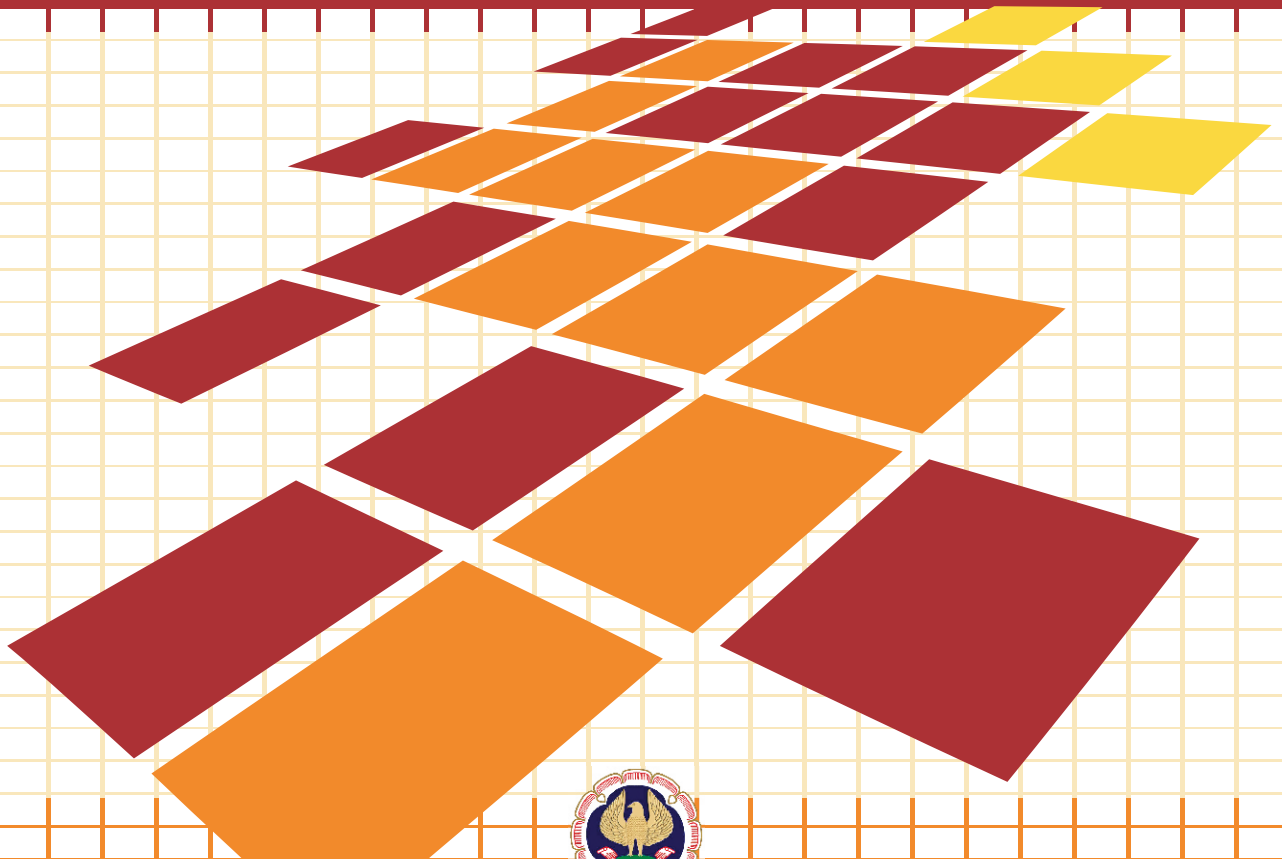


FINAL (NEW) COURSE

DIRECT TAX LAWS

Vol. 2
A.Y. 2010-11



Board of Studies
The Institute of Chartered Accountants of India
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FINAL COURSE STUDY MATERIAL

PAPER 7

Direct Tax Laws

Assessment Year 2010-11

[Relevant for students appearing for
May 2010 and November 2010 examinations]

Volume – 2



**BOARD OF STUDIES
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA**

This study material has been prepared by the faculty of the Board of Studies. The objective of the study material is to provide teaching material to the students to enable them to obtain knowledge and skills in the subject. Students should also supplement their study by reference to the recommended text book(s). In case students need any clarifications or have any suggestions to make for further improvement of the material contained herein they may write to the Director of Studies.

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PREFACE

Direct tax laws and Indirect tax laws are important elements of the core competence areas of the Chartered Accountants. A thorough knowledge of direct tax laws and indirect tax laws is, therefore, necessary for the students of the CA Final course. In the new Final course, "Direct Tax Laws" constitutes Paper-7. Students are expected to acquire advanced knowledge of the provisions of direct tax laws after undergoing this course and apply such knowledge to various situations in actual practice.

The first part of this study material deals with income-tax. There are 28 chapters under income-tax. The inter-relationship between accounting and taxation is discussed in chapter 12. The concept and significance of "ethics" in taxation has been discussed in the chapter of "Tax Planning". The second part of this study material is on wealth-tax. There are 3 chapters under wealth-tax. The subject matter in this study material is based on the law as amended by the Finance (No.2) Act, 2009. In this study material, efforts have been made to present the complex direct tax laws in a lucid manner. The latest amendments have been given in italics. Chapters are organised in a logical sequence to facilitate easy understanding. Another helpful feature in this study material is the addition of self-examination questions at the end of each chapter, which will be useful to test understanding of the provisions discussed in the chapter. Answers have been given in respect of those questions which are based on judicial decisions or involving legal interpretations.

The taxation laws in our country undergo many amendments. In order to help the students to update their knowledge relating to the statutory developments in the field of direct and indirect taxes, the Board of Studies brings out, every year, a "Supplementary Study Paper" containing all the amendments in direct and indirect taxes. This is an essential read for all our students. Another important publication, "Select cases in Direct and Indirect Taxes – An essential reading for the final course", is meant for updating the knowledge regarding judicial decisions.

A word of advice to the students – please make it a habit of referring to the bare acts as often as possible. This will not only facilitate the process of understanding the law and the sequence of sections in these Acts, but will also equip them with the professional expertise that is expected.

Study Material of Direct Tax Laws is made in two volumes for ease of handling by the students. Volume – 1 contains Chapters 1 – 14 of Income Tax, and Volume – 2 contains Chapters 15 – 28 of Income Tax and Chapters 1 – 3 of Wealth Tax.

Finally, we would welcome suggestions to make this study material more useful to the students. In case of any doubt, students are welcome to write to the Director of Studies, The Institute of Chartered Accountants of India, A-94/4, Sector-58 Noida-201 301, India.

SYLLABUS

PAPER – 7 : DIRECT TAX LAWS

(One paper — Three hours – 100 Marks)

Level of Knowledge: Advanced knowledge

Objectives:

- (a) To gain advanced knowledge of the provisions of direct tax laws,
- (b) To acquire the ability to apply the knowledge of the provisions of direct tax laws to various situations in actual practice.

Contents:

- I. The Income-tax Act, 1961 and Rules thereunder (90 marks)
- II. The Wealth-tax Act, 1957 and Rules thereunder (10 marks)

While covering the direct tax laws, students should familiarise themselves with considerations relevant to tax management. These may include tax considerations with regard to specific management decisions, foreign collaboration agreements, international taxation, amalgamations, tax incentives, personnel compensation plans, inter-relationship of taxation and accounting, with special reference to relevant accounting standards and other precautions to be observed to maximise tax relief. Further, they should have a basic understanding about the ethical considerations in tax management and compliance with taxation laws.

Note – If new legislations are enacted in place of the existing legislations relating to income tax and wealth tax, the syllabus will accordingly include such new legislations in the place of the existing legislations with effect from the date to be notified by the Institute.

Volume – 2

INCOME TAX

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INCOME TAX

15.1 CONCEPT OF DOUBLE TAXATION RELIEF

In the present era of cross-border transactions across the globe, the effect of taxation is one of the important considerations for any trade and investment decision in other countries. One of the most significant results of globalisation is the visible impact of one country's domestic tax policies on the economy of another country. This has led to the need for continuously assessing the tax regimes of various countries and bringing about necessary reforms. Where a taxpayer is resident in one country but has a source of income situated in another country it gives rise to possible double taxation. This arises from the two basic rules that enables the country of residence as well as the country where the source of income exists to impose tax namely, (i) the source rule and (ii) the residence rule. The source rule holds that income is to be taxed in the country in which it originates irrespective of whether the income accrues to a resident or a non-resident whereas the residence rule stipulates that the power to tax should rest with the country in which the taxpayer resides. If both rules apply simultaneously to a business entity and it were to suffer tax at both ends, the cost of operating on an international scale would become prohibitive and would deter the process of globalisation. It is from this point of view that Double Taxation Avoidance Agreements (DTAA) become very significant.

DTAAs lay down the rules for taxation of the income by the source country and the residence country. Such rules are laid for various categories of income, for example, interest, dividend, royalties, capital gains, business income etc. Each such category is dealt with by separate article in the DTAA.

Double taxation means taxing the same income twice in the hands of an assessee. In India, a person is taxed on the basis of his residential status. Likewise, it may so happen that he is taxed on this basis or some other basis in another country on the same income. However, it is a universally accepted principle that the same income should not be subjected to tax twice. In order to take care of such situations, the Income-tax Act, 1961 has provided for double taxation relief.

15.2 Income Tax

15.2 TYPES OF RELIEF

Relief from double taxation can be provided in mainly two ways: (i) Bilateral Relief ; and (ii) Unilateral relief

15.2.1 Bilateral Relief : Under this method, the Governments of two countries can enter into an agreement to provide relief against double taxation by mutually working out the basis on which the relief is to be granted. India has entered into agreements for relief against or avoidance of double taxation with about 50 countries which include Sri Lanka, Switzerland, Sweden, Denmark, Japan, Federal Republic of Germany, Greece, etc..

Bilateral Relief may be granted in either one of the following methods:

- (a) Exemption method, by which a particular income is taxed in only one of the two countries; and
- (b) Tax relief method, under which, an income is taxable in both countries in accordance with their respective tax laws read with the double taxation avoidance agreement. However, the country of residence of the tax payer allows him credit for the tax charged thereon in the country of source.

In India, double taxation relief is provided by a combination of the two methods.

15.2.2 Unilateral Relief : This method provides for relief of some kind by the home country even where no mutual agreement has been entered into between the two countries.

15.3 DOUBLE TAXATION RELIEF PROVISIONS UNDER THE ACT

Sections 90 and 91 of the Income tax Act, 1961 provide for double taxation relief in India.

15.3.1 Agreement with foreign countries or specified territories - Bilateral relief [New Section 90]

- (i) *Sub-section (1) of new section 90 provides that the Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India,—*
 - (a) *for the granting of relief in respect of—*
 - (i) *income on which income-tax has been paid both in India and in that country or specified territory; or*
 - (ii) *income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory to promote mutual economic relations, trade and investment; or*
 - (b) *for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory; or*

Accordingly, the Central Government has notified that where such an agreement provides that any income of a resident of India may be taxed in the other country then, such income shall be included in his total income chargeable to tax in India in accordance with the provisions of the Income-tax Act, 1961, and relief shall be granted in accordance with the method for elimination or avoidance of double taxation provided in such agreement [Notification No. 91/2008, dated 28.8.2008].

- (c) *for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory or investigation of cases of such evasion or avoidance; or*
- (d) *for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory.*

The Central Government may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.

- (ii) *Where the Central Government has entered into such an agreement with the Government of any country outside India or specified territory outside India for granting relief of tax, or for avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.*
- (iii) *Any term used but not defined in this Act or in the agreement referred to above shall have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf, unless the context otherwise requires, provided the same is not inconsistent with the provisions of this Act or the agreement.*
- (iv) *The charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.*

The position of law is that the double taxation avoidance treaties entered into by the Government of India override the domestic law. This has been clarified by the CBDT vide circular no.333 dated April 2, 1982, which provides that a specific provision of the DTAA will prevail over the general provisions of the Income-tax Act. Therefore, where a DTAA provides for a particular mode of computation of income, this mode will take precedence over the Income-tax Act. However, where there is no specific provision in the treaty, then the Income-tax Act will apply.

The Hon'ble Supreme Court had an occasion to examine the DTAA entered into with the Government of Mauritius in the case of *Union of India v. Azadi Bachao Andolan* (2003) 132 Taxman 373. Under the DTAA, capital gains accruing in India to a resident of Mauritius is not liable to tax in India subject to certain exceptions. This was clarified by the CBDT by Circular No.682 dated 30.3.94 by stating that capital gains of any resident of Mauritius by alienation of shares of an Indian company shall be taxable only in Mauritius

15.4 Income Tax

and the same will not be liable to tax in India. Subsequently, the issue of 'treaty shopping' by non-resident foreign companies to avoid capital gains tax on transfer of shares in Indian companies arose. In order to clarify the situation, the CBDT issued Circular No.789 dated 13.4.2000 stating that a certificate of residence issued by Mauritius authority will be conclusive proof of residential status and beneficial ownership in Mauritius for the purpose of applying the DTAA.

The Delhi High Court in *Shiva Kant Jha v. Union of India* (2002) 256 ITR 536 held that Circular No.789 dated 13.4.2000 was invalid because the Circular did not show that it had been issued under section 119 of the Income-tax Act and as such it would not be legally binding on the revenue. The Court observed that the CBDT could not issue any instruction which would be ultra vires the provisions of the Income-tax Act, 1961. Circular No.789, having directed the income-tax authorities to accept certificate of residence issued by the authorities of Mauritius as sufficient evidence as regards residential status and beneficial ownership in Mauritius, would be ultra vires the powers of the CBDT. The Court held that the ITO was entitled to lift the corporate veil in order to see whether a company was actually resident of Mauritius or not or whether the company was paying income-tax in Mauritius or not and this function of the ITO was quasi judicial. Any attempt by the CBDT to interfere with the exercise of this quasi judicial power was contrary to the intendment of the Income-tax Act. The Court held that 'treaty shopping' by which the resident of a third country takes advantage of a fiscal treaty between States was illegal and thus necessarily forbidden.

