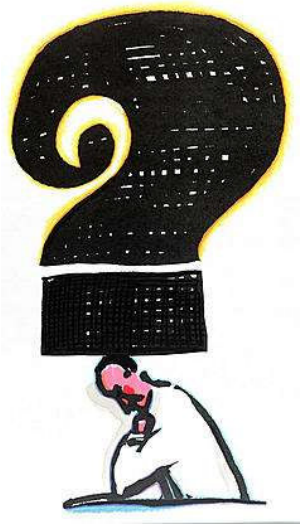
Section 115JB, read with section 10A/10B, of the Income-tax Act, 1961 - Minimum alternate tax. It was held that for determination of book profit any mode and manner of computation of total income under Act has not to be applied and reference is to be made only to profit and loss account prepared in accordance with provisions of Parts II and III of Schedule VI of Companies Act. The court took the view that while computing book profit under section 115JB amount to be reduced is income which is eligible for exemption under section 10A/10B as computed on basis of book profits as per Parts II and III of Schedule VI of Companies Act and not on basis of provisions of Act.

Section 147 of the Income-tax Act, 1961 - Income escaping assessment - Non-disclosure of primary facts - Where Assessing Officer had reopened assessment of assessee on grounds that book profit under section 115JB and deduction under section 10A were wrongly computed without bringing any fresh material/information on record, such reopening of assessment on mere change of opinion, was not valid and was liable to be cancelled.

Valueline Securities (India) Ltd. V. ACIT 108 ITD 639 (2007)

Section 158B, read with section 68, of the Income-tax Act, 1961 - Block assessment in search cases - Undisclosed income - Block period from 1986-87 to 1996-97 - Assessee-company was engaged in

hire-purchase, leasing, purchase and sale of shares and other related activities - Authorised Officer conducted search under section 132 on 24-1-1996 at registered office of assessee-company and residential premises of its two directors 'Y' and 'B' and seized certain share certificates - Before conclusion of search, 'B', 'Y' and other promoters of assessee-company filed affidavits, admitting total undisclosed income of Rs. 40 lakh - Thereafter, assessee-company in response to notice issued under section 158BC on 22-4-1996 filed block return disclosing total undisclosed income at Nil - Assessing Officer, however, made assessment under section 158BC on 30-5-1997 determining total undisclosed income at Rs. 38,64,000, which comprised of certain amounts introduced in names of investors and value of share certificates seized during search operation - Assessing Officer treated those amounts and value of share certificates as benami investments in share capital of assessee-company and added same as unexplained cash credits under section 68, in hands of assessee - Whether share capital introduced in assessee-company, which was recorded in account books of assessee-company and had been part of record furnished by assessee to department, could be considered as undisclosed income for purposes of Chapter XIV-B - Held, no - Whether therefore, impugned additions made to income of assessee-company was beyond jurisdiction of Chapter XIV-B and same was to be deleted - Held, yes



Section 158BE, read with section 158BC, of the Income-tax Act, 1961 - Block assessment in search cases - Time-limit for completion of - Block period from 1986-87 to 1996-97 - A search conducted under section 132 on 24-1-1996 at registered office of assessee-company, was concluded on 22-4-1996 - Assessing Officer gave a notice under section 158BC to assessee-company on 22-4-1996, whereas search proceedings against assessee were concluded after 22-4-1996 - Thereafter, Assessing Officer passed assessment order under section 158BC on 30-5-1997 - Whether, by issuing a notice under section 158BC prior to conclusion of search, Assessing Officer had invoked a particular provision and, thus, was bound by time-limit prescribed under section 158BE - Held, yes - Whether therefore, assessment should have been completed on 30-4-1997 but same being completed only on 30-5-1997, was barred by limitation - Held, yes

CIT V. Bal Krishan Jagdish Chand 164 Taxman 459 (Pun & Har.)

