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SNK Newsletter

DIRECT TAXES

Judicial Pronouncements

ACIT v. Reliance Consolidated Enterprises Pvt. Ltd. (2009)-TIOL-233-ITATMumbai

As investments in shares were not out of the borrowed funds, interest on the same cannot be disallowed under section 14A

The tribunal held that from the details submitted by the taxpayer it was quiet clear that no part of the borrowings was invested in shares and therefore, the provision of section 14A were not applicable to the facts of the present case. Accordingly, the tribunal set aside the order of the CIT(A) on this issue and directed the AO not to disallow any amount on account of interest by applying the provisions of section 14A of the Act. However, as regards the administrative expenses, the disallowance of an amount of INR 0.1 million on ad-hoc basis being attributable towards earning the exempted dividend income was justified.

Mimosa Investment Co.(P.)Ltd. v. ITO (2009) 28 SOT 470 (Mumbai)

When the taxpayer gives an appropriate note in the return of income, no penalty can be levied while making disallowance under section 14A

The tribunal observed that the taxpayer had furnished a note along with the return of income stating that the interest expenditure was not considered as disallowed under section 14A as the investments had not been made for the purpose of earning dividend income but for business consideration including capital appreciation. It further observed stated that if any interest was to be considered as being in relation to dividends earned, disallowance would amount to INR 4.1 million.

The tribunal held that the taxpayer had disclosed all the relevant material facts for the purpose of computation of income.

The taxpayer had also offered explanation in this regard, which was not found to be false by the AO. Thus, the explanation of the taxpayer regarding claim of interest expense was bona fide. Mere fact that there was a difference in the total income calculated by the taxpayer and AO, it could not be held that the taxpayer had concealed the income.

Thus, mere non acceptance of the explanation offered by the taxpayer cannot form the basis for initiating the penalty proceeding under section 271(1)(c) of the Act.

In view of above, the penalty levied by the AO under section 271(1)(c) of the Act, was deleted.

ITO vs. VRM Share Broking (P.) Ltd. (2009) 27 SOT 469 (Mum.)

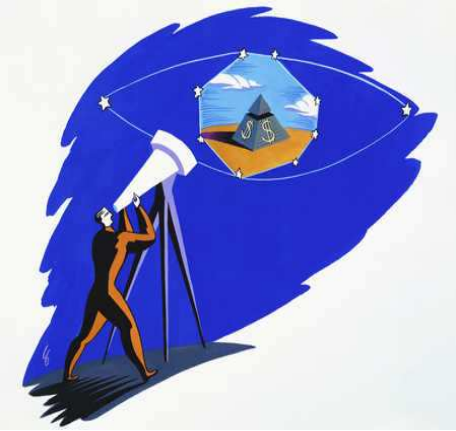
Business Expenditure - Section 28(i) & 37(1)

Penalty paid on account of failure to maintain, margin money and not recovered from client, was an allowable loss. Moreover, penalty paid to SEBI for 'excess utilisation limits' was an allowable business expense.

BASF India Ltd. v. Addl. CIT (ITA NO. 4287/MUM/2005)(Mumbai ITAT)

Taxability of receipts for the transfer of marketing rights and non-compete fee

Where an amount is received by the assessee towards its income generating assets, then it is a capital receipt; on the other hand, if the receipt is towards the loss of income and not the source of income, then it is of revenue nature attracting the liability to tax.



Accelerated Freez & Drying Co. Ltd. v. DCIT (ITA No. 971/ Coch/2008)

Assessability of term loan when waived by banks under one-time settlement scheme

The waiver amount of term loan availed by the assessee does not partake the character of assessable income either under section 28(iv) or under section 41(1) of the Income-tax Act, 1961.

Tamil Nadu Road Development Co. Ltd. v. ACIT (Chennai ITAT)

Allowability of depreciation on construction of road wherein optical fibre lines have been laid

Merely because some optical fibre lines or connection lines have been laid, the road cannot get converted into a plant; even if the assessee constructs some restaurant etc., on a particular road or provides some other amenities, then on such assets depreciation may be claimed as per Appendix but that would not convert the nature of the main asset i.e., the road into plant.

Rotork Controls vs. CIT (Supreme Court) (Civil Appeal Nos. 3506-3510 Of 2009)

Estimated expenditure towards warranty is allowable u/s 37 (1)

The assessee sold valve actuators. At the time of sale, the assessee provided standard warranty that if the product was defective within the stated period, the product would be rectified or replaced free of charge. For AY 1991-92, the assessee made a provision for warranty at Rs.10,18,800 at the rate of 1.5% of the turnover. As the actual expenditure was only Rs. 5,18,554, the excess provision of Rs.5,00,246 was reversed and only the net provision was claimed. The Tribunal allowed the claim on the basis that the provision had been consistently made and on a realistic manner. The High Court reversed the Tribunal on the basis that the liability was contingent and not allowable u/s 37 (1). HELD, reversing the High Court that:

(1) A provision is a liability which can be measured only by using a substantial degree of estimation. A provision is recognized when: (a) an enterprise has a present obligation as a result of a past event; (b) it is probable that an outflow of resources will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision can be recognized;