The Supreme Court reversed the above decision of the Delhi High Court and made wide-ranging observations on many matters including tax planning considerations. The Court held that the judicial consensus in India has been that section 90 is specifically intended to enable and empower the Central Government to issue a notification for implementation of the terms of a DTAA. Therefore, the provisions of such an agreement would operate even if inconsistent with the provisions of the Income-tax Act. Circular 789 is a circular within the meaning of section 90, therefore, it must have the legal consequences contemplated by section 90(2). In other words, the circular shall prevail even if it is inconsistent with the provisions of the Income-tax Act, insofar as assessee covered by the provisions of DTAA are concerned.

The Court observed that many developed countries tolerate or encourage "treaty shopping", even if it is unintended, improper or unjustified, for other non-tax reasons, unless it leads to significant loss of tax revenue. The Court cannot judge the legality of "treaty shopping" merely because one section of thought considers it improper. The court cannot characterize the act of incorporation under the Mauritian law as a sham or a device actuated by improper motives. The Court held that the impugned circular was issued under section 119 and hence valid.

The Supreme Court recognized that the Treaties are negotiated and entered into at political level and have several considerations as their bases. This was an important principle to be kept in mind in the interpretation of the provisions of an international treaty. The Court observed that if it was intended that a national of a Third State should be precluded from the benefits of a DTAA, then a suitable limitation to that effect must find place in the DTAA itself. In the absence of a limitation specifically provided in the DTAA, the same cannot be read into it.

The Supreme Court observed that not only is the principle in *IRC v. Duke of Westminster* (1936) AC 1 alive and kicking in England, but it also seems to have acquired judicial benediction of the Constitutional Bench in India, notwithstanding the temporary turbulence created in the wake of *McDowell & Co. Ltd. v. CTO* (1985) 154 ITR 148 (SC).

The Supreme Court held that if notwithstanding a series of legal steps taken by an assessee, the intended legal result has not been achieved, the Court might be justified in overlooking the intermediate steps, but it would not be permissible for the Court to treat the intervening legal steps as *non-est* based upon some hypothetical assessment of the 'real motive' of the assessee.

Certain terms used in the DTAAs have not been defined either in the agreements or in the Income-tax Act. In order to address the problems arising due to conflicting interpretations of such terms, sub-section (3) empowers the Central Government to define such terms by way of notification in the Official Gazette.

However, the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

Models of Treaties

Tax treaties are generally based on certain models. The most common ones are :

- (i) OECD model (Organisation of Economic Co-operation and Development) - Most of India's treaties are based on this model.
- (ii) U.N. models Double Taxation Convention, 1980 between developed and developing countries.

15.3.2 Double taxation relief to be extended to agreements (between specified associations) adopted by the Central Government [Section 90A]

- (i) Section 90A provides that any specified association in India may enter into an agreement with any specified association in the specified territory outside India and the Central Government may, by notification in the Official Gazette, make the necessary provisions for adopting and implementing such agreement for -

15.6 Income Tax

- (1) grant of double taxation relief,
- (2) avoidance of double taxation of income,
- (3) exchange of information for the prevention of evasion or avoidance of income-tax, or
- (4) recovery of income-tax.

Section 90A(1) provides that an agreement may be entered into by any specified association in India with any specified association in the specified territory outside India which may be adopted by the Central Government by way of notification in the Official Gazette, for granting relief of tax or, as the case may be, for avoidance of double taxation. The Central Government has, vide Notification No.90/2008 dated 28.8.2008, notified that where such an agreement provides that any income of a resident of India may be taxed in the other country then, such income shall be included in his total income chargeable to tax in India in accordance with the provisions of the Income-tax Act, 1961, and relief shall be granted in accordance with the method for elimination or avoidance of double taxation provided in such agreement.

- (ii) In relation to any assessee to whom the said agreement applies, the provisions of the Income-tax Act shall apply to the extent they are more beneficial to that assessee.
- (iii) Any term used but not defined in the Income tax Act or in the said agreement shall have the same meaning as assigned to it in the said notification, unless the context requires otherwise, and it is not inconsistent with the provisions of the Income tax Act or the said agreement.
- (iv) The charge of tax at a higher rate for a company incorporated in the specified territory outside India as compared to a domestic company would not be considered as less favourable charge or levy of tax in respect of such company.
- (v) For the purpose of this section, the 'specified association' means any institution, association or body, whether incorporated or not, functioning under any law for the time being in force in India or the laws of the specified territory outside India and which may be notified as such by the Central Government and 'specified territory' means any area outside India which may be notified by the Central Government.

15.3.3 Countries with which no agreement exists - Unilateral Agreements

[Section 91] : In the case of income arising to an assessee in countries with which India does not have any double taxation agreement, relief would be granted under Section 91 provided all the following conditions are fulfilled:

- (a) The assessee is a resident in India during the previous year in respect of which the income is taxable.

- (b) The income accrues or arises to him outside India.
- (c) The income is not deemed to accrue or arise in India during the previous year.
- (d) The income in question has been subjected to income-tax in the foreign country in the hands of the assessee.
- (e) The assessee has paid tax on the income in the foreign country.
- (f) There is no agreement for relief from double taxation between India and the other country where the income has accrued or arisen.

In such a case, the assessee shall be entitled to a deduction from the Indian income-tax payable by him. The deduction would be a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax in the said country, whichever is lower, or at the Indian rate of tax if both the rates are equal.

Sub-section (2) provides that where a person who is resident in India in any previous year has any agricultural income in Pakistan in respect of which he has paid the income tax payable in that country, he shall be entitled to a deduction from the Indian income-tax payable by him to the following extent:

- (i) of the amount of tax paid in Pakistan on such income which is liable to tax under this Act, also; or
- (ii) of a sum calculated on that income at the Indian rate of tax, whichever is less.

Sub-section (3) provides for relief to a non-resident assessee in respect of his share in the income of a registered firm assessed as resident in India in any previous year, provided all the following conditions are fulfilled –

- (i) The share income from the firm should include income accruing or arising outside India during that previous year;
- (ii) Such income should not be deemed to accrue or arise in India;
- (iii) The income should accrue or arise in a country with which India has no agreement under section 90 for the relief or avoidance of double taxation;
- (iv) The assessee should have paid income-tax in respect of such income according to the law in force in that country.

In such a case, the assessee will be entitled to a deduction from the Indian income-tax payable by him. The deduction will be a sum calculated on such doubly taxed income so included, at the Indian rate of tax or the rate of tax of the said country, whichever is lower, or at the Indian rate of tax, if both the rates are equal.

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15.4 TAXATION OF BUSINESS PROCESS OUTSOURCING UNITS IN INDIA

The provisions containing taxation of IT-enabled business process outsourcing units are not contained in the Income-tax Act, 1961 but are given in Circular No.5/2004 dated 28.9.2004 issued by CBDT. The provisions are briefed hereunder -

- (a) A non-resident entity may outsource certain services to a resident Indian entity. If there is no business connection between the two, the resident entity may not be a Permanent Establishment of the non-resident entity, and the resident entity would have to be assessed to income-tax as a separate entity. In such a case, the non-resident entity will not be liable under the Income-tax Act, 1961.
- (b) However, it is possible that the non-resident entity may have a business connection with the resident Indian entity. In such a case, the resident Indian entity could be treated as the Permanent Establishment of the non-resident entity.
- (c) The non-resident entity or the foreign company will be liable to tax in India only if the IT enabled BPO unit in India constitutes its Permanent Establishment.
- (d) A non-resident or a foreign company is treated as having a Permanent Establishment in India if the said non-resident or foreign company carries on business in India through a branch, sales office etc. or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts or regularly delivers goods or merchandise or habitually secures orders on behalf of the non-resident principal. In such a case, the profits of the non-resident or foreign company attributable to the business activities carried out in India by the Permanent Establishment becomes taxable in India.
- (e) If a foreign enterprise carries on business in another country through a Permanent Establishment situated therein, the profits of the enterprise may be taxed in the other country but only so much of them as is attributable to the Permanent Establishment.
- (f) Profits are to be attributed to the Permanent Establishment as if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a Permanent Establishment.
- (g) In determining the profits of a Permanent Establishment there shall be allowed as deduction, expenses which are incurred for the purposes of the Permanent Establishment including executive and general administrative expenses so incurred, whether in the State in which the Permanent Establishment is situated or elsewhere.
- (h) The expenses that are deductible would have to be determined in accordance with the accepted principles of accountancy and the provisions of the Income-tax Act, 1961.
- (i) The profits to be attributed to a Permanent Establishment are those which that Permanent Establishment would have made if, instead of dealing with its Head Office,

it had been dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market. This corresponds to the “arm’s length principle”.

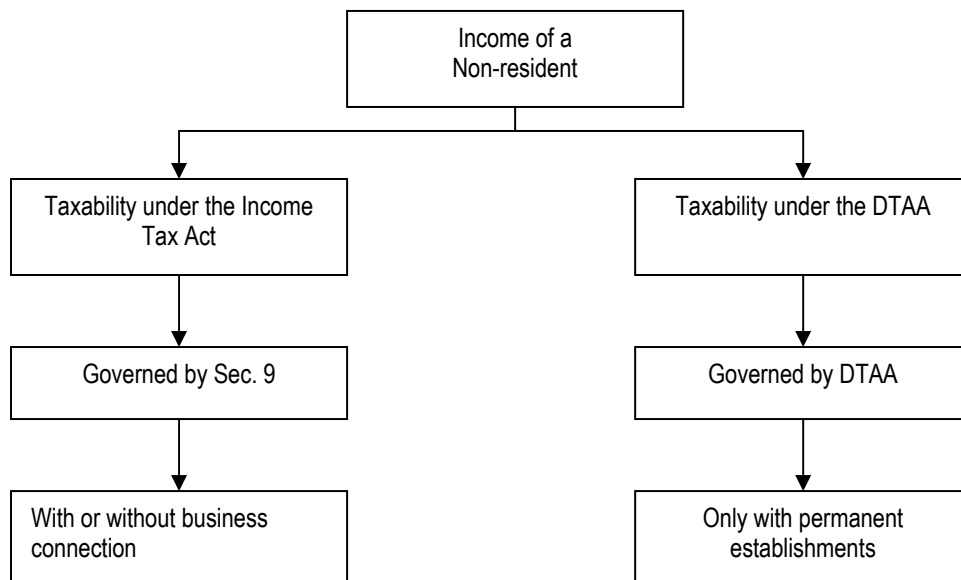
- (j) Hence, in determining the profits attributable to an IT-enabled BPO unit constituting a Permanent Establishment, it will be necessary to determine the price of the services rendered by the Permanent Establishment to the Head office or by the Head office to the Permanent Establishment on the basis of “arm’s length principle”.

15.5 CONCEPT OF PERMANENT ESTABLISHMENT

In order to determine the taxability of business income of foreign enterprises operating in India, it is important to determine the existence of a Permanent Establishment (‘PE’). Article 5(1) of the DTAA provides that for the purpose of this convention the term ‘Permanent Establishment’ means a fixed place of business through which the business of an enterprise is wholly or partly carried on. The term ‘Enterprise’ has been defined in section 92F(iii) [See page 16.23 Chapter 16].