The assessee had made certain payments in cash to two parties on one day in small instalments. In each transaction individual cash payment was below Rs. 2,500 (Now Rs. 20,000/-). The ITO, however, aggregated the aforesaid amounts and added same to the assessee's income on the ground that cash payments were made in violation of section 40A(3). On appeal, the Commissioner (Appeals) held that clubbing of several cash payments made to two firms on one day was unwarranted and different entries recorded in the books of account on a particular day were required to be treated as independent entries. The Commissioner (Appeals), accordingly, held that section 40A(3) could not be applied. The appellate authority had also relied upon rule 6DD(j) and the Board Circular No. 220, dated 31-5-1977 and, thus, deleted the additions. On revenue's appeal, the Tribunal upheld the order of the Commissioner (Appeals).

The Hon'ble High Court held that a perusal of section 40A(3) shows that no deduction concerning payments made by an assessee is to be allowed, if the payment exceeding Rs. 2,500 has been made otherwise than by a crossed-cheque. A perusal of the accounts submitted by the assessee as reproduced in the assessment order would show that an amount of Rs. 2,500 or even less than that amount had been paid by the respondent-assessee. Once this was the factual position, then the rigours of section 40A(3) as it

stood in the assessment year 1986-87, would not be attracted to the facts of the instant case. [Para 6]

There were further findings that the payments had been found to be made after banking hours which had been found to be appropriate after looking into the exigencies of business. Further the Tribunal had also correctly applied the view taken by the Orissa High Court in CIT v. Aloo Supply Co. [1980] 121 ITR 680. [Para 7]

Therefore, the Tribunal was right in law in holding that various cash payments made to one party on one day were not required to be clubbed and treated as one cash payment and, for that reason, total cash payments exceeding Rs. 2,500 in a day to that party were not to be held as violative of section 40A(3).

Narita Investments (P.) Ltd. V. CIT 17 SOT 428 (Mum.)

Section 271(1)(c) of the Income-tax Act, 1961 - Penalty - For concealment of income - Assessment year 1998-99 - Whether mere mentioning at bottom of assessment order that penalty proceedings is to be initiated is not sufficient to hold that Assessing Officer has satisfaction before initiating penalty proceedings under section 271(1)(c) and recording of satisfaction should be properly worded in assessment order - Held, yes - Assessee-builder was following completed project method of accounting - Subsequently, assessee on basis of expert opinion changed method of valuation of closing stock and revalued work-in-progress in respect of its commercial and residential projects - Assessing Officer discarded method of accounting followed by assessee and recomputed profits of assessee and, accordingly, made certain addition to income of assessee - Further, he also added footnote in assessment order with a direction to issue penalty notice under section 271(1)(c) and, accordingly, levied penalty upon assessee - Whether since in entire body of assessment order no satisfaction regarding any condition which attracted penalty under section 271(1)(c) was recorded by Assessing Officer, penalty under section 271(1)(c) could not be levied upon assessee simply by adding footnote in assessment order regarding same - Held, yes

Circulars / Notifications

[F.No.142/25/2007-TPL]

Valuation of specified security or sweat equity share being a share in the company.

40C. (1) For the purposes of clause (ba) of sub-section (1) of section 115WC, the fair market value of any specified security or sweat equity share, being an equity share in a company, on the date on which the option vests with the employee, shall be determined in accordance with the provisions of sub-rule (2) or sub-rule (3).

(2) In a case where, on the date of the vesting of the option, the share in the company is listed on a recognized stock exchange, the fair market value shall be the average of the opening price and closing price of the share on that date on the said stock exchange:

Provided that where, on the date of vesting of the option, the share is listed on more than one recognized stock exchanges, the fair market value shall be the average of opening price and closing price of the share on the recognised stock exchange which records the highest volume of trading in the share:

Provided further that where, on the date of vesting of the option, there is no trading in the share on any recognized stock exchange, the fair market value shall be -

(a) the closing price of the share on any recognised stock exchange on a date

closest to the date of vesting of the option and immediately preceding such date; or

(b) the closing price of the share on a recognised stock exchange, which records the highest volume of trading in such share, if the closing price, as on the date closest to the date of vesting of the option and immediately preceding such date, is recorded on more than one recognized stock exchange.

(3) In a case where, on the date of vesting of the option, the share in the company is not listed on a recognized stock exchange, the fair market value shall be such value of the share in the company as determined by a merchant banker on the specified date.