(2) A Liability is defined as a present obligation arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits;

(3) A past event that leads to a present obligation is called as an obligating event. The obligating event is an event that creates an obligation which results in an outflow of resources. It is only those obligations arising from past events existing independently of the future conduct of the business of the enterprise that is recognized as provision. For a liability to qualify for recognition there must be not only present obligation but also the probability of an outflow of resources to settle that obligation. Where there are a number of obligations (e.g. product warranties or similar contracts) the probability that an outflow will be required in settlement, is determined by considering the said obligations as a whole;

(4) In the case of a manufacture and sale of one single item the provision for warranty could constitute a contingent liability not entitled to deduction u/s 37 of the said Act. However, when there is manufacture and sale of an army of items running into thousands of units of sophisticated goods, the past event of defects being detected in some of such items leads to a present obligation which results in an enterprise having no alternative to settling that obligation;

(5) On facts, the assessee has been manufacturing and selling Valve Actuators in large numbers since 1983-84 onwards. Statistical data indicates that every year some Actuators are found to be defective. The data over the years also indicates that being sophisticated item no customer is prepared to buy the Valve Actuator without a warranty. Therefore, warranty became integral part of the sale price of the Valve Actuator(s). In other words, warranty stood attached to the sale price of the product and a reliable estimate of the expenditure towards such warranty was allowable.

CIT v. Mcdowell & Co. Ltd. (Civil Appeal No. 3471 of 2007)(SC)

Furnishing of bank guarantee cannot be equated with actual payment which requires that money must flow from assessee to public exchequer as required under Section 43B of IT Act

By no stretch of imagination it can be said that furnishing of bank guarantee is actual payment of tax or duty in cash; the bank guarantee is nothing but a guarantee for payment on some happening and that cannot be actual payment as required under section 43B for allowance as deduction in the computation of profits.

ITO v. AIR Developers (ITA NO. 447/Nag/2007)(Nagpur ITAT)

Eligibility of exemption under section 80-IB (10) of IT Act, 1961

If an assessee has developed a housing project, wherein the majority of the residential units has a built-up area of less than 1500 sq.ft. i.e., the limit prescribed by section 80-IB(10) and only a few residential units are exceeding the built-up area of 1500 sq. ft., there would be no justification to disallow the entire deduction under section 80-IB(10); it would be fair and reasonable to allow the deduction on proportionate basis in that case.

CIT vs. Ajanta Pharma (Bombay High Court) (ITA No. 1005 OF 2008)

Sunset clause of s. 80HHC (1B) applies to s. 115JB

In respect of AY 2001-2002, the assessee claimed that though s. 80HHC (1B) limited the deduction to 80% of the profits eligible for deduction u/s 80HHC, this limitation did not apply for purposes of "book profits" u/s 115JB and that 100% of the 80HHC profits were deductible. The Tribunal allowed the claim by relying on the Special Bench judgement in Syncome Formulations 106 ITD 193 (Mum) (SB) and the Budget speech of the Finance Minister. On appeal by the Revenue, HELD, reversing the Tribunal's order:

(1) S. 115JB allows a deduction from the "book profits" of "the amount of profits eligible for deduction u/s 80HHC, computed under clause (a) …. of sub-section (3) …. subject to the conditions specified in that section." Ss (3) and (3A) provide for the method for computation of profits. Once the profits are worked out, then only the profit which is eligible can be deducted. In computing the "eligibility", the limits of s. 80HHC (1B) have to be read in;

(2) Accepting the argument that MAT companies are not subject to the limits of s. 80HHC (1B) would mean that they are treated more advantageously than other export companies. There is no rational reason why the legislature would give MAT companies additional benefits than that given to other companies;

(3) The argument also renders s. 80HHC (1B) irrelevant and otiose for s. 115JB and results in the absurdity that MAT companies will enjoy exemption even after AY 2005-2006 when s. 80HHC ceases to operate;

(4) The Budget Speech and the Memorandum explaining the Bill are external aids to construction and reliance on them is not permissible as there is no absurdity on a literal reading of s. 80 HHC r.w.s. 115JB(2);

Genom Biotech v. DIT (Writ Petition No. 2429 of 2008) (Bombay HC)

Reasons for search action u/s 132 need not be given to the assessee

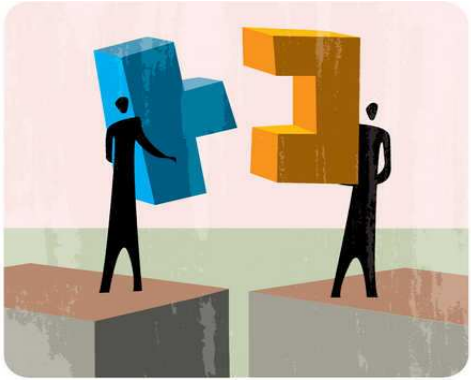
Search & seizure action u/s 132 was undertaken at the assessee's premises. Thereafter an order of provisional attachment u/s 281B was passed. The assessee filed a writ petition challenging the validity of the search and the provisional attachment. HELD dismissing the Petition:

(1) Search action u/s 132 can be initiated only if the designated authority forms a reasonable belief on the basis of information that one of the three conditions of s. 132 exist. However, it is not the mandate of s. 132 that the reasonable belief recorded by the designated authority must be disclosed to the assessee.