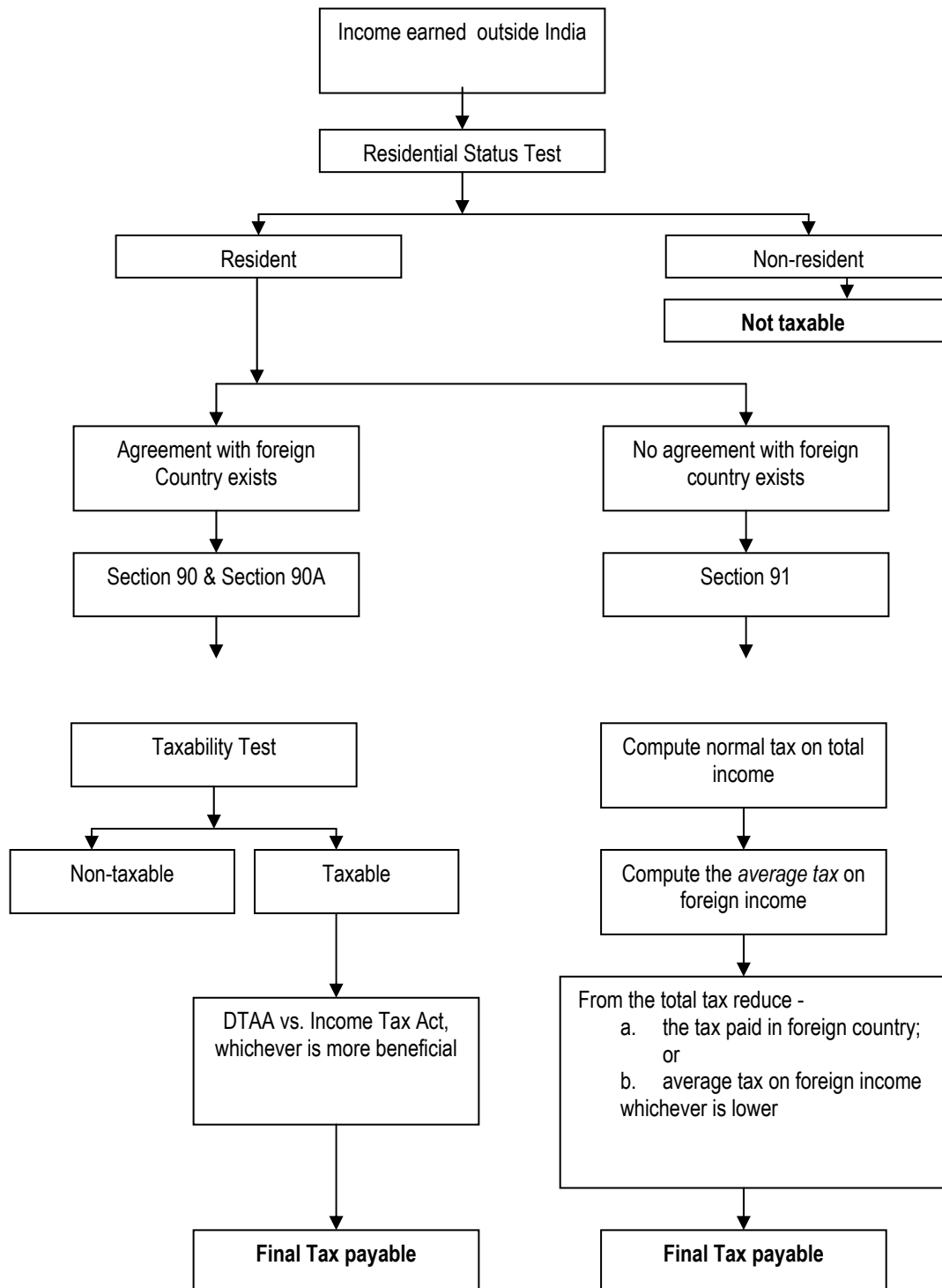
According to Article 5(2), which enumerates various instances of PE, the term PE includes (a) a place of management; (b) a branch; (c) an office; (d) a factory; (e) a workshop; (f) a sales outlet; (g) a warehouse; (h) a mine, an oil or gas well, a quarry or other place of extraction of natural resources (but not exploration).

- 1) Permanent establishment means a fixed place of business through which the business of an enterprises is wholly or partly carried on.
- 2) Every DTAA has a specific clause, which will deal with an explanation of permanent establishment for the purpose of such DTAA.
- 3) Business Income of a non resident will not be taxed in India, unless such non-resident has a permanent establishment in India.
- 4) Distinguishment of taxability of income under business connection and permanent establishment is explained here below :



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15.6 TAXING FOREIGN INCOME



15.7 MEANING OF IMPORTANT TERMS

- (i) "Indian rate of tax" means the rate determined by dividing the amount of Indian income-tax after deduction of any relief due under the provisions of the Act but before deduction of any double taxation relief due to the assessee.
- (ii) "Rate of tax of the said country" means income-tax and super-tax actually paid in that country in accordance with the corresponding laws in force in the said country after deduction of all relief due, but before deduction on account of double taxation relief due in the said country, divided by the whole amount of income assessed in the said country.
- (iii) The expression "income-tax" in relation to any country includes any excess profits tax or business profits tax charged on the profits by the Government of any part of that country or a local authority in that country.

15.8 TREATY OVERRIDES DOMESTIC LAW:

The specific provisions of the Agreement for Avoidance of Double Taxation should override the general provisions of the Income Tax Act 1961 clarified by circular of CBDT No 333 and Sec 90(2) of Income Tax Act 1961

Self-examination questions

1. What is double taxation relief? Explain.
2. Explain the types of double taxation relief.
3. State the models on which tax treaties are generally based.
4. "Double taxation relief has now been extended to certain agreements adopted by the Government" - Discuss the correctness or otherwise of this statement.
5. How are IT-enabled Business Process Outsourcing units in India taxed? Are there any provisions in the Income-tax Act, 1961 governing taxation of such units?
6. Explain briefly the concept of permanent establishment.
7. Explain the meaning of the following terms -
 - (a) Indian rate of tax
 - (b) Rate of tax of the said country.
8. An individual resident in India, having income earned outside India in a country with which no agreement under section 90 exists asks you to explain whether the credit of

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the tax paid on the income in that country will be allowed to him in India.

9. The Income-tax Act, 1961 provides for taxation of a certain income earned by Mr.X. The Double Taxation Avoidance Agreement, which applies to Mr.X, excludes the income earned by Mr.X from the purview of tax. Is Mr.X liable to pay tax on the income earned by him? Discuss.
10. Treaty Shopping is illegal and should be necessarily forbidden – Discuss the correctness of this statement.
11. Mr. Mahesh is a resident both in India and Malaysia. He owns some immovable properties (Rubber Plantations) in Malaysia. During the previous year 2009-10, he earned income from rubber estates in Malaysia. The Assessing Officer contended that the business income is assessable in India and brought the same to tax. Discuss the correctness of the contention of the Assessing Officer, taking into consideration the following -
 - (i) Mahesh has no permanent establishment in India in respect of the business of rubber plantations.
 - (ii) Article 4 of the Double Taxation Avoidance Agreement between India and Malaysia provides that where an individual is a resident of both the Contracting States, he shall be deemed to be a resident of the Contracting State in which he has a permanent home available to him. If he has a permanent home available to him in both Contracting States, he shall be deemed to be resident of the Contracting State with which his personal and economic relations are closer.

Answers

9. Section 90(2) makes it clear that where the Central Government has entered into a Double Taxation Avoidance Agreement, then in respect of an assessee to whom such agreement applies, the provisions of the Act shall apply to the extent they are more beneficial to the assessee. This means that where tax liability is imposed by the Act, the Double Taxation Avoidance Agreement may be resorted to for reducing or avoiding the tax liability.

The Supreme Court has held, in *CIT v. P.V.A.L. Kulandagan Chettiar (2004) 267 ITR 654*, that in case of any conflict between the provisions of the Double Taxation Avoidance Agreement and the Income-tax Act, 1961, the provisions of the Double Taxation Avoidance Agreement would prevail over those of the Income-tax Act. X is, therefore, not liable to pay tax on the income earned by him.

10. Treaty shopping is a process by which a resident of a third country takes advantage of a fiscal treaty between two countries. The Supreme Court in *Union of India v. Azadi Bachao Andolan (2003) 132 Taxman 373*, observed that many developed countries tolerate or encourage “treaty shopping”, even if it is unintended, improper or unjustified, for other non-tax reasons, unless it leads to significant loss of tax revenue. The Court cannot judge the legality of “treaty shopping” merely because one section of thought considers it improper. The Supreme Court recognized that the Treaties are negotiated and entered into at political level and have several considerations as their bases. This was an important principle to be kept in mind in the interpretation of the provisions of an international treaty. The Court observed that if it was intended that a national of a Third State should be precluded from the benefits of a DTAA, then a suitable limitation to that effect must find place in the DTAA itself. In the absence of a limitation specifically provided in the DTAA, the same cannot be read into it.
11. The issue arising in this case is similar to the issue which has been settled by the Apex Court in *CIT v. P.V.A.L. Kulandagan Chettiar (2004) 137 Taxman 460*. In this case, the Apex Court observed the following -
 - (1) Section 90(2) of the Income-tax Act, 1961 makes it clear that in case of any conflict between the provisions of Double Taxation Avoidance Agreement (DTAA) and the Income-tax Act, 1961, the provisions of the DTAA would prevail over the provisions of the Act.
 - (2) The tax liability arising in respect of a person residing in both the contracting States has to be determined with reference to that State with which his personal and economic relations are closer. The person shall be deemed to be a resident of that contracting State in which he has an habitual abode.
 - (3) The immovable property in question (i.e. Rubber Plantations) is situated in Malaysia and income was derived from that property. Further, there was no permanent establishment (PE) in India in regard to the business of rubber plantations. Therefore, the business income from rubber plantations could not be taxed in India because of closer economic relations between the assessee and Malaysia, being the place where
 - (a) the property is located and
 - (b) the PE has been set up.

These two factors go to determine the fiscal domicile.

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- (4) If an assessee is deemed to be a resident of a contracting State where his personal and economic relations are closer, then in such a case, the fact that he is a resident in India to be taxed in terms of sections 4 and 5 would become irrelevant, since the DTAA prevails over sections 4 and 5.

Therefore, in this case, the contention of the Assessing Officer is not correct.

TRANSFER PRICING AND OTHER PROVISIONS TO CHECK AVOIDANCE OF TAX

In the present age of commercial globalisation, it is a universal phenomena that Multinational Companies (MNCs) have branches/subsidiaries/divisions operating in more than one country. In such a situation, it is a common event for MNCs to transfer goods produced by a branch in one tax jurisdiction to an associate branch operating in another tax jurisdiction. While doing so, the MNC concerned has in mind the goal of minimizing tax burden and maximizing profits but the two tax jurisdictions/countries have also the consideration of maximizing their revenue while making laws that govern such transactions. It is an internationally accepted practice that such 'transfer pricing' should be governed by the Arm's Length Principle (ALP) and the transfer price should be the price applicable in case of a transaction of arm's length. In other words, the transaction between associates should be priced in the same way as a transaction between independent enterprises.

The principles governing the taxation of MNCs are embodied in the OECD Model Tax Convention of Income and Capital (OECD Model Convention), which serves as the basis for the bilateral income-tax treaties between OECD member countries and between OECD member and non-OECD member countries. According to these guidelines, "Transfer prices" are the prices at which an enterprise transfers physical goods and intangible property or provides services to associated enterprises. Two enterprises are "associated enterprises" if one of the enterprises participates directly or indirectly in the management, control or capital of the other or if both enterprises are under common control. Since international transfer pricing involves more than one tax jurisdiction, any adjustment to the transfer price in one jurisdiction requires a corresponding adjustment in the other jurisdiction. If a corresponding adjustment is not made, double taxation will result.

16.1 MEANING OF THE TERM "ARM'S LENGTH PRINCIPLE"

The Arm's Length Price of a transaction between two associated enterprises is the price that would be paid if the transaction had taken place between two comparable independent and unrelated parties, where the consideration is only commercial.

The Arm's Length Principle (ALP), in the context of taxation, is explained in the OECD Model Tax Convention as under:

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“Where conditions are made or imposed between two associated enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly.”

The OECD transfer pricing guidelines provides guidance on the application of the arm's length principle in order to arrive at the proper transfer pricing range between associated enterprises. Market forces determine business relations between independent parties. The Arm's length principle seeks to adjust the profits between two associated enterprises by comparing the same as if the transaction is carried out between two independent enterprises. It treats each enterprise as a separate independent entity rather than as inseparable parts of a single unified business.

16.2 SIGNIFICANCE OF ARM'S LENGTH PRINCIPLE

There are several reasons as to why the OECD member countries and other countries have adopted the ALP.

Parity between MNCs and independent enterprises – A major reason is that the ALP provides broad parity of tax treatment for MNCs and independent enterprises. Since the ALP puts associated and independent enterprises on a more equal footing for tax purposes, it avoids the creation of tax advantages and disadvantages that would otherwise distort the relative competitive positions of these entities. The ALP, thus promotes the growth of international trade and investment by removing these tax considerations from economic decisions.

Determines real taxable profits - The transfer price adopted by a multinational has a direct bearing on the proportional profit it derives in each country in which it operates. If inadequate or excessive consideration is paid for the transfer of goods, services or intangible property between the members of an MNC group, the income calculated for each of those members will be inconsistent with their relative economic contributions. An 'arm's length' price – a price two independent firms operating at arm's length would agree on – is needed to determine taxable profits earned in each country. The arm's length doctrine permits the taxing authorities to rectify the accounts of the enterprise so as to reflect correctly the income that the establishment would have earned if it were an independent enterprise.

Reduction of artificial price distortion - If the ALP is not followed, an MNC will sell goods/provide services to a controlled entity in a high tax regime at a high price (which exceeds the market price) and to an entity in a low-tax regime or a tax haven at a low price (which is lower than the market price). This would result in extreme price distortion of goods and services in the international market.

Minimization of double taxation – The ALP is an international concept and it represents the international norm. The potential for double taxation is minimized, since in international transfer pricing, adjustment to the transfer price in one tax jurisdiction requires a corresponding adjustment in the other tax jurisdiction.

Accurate measurement of economic contribution – The ALP provides accurate measurement of the fair market value of the economic contribution units of an MNC. The focus of the ALP is to ensure that the proper amount of income is attributed to where it is earned. This results in each unit of the MNC earning a return commensurate with its economic contribution and risk assumed.

16.3 PRACTICAL DIFFICULTIES IN APPLICATION OF ALP

There are however, certain practical difficulties in applying the ALP, which are described hereunder:

True comparison difficult in certain cases – The commercial and financial conditions governing a transaction between independent enterprises are, by and large, never similar to those existing between associated enterprises. As a result, there cannot be a true comparison. The economies of scale and integration of various business activities of the associated enterprise may not be truly appreciated by arm's length principle. Further, associated enterprises may enter into transactions which independent enterprises may not enter into, like say, licensing of valuable intangible or sharing the benefits of research. The owner of an intangible may be hesitant to enter into licensing arrangements with independent enterprises for fear of the value of the intangible being degraded. In contrast, he may be prepared to offer terms that are less restrictive to associated enterprises because the use of the intangible can be closely monitored. Further, there is no risk to the overall group's profit from a transaction of this kind between members of an MNC group. In such situations, where independent enterprises seldom undertake transactions of the type entered into by associated enterprises, the ALP is difficult to apply because there is little or no direct evidence of what conditions would have been established by independent enterprises.