(4) For the purpose of this rule,-

(a) "closing price" of a share on a recognised stock exchange on a date shall be the price of the last settlement on such date on such stock exchange:

Provided that where the stock exchange quotes both "buy" and "sell" prices, the closing price shall be the "sell" price of the last settlement.

(b) "merchant banker" means category I merchant banker registered with Security and Exchange Board of India established under section 3 of the Securities and Exchange Board of India Act, 1992 (15 of 1992);

(c) "opening price" of a share on a recognised stock exchange on a date shall be the price of the first settlement on such date on such stock exchange:

Provided that where the stock exchange quotes both "buy" and "sell" prices, the opening price shall be the "sell" price of the first settlement.

(d) "recognised stock exchange" shall have the same meaning assigned to it in clause (f) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);

(e) "specified date" means,-

(i) the date of vesting of the option; or

(ii) any date earlier than the date of the vesting of the option, not being a date which is more than 180 days earlier than the date of the vesting;

(f) "equity share" shall have the meaning assigned to it in section 85 of the Companies Act, 1956 (1 of 1956).

F. No. 225/147/2007-IT(A-II)(Pt.), Dated 31-10-2007

In view of the technical difficulties being faced by taxpayers in filing their returns in electronic format, the Central Board of Direct Taxes, in exercise of powers conferred under section 119 of the Income-tax Act, 1961, hereby allows the returns and reports of audit detailed below to be filed up to 15th day of November, 2007 instead of 31st day of October, 2007 in case of companies and firms which are required to furnish e-returns for assessment year 2007-08.

1. Report of audit under section 44AB of the Income-tax Act, 1961 and the return of income under sub-section (1) of section 139.

2. Return of fringe benefits under sub-section (1) of section 115WD.

Circular No. 7/2007 dated 23-10-2007

The Board had issued Circular No. 790 dated 20th April, 2000, laying down the procedure for refund of tax deducted under section 195, in certain situations to the person deducting the tax at source from the payment to the non-resident. Representations have been received in the Board from taxpayers requesting that the said Circular may be amended to take into account situations where genuine claim for refund arises to the person deducting the tax at source from payment

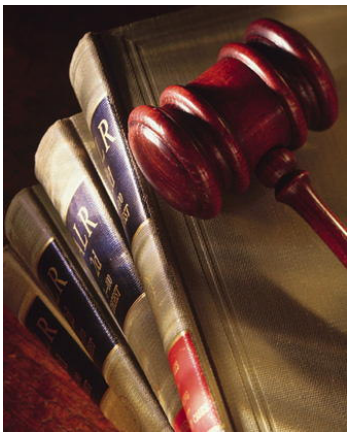
to the non-resident and it does not fall in the purview of the said Circular.

The cases which are being referred to the Board mainly relate to circumstances where, after the deposit into Government account of the tax deducted at source under section 195,

a) the contract is cancelled and no remittance is made to the non-resident;

b) the remittance is duly made to the non-resident, but the contract is cancelled. In such cases, the remitted amount has been returned to the person responsible for deducting tax at source;

c) the contract is cancelled after partial execution and no remittance is made to the non-resident for the non-executed part;



d) the contract is cancelled after partial execution and remittance related to non-executed part is made to the non-resident. In such cases, the remitted amount has been returned to the person responsible for deducting the tax at source or no remittance is made but tax was deducted and deposited when the amount was credited to the account of the non-resident;

e) there occurs exemption of the remitted amount from tax either by amendment in law or by notification under the provisions of Income-tax Act, 1961;

f) an order is passed under section 154 or 248 or 264 of the Income-tax Act, 1961 reducing the tax deduction liability of a deductor under section 195;

g) there occurs deduction of tax twice from the same income by mistake;

h) there occurs payment of tax on account of grossing up which was not required under the provisions of the Income-tax Act, 1961;

i) there occurs payment of tax at a higher rate under the domestic law while a lower rate is prescribed in the relevant double taxation avoidance treaty entered into by India.

In the cases mentioned above, income does not either accrue to the non-resident or it accrues but the excess amount in respect of which refund is claimed, is borne by the deductor. The amount deducted as tax under section 195 and paid to the credit of the Government therefore belongs to the deductor. At present, a refund is given only on a claim being made by the non-resident with whom the transaction was intended or in terms of Circular No. 790 dated 20th April, 2000.