(2) On facts, the search was justified as the information received showed that the assessee had evaded tax by claiming deduction of business expenditure of Rs.170 allegedly paid to Cyprus / UK based companies towards marketing and advertisement expenses, but which were in fact credited by the said Cyprus & U.K. based companies in the private bank account of the assessee's CMD in Cyprus.

(3) Attaching the properties of an assessee u/s 281B even before crystallization of the demand is a drastic step and has to be exercised only in extreme circumstances. On facts, as the incriminating documents prima facie established large scale tax fraud and as the assessee and as the assessee had failed to explain the same, the provisional attachment to protect the revenue's interests was justified.

(4) Provisional attachment u/s 281B can be levied even where proceedings are yet to be initiated. Accordingly, the fact that notice u/s 153A and the order u/s 281B were issued on the same date did not affect the validity of the provisional attachment.



S.R. Batliboi & Co. V. DIT (Investigation) (Delhi HC)

Auditors cannot be forced to part with information of clients not related to search found in their laptops

During the audit of EMAAR, laptops were seized. Petitioner on request of Deputy Director, Income Tax (DDIT) provided the electronic data relating to three companies of the EMAAR Group together with the print copies of the data. Nevertheless, the DDIT insisted on securing total and unrestricted access to the laptops obviously in order to gain information and data of all the other clients of the Petitioner. Held that Revenue is not empowered to make use of material stumbled in a Search against a third party. Impugned summons are set aside, and Respondents are directed to return the laptops to Petitioner.

Dresser Valve India Pvt. Ltd. v. ACIT (ITA No. 6464/Mum/2007)(Mumbai ITAT)

Determination of book profit vis-à-vis provision of gratuity

The provision of gratuity is an ascertained liability and the same falls outside scope of the provisions of clause (c) of the Explanation 1 to section 115JB of the Income-tax Act, 1961 warranting no addition to the `book profits'

ITO v. Vijeta Educational Society (2009) 118 ITD 382 (LUCK.)

Estimate by Valuation Officer in certain cases

Reference to valuation cell under section 142A can be made during course of assessment and reassessment and not for purpose of initiating reassessment. Further, where Assessing Officer had not rejected books of account by pointing out any defect, reference to DVO for valuation of cost of construction of building incurred by assessee was not valid and, therefore, DVO's report could not be utilised for framing assessment/ reassessment even if such a report was considered to be obtained under section 142A.

Microsoft Regional Sales Corpn. v. ADIT (ITA NO. 991 & 992/DEL/2005) (Delhi ITAT)

Power of Assessing Officer to change nature and character of income under section 143(1) of IT Act, 1961

Nature and character of income as disclosed in return of income cannot be changed to, or substituted by, another nature and character while determining tax payable on that income shown in the return, under section 143 (1); the Assessing Officer's jurisdiction under section 143(1) is limited to determining tax payable or refund due on the basis of return of income and not otherwise.

Dawood Sons v. ACIT (ITA NO. 2614/MDS/2007)(Chennai ITAT)

Change in constitution of a firm

When there is a change in the constitution of a firm, it is for the assessee to seek again the status of the "firm" for the purpose of assessment by filing a certified copy of the revised deed of

partnership; it is for the assessee to choose whether to be assessed as a "firm" or to be assessed as an Association of Persons (AOP) on the constitution of a firm or on the reconstitution of a firm; if the assessee has satisfied provisions of section 184 of the Income-tax Act, it shall be assessed as a "firm" and if not, it shall be assessed as an AOP; neither the Assessing Authority nor the assessee has to go beyond this.

ACIT v. Prem Chang Garg (ITA NOS. 2250 & 2251/Del/2007)

Levy of penalty under section 271 (1)(c) of IT Act, 1961

Mere omission of the surrendered income from the return of an item of receipt does neither amount to concealment nor furnishing of inaccurate particulars of income; mere asking of a question or simply raising of an enquiry about any loan/gift does not tantamount to detection of concealment.

Judicial Pronouncements - International Taxation

Mahindra & Mahindra Ltd. v. DCIT (2009) 22 DTR (Mumbai)(SB)(Trib) 361

Question of limitation for raising additional ground in an appeal before the Tribunal

Special Bench having been constituted for deciding the question of limitation on the request of Revenue, the objection as to raising of additional ground by assessee is not maintainable now. Further, there can be no embargo on any party to raise a legal ground for the first time before the Tribunal provided the relevant material for deciding that question already exists on record and no further investigation of facts is required. Question of limitation goes to the very jurisdiction of the matter. It is not only the right of the parties but also the duty of the Tribunal to consider the question of limitation notwithstanding the fact that it is not raised before it. Additional ground admitted.