Availability of data and reliability of available data – There may be difficulty in getting adequate and reliable information and data in order to apply arm's length principle. The comparison of controlled and uncontrolled transactions between associated and independent enterprises usually requires a large quantum of data. Easily accessible information may be incomplete and difficult to interpret while the relevant and required information may be difficult to obtain due to geographical constraints or secrecy and confidentiality aspects. In other cases, information about an independent enterprise which could be relevant may not exist at all. Due to these difficulties, the tax administration and tax payers may have to exercise reason and judgment when applying the ALP.

Absence of market price - There must be a reasonably reliable and comparable uncontrolled market price. The ALP does not meet this condition because of the nature of the market place. A market price is an outcome of unique negotiations. It may be possible to know the price range, but it is very difficult to know the actual market price unless a market transaction actually takes place.

Absence of comparable market price for "intangible" transactions - The ALP reaches a comparable uncontrolled market price that is reasonably reliable for standard transactions where the price range is narrow and market price is certain. However, the

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ALP generally fails to achieve a comparable market price for transactions involving intangibles because they are unique. The unique nature of these transactions creates a very wide price range.

Administrative burden - In certain cases, the arm's length principle may result in an administrative burden for both the taxpayer and the tax administrations of evaluating significant numbers and types of cross-border transactions.

Time lag - Although an associated enterprise normally establishes the conditions for a transaction at the time it is undertaken, at some point the enterprise may be required to demonstrate that these are consistent with the arm's length principle. The tax administration may also have to engage in the verification process perhaps some years after the transactions have taken place. It may result in substantial cost being incurred by the tax payer and the tax administration. It is also difficult to appreciate the business realities which prevailed at the time when the transactions were entered into. This may lead to bias against the tax payer.

In spite of the practical difficulties listed above, OECD member countries are of the view that the ALP does provide a sound basis to appreciate the transfer pricing between associated enterprises. It has so far provided acceptable solutions to both taxpayers and the tax administrations. The experience gained so far should be effectively used to remove the practical difficulties and improve the administration.

16.4 GUIDELINES FOR APPLYING THE ARM'S LENGTH PRINCIPLE

The OECD guidelines advocate the principle of arm's length for determining the transfer price. The guidelines suggest various acceptable methods of arriving at arm's length consideration i.e. comparable uncontrolled price, resale price, cost plus, transactional profit split method etc. The choice of method to arrive at arm's length price will depend on the type of property transferred, whether it is outright sale or license/lease, whether it is for a specified period, whether the consideration is lumpsum or a stream of royalty payments etc. In a given circumstance, a combination of more than one method may be used.

(1) Comparability analysis - An application of the ALP is generally based on a comparison of a controlled transaction between associated enterprises and an uncontrolled transaction between two independent enterprises. The economics of the transactions must be sufficiently comparable for such comparisons to be useful. To be comparable means that none of the differences, if any, between the situations being compared has any material effect on the condition being examined in the methodology (e.g. price or margin), or that reasonably accurate adjustments can be made to eliminate the effect of any such differences. In order to determine the degree of comparability it is necessary to understand how independent enterprises evaluate the terms of a potential transaction. When evaluating the terms of a potential transaction, an independent enterprise compares the proposed transaction to other options realistically available and will only enter into the transaction if no alternative is more attractive. Since independent enterprises generally take into account any economically relevant difference between the

options realistically available when valuing those options, tax administrations should also take into account these differences for determining comparability. In order to determine the degree of actual comparability and to establish arm's length prices, the following factors which affect the arm's length dealing must be examined –

Characteristics of the property or services transferred - When comparing controlled and uncontrolled transactions, differences in specific characteristics of goods or services result in different market values. Thus for transfer pricing purposes, it may be important to consider the physical features of tangible property, its quality and reliability, as well as its availability and supply. For services, the nature and extent of the services must be considered. For intangible property, the form of the transaction, the type of property, the length and degree of protection and the anticipated benefits from the property are critical factors.

Functional analysis - A functional analysis seeks to compare the economically significant activities and responsibilities undertaken by independent and related parties. While one party may provide a number of functions to the other party, it is not the volume of functions but rather the economic significance of those functions in terms of their frequency, nature and value to the parties that is important for transfer pricing comparability. Comparable functions include design, manufacturing, assembling, research and development, servicing, purchasing, distribution, marketing, advertising, transportation, financing and management. The assets used should also be taken into consideration when comparing functions.

Functional analysis, however, is incomplete without considering the material risks assumed by each party. Controlled and uncontrolled transactions are not comparable if there are significant differences in the risks assumed unless appropriate adjustments are made. The risks to be considered include: market risks; price fluctuations; risks of loss of investments in property, plant and equipment, research and development; exchange rates and interest rates; financial and credit risks; etc.

The functions carried out (taking into account the assets used and the risks assumed) will determine to a certain extent the allocation of risks between the parties. The best evidence of the true allocation of risk is the conduct of the parties which reveals the economic substance of the transaction. A careful analysis will reveal to what extent each party to a transaction bears true risk in practice.

Contractual terms - The contract terms define how responsibilities, risks and benefits are to be allocated between parties in an arm's-length transaction, and hence, the analysis of contractual terms should form part of a functional analysis. The terms of a transaction may also be found in correspondence/communications between parties apart from the written contract. Where no written terms exist, the contractual relationships of the parties must be established from their conduct and the economic principles that generally govern relationships between independent enterprises. It is important to determine whether the conduct of the parties conforms to the contract or whether the parties' conduct indicates that the contractual terms have not been fulfilled or are a sham.

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Economic circumstances – Economic circumstances vary from market to market. The requirement of applying arm's length principle is that markets in which independent and related parties operate are comparable, and that differences do not have a material effect on price or that appropriate adjustments can be made. It is very important to determine the relevant market or markets for goods and services before analysing market comparability. Economic circumstances that may affect market comparability include geographic location, market size, competition, the availability of substitute goods and services, levels of supply and demand, consumer purchasing power, government regulations, cost of production, transport costs, type of market, timing of transactions, etc.

Business strategies - Business strategies must be taken into account while determining the comparability of controlled and uncontrolled transactions. In this context, it is important to determine whether business strategies have been planned by the MNC group or by a member of the group acting independently and whether the business plan requires the participation of other members of the multinational group. Generally, business strategies take into account many aspects of an enterprise, such as innovation and new product development, degree of diversification, risk aversion, assessment of political changes and other factors influencing the normal conduct of business.

Some business strategies, such as those designed to penetrate new markets or to expand market share, often reduce the taxpayer's current profits in anticipation of greater profits in the future. When evaluating a taxpayer's claim that it was following a business strategy that temporarily decreased profits in return for higher long-run profits, the factors to be taken into consideration are –

(i) the conduct of the parties, as to whether they are consistent with the professed business strategy;

For example, if a manufacturer charges its related distributor a price below the market price as part of a market penetration strategy, the cost savings to the distributor may be reflected in the price charged by the distributor from his customers or in further market penetration expenses incurred by the distributor. Further, a market penetration strategy would be accompanied by intensive marketing and advertising efforts.

(ii) the nature of relationship between the parties to a controlled transaction, whether the same would be consistent with the taxpayer bearing the costs of a business strategy;

For example, in an arm's length transaction, the cost of market penetration strategy would not be borne by a sole-selling agent, since he has little or no responsibility for long-term market development.

(iii) whether there is a reasonable expectation that the business strategy would produce a return sufficient to justify its costs within a period of time that would be acceptable in an arm's length arrangement and

(iv) whether, while recognising that the strategy might fail, the said strategy could reasonably be expected to prove profitable within the foreseeable future and whether the

party operating at arm's length is prepared to sacrifice profitability for a similar period under such economic circumstances and competitive conditions.

(2) Recognition of the actual transactions undertaken

A controlled transaction should be examined by the tax administration on the basis of the actual transaction undertaken by the associated enterprises, as it has been structured by them, using the methods applied by the taxpayer to the extent they are consistent with the methods described in para 16.5 below. In other than exceptional cases, the tax administration should not disregard the actual transactions or substitute other transactions for them. Restructuring of legitimate business transactions would be a wholly arbitrary exercise, the inequity of which could be compounded by double taxation created where the other tax administration does not share the same views as to how the transaction should be structured.

However, there are two particular circumstances in which it may, exceptionally, be both appropriate and legitimate for a tax administration to consider disregarding the structure adopted by a taxpayer in entering into a controlled transaction.

(i) Where economic substance differs from form

The first circumstance arises where the economic substance of a transaction differs from its form. In such a case, the tax administration may disregard the parties' characterisation of the transaction and re-characterise it in accordance with its substance. An example of this circumstance would be an investment in an associated enterprise in the form of interest-bearing debt when, at arm's length, having regard to the economic circumstances of the borrowing company, the investment would not be expected to be structured in this way. In this case, the tax administration may appropriately characterise the investment in accordance with its economic substance with the result that the loan may be treated as a subscription of capital.

(ii) Arrangements made in relation to the transactions which impede the determination of Transfer Price at Arm's length

The second circumstance arises where, while the form and substance of the transaction are the same, the arrangements made in relation to the transaction, viewed in their totality, differ from those which would have been adopted by independent enterprises behaving in a commercially rational manner and the actual structure practically impedes the tax administration from determining an appropriate transfer price. An example of this circumstance would be a sale under a long-term contract, for a lump sum payment, of unlimited entitlement to the intellectual property rights arising as a result of future research for the term of the contract. In this case, though it may be proper to view the transaction as a transfer of commercial property, the tax administration should, however, compare the terms of that transfer as a whole to those terms had the transfer of property been the subject of a transaction involving independent enterprises. Thus, in the case described above, it might be appropriate for the tax administration to adjust the conditions of the agreement in a commercially rational manner as a continuing research agreement.

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(3) Evaluation of separate and combined transactions

In order to arrive at the most precise approximation of fair market value, the arm's length principle should be applied on a transaction-by-transaction basis. However, there are often situations where separate transactions are so closely linked or continuous that they cannot be evaluated adequately on a separate basis. For example, long-term contracts for supply of goods or services, right to use intangible property etc. where it is very difficult and impractical to determine pricing for each individual product or transaction. Further, where a part of a transaction is routed through an associated enterprise, it is more appropriate to view the transaction as a whole rather than to consider only that part of the transaction which is routed.

Some separately contracted transactions between associated enterprises may need to be evaluated together to see whether the conditions are at arm's length whereas some other transactions contracted as a package need to be evaluated separately for the said purpose. For example, an MNC might enter into a package deal and establish a single price for a number of benefits like licences for patents, know-how and trademark, provision of technical and administrative facilities and use of production facilities. However, in some cases, it may not be feasible to evaluate the transaction as a whole and therefore it becomes necessary that the different elements are segregated. In such cases, after determining the transfer price for separate elements, the tax administration should consider whether the transfer pricing for the entire package in total is at arm's length.

A package deal may also combine elements that are subject to different tax treatment under domestic tax laws or an income-tax convention. For example, royalty payments may be subject to withholding tax but lease payments may be subject to net taxation. It may be appropriate to determine the transfer pricing on a package basis even in such a case, and thereafter the tax administration can determine whether it is necessary to allocate the price to the separate elements of the package for other tax reasons. The tax administrations should examine the package deal between associated enterprises in the same way as they would examine a similar deal between independent enterprises for determining the transfer price.

(4) Use of an arm's length range

Since transfer pricing is not an exact science, the application of the most appropriate transfer pricing method may yield a range of reliable arm's length prices. A range of arm's length prices may result from the fact that independent enterprises engaged in comparable transactions in comparable circumstances may not establish the same price for a transaction or that the application of the ALP to related parties only produces an approximation of conditions that would have been established between independent enterprises. A range of arm's length prices may also result when more than one pricing method is used to determine the arm's length price for a controlled transaction. The usefulness of such range of prices, however, depends on the reliability of the methods used to determine the ranges and the quality of information used in applying the different methods.

In some cases, the arm's length range may be very wide indicating substantial deviation between the values calculated. In such cases, the data used in establishing some of the values in the range may not be reliable or that the data requires certain adjustments, which have not been carried out, resulting in substantial deviation. In these cases, the values must be further analysed to evaluate their suitability for inclusion in the range.

In general, adjustments should be made to that price in the range that best reflects the facts and circumstances of the controlled transaction. If the price or margin is within the arm's length range, no adjustment should be made. However, if the same are outside the range as determined by the tax administration, then the taxpayer must convince the tax administration that the price or margin satisfies the arm's length principle and that the results are within the arm's length range. If the tax administration is not convinced, it must make adjustments to achieve an arm's length result.

(5) Use of multiple year data

Analysis of data for the year in which the transaction actually took place and prior years may reveal certain facts that may have influenced the determination of a transfer price and help in obtaining a complete understanding of the facts and circumstances surrounding the controlled transaction. For example, the use of data from past years will show whether a taxpayer's reported loss on a transaction is part of a history of losses on similar transactions, the result of particular economic conditions in a prior year that increased costs in the subsequent year, or a reflection of the fact that a product is at the end of its life cycle.

Multiple year data also provides information about the relevant business and product life cycles of the comparables. The differences in business or product life cycles may have a material effect on transfer pricing conditions that needs to be assessed in determining comparability. Past years' data may reveal whether the independent enterprises engaged in a comparable transaction was affected by comparable economic conditions in a comparable manner, or whether different conditions in an earlier year materially affected its price or profit so that it should not be used as a comparable.

Data from the years following a transaction may be relevant for analysing transfer prices, especially when comparing product life-cycles of controlled and uncontrolled transactions or when examining the conduct of the parties in view of the arrangements between them.