In the type of cases referred to in sub-paragraph (a) of paragraph 2, the non-resident not having received any payment would not apply for a refund. For cases covered by sub-paragraph (b) to (i) of paragraph 2, no claim may be made by the non-resident where he has no further dealings with the resident deductor of tax or the tax is to be borne by the resident deductor. This resident deductor is therefore put to genuine hardship as he would not be able to recover the amount deducted and deposited as tax.

The matter has been considered by the Board. In the type of cases referred to above, where no income has accrued to the non-resident due to cancellation of contract or where income has accrued but no tax is due on that income or tax is due at a lesser rate, the amount deposited to the credit of Government to that extent under section 195, cannot be said to be “tax”.

It has been decided that, this amount can be refunded, with prior approval of the Chief Commissioner of Income-tax or the Director General of Income-tax concerned, to the person who deducted it from the payment to the non-resident, under section 195.

INDIRECT TAXES

Judicial pronouncements

K.R. Alloys Ltd. V. Commissioner of Central Excise 10 STT 510 (2007)

Section 65 of the Finance Act, 1994 - Management consultant - Whether essence of management consultancy is that service should be rendered only to an organization and service rendered to an individual cannot be considered as management consultancy service - Held, yes - Whether where assessee helped 'R' in purchasing assets of some other company for which it received consideration, amount paid by 'R' was in nature of commission and, therefore, assessee could not be held liable to pay service tax under category of 'Management consultancy service' - Held, yes [Paras 2 and 3]

Where the assessee engaged in sugar manufacturing process took over the management of another mill under an agreement and revenue treated said contract as a management consultancy agreement and demanded service tax, since the assessee was in charge of operation of the factory, it was performing management function and was not a management consultant.

Metro Shoes (P.) Ltd. V. Commissioner of Central Excise 10 STT 462 (2007)

Rule 2(l) of the Cenvat Credit Rules, 2004 - Cenvat credit - Input service - Whether commission agents prima facie do promote sale and once definition of 'input service' includes services used for advertisement or sale promotion and market research, same shall be squarely covered by definition of 'input service', more so when it forms part of assessable value for which no deduction is permissible - Held, yes - Whether where assessee-manufacturer claimed Cenvat credit for service tax paid in respect of commission agent services for promoting sale of goods manufactured by it and in respect of advertisement services, assessee was entitled to such credit and, therefore, was entitled to waiver of pre-deposit of tax demanded on denial of such credit - Held, yes [Para 3]

OTHER LAWS

Sabitha Ramamurthy V. R.B.S. Channabasavaradhya [2007] 79 SCL 55 (SC) (Mag.)

Section 141 of the Negotiable Instruments Act, 1881 - Dishonour of cheque for insufficiency, etc., of funds in account - Offences by companies - Whether a person can be made vicariously liable for offence committed by company, only if requisite statements, which are required to be averred in complaint petitions, are made - Held, yes - Whether where no averment was made in complaint that appellants were in charge of business of company at relevant time, processes issued by Court against appellants were to be quashed - Held, yes

***P.P. Zibi Jose* v. *Catholic Syrian Bank Ltd* 79 SCL 345 (CLB) Chennai**

Section 111A of the Companies Act, 1956 - Transfer of shares - Rectification of register on - Whether a shareholder of a public company has every right to decide number of shares to be transferred out of his total holding and, therefore, no restriction can be imposed on any shareholder in respect of number of shares which can be transferred or sold by such a shareholder - Held, yes

The best way to find yourself is to lose yourself in the service of others.

Circulars / Notifications

RBI/2007-08/171 A. P. (DIR Series) Circular No. 15 October 29, 2007

Booking of Forward Contracts - Liberalisation

The persons resident in India have been allowed to enter into forward contracts on the basis of underlying exposures. Further, exporters and importers have also been allowed to book forward contracts on the basis of declaration of exposures and based on past performances, subject to specified conditions.