Failure to deduct tax vis-a-vis failure to deduct and deposit the tax - Assessee in default

Finance Act, 2008 has substituted s. 201(1) with retrospective effect from 1st June, 2002 by which the hitherto expression "if any such person referred to in s. 200" has been substituted with "where any person". Even prior to the amendment, s. 201(1) was applicable not only to the person who failed to deposit the tax but also who had not deducted the tax. Amendment was clarificatory in nature. By no stretch of imagination the words 'such person' referred to in s. 201 can be construed as the only person who has deducted the tax at source within the meaning of s. 200. It clearly refers to the person responsible for deducting tax at source notwithstanding whether he has failed to deduct tax at source or after deducting failed to deposit the same with the Central Government. Thus, s. 201(1) also encompasses within its ambit the person failing to deduct tax at source.

Limitation for passing order under s. 201(1) - Assessee in default

Sub-ss. (1) and (1A) of s. 201 do not prescribe any time-limit for the initiation of the proceedings or the passing of the order. In the absence of any provision for limitation, it is to be impliedly inferred by taking into consideration the scheme of the relevant provisions. Order under s. 201(1) is to be treated as an order of assessment or at least akin to the assessment order. Person responsible for deducting tax at source is to be deemed to be an assessee in default for failure to deduct tax or failure to pay TDS only if the payee of the income has also failed to pay such tax directly. Thus, the liability of the payer is dependent on the conduct of the payee, and the action under s. 201(1) is dependent on the outcome of the assessment of the payee. Both the initiation of proceedings under s. 201(1) as well as completion of such proceedings by passing order have to be prior to the time-limit within which the tax can be determined in the hands of the payee. With the expansion of scope of s. 147, the assessment of payee shall also include assessment under s. 147. Hence, proceedings under s. 201(1) can be initiated within a period of six years from the end of the relevant assessment year if the income chargeable to tax in the hands of the payee by virtue of sum paid without TDS is equal to or more than Rs. 1 lakh, and four years if such amount is less than Rs. 1 lakh. Going by the same logic and taking assistanfe from s. 153(2), the order under s. 201(1) has to be passed within one year from the end of the financial year in which proceedings under s. 201(1) are initiated. Same time-limits are applicable for initiation and passing of orders under s. 201(1 A) also—Therefore, order passed under s. 195 r/w s. 201(1) or s. 201(1A) is not barred by limitation if it is not passed within four years from the end of the relevant financial year.

Assessment not made in the hands of payee - Assessee in default

As per Explanation to s. 191, both the conditions viz., failure of the person responsible to perform his obligation and non-payment of tax by the payee directly should be cumulatively satisfied so as to treat the person responsible as the assessee in default. If only one of these two conditions is satisfied, then the person responsible cannot be treated as assessee in default. Thus, where the payee has satisfied the tax liability on his total income including the amount on which tax was deductible but not deducted, the payer cannot be treated as assessee in default. Also, if there is no or lower liability of the payee to tax on the income received without deduction of tax at source, the payer cannot be treated as assessee in default for the whole or that part of the amount, as the case may be. Thus, the question of treating the person responsible for paying the income as assessee in default is inter alia, tied with the tax liability of the payee on such sum. If no liability of the payee to tax exists at the relevant time or the liability of the payee to tax has not been determined by passing any order in his hands and the time-limit for taking action on the payee under any provision has passed out, order under s. 201(1) cannot be passed against the payer. This is so because the tax collected from the payer of income under such order would be incapable of adjustment against the tax liability of the payee as such liability cannot be created after the expiry of time-limit. In the instant case, no assessment has been made in the hands of the payee in respect of the amount paid by the assessee. Time-limit for issuing notice under.s. 148 has also come to an end. Hence, no course is left to the Revenue for making the assessment of the payee. Thus, impugned order passed under s. 195 r/w s. 201(1) or s. 201(1A) is not valid.

Payment to non-resident - TDS from Commission to lead managers in respect of GDR and FCCB

Lead managers deducted and retained their commission from the subscription money and remitted only the net amount to the assessee in India. When the total commission was retained by the non-resident lead managers, assessee credited their account directly or indirectly. Secondly, retention of the amount by the non-residents did tantamount to making of payments to them. Assessee had not only made the payment of commission to the non-residents but also credited their accounts. Hence, provisions of s. 195(1) are applicable.

Scope of appeal with Tribunal when Submission of Departmental Representative contrary to finding of AO

AO examined the provisions of DTAA between India and UK for deciding the taxability of the sums paid by the assessee to the non-residents and referred to various articles of the said DTAA at several places in his order. Thus, it is impermissible for the Departmental Representative to come out with the submission that DTAA with UK is not relevant as both the lead managers (payees) were residents of countries other than UK. Departmental Representative cannot be permitted to take a stand contrary to the one taken by the AO. He cannot set up an altogether different case

DTAA between India and UK - Fees for technical services vis-a-vis management commission, selling commission, underwriting commission etc. in respect of issues of GDR/ FCCB

Services rendered by the non-resident lead manager to the assessee company in bringing out FCCB issue in the year 1996 are in the nature of technical, managerial or consultancy services and thus the management commission as well as the selling commission fall within the scope of "fees for technical services" under s. 9(l)(vii). As regards underwriting commission, it is paid only for incurring the liability of subscribing to the unsubscribed portion left over by the general public and hence cannot fall within the scope of fees for technical services under s. 9(l)(vii). Reimbursement of expenditure cannot be considered to be in the nature of income and thus it is not income by way of fees for technical services. As regards the second DTAA between India and UK, technical knowledge, experience, skill, etc. must be made available to the assessee so as to be covered within the scope of sub-cl. (c) of cl. (4) of art. 13 and mere providing of such services without making them available to the assessee is not sufficient. Though the lead managers rendered technical, managerial or consultancy services for bringing out the FCCB issue, such services were not made available to the assessee inasmuch as it only derived the benefit from the technical services provided by the lead managers without getting any technical knowledge, experience or skill in its possession for use as its own.