(6) Losses

A situation where an associated enterprise incurs losses continuously while the MNC group as a whole is profitable requires special scrutiny, even though there may be genuine reasons like incurring of heavy start-up costs, unfavourable economic conditions etc. However, it is to be noted that whereas an independent enterprise cannot afford to continue operations for a long time with such losses, an associated enterprise may continue to do so if it is profitable to the MNC group as a whole.

The tax administrations should examine such cases where an associated enterprise is continuously incurring losses while undertaking business transactions with profit-making

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members of the same group. The reason may be that all or most of the loss-making products are produced by the associated enterprise whereas the profit-making products are produced by other members of the group. Since an independent enterprise would undertake such a task only for an adequate service charge, the tax administration should determine the transfer price under ALP by assuming that the associated enterprise also receives similar type of service charge.

Since business strategies differ between MNC groups, the reason for losses should be determined with reference to these business strategies. For example, an associated enterprise may incur losses continuously during the initial years due to fixing low selling prices as part of its market penetration strategy to enter a new market, capture a good market share and then raise its price and earn higher profits. In such cases, the tax administration should ensure that such low prices continue only for a reasonable period of time. If the pricing strategy continues beyond a reasonable period as estimated by the tax administration, then appropriate adjustment to the transfer price must be made, especially where the period is much longer than the period adopted for such a strategy for comparable products by independent enterprises.

(7) The effect of government policies

The government interventions such as price controls, interest rate controls, controls over payment of royalties, exchange control, anti-dumping duties etc. should be treated as market conditions in the particular country, and should be taken into account in determining the taxpayer's transfer price in that market. The issue is whether in light of these conditions, the transactions undertaken by the associated enterprises are consistent with the transactions between independent enterprises. Where government intervention applies equally to transactions between related parties and transactions between unrelated parties, and controlled transactions are consistent with uncontrolled transactions, then such government interventions will not require adjustments to transfer prices. Where government intervention applies only to transactions between associated enterprises, such as when a country prevents or "blocks" payments owed by one associated enterprise to another, the ALP can be applied by treating the intervention as a condition affecting the terms of the transaction.

The stage at which a price control affects the price of a product or service is to be determined. Mostly the direct impact will be on the final price to the consumer, but the impact may also be on the prices at the intermediate stages. MNCs may not make any adjustment in their transfer prices to take account of such controls and may leave the final seller to bear the impact or the burden may be shared between the final seller and the intermediate supplier in some way. The fact to be taken into consideration is that whether an independent enterprise would bear the cost of these controls or alternatively change its business line.

(8) Intentional set-offs

An intentional set-off occurs when one associated enterprise derives some benefit from another enterprise in the same group which is balanced to an extent by the benefits

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received from that enterprise in return. These enterprises claim that only the net gain should be considered for tax purposes. For example, an associated enterprise may allow another enterprise in the group to use its spare production facilities in return for provision of know-how to it by the other enterprise and claim that these transactions result in no profit no loss to either party. Such transactions may sometimes take place between independent enterprises also and the ALP has to be applied to find out the real benefits and gains of individual transactions without set-off.

Intentional set-offs may be in the form of simple balancing of two transactions between enterprises or in the form of balancing of transactions between these enterprises over a period of time. It is to be noted that set-offs between independent enterprises are most likely to be of the former type and the latter would be applicable in case of set-offs between associated enterprises. This is because independent enterprises would not like to enter into long-term arrangements unless it is possible that the benefits can be accurately quantified and an advance contract can be entered into.

These transactions are to be evaluated separately to determine whether they satisfy the ALP. If the transactions are to be evaluated together, then care should be taken that the transactions are comparable. The terms of set-off relating to international transactions between associated enterprises may not be consistent with the terms of set-off relating to domestic transactions between independent enterprises since the tax treatment of set-offs would vary between nations or differences in treatment under a bilateral tax treaty.

(9) Use of customs valuation

The ALP is applied by the Customs' authorities to compare the value of goods imported by an associated enterprise with the value of similar goods imported by an independent enterprise. The tax administration can use the value of goods determined by the customs authorities for transfer pricing purposes since both for tax and customs purposes the value is determined at the same point of time i.e. at the time when they are transferred or imported. Further, the customs authorities generally have contemporaneous documentation regarding the transaction which would prove useful for transfer pricing purposes.

The tax administration and the customs authorities have similar reasons for examining the value of an international transaction between an associated enterprise. However, the taxpayer might value the goods differently for tax and customs purposes. For customs purposes, the taxpayer might set a low price for the transaction so that the custom duty payable can be minimised whereas for tax purposes, he might set a higher price so that he can claim a higher deduction for cost of goods imported. Therefore, it would be very useful for the Customs and tax departments to co-ordinate with each other so that there can be free flow of information between them which would help in determining the real value of the transactions for transfer pricing.

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16.5 METHODS FOR CALCULATING ARM'S LENGTH PRICE

The methods set forth hereunder establish whether the conditions imposed in the commercial or financial relations between associated enterprises are consistent with the arm's length principle.

(1) Traditional Transaction Methods

(i) **Comparable Uncontrolled Price (CUP) Method** – Under this method, the price charged for property or services transferred in a controlled transaction between associated enterprises is compared with the price charged for comparable property or services transferred in an uncontrolled transaction between independent enterprises under comparable circumstances. Any difference between the two prices would indicate that the transaction between the associated enterprises is not at arm's length, and therefore, the price charged in a comparable uncontrolled transaction would have to be substituted for the price charged in a controlled transaction. Thus, CUP is the most reliable method where comparable uncontrolled transactions are available. However, where differences exist between controlled and uncontrolled transactions, reasonably accurate adjustments have to be made to eliminate the impact on price. The reliability of CUP method depends upon the accuracy of any adjustment needed to achieve comparability.

This method assumes :

- availability of comparable uncontrolled transactions for every international transaction entered into by an associated enterprise.
- all the terms of contract (including price) are identical for both international and uncontrolled transactions. If they are not identical, the differences are quantifiable and can be adjusted.

However, if a reasonably accurate adjustment cannot be made, it may be necessary to combine the CUP method with other less direct methods, or to use other methods instead.

Advantages - This method is considered to be most reliable as it is highly objective. This method is particularly reliable where an independent enterprise sells the same product as is sold between two associated enterprises. It is also independent of the perspectives of the parties involved.

Limitations – The requirement of a high degree of comparability limits the use of this method. For example, a minor difference in the property transferred in the controlled and uncontrolled transactions could materially affect the price even though the nature of business activities undertaken may be sufficiently similar to generate the same overall profit margin. In such cases, adjustments would have to be made and the extent and reliability of such adjustments will affect the relative reliability of the analysis under the CUP method. Further, in certain cases, even where comparables are available, the overheads involved in searching for them are restrictive.

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(ii) Resale Price Method - This method determines the appropriate transfer price by ascertaining the price at which a product that has been purchased from a related enterprise is resold to an independent enterprise. This price is the “resale price”. The arm’s length price is computed by deducting the resale price margin from the resale price. The resale price margin is the amount that represents the selling and operating expenses and the normal gross profit margin of the seller who resells the goods. This method assumes that the goods are resold without any value additions.

For the purposes of the resale price method, an uncontrolled transaction is comparable to a controlled transaction if any one of the following two conditions are satisfied :

- any of the differences between the transactions being compared or between the enterprises undertaking those transactions do not affect the resale price margin in the open market; or
- reasonably accurate adjustments can be made to eliminate the material effects of such differences.

Applicability - This method would ideally apply in cases where there is a manufacturer-distributor arrangement, where the manufacturer bears a higher degree of risk whereas the distributor has only the routine functions and risks. The resale price method, when applied in these cases, using either transactions between closely comparable third parties or the distributor’s own transactions will help in appropriate determination of the arm’s length price.

Advantages – This method is easy to apply as the gross margins are calculated for a party having relatively routine and uncomplicated activities for which comparables can be easily identified.

Limitations – Since the resale price method depends on the comparability of functions performed, it may become less reliable when there are differences between the controlled and uncontrolled transactions and the parties to the transactions, and those differences have a material effect on the resale price margin realised. These differences should be adjusted and the extent and reliability of the adjustments will affect the relative reliability of the analysis under the resale price method. Another disadvantage is that this method can be applied only when the reseller does not add substantially to the value of the product.

(iii) Cost-plus method - Under this method, the arm’s length price is determined by adding an arm’s length mark-up to the costs of the supplier supplying goods to a related purchaser. The mark-up should be ideally established by reference to the cost plus mark up charged by the enterprise from a third party in a similar transaction or by an unrelated enterprise in a comparable uncontrolled transaction.

For the purposes of applying cost plus method, an uncontrolled transaction is comparable to a controlled transaction if any one of the two conditions are met:

- none of the differences between the transactions compared or between the enterprises undertaking the transactions materially affect the cost plus mark up in the open market; or

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- reasonably accurate adjustments can be made to eliminate the material effects of such differences.

Applicability - This method can be employed where semi-finished goods are sold between related parties, where related parties have concluded joint facility agreements or long term buy-and-supply arrangements, or where the controlled transaction is the provision of services.

Limitations - There is no mapping to the market prices, which is the case in CUP and resale price method. Further, since the method is applicable with respect to transfer of semi-finished goods, there is a limitation in applicability that comparables are required at every stage of the value chain, which might not be possible in every case.

(2) Transactional Profit Methods

Transactional profit methods are applied when traditional transaction methods cannot be reliably applied on a stand-alone basis or in exceptional circumstances when they cannot be applied at all. Transactional profit methods examine the profits that arise from particular transactions with associated enterprises. According to the OECD guidelines, the Profit Split Method and Transactional Net Margin Method are the acceptable methods for determining arm's length prices. Therefore, in those exceptional cases where traditional methods cannot be applied, these two methods can be applied for determining the transfer price in a manner consistent with the ALP provided all the relevant safeguards for applying these methods are observed.

(i) Profit Split Method – This method seeks to eliminate the effect on profits of special conditions made or imposed on a controlled transaction by determining the division of profits which the independent enterprises would have expected to realise from engaging in the transaction or transactions. This method first identifies the profit to be split between the related parties from the controlled transactions in which they are engaged. It then splits this profit between the associated enterprise on an economically valid basis which would have resulted had the profits been divided in an arm's length agreement. The contribution of each enterprise is to be based upon a functional analysis of the functions performed taking into account the assets used and risks assumed by each enterprise, and valued to the extent possible by any available reliable external market data. While using the profit split method to establish the conditions of controlled transactions, the associated enterprises seek to achieve the division of profit that independent enterprises would have realised. However, it must be ensured that this method is applied only on the basis of available information or information which can be foreseen by the associated enterprises at the time the transactions were entered into, to avoid the use of hindsight. Contribution analysis and Residual analysis are the two main approaches for estimating the division of profits based on either actual or projected profits that independent enterprises would have expected to realise.

Advantages - Since both the parties to the transaction are evaluated, the determination of transfer price will be as per the arm's length principle. This method can be used when there are no closely comparable transactions between independent enterprises. Further,

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it is less likely that either party will be left with an extreme and improbable result, because both parties are evaluated under this method.

Limitations – The external market data considered in valuing the contribution each associated enterprise makes to the controlled transactions will be less closely connected to those transactions than in the case with other methods. Further, the associated enterprises and tax administrations may have difficulty in accessing information from foreign affiliates.

(ii) Transactional net margin method (TNM) – This method determines the net profit margin relative to a base of costs, sales, or assets, etc. that a taxpayer realises from a controlled transaction. The net margin of the taxpayer from the controlled transaction should be established by reference to the net margin that the same taxpayer earns in comparable uncontrolled transactions. Where this is not possible, the net margin that would have been earned in comparable uncontrolled transactions may be used. A functional analysis of one of the related parties and of the independent enterprise, where appropriate, must be made to determine whether the transactions are comparable and what adjustments may be necessary to obtain reliable results.

Advantages – This method is based on net margins (e.g. return on assets, operating income to sales etc.) which are less affected by transactional differences than is the case with price, as used in CUP method. The net margins are also more tolerant to functional differences between controlled and uncontrolled transactions than gross profit margins since differences in the functions performed between enterprises are often reflected in variations in operating expenses. Another advantage is that it is not necessary to determine the functions performed and responsibilities assumed by more than one of the associated enterprises. Similarly, it is often not necessary to state the books and records of all participants in the business activity on a common basis or to allocate costs for all participants. This is of advantage when one of the parties to the transaction is complex and has many interrelated activities or when it is difficult to obtain reliable information about one of the parties.

Limitations – The net margin of a taxpayer can be influenced by some factors that either do not have an effect, or have a less substantial or direct effect, on price or gross margins. These aspects make accurate and reliable determinations of arm's length net margins difficult. In addition, taxpayers may not have access to enough specific information on the profits attributable to uncontrolled transactions to make a valid application of the method.

16.6 APPLYING THE ALP TO INTANGIBLES

(1) Meaning and Types of Intangible property

"Intangible property" - includes right to use industrial assets such as patents, trademarks, trade names, designs or models, literary and artistic property rights, and intellectual property such as know-how and trade secrets.

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“Commercial intangibles” - include patents, know-how, designs, and models that are used for the production of goods or the provision of services, as well as intangible rights that are themselves business assets transferred to customers or used in the operation of business. Commercial intangibles also known as trade intangibles are generally created through risky and costly research and development activities, and do not include marketing intangibles.

“Marketing intangibles” - include trademarks and trade names that aid in the commercial exploitation of a product or service, customer lists, distribution channels, and unique names, symbols or pictures that have an important promotional value for the product concerned. Intellectual property such as know-how and trade secrets can be either trade intangibles or marketing intangibles.