With a view to provide greater flexibility to the Small and Medium Enterprises (SME) sector and resident individuals, it has been decided to further liberalise the scope and range of forward contracts to facilitate such entities to hedge their foreign currency exposures on a dynamic basis. In order to enable Small and Medium Enterprises (SMEs), having direct and / or indirect exposures to foreign exchange risk to manage their exposures effectively, it has been decided to allow AD Category – I banks to permit such entities to book / cancel / rebook / roll over forward contracts without production of underlying documents, subject to certain conditions as specified.

SMEs are also permitted to use foreign currency rupee options for hedging their exposures after production of underlying documents or under past performance route.

In order to enable resident individuals to manage / hedge their foreign exchange exposures arising out of actual or anticipated remittances, both inward and outward, it has been decided to permit them to book forward contracts, without production of underlying documents, up to a limit of USD 100,000, based on self declaration. The contracts booked under this facility would normally be on a deliverable basis. However, in case of mismatches in cash flows or other exigencies, the contracts booked under this facility may be allowed to be cancelled and re-booked. The notional value of the outstanding contracts should not exceed USD 100,000 at any time. Further, the contracts may be permitted to be booked up to tenors of one year only.

Such contracts may be booked through AD Category I banks with whom the resident individual has banking relationship, on the basis of an application-cum-declaration in the format given in Annex I. The AD Category – I banks should satisfy themselves that the resident individuals understand the nature of risk inherent in booking of forward contracts and should carry out due diligence regarding "*user appropriateness*" and *"suitability*" of the forward contracts to such customer.

AD Category – I banks are required to submit a quarterly report to the Chief General Manager, Reserve Bank of India, Foreign Exchange Department, Central Office, Forex Markets Division, Central Office Building, Mumbai - 400 001 within the first week of the following month, as per format given in Annex II. The first quarterly report should be submitted for the quarter ended December 2007 so as to reach Reserve Bank within the first week of January 2008.

Necessary amendments to Notification No. 25/2000-RB dated 3rd May 2000 [Foreign Exchange Management (Foreign Exchange Derivative Contracts) Regulations, 2000] are being issued separately.

RBI/2007-08/161 A. P. (DIR Series) Circular No. 14 A. P. (FL Series) Circular No. 01 October 17, 2007

Attention of all Authorised Persons is invited to the Anti-Money Laundering guidelines for Authorised Money Changers. In view of the difficulties expressed by Money Changers Association in implementing some of the guidelines, it has been decided to amend the following instructions of the aforementioned circulars (the Circulars).

(a) In terms of paragraph 4 (c) of the Annex to A. P. (DIR Series) Circular No.39 {A. P. (FL Series) Circular No.02} dated June 26, 2006 requests for payment in cash by foreign visitors /

non-resident Indians may be acceded to the extent of USD 2000 or its equivalent. This limit has been raised to USD 3000. All other provisions of paragraph 4(c) of the Annex to the Circulars remain unchanged.

(b) In terms of paragraph 6 of Annex to A. P. (DIR Series) Circular No.18 {A.P. (FL Series) Circular No.01} dated December 2, 2005, relationship with a business entity like a company / firm should be established only after obtaining and verifying suitable documents in support of the name, address and business activity, such as certificate of incorporation under the Companies Act 1956, Memorandum of Association, Articles of Association, registration certificate of a firm (if registered), partnership deed, etc. It has now been decided that in addition to the above mentioned documents, PAN Card may also be accepted as a suitable document for establishing the relationship with the company / firm. All other provisions of paragraph 6 of the Annex to aforementioned circular shall remain unchanged.

(Full text of any circular/notification/judicial pronouncement can be sent from our office)

Due Dates of key compliances pertaining to the month of November - 07:

5th Nov.	**Payment of Service Tax & Excise duty for October**
6th Nov.	**Payment of Excise duty paid electronically through internet banking**
7th Nov.	**TDS/TCS Payment for October**
10th Nov.	**Excise Return ER1 / ER2 /ER6**
15th Nov.	**PF Contribution for October, Excise payment by SSI**
15th Nov.	**Return of Income for Corporate Assessees**
	ROI for non-corporate Assessees whose accounts are required to be audited under any law
21st Nov.	**ESIC Payment for October**

On Diwali and in the coming year,
May you be blessed with
Success, Prosperity and Happiness !

SUBH DIWALI

There is more to life than simply increasing its speed.