Therefore, art. 13 of said DTAA is not applicable and management and selling commission cannot be taxed in India. AO has not controverted the contention of the assessee that the non-resident had no PE in India and the AO has not treated any place as PE of the non-resident. In the absence of any PE of the non-resident in India, the 'business profits' cannot be charged to tax under art. 7 and hence underwriting commission is also outside the ambit of tax as per DTAA. Consequently, there was no obligation on the assessee to deduct tax at source under s. 195 and it cannot be treated as assessee in default for not deducting tax. However, the payments in connection with the GDR issue which was brought out in the year 1993 are governed by first DTAA between India and UK. Definition of 'fees for technical services' given in Expln. 2 to s. 9(l)(vii) has been identically incorporated in art. 13 of the first DTAA and the concept of making available technical knowledge, experience, skill, etc. as introduced in art. 13(4)(c) of second DTAA was missing in the earlier treaty. Thus, the management commission and selling commission paid to the non-resident was liable to tax in India and there was obligation to deduct tax at source under s. 195.

U.A.E. Exchange Centre Ltd. v. UOI & Anr. (2009) 22 DTR (Del) 33

Advance ruling—Maintainability of writ—Scope

Though the ruling of the Authority for Advance Rulings is binding on the applicant, the CIT and the IT authorities subordinate to him in respect of the applicant and the transaction in question as per s. 245S, it does not exclude the jurisdiction of the Courts either expressly or by implication. There is no provision which gives finality to the decision of the authority. Sec. 245S cannot be construed as an ouster clause, ousting the jurisdiction of the Court. Authority constituted under Chapter XIX-B of the Act is a Tribunal as it is invested with powers of a Civil Court by virtue of provisions of s. 131. Cumulative effect of the said powers and the attributes of the Authority show that it has the 'trappings of a Court' and would Qualify as a Tribunal within the meaning of Art. 227. Thus, the ruling of the Authority is amenable to jurisdiction under Art. 227 and more so under Art. 226 which has a wider reach.

Agreement between India and UAE - Permanent establishment

Where India has entered into a treaty for avoidance of double taxation referred to in s. 90, the contracting parties are governed by the provisions of the treaty which overrides the provisions of the Act. The Authority proceeded on a wrong premise, inasmuch as, it firstly examined the case from the point of view of s. 5(2)(b) and s. 9 (1)(i) while it was required to look at the provisions of DTAA for ascertaining the petitioner's liability to tax. Admittedly, petitioner maintains liaison offices in India and same fall within the definition of PE as per the provisions of art. 5(2)(c). However, the only activity of the liaison offices in India is to download information from the main servers located in UAE for drawing cheques on banks in India which are couriered or despatched to the beneficiaries as per the instructions of the NRI remitter. This activity is in 'aid' or 'support' of the main activity. Once an activity is construed as being subsidiary or in aid or support of the main activity, it would fall within the exclusionary clause in art. 5(3)(e). Activity carried on by the liaison offices in India did not in any manner whatsoever contribute directly or indirectly to the earning of profits by the petitioner in UAE. Thus, the impugned ruling of the Authority holding that the income of the petitioner is to be deemed to be accruing in India in India in view of s. 5 (2)(b) and s. 9(1)(i) ignoring the exclusionary clause in art. 5(3)(e) of the DTAA suffered from a mistake apparent on the face of record amenable to writ jurisdiction. Same quashed.

DIT v. Galileo International Inc. (2009) 22 DTR (Del) 254

Income deemed to accrue or arise in India - Business connection

International computerised reservation system for airlines and hotels. Assessee, a US company deriving income through computerised reservation system (CRS) installed and maintained in USA through agent in India. Tribunal having come to the conclusion that assessee non-resident's income was chargeable to tax in India under s. 5(2) r/w s. 9(1)(i) as it had business connection in India and that 15 per cent of the revenue accruing to assessee in respect of bookings made in India should be treated as its income chargeable to tax in India and since the revenue attributable in respect of the booking made in India is only 0.45 Euro (15 per cent of Euro 3) and commission paid to agent in India was Euro 1, there was no income which was taxable in India. These findings of the Tribunal are unexceptionable and no substantial question of law arises. Contention of Revenue that Tribunal seriously erred in attributing "revenue" and not "profits" though

attractive, does not stand scrutiny as the Tribunal has in fact attributed "profits" and in doing so, the Tribunal had referred to DTAA between India and USA, Circular No. 23, dt. 23rd July, 1969, allowed commission to agent and arrived at nil income. Even by AO and CIT(A), entire payment made by assessee to its agent in India was allowed as expenses in computing income chargeable to tax in India.