(2) Applying the ALP to Intangibles

Certain special considerations arise when determining whether the condition made or imposed in transactions between associated enterprises involving intangible property reflect arm's length prices -

General rules – The general rules for applying the ALP also pertain to intangible property transactions between associated enterprises. However, a transfer pricing analysis of intangible property must take into account the perspectives of both the transferor and the transferee. For the transferor, the ALP requires examining the price at which a comparable independent enterprise would be willing to transfer the property. For the transferee, whether a comparable independent enterprise would be prepared to pay a given price depends on the value and usefulness of the intangible property to the transferee in its business. Thus, all the facts and circumstances must be taken into consideration when determining the comparability of intangible transactions.

Arrangements made for transfer of intangible property - Intangible property is transferred either through outright sale or by a royalty under a licensing agreement. Compensation for the use of intangible property may be included in the price charged for the sale of goods, or the transfer price may be a package price for the goods and for the intangible property. In some cases, intangible property would be comprised in a package contract which includes right to patents, trademarks and know-how. In such cases, the parts of the package may have to be considered separately to verify the arm's length character of the transfer.

Factors for comparison – Special factors which are used to compare controlled and uncontrolled transactions involving intangible property are the expected benefits from intangible property; limitations on the geographical area in which the rights may be exercised; exclusive character of any rights transferred; export restrictions on goods produced by virtue of rights transferred; the capital investments, the start-up work, and the development work required in the market etc. For patents, the comparability analysis should take into account the nature of the patent, the degree and duration of the protection afforded under the patent laws of the relevant countries, and the duration of the economic value of the patent.

Calculation of an arm's length price – Generally, the CUP or resale price method should be used to determine an arm's length price for intangibles. Where the same owner has transferred or licensed comparable intangible property under comparable circumstances to independent enterprises, it is possible to use the CUP method to establish the ALP for sale or license of intangible property. Comparables can be identified in offers to unrelated parties or genuine bids of other competing licenses or the amount of consideration charged in comparable transactions between independent enterprises in the same industry. The Resale Price Method can be used if the associated enterprise subleases the intangible property to a third party. In cases involving highly valuable intangible property, it is difficult to apply the traditional methods and the transactional net margin method since it is difficult to find comparable uncontrolled transactions. In such cases, where both parties to a transaction own valuable intangibles, the profit split method can be used.

Comparability analysis – A comparability analysis for trade intangibles should examine the value to be attributed to such intangibles and also the importance of continuing the research and development functions. A comparability analysis for marketing intangibles should consider the value addition on account of the trademark, patent, know how etc. taking into consideration consumer acceptability, geographical significance, market shares, sales volume, and other factors.

16.7 APPLYING THE ALP TO INTRA-GROUP SERVICES

Main issues – The two main issues in the analysis of transfer pricing for intra-group services are whether services have been provided by one member of an MNC group to other members of that group and, if so, how to establish arm's length pricing for those intra-group services.

Determining whether intra-group services have been rendered – In order to determine whether intra-group services have been rendered it is necessary to examine whether the activity provides the group member with economic or commercial value to enhance its commercial position. If the activity is not one that an independent enterprise in comparable circumstances would have been willing to pay for or would have performed for itself in-house, then the activity ordinarily should not be considered to be an intra-group service under the ALP.

Determining the arm's length charge - The charge for intra-group services should be that which would have been made and accepted in comparable circumstances between independent enterprises. It is necessary to examine the actual arrangement between associated enterprises in order to determine the amount charged for services. There are two methods used – the direct charge method and the indirect charge method.

Direct-charge method – The direct-charge method charges associated enterprises a set price for specific services. This arrangement is most useful for MNCs that render similar services to both group members and to independent enterprises. Although the direct-

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charge method simplifies the determination of whether a charge is consistent with the ALP, it may be difficult to apply in practice.

Indirect-charge method – This method of cost allocation and apportionment may be used to determine an arm's length price in cases where intra-group charges are readily identifiable but not based on a direct-charge method or are not readily identifiable and either incorporated into the charge for other transfers, allocated among group members on some basis, or not allocated at all. Any indirect-charge method should reflect the facts and circumstances of each individual case, contain safeguards against manipulation, follow sound accounting principles, and produce charges or allocations of costs that are commensurate with the actual expected benefits to the recipient of the service, keeping in mind the extent to which comparable services are provided between independent enterprises.

Calculating the arm's length price –The factors to be taken into consideration for determining the arm's length price for intra-group services are the value of the service to the person in receipt of the same and the comparability of the amount paid for similar services provided to an independent enterprise and the costs to the person providing the service. These factors have to be taken into consideration while deciding the method to be adopted for calculating an arm's length price. CUP method would be ideal where there is a comparable service provided between independent enterprises, or provided by the associated enterprise to an independent enterprise under comparable circumstances. Cost-plus method may be used where the nature of activities involved, assets used, and risks assumed are comparable to those undertaken by independent enterprises.

16.8 THE INDIAN SCENARIO

In order to provide a statutory framework empowering the tax authorities to determine reasonable, fair and equitable profits and tax in respect of cross-border transactions, new sections 92 to 92F have been included in Chapter X of the Income-tax Act, through the Finance Act, 2001, providing for a transfer pricing mechanism based on computation of income from cross-border transactions. The following conditions must be satisfied in order to attract the special provisions of Chapter X relating to avoidance of tax:

- (i) There must be an international transaction;
- (ii) Such international transaction should be between two or more associated enterprises either or both of whom are non-residents;
- (iii) Such international transaction should be in the nature of:
 - (a) purchase, sale or lease of tangible or intangible property; or
 - (b) provision of service; or
 - (c) lending or borrowing money; or
 - (d) any other transaction having a bearing on the profits, income, losses or assets of such enterprise

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(iv) Further, such transaction may also involve allocation or apportionment of, or any contribution to any cost or expenses incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of the associated enterprises on the basis of mutual agreement or arrangement between such associated enterprises.

(v) Such international transaction must be done at arm's length price and if such international transaction has been done at less than the arm's length price, it shall require determination of income or apportionment of cost or expense on the basis of arm's length price.

(vi) The above adjustment should either result in an increase of income or decrease of loss returned by the assessee. In other words, the adjustment should not have the effect of reducing the income chargeable to tax or increasing the loss.

The Finance Act, 2001, has introduced provisions relating to pricing of international transaction between the assessee and associated enterprises. These provisions are contained in sections 92 to 92F of the Income-tax Act. These provisions apply to international transactions entered into with effect from 1st April, 2001. Rules 10A to 10E have been inserted in the Income-tax Rules by a notification dated 21st August, 2001. These sections of the Income-tax Act and the Rules will affect all non-corporate and corporate assesseees who have dealings with non-residents for import or export of goods, properties or services. In other words, price paid for import of goods, properties or services and price received for export of goods, properties or services will now be subject to scrutiny by the Assessing Officer. Therefore, it is necessary to make a detailed study of these provisions. All assesseees who have such dealings with non-residents will have to keep detailed records as prescribed under the Rules and will have to furnish audit report every year with the return of income about their international transactions.

The presence of multinational enterprises in India and their ability to allocate profits in different jurisdictions by controlling prices in intra-group transactions prompted the Government to set up an Expert Group to examine the issues relating to transfer pricing. There is a possibility that two or more entities belonging to the same multinational group can fix up their prices for goods and services and allocate profits among the enterprises within the group in such a way that there may be either no profit or negligible profit in the jurisdiction which taxes such profits and substantial profit in the jurisdiction which is tax haven or where the tax liability is minimum. This may adversely affect a country's share of due revenue. The increasing participation of multinational groups in economic activities in India has given rise to new and complex issues emerging from transactions entered into between two or more enterprises belonging to the same multinational group. The profits derived by such enterprises carrying on business in India can be controlled by the multinational group, by manipulating the prices charged and paid in such intra-group transactions, which may lead to erosion of tax revenue. Therefore, transfer pricing provisions have been brought in by the Finance Act, 2001 with a view to provide a

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statutory framework which can lead to computation of reasonable, fair and equitable profits and tax in India, in the case of such multinational enterprises.

16.8.1 Computation of income from transaction with non-resident [Section 92]

Section 92 provides that any income arising from an “international transaction” shall be computed having regard to “the arm’s length price”. For this purpose the allowance for any expense or interest shall be determined on the basis of arm’s length price. The section further provides that in an international transaction between two or more ‘associated enterprises’ when there is a mutual agreement or arrangement for the allocation or apportionment of, or any contribution to, any cost or expenses in connection with a benefit, service or facility provided to any one or more of such enterprises, the allocation of cost, expenses etc. shall be determined having regard to arm’s length price of such benefit, service or facility. Similarly, the price received for exports and amounts received for services rendered to associated enterprise will be determined on the basis of arm’s length price. It will be noticed that in the international transaction, the income or expense will have to be at arm’s length price if the transaction is between associated enterprises.

While determining Arm’s Length Price under the provisions of transfer pricing regulations, if the income works out to a figure lower than the income shown in the books of accounts, the provision of transfer pricing regulations will not apply.

The Assessing Officer will have wide powers to determine what is an arm’s length price for such transactions and make adjustments for computation of income. The keywords in section 92 are (i) associated enterprises, (ii) international transactions and (iii) arm’s length price. These terms are defined in sections 92A, 92B and 92C.

16.8.2 Associated Enterprises [Section 92A] : The term “associated enterprise” in relation to another enterprise is defined in section 92A(1). It means an enterprise -

- (a) which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or
- (b) in respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control of the other enterprise.

Section 92A(2) provides that two enterprises shall be deemed to be associated enterprises for the purposes of sub-section(1) if, at any time during the previous year -

- (i) one enterprise holds, directly or indirectly, shares carrying not less than twenty six per cent of the voting power in the other enterprise; or
- (ii) any person or enterprise holds, directly or indirectly, shares carrying not less than twenty-six per cent of the voting power in each of such enterprises; or
- (iii) a loan advanced by one enterprise to the other enterprise constitutes not less than

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fifty one per cent of the book value of the total assets of the other enterprise; or

- (iv) one enterprise guarantees not less than ten per cent of the total borrowing of the other enterprise; or
- (v) more than half of the board of directors or members of the governing board, or one or more executive directors or executive members of the governing board of one enterprise, are appointed by the other enterprise; or
- (vi) more than half of the directors or members of the governing board, or one or more of the executive directors or members of the governing board, of each of the two enterprises are appointed by the same person or persons; or
- (vii) the manufacture or processing of goods or articles or business carried out by one enterprise is wholly dependent on the use of know-how, patent, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights; or
- (viii) ninety per cent, or more of the raw materials and consumables required for the manufacture or processing of goods or articles carried out by one enterprise are supplied by the other enterprise, or by persons specified by the other enterprise, and the prices and other conditions relating to the supply are influenced by such other enterprise; or
- (ix) the goods or articles manufactured or processed by one enterprise, are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by such other enterprise; or
- (x) where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual; or
- (xi) where one enterprise is controlled by a Hindu undivided family, the other enterprise is controlled by a member of such Hindu undivided family, or by a relative of a member of such Hindu undivided family, or jointly by such member and his relative; or
- (xii) where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds not less than ten per cent interest in such firm, association of persons or body of individuals; or
- (xiii) there exists between the two enterprises, any relationship of mutual interest, as may be prescribed. It may be noted that the Rules 10A to 10E do not refer to any relationship of mutual interest.

Section 92A(1) lays down the circumstances when two enterprises can be considered as associated enterprises. The mere fact of participation by one enterprise in the management, control or capital of the other enterprise, or participation by one or more

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persons in the management, control or capital of both the enterprises is not sufficient unless the tests laid down in section 92A(2) are fulfilled. In other words, the deeming tests contained in section 92A(2) are exhaustive and should be applied to determine the association between two or more enterprises

Enterprise : The term “enterprise” is defined in section 92F to mean a person (including its certain specified Permanent Establishment) who is, or has been, or is proposed to be, engaged in any activity, relating to the production, storage, supply, distribution, acquisition or control of articles or goods, or know-how, patents, copy rights, trade-marks, licences, franchises or any other business or commercial rights of similar nature or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights, or the provision of services of any kind, or in carrying out any work in pursuance of a contract, or in investment, or providing loan or in the business of acquiring, holding, underwriting or dealing with shares, debentures or other securities of any other body corporate, whether such activity or business is carried on, directly or through one or more of its units or divisions or subsidiaries, or whether such unit or division or subsidiary is located at the same place where the enterprise is located or at a different place or places.

“Permanent establishment” includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.

16.8.3 International Transaction [Section 92B]: Section 92B defines the term “international transaction” to mean a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises. It shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expenses incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

Sub-section (2) provides for circumstances where, even a transaction with an enterprise which is not an associated enterprise as defined above, may be construed as transaction with an associated enterprise. It provides that a transaction entered into by an enterprise with a person other than an associated enterprise shall be deemed to be a transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise; or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise.

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Transaction: The word “transaction” has been defined in section 92F to include an arrangement, understanding or action in consent

- (i) Whether or not such arrangement, understanding or action is formal or in writing; or
- (ii) Whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings.”

It may be noted that one of the parties to the international transaction should be a non-resident. Therefore, transactions between a resident assessee (“A” Ltd.) and its foreign branches or between its two or more foreign branches will not be considered as international transactions. This is for the reason that when “A” Ltd. is a resident in India, all its foreign branches will be deemed to be resident in India and transactions between Head Office and branches or between branches inter-se will be considered as transactions between residents. Even otherwise there can be no avoidance of income in the transactions between Indian Head Office and foreign branches.