ADIT (International Taxation) v. Delta Airlines Inc. (2009) 22 DTR (Mumbai)(Trib) 204

DTAA between India and USA - Income from business of international transport

Assessee a company incorporated in and tax resident of USA was engaged, in addition to the business of international air transport, in providing security screening to other airlines, and third party charter handling services. While the expression 'profits derived by an enterprise from operation of ships or aircraft in the international traffic' cannot be construed narrowly but the expression having been defined in para 2 of art. 8 of the DTAA between India and USA, the claim of exemption can be made/allowed only in accordance with such definition and cannot be extended beyond that. Neither the OECD Commentary nor the US Technical Explanation can be looked into. Any other activity directly connected with, such transportation is also exempt under art. 8(2)(b) but it is only that activity which is directly related to the transportation of passengers, etc. by the assessee itself as owner/lessee/charterer of aircraft and not by other airlines. Therefore, screening of luggage belonging to passengers of other airlines and third party charter and maintenance would be outside the scope of art. 8(2)(b) of the DTAA.

Interest on FD placed for possible income-tax liability – Exemption under Article 8 of DTAA with USA

Moreover, AO asked the assessee to hold back a sum of Rs. 6 crores in view of possible income-tax demand that may be raised on completion of the assessments. In compliance, assessee made FDs in the sum of Rs. 6 crores and earned a sum of Rs. 56.95 lacs towards interest and claimed exemption under para 5 of art. 8 of the DTAA. Claim not allowable. Deposit of amount in FDR cannot be said to be connected with the business of operation of aircrafts and so also the interest thereon.

Chargeability of Interest under s. 234B - Income subject to TDS

Tax on income being deductible at source, question of levy of interest u/s. 234B does not arise (Motorola Inc. v. DCIT (2005) 96 TTJ (Del)(SB) 1 followed).

Canoro Resources Ltd., In Re (2009) 223 CTR (AAR) 339

Advance ruling - Rejection of application under s, 245R(2), proviso— Transaction or issue designed prima facie for the avoidance of income-tax

Applicant company, registered in Canada, engaged in the business of exploration and production of petroleum and natural gas in India, holds participating interest in three oil blocks, out of which only A block has started commercial production and the remaining two are in the exploration stage. Applicant states that it proposes to restructure its business in India by transferring its participating interest in A block to a partnership firm to be formed in Canada between it and its wholly owned subsidiary company, namely, LP which is incorporated in Canada. This arrangement will make A a separate venture of the applicant and that after the proposed restructuring, A block would look more attractive to the potential investors. The objection of Revenue that in future, applicant may exit any time from A block by transferring its interest to somebody and in that event no taxes will be payable in India and thus the transaction being aimed at avoiding tax and accordingly, the application is not maintainable, is not acceptable.

Applicant has, prima facie, given a convincing explanation for restructuring its business and there is no material to view the transaction otherwise. Revenue cannot complain, when a taxpayer resorts to a legal method available to him to plan his tax liability, that the result would be more beneficial to the taxpayer. As a matter of fact, the case of the Revenue is not really that the proposed transaction itself is a tax avoidance device, but that the possible future transactions might lead to loss of revenue. Whenever that firm transfers its participating interest in A block, it would be liable to capital gains tax in India. Therefore, the Revenue's plea that prima facie the transaction is designed only with a view to avoid tax is rejected.

Assessment of Partnership Firm constituted under Partnership Act of Alberta

Partnership law of both the countries is similar. Under both the taws, the firm is not an incorporated entity separate from its members. Thus, the proposed partnership of the assessee under the Alberta Act will be a partnership firm as understood under the Indian Partnership Act notwithstanding the fact that shares of individual partners have been specified in the draft partnership agreement in terms of units. From a construction of the partnership deed as a whole individual shares of partners being clearly ascertainable, requirement of cl. (ii) ofs. 184(1) is satisfied. So far as taxability of the firm is concerned, its residential status is not relevant, as the rate rate of tax applicable to every firm is 30 per cent.

Applicability of s. 45(3) vis-a-vis transfer pricing provisions to international transaction in Computation of Capital gains

When a transaction referred to in s. 45 (3) is in the nature of international transaction, the value of consideration shall not be the value as recorded in the firm's account books, but the same shall be determined on the basis of arm's length price in accordance with transfer pricing provisions contained in Chapter X. Apprehension of price manipulation is real even in international transactions between partners and firm, who are associated persons

Applicability of provisions of Chapter X vis-à-vis Capital gains under s. 45(3) in case of International Transaction

When a transaction referred to in s. 45 (3) is in the nature of international transaction, the value of consideration shall not be the value as recorded in the firm's account books, but the same shall be determined on the basis of arm's length price in accordance with transfer pricing provisions contained in Chapter X

DTAA between India and Canada - Applicability of non-discrimination clause

Sec. 92B makes a distinction between enterprises on the basis of their residential status, and not with reference to their nationality. In view of the fact that a cross-border transaction between Indian nationals, one or both of whom are non-residents and who are associated enterprises, will also attract the transfer pricing provisions, as they would apply to similarly situated Canadian nationals, the plea o discrimination raised by applicant, a Canadian company, has no basis.

E-Gain Communication (P.) Ltd. v. ITO (2009) 118 ITD 243 (PUNE)

Section 92C of the Income-tax Act, 1961, read with1962 - Computation of arm's length price Rule 10B of the Income-tax Rules,

Assessee-company was engaged in business of software product development and was a 100% EOU unit approved by Software Technology Park of India under STPI Scheme. Assessee had supplied software developed by it to its parent company in US as per specific requirement of parent company. As per agreement between assessee and its parent company, it was to receive actual cost plus 5 per cent markup for software developed and supplied to parent company. For relevant assessment year assessee as per audited accounts declared certain profit. Assessing Officer, after noticing details of transac-tions of assessee with its associated concern, referred case to Transfer Pricing Officer (TPO) for computation of arm's length price. TPO noted that assessee had claimed net profit margin on cost at 5.16% against average profit of 16.12%. Comparable enterprises were taken into account for applying Transactional Net Margin Method (TNMM). Profit Before Income (PBIT) with reference to Total Turnover (TO) and total expenses were taken at 13.29% and 16.12%, respectively. Thereupon, TPO after having issued show-cause notice to assessee made adjustment of Rs. 1.08 crore in arm's length price. Commis-sioner (Appeals) upheld action of Assessing Officer. On instant appeal, it was seen from records that while making addition Commissioner (Appeals) had taken into account only turnover of comparable companies but had ignored large number of other material factors such as function performed; assets employed; risk taken (FAR) analysis, etc. Moreover, assessee had shown that out of 20 comparables, two companies were showing extraordinary profits as they had income from sources other than business of software development. It was further noted that as per working given, profit margin of assessee was quite comparable with aver-age profit margin taken into account by revenue other than for two companies mentioned above. It was held that in the aforesaid circumstances, there was no justification for making addition or adjustment for arm's length price shown by assessee, therefore, impugned addition made by authorities below was to be set aside.

ACIT v. Kin Ship Services (I) Pvt. Ltd. (ITA NO. 537/COCH/2007) (Cochin ITAT)

Charter ship hire payments do not fall under category of "royalty" within meaning of section 9 of IT Act

Payments for chartering ships on hire for doing the business outside India do not satisfy the test laid down in section 9; when section 9 is not satisfied, there cannot be a case that income is deemed to accrue or arise in India as a result of hire payments made by the assessee-company to foreign ships.

Circulars / Notifications

Notification No. 46/2009, dated 22-5-2009

Section 43(5)(*d*)(*ii*) of the Income-tax Act, 1961 - Speculative transactions - Notified recognised stock exchange

In exercise of the powers conferred by clause (*ii*) in the Explanation to clause (*d*) of the proviso to sub-section (5) of section 43 of the Income-tax Act, 1961 (43 of 1961), read with rule 6DDB of the Income-tax Rules, 1962, the Central Government **hereby notifies MCX Stock Exchange Ltd. as a recognized stock exchange** for the purpose of the said clause with effect from the date of publication of this notification in the Official Gazette.

2. MCX Stock Exchange Ltd. shall separately maintain data regarding all transactions registered in the system in which client codes have been allowed to be changed for periodical inspection by the Director-General of Income-tax (Investigation) having jurisdiction over such exchange and provide copies of the relevant information as and when required.
3. The Central Government may withdraw the recognition granted to MCX Stock Exchange Ltd. if any of the conditions specified in rule 6DDA of the Income-tax Rules, 1962, subject to which the recognition is granted, is violated.
4. This notification shall remain in force until the approval granted by the Securities and Exchange Board of India is withdrawn or expires, or this notification is rescinded by the Central Government as provided in sub-rule (5) of rule 6DDB of the Income-tax Rules, 1962.

[F. No. 142/25/2008-TPL]

Circular No. 02 / 2009, Dated 21-5-2009

New Tds And Tcs Payment And Information Reporting System-Notification No. 858(E), Dated 25th March, 2009 Published In Official Gazette.

INDIRECT TAXES

Judicial Pronouncements

CCE & C v. Zodiac Advertisers (CE Appeal No. 21 of 2006)(Kerala HC)

Activities which answer description of "advertisement" and "advertising agency" under definition clause of Finance Act, 1994

The making and sale of advertising materials for customers in the form of banner or hoarding or film-slide, etc. is `advertisement' as defined under section 65(2); all commercial concerns engaged in any of the activities connected with advertisement, which includes making, preparing, displaying or exhibition of advertisement, answer the description of `advertising agency'.

Kopran Ltd. v. CCE (Application No. ST/S/1046/08)(In Appeal No. ST/158/08)(CESTAT-Mumbai)

Levy of Service tax on transfer of trade mark/brand name

The transfer of brand name does not have any meaning for the buyer until and unless the know-how for the manufacture of the formulations sold under that particular brand name, is also transferred.