On the other hand, if an Indian branch of a foreign company (“B” Ltd.) is having a transaction with the head office the same will be covered by the definition of international transaction between associated enterprises. This is because the Indian branch (permanent establishment of “B” Ltd.) will be liable to tax in India in respect of its Indian operations and, therefore, any transaction between the Indian branches of “B” Ltd. with its head office in U.K. or with any of the branches of “B” Ltd. outside India will be considered as an international transaction and it will have to establish that the transaction is at an arm’s length price. This will be the position even in respect of transactions between a parent company (“A” Ltd.) and its foreign subsidiary and, therefore, such transactions will have to comply with the provisions of transfer pricing regulations.

16.8.4 Arm’s Length Price [Section 92C]: “Arm’s length price” is defined in section 92F(ii) to mean price which is applied or proposed to be applied in a transaction between persons other than associated enterprises in uncontrolled conditions. Section 92C deals with the method for determining arm’s length price and the factors which are to be considered for applicability or non-applicability of a particular method to a given situation. The factors as well as methods incorporated in this section are not exhaustive and the CBDT may prescribe further factors and methods. Section 92C provides that the arm’s length price in relation to an international transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe.

- (a) comparable uncontrolled price method;
- (b) resale price method;
- (c) cost plus method;

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- (d) profit split method;
- (e) transactional net margin method;
- (f) such other method as may be prescribed by the Board. So far no other method is prescribed.

Out of the above, the most appropriate method shall be selected in the manner as may be prescribed by the Rules. However, if under the most appropriate method two prices of the goods, services or intangibles are possible then the arithmetical mean of such prices shall be taken as Arm's Length Price.

Section 92C(2) provides that where more than one price is determined by the most appropriate method, the arm's length price shall be taken to be the arithmetical mean of such price. However, if the arithmetical mean, so determined, is within five per cent of the transfer price, then the transfer price shall be deemed to be the arm's length price and no adjustment is required to be made.

Example

Case	Transfer Price	ALP determined by applying the arithmetical mean	ALP for the Transfer Pricing Adjustment
1	100	105.1	105.1
2	100	104.9	100

Rule 10B(1) provides for determination of arm's length price under section 92C. This rule explains how the arm's length price under the five methods stated in (a) to (e) of Para 4.1 above is to be determined in respect of any goods, property or services (hereinafter referred to as "items") purchased or sold under any international transaction.

(i) Comparable Uncontrolled Price Method

- (a) Under this method the price charged or paid for any item under any comparable uncontrolled transaction or transactions should be identifiable.
- (b) Adjustment to account for differences between the international transaction and comparable uncontrolled transactions or between the enterprises entering into such transactions which could materially affect the price in the open market can be made.
- (c) The adjusted price as worked out under (b) will be considered as an arm's length price for the item.

(ii) Resale Price Method

- (a) Under this method, the price at which the item purchased by the enterprise from an associated enterprise is resold to an unrelated enterprise should be identifiable.
- (b) The following adjustments can be made to such resale price.

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For normal gross profit margin

For expenses incurred in connection with the purchase of the item.

For functional and other differences, including differences in accounting practices which could affect the gross profit margin in the open market.

- (c) The adjusted price as stated in (b) above will be considered as the arm's length price for the item.

(iii) Cost Plus Method

- (a) Under this method, the direct and indirect costs of production incurred by the enterprise for the item should be determined.
- (b) The amount of a normal gross profit mark-up to such costs arising from the same or similar item or by an unrelated enterprise in comparable uncontrolled transaction should be determined.
- (c) The above normal gross profit mark-up can be adjusted to take into account the functional and other differences which could materially affect such profit mark-up in the open market.
- (d) Costs referred to in (a) above should be increased by the adjusted profit mark-up as stated in (c) above and the price so arrived at will be considered as an arm's length price of the item.

(iv) Profit Split Method

- (a) This is a method which may be applicable mainly in international transactions involving transfer of unique intangibles or in multiple international transactions which are so inter-related that they cannot be evaluated separately for the purpose of determining the arm's length price of one transaction.
- (b) Under this method, combined net profit of the associated enterprises arising from the international transactions in which they are engaged is first determined.
- (c) The relative contribution of each associated enterprise to the earning of such combined net profit is then evaluated on the basis of the functions performed, assets employed and risks assumed by each enterprise. This evaluation is to be made on the basis of reliable external market data which can indicate how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances.
- (d) The combined net profit is then split amongst the enterprises in proportion to their relative contributions. The profit thus apportioned to the assessee is taken into consideration to arrive at an arm's length price in relation to the international transaction.
- (e) In certain cases the combined net profit referred to in (b) above may, in the first

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instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction in which it is engaged. This has to be determined with reference to market returns achieved for similar types of transactions by independent enterprises. Thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises as stated in (c) and (d) above. In such a case the aggregate of net profit allocated in the first instance together with the residual profit allocated should be considered for arriving at the arm's length price of the international transaction.

(v) Transactional Net Margin Method

- (a) In this method, the net profit margin realised by the enterprise from an international transaction with an associated enterprise is computed having regard to costs incurred or sales effected or assets employed or having regard to any other relevant base.
- (b) The net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction by applying the same base as in (a) above is computed. This profit margin is adjusted to take into account the differences which could materially affect the net profit margin in the open market having regard to international transaction and comparable uncontrolled transactions or having regard to the enterprise entering into such transactions.
- (c) If the net profit margin realised by the enterprise as in (a) above is established to be the same as the net profit margin as in (b) above, then the same is taken into consideration to arrive at an arm's length price in relation to the international transaction.

For applying the above methods, the comparability of the international transaction with an uncontrolled transaction is to be judged with reference to the following factors:

- (i) The specific characteristics of the property transferred or services provided in either transaction;
- (ii) The functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;
- (iii) The contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions;
- (iv) Conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, the laws and government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail.

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Rule 10B also provides that an uncontrolled transaction shall be comparable to an international transaction if none of the differences between the transactions being comparable or the enterprises entering into such transactions is likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market or reasonably accurate adjustments can be made to eliminate the material effects of such differences. Further, the date to be used for the above comparison should relate to the financial year in which the international transaction has been entered into. It is also provided that similar date relating to earlier two years can also be used for the comparison if such data is relevant for the purpose.

Determination of the most appropriate method

Rule 10C deals with the determination of most appropriate method. Under this Rule, the method which is best suited to the facts and circumstances and which provides the most reliable measure of an arm's length price in relation to the international transaction will be considered to be the most appropriate method.

For the purpose of selecting the most appropriate method, the following factors should be taken into account.

- (i) The nature and class of the international transaction;
- (ii) The class, or classes of associated enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises;
- (iii) The availability, coverage and reliability of data necessary for application of the method;
- (iv) The degree of comparability existing between the international transaction and the uncontrolled transaction and between the enterprises entering into such transactions;
- (v) The extent to which reliable and accurate adjustments can be made to account for difference, if any, between the international transaction and the comparable uncontrolled transaction or between the enterprises entering into such transactions;
- (vi) The nature, extent and reliability of assumptions required to be made in application of a method.

16.8.5 Reference to Transfer Pricing Officer [Section 92CA] : This section provides for a procedure for reference to a Transfer Pricing Officer (TPO) of any issue relating to computation of arm's length price in an international transaction. The procedure is as under -

- (1) The option to make reference to TPO is given to the Assessing Officer. He may make this reference if he considers it necessary or expedient to do so. This option is not available to the assessee.

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- (2) The Assessing Officer has to take the approval of the CIT before making such a reference.
- (3) Any Joint /Deputy/Assistant Commissioner of Income Tax, authorised by CBDT, can be appointed as TPO.
- (4) When such reference is made, TPO can call upon the assessee to produce evidence in support of the computation of arm's length price made by him.
- (5) The TPO has to pass an order determining the arm's length price after considering the evidence, documents, etc. produced by the assessee and after considering the material gathered by him. He has to send a copy of his order to Assessing Officer as well as the assessee.
- (6) The order of the Transfer Pricing Officer determining the arm's length price of an international transaction is now binding on the Assessing Officer and the Assessing Officer shall proceed to compute the total income in conformity with the arm's length price determined by the Transfer Pricing Officer [Sub-section (4)].
- (7) In order to provide sufficient time to the Assessing Officer to complete the assessment in a case where reference is made to the Transfer Pricing Officer, sub-section (3A) has been inserted in section 92CA to provide for determination of arm's length price of international transactions by the Transfer Pricing Officer at least 60 days before the expiry of the time limit under section 153 or section 153B for making an order of assessment by the Assessing Officer. This provision would apply in a case where reference is made on or after 1.6.2007 or in a case where reference is made before that date but the order of the Transfer Pricing Officer is pending on that date [Sub-section (3A)].
- (8) TPO has power to rectify his order under section 154 if any mistake apparent from the record is noticed. If such rectification is made, the Assessing Officer has to rectify the assessment order to bring it in conformity with the same.
- (9) TPO can exercise all or any of the powers specified in clause (a) to (d) of section 131(1) or section 133(6) for determination of arm's length price once the above reference is made to him.

16.8.6 Safe harbour rules to be introduced for determination of arm's length price in case of international transactions [Section 92CB]

- (i) *Section 92C provides for adjustment in the transfer price of an international transaction with an associated enterprise if the transfer price is not equal to the arm's length price. This has resulted in a large number of such transactions being subjected to adjustment giving rise to considerable dispute.*
- (ii) *Therefore, section 92CB has been introduced to empower the CBDT to formulate safe harbour rules to determine the arm's length price under section 92C and 92CA. Safe*

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harbour means circumstances in which the income-tax authorities shall accept the transfer price declared by the assessee.

16.8.7 Records to be maintained [Section 92D] : Section 92D imposes responsibility on every person who enters into an international transaction to keep and maintain such information and documents in respect thereof as may be prescribed by CBDT. The Board is empowered to prescribe the period for which the information and documents shall be kept and maintained. Further, the Assessing Officer or the Commissioner (Appeals) may, in the course of any proceedings under the Income-tax Act, require any person who has entered into an international transaction to furnish any such prescribed information or documents within a period of thirty days from the date of receipt of a notice issued in this regard. The requisition period may, on request, be extended further for a period not exceeding thirty days by the Assessing Officer or the Commissioner (Appeals).

Rule 10D(1) provides for the information and documents to be kept and maintained by the assessee. Under this Rule following information and documents have to be maintained:

- (i) A description of the ownership structure of the assessee enterprise with details of shares or other ownership interest held therein by other enterprises;
- (ii) A profile of the multinational group of which the assessee enterprise is a part along with the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom international transactions have been entered into by the assessee, and ownership linkages among them;
- (iii) A broad description of the business of the assessee and the industry in which the assessee operates, and the business of the associated enterprises with whom the assessee has transacted;
- (iv) The nature and terms (including prices) of international transactions entered into with each associated enterprise, details of property transferred or services provided and the quantum and the value of each such transaction or class of such transaction;
- (v) A description of the functions performed, risks assumed and assets employed or to be employed by the assessee and by the associated enterprises involved in the international transactions;
- (vi) A record of the economic and market analyses, forecasts, budgets or any other financial estimates prepared by the assessee for the business as a whole and for each division or product separately, which may have a bearing on the international transactions entered into by the assessee;
- (vii) A record of uncontrolled transactions taken into account for analysing their comparability with the international transactions entered into, including a record of the nature, terms and conditions relating to any uncontrolled transaction with third parties which may be of relevance to the pricing of the international transactions;

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- (viii) A record of the analysis performed to evaluate comparability of uncontrolled transactions with the relevant international transaction;
- (ix) A description of the methods considered for determining the arm's length price in relation to each international transaction or class of transaction, the method selected as the most appropriate method along with explanation as to why such method was so selected, and how such method was applied in each case;
- (x) A record of the actual working carried out for determining the arm's length price, including details of the comparable data and financial information used to apply the most appropriate method, and adjustments, if any, which were made to account for differences between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions;
- (xi) The assumptions, policies and price negotiations, if any, which have critically affected the determination of the arm's length price;
- (xii) Details of the adjustments, if any, made to transfer prices to align them with arm's length prices determined under the Income-tax Rules and consequent adjustment made to the total income for tax purposes;
- (xiii) Any other information, data or documents, including information or data relating to the associated enterprise, which may be relevant for determination of the arm's length price.

Rule 10D(2) provides that in a case where the aggregate value of international transactions does not exceed Rs.1 crore, it will not be obligatory for the assessee to maintain the above information and documents. Considering the wording of this Rule it appears that this limit will apply with reference to the aggregate value of the international transactions with each associated enterprise and not with reference to the aggregate value of the international transactions with all associated enterprises during the financial year put together.

However, it is provided that in the above cases also the assessee will have to substantiate that the income arising from the international transactions with associated enterprises, as disclosed by the accounts, is in accordance with section 92. This will mean that, even if the aggregate value of the international transactions is less than Rs.1 crore, the assessee will have to maintain adequate records and evidence to show that the international transactions with associated enterprises are on the basis of arm's length principles.

The information to be maintained by the assessee, is to be supported by authentic documents. These documents may include the following:

- (i) Official publications, reports, studies and data bases from the Government of the country of residence of the associated enterprise, or of any other country;

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- (ii) Reports of market research studies carried out and technical publications brought out by institutions of national or international repute;
- (iii) Price publications including stock exchange and commodity market quotations;
- (iv) Published accounts and financial statements relating to the business affairs of the associated enterprises;
- (v) Agreements and contracts entered into with associated enterprises or with unrelated enterprises in respect of transactions similar to the international transactions;
- (vi) Letters and other correspondence documenting any terms negotiated between the assessee and the associated enterprise;
- (vii) Documents normally issued in connection with various transactions under the accounting practices followed.