UOI vs. Rajasthan Spinning (Supreme Court) (Civil Appeal No. 3527 OF 2009)

Supreme Court explains UOI vs. Dharmendra Textile 306 ITR 277 (SC)

Held in the context of s. 11AC of the Excise Act (which provides that where any duty of excise has not been .. paid .. by reasons of fraud, collusion or any willful mis-statement or suppression of facts ….. or contravention of any of the provisions of this Act … with intent to evade payment of duty,

the person who is liable to pay duty as determined under sub-section (2) of section 11A, shall also be liable to pay a penalty equal to the duty so determined) that

(1) "At this stage, we need to examine the recent decision of this Court in Dharemendra Textile (supra). In almost every case relating to penalty, the decision is referred to on behalf of the Revenue as if it laid down that in every case of non-payment or short payment of duty the penalty clause would automatically get attracted and the authority had no discretion in the matter. One of us (Aftab Alam,J.) was a party to the decision in Dharmendra Textile and we see no reason to understand or read that decision in that manner."

(2) After quoting from Dharmendra Textiles "we fail to see how the decision in Dharamendra Textile can be said to hold that section 11AC would apply to every case of non-payment or short payment of duty regardless of the conditions expressly mentioned in the section for its application."

(3) "There is another very strong reason for holding that Dharamendra Textile could not have interpreted section 11AC in the manner as suggested because in that case that was not even the stand of the revenue."

(4) "The decision in Dharamendra Textile must, therefore, be understood to mean that though the application of section 11AC would depend upon the existence or otherwise of the conditions expressly stated in the section, once the section is applicable in a case the concerned authority would have no discretion in quantifying the amount and penalty must be imposed equal to the duty determined under sub-section (2) of section 11A. That is what Dharamendra Textile decides".

OTHER LAWS

FEMA

Foreign Exchange Management (Current Account Transactions) (Amendment) Rules, 2009

Notification No. G.S.R. 349(E), dtd. 31-05-2009

In exercise of the powers conferred by sub-section (1) and clause (*a*) of sub-section (2) of section 46 of the Foreign Exchange Management Act, 1999 (42 of 1999) and in consultation with the Reserve Bank, the Central Government, having considered it necessary in the public interest, hereby makes the following further amendments in the Foreign Exchange Management (Current Account Transactions) Rules, 2000, namely:—

1. Short title and commencement - (1) These rules may be called the Foreign Exchange Management (Current Account Transactions) (Amendment) Rules, 2009

(2) They shall come into force on such date as specified in the provisions of these rules.

2. In the Foreign Exchange Management (Current Account Transactions) Rules, 2000, in Schedule III,-

(1) (i) for item numbers 2 and 3 and the entries relating thereto, the following item numbers and the entries shall be substituted, namely :—

"2. Release of exchange exceeding US$ 10,000 or its equivalent in one financial year for one or more private visits to any country (except Nepal and Bhutan).

3. Gift remittance exceeding US$ 5,000 per financial year per remitter or donor other than resident individual;"

(ii) the amendments made to item numbers 2 and 3 shall be deemed to have come into force on the 20th December, 2006.

(2) for item 4 and the entries relating thereto, the following item number and the entries shall be substituted, namely:—

"4. (i) Donation exceeding US$ 5,000 per financial year per remitter or donor other than resident individual;

(ii) Donations by corporate, exceeding one per cent of their foreign exchange earnings during the previous three financial years or US$ 5,000,000, whichever is less, for,-

(a) creation of Chairs in reputed educational institutes;

(b) to funds (not being an investment fund) promoted by educational institutes; and

(c) to a technical institution or body or association in the field of activity of the donor company.

Explanation : For the purposes of these item numbers 3 and 4, remittance of gift and donation by resident individuals are subsumed under the Liberalised Remittance Scheme."

(3) for item number 15 and the entries relating thereto, the following item number and the entries shall be substituted, namely :—

"15. Remittances exceeding US$ 10,000,000 per project, for any consultancy services in respect of infrastructure projects and US$ 1,000,000 per project for other consultancy services procured from outside India.

Explanation : For the purposes of this item number 'infrastructure project' is those related to -

(i) Power,

(ii) Telecommunication,

(iii) Railways,

(iv) Roads including bridges,

(v) Sea port and airport,

(vi) Industrial parks, and

(vii) Urban infrastructure (water supply, sanitation and sewage)".

(4) after item number 16 and the entries relating thereto, the following item number and the entries shall be inserted, namely :-

"17 Remittances exceeding five per cent of the investment brought into India or US$ 1,00,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses."

(5) the amendments made to item numbers 4, 15 and 17 shall be deemed to have come into force on the 30th April, 2007.

Due Dates of key compliances pertaining to the month of June 2009:

5th June	***Payment of Service Tax & Excise duty for May***
6th June	***Payment of Excise duty paid electronically through internet banking***
7th June	***TDS/TCS Payment for May***
10th June	***Excise Return ER1 / ER2 /ER6***
15th June	***PF Contribution for May, Excise payment by SSI***
15th June	***Due date for payment of Advance Income Tax and Fringe Benefit Tax***
15th June	***Filing of last quarter TDS return for the year 2009***
21st June	***ESIC Payment for May***