It is also provided that the information and documents to be maintained should be contemporaneous and should exist latest by the date specified for getting the audit report. In the case of international transactions which continue to have effect over more than one financial year, fresh documents will not be required to be maintained for each year if there are no significant change which may affect the determination of arm's length price. The above information and documents are required to be maintained for a period of eight years from the end of the relevant assessment year.

16.8.8 Power of Assessing Officer : Section 92C(3) and (4) gives power to the Assessing Officer to determine the arm's length price under the following circumstances and also empowers the Assessing Officer to re-compute total income of the assessee having regard to arm's length price determined by him. It also provides that deduction under section 10A, 10AA, 10B and Chapter VI-A shall not be allowed from the additional income computed by him. For example, if the total income declared by the assessee in his return of income is, say Rs.7 lakhs and the total income computed by the Assessing Officer applying the arm's length principle is, say Rs.9 lakhs, the difference of Rs.2 lakhs will not qualify for deduction under section 10A/10AA/10B or Chapter VIA.

The circumstances under which the Assessing Officer may invoke the power to determine arm's length price are as follows:

- (a) The price charged or paid in an international transaction has not been determined in accordance with section 92(1) and (2); or
- (b) Any information and documents relating to an international transaction has not been kept and maintained by the assessee in accordance with the provisions contained in section 92D(1) and the rules made in this behalf (Rule 10D); or
- (c) The information or data used in computation of the arm's length price is not reliable or correct; or

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- (d) The assessee has failed to furnish within the specified time, any information or documents which he was required to furnish by a notice issued under section 92D(3).

However, the CBDT has clarified in its Circular No.12 of 2001 dated 23.8.2001 that in the initial years of its implementation, there may be room for different interpretations leading to uncertainties with regard to determination of arm's length price of an international transaction. While it would be necessary to protect our tax base, there is a need to ensure that the tax payers are not put to avoidable hardship in the implementation of these regulations.

In this background the Board have decided the following.

- (i) The Assessing Officer shall not make any adjustment to the arm's length price determined by the tax payer, if such price is up to 5% less or up to 5% more than the price determined by the Assessing Officer. In such cases the prices declared by the tax payer may be accepted.
- (ii) It should be made clear to the concerned Assessing Officers that where an international transaction has been put to a scrutiny, the Assessing Officer can have recourse to sub-section (3) of section 92C only under the circumstances enumerated in clause (a) to (d) of that sub-section and in the event of material information or document in his possession on the basis of which an opinion can be formed that any such circumstance exists. In all other cases, the value of the international transaction should be accepted without further scrutiny.

Section 92C provides that if the total income of an associated enterprise is computed under this section on the determination of arm's length price paid to another associated enterprise, from which tax is deducted at source, the income of the other associated enterprise shall not be recomputed on this count. Therefore, if "A" Ltd. has paid royalty to "B" Ltd. (Non-Resident) @ 10% of sales and tax is deducted at source, "B" Ltd. cannot claim refund if the Assessing Officer has determined 8% as arm's length price in the case of "A" Ltd. and disallowed 2% of the royalty amount.

16.8.9 Audit Report [Section 92E]: Under section 92E, every person who enters into an international transaction during a previous year is required to obtain a report from a chartered accountant and furnish such report on or before the specified date on the prescribed form.

"Specified date" shall have the same meaning as assigned to due date in Explanation 2 below sub-section (1) of section 139.

Rule 10E provides that the auditor's report shall be in Form No.3CEB. This report is in two parts. The first part requires the auditor to state that he has examined the accounts and records of the assessee relating to the international transactions entered into by the assessee during the relevant year. He has also to give his opinion whether the prescribed information and documents relating to the above transactions have been kept by the

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assessee. Further, he has to state that the particulars stated in the Annexure to his report are true and correct.

In the second part of the report i.e. Annexure, the particulars about the international transactions are required to be stated. Broadly stated these particulars include list of associated enterprises, particulars and description of transactions relating to purchase, sales, provisions of service, loans, advances, etc.

It may be noted that the auditor is only required to give particulars about international transactions with associated enterprises. These particulars have to be classified under the different heads stated in the form. He is not required to give his opinion as to whether a particular transaction is at arm's length price or whether the method adopted by the assessee is the most appropriate method.

16.8.10 Penalties: Stringent penalties are provided in various sections for non-compliance with the above provisions. These are as under:

Section 271 provides for penalty in the cases where the Assessing Officer adjusts total income by determining arm's length price.

The penalty for such concealment is minimum 100% and maximum 300% of tax on such concealed income.

Sections 271AA and 271G provide for penalty for failure to keep and maintain transfer pricing information or documentation or to produce the same during assessment proceedings. It is provided that, if any person fails to keep and maintain any such information and documents as required by section 92D(1) and (2) or produce the same under section 92D(3), the Assessing Officer or Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to 2 per cent of the value of each international transaction entered into by such person.

Further, section 271BA provides for penalty for failure to furnish accountant's report. If any person fails to furnish a report from a chartered accountant as required by section 92E, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of Rs.1 lakh.

In all the above cases, if the assessee can show that there was reasonable cause for the failure, no penalty will be leviable.

16.9 TRANSFER OF INCOME TO NON-RESIDENTS [SECTION 93]

Section 93 hits at transactions which are effected with a view to avoiding liability to taxation. For the purpose, the word "non-resident" also includes a person who is not ordinarily resident. In order to attract the provisions of this section, all the following conditions must be satisfied:

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- (a) There is a transfer of assets - whether movable or immovable and whether tangible or intangible.
- (b) The transfer is made by any person in India or outside irrespective of his residential status or citizenship.
- (c) The transfer is made either alone or in connection with associated operations.
- (d) The assets transferred directly yield income chargeable to tax under this Act.
- (e) The transfer of assets is effected in such a manner that the income becomes payable to a person outside India who is either a non-resident or a not ordinarily resident in India.
- (f) The transferor acquires any right by virtue of which he gets the power to enjoy the income whether immediately or in future.
- (g) The Assessing Officer is satisfied that avoidance of liability to tax in India is the purpose of the transfers.

In particular, this section deems any income of a non-resident person which, if it were the income of a resident person, would be chargeable to tax in India (in the absence of this Section), as the income of the resident person in India for all purposes of the Act provided that all the conditions stated above are satisfied. This Section also covers a variety of transactions constituting a transfer including cases where assets are transferred to a non-resident person and the transferor indirectly derives income under the guise of obtaining loans or repayment of loans. If the aforesaid conditions are fulfilled, the income from the assets transferred should be treated as the income of the transferor and would accordingly be taxable in his hands. Therefore, where assets are transferred to a non-resident limited company, in consideration of shares allotted by it to the transferor, he (the transferor), will become assessable under this section in respect of the income of the company derived by it from those assets. By holding sufficiently large number of shares the transferor can be said to have acquired a right by virtue of which he has the power to enjoy the income of the company whether directly or indirectly and whether forthwith or in the future [*Chidambaram Chettiar vs. CIT (1960) 60 ITR 28 (SC)*].

This section will not, however, apply to cases where (i) the transfer is effected bonafide for adequate consideration and (ii) it is provided to the satisfaction of the Assessing Officer that the transfer was effected for *bonafide* commercial purpose and with no intent to avoid tax.

The income which is deemed to be that of the transferor under this section may arise either as a result of the transfer in connection with associated operations. But in both the cases, the treatment of the income would be the same. The expression 'associated operation,' in relation to a transfer as defined in sub-section (4)(b) of the section means an operation of any kind effected by any person in relation to:

- (i) any of the assets transferred;
- (ii) any assets representing, whether directly or indirectly any of the assets transferred;

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- (iii) any income arising from such assets;
- (iv) any assets representing, whether directly or indirectly, the accumulation of income arising from such assets.

In order to determine the liability of the assessee in respect of the deemed income it is immaterial if the income or benefits from the transfer (i) are actually received or not or (ii) are received or are receivable in cash or kind or (iii) are receivable directly or indirectly. For purposes of this section, a person is deemed to have the power to enjoy the income of a non-resident if:

- (i) the income, in fact, so dealt with by any person as to be calculated at some point of time to enure for the benefit of the transferor, whether in the same form of the income or otherwise;
- (ii) the receipt or accrual of the income operates to increase value of any assets held by the transferor or for his direct or indirect benefit;
- (iii) the transferor receives or is entitled to receive at any time any benefit out of the income or out of any money available for the purpose by reason of the effect or successive effects of the associated operations on that income and the assets which represent that income;
- (iv) the transferor is in a position to obtain for himself the beneficial enjoyment of the income by exercising any power of appointment or power of revocation or otherwise, whether with or without the consent of any other person, or
- (v) the transferor is able to control directly or indirectly the application of the income in any manner whatsoever.

But in determining whether a person has the power to enjoy the income due regard shall be had to the substantial result and effect of the transfer and any associated operations must be taken into consideration irrespective of the nature or form of the benefits.

However, where an assessee has been charged to tax in respect of a sum deemed to be his income under this section, the subsequent receipt of that sum by the assessee, whether as income or in any other form, shall not be liable to tax in his hands at the time of receipt.

16.10 TRANSACTIONS IN SECURITIES [SECTION 94]

Section 94 aims at preventing avoidance of tax by an assessee by sale or purchase of securities in devices and under different circumstances. In all cases where there is a transfer of shares or securities whereby the transferor avoids tax or shifts the burden of tax to some other person, the income from the securities transferred shall be deemed to be that of the owner (being the transferor) and shall be assessable in his hands accordingly. In order to attract the provisions of the section, the following conditions must co-exist as was held in *CIT vs. Sakarlal Balabhi (1986) 69 ITR 186* :

- (a) The transfer is of shares or securities;

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- (b) The income arising from the shares or securities is chargeable to tax as dividend or interest;
- (c) The transferor is the legal or beneficial owner of or a person having a beneficial interest in the shares or securities;
- (d) The income from the shares or securities becomes payable to a person other than the owner by virtue of the transfer;
- (e) The transfer may or may not have been effected for adequate consideration;
- (f) The assessee must effect the transfer deliberately with the intent to avoid tax. In other words, he must receive the amount which would have been liable to tax as his income but on which he avoids tax by some article or device.

Bond washing transactions : Bond washing transactions, i.e. cases of sale of securities and shares cum-interest or cum-dividend would fall within the provisions of the section. Income by way of interest on securities or dividends does not accrue day by day on certain fixed date or on the date of declaration, as the case may be. Accordingly, the seller of securities cum-interest or shares cum-dividends, on accrual of the interest, is not assessable on the interest or dividend income on the securities or shares sold by him since that part of the consideration received would be part of the capital price realised on sale. As a result, if a person, on the eve of payment of interest, sells or otherwise transfers his securities to another and buys back or re-acquires the same after the interest income had been received by the transfer would escape tax thereon. This would amount to either total avoidance of tax or shifting the burden of tax by the transferor indirectly and transactions of this type are commonly known as bond washing transaction. In order to prevent this type of avoidance of tax by the assessee, sub-section (1) specifically provides that where the owner of any shares or securities sells or otherwise transfers them and then buys them back or otherwise re-acquires them, the interest received by the transferee shall be the income of the transferor.

Similarly, in cases where shares or securities are sold by the owner of such shares or securities or by a person having beneficial interest therein and, as a result of the sale, the transferor receives either no income or less income from the securities or shares than that which would have been received by him, had the sale not been made, then the income from such securities or shares of such year shall be deemed to be the income of the transferor. Thus sub-section (2) applies only to cases where (i) the income accrues or falls due periodically and (ii) the income in question is of a recurring nature, though the interval of time between the two dates of accrual may not equal (e.g., dividends). However, the notional dividends specified in Section 2(22) would not be covered by this section and the assessment of such fictional dividends should be made only in the hands of the person who is entitled to the same and not in the hands of the transferor.

There is however, one exception to both the above provisions given in sub-section (3). According to the exception, the provisions of sub-section (1) and (2) would not

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apply (i) if there has been no avoidance of tax, (ii) if the avoidance was exceptional and not systematic and there was no avoidance of income-tax by the assessee during the three years immediately preceding the previous year. It is for the assessee to prove to the satisfaction of the Assessing Officer that there had been no avoidance of tax or that the avoidance of tax is exceptional and not systematic.

Where any person carrying on business, wholly or in part, as a dealer in shares and securities, buys or acquires any security and sells back or re-transfers the same, then, the interest, received or receivable by him in respect of such securities, which is deemed to be the income of the transferor, shall not be taken into account for computing his business income.

The Assessing Officer is empowered to issue a notice in writing requiring any person to furnish to him within a specified time (not being less than 28 days) in respect of all securities of which such person was the owner or in which he had a beneficial interest at any time during the period specified by him in the notice, such particulars as he may consider necessary for purposes of this Section and for the purpose of ascertaining whether tax has been borne in respect of interest or dividends on all those securities or shares.

The section also provides that where

- (a) any person buys or acquires any securities or unit within a period of three months prior to the record date and
- (b) such person sells or transfers –
 - (i) such securities within a period of three months after such date, or
 - (ii) such unit within a period of nine months after such date and
- (c) the dividend or income on such securities or unit received or receivable by such person is exempted,

then, the loss, if any, arising therefrom shall be ignored for the purposes of computing his income chargeable to tax. Such loss should not exceed the amount of dividend or income received or receivable on such securities or unit [Sub-section (7)].

Sub-section (8) provides that where –

- (a) any person buys or acquires any units within a period of 3 months prior to the record date;
- (b) such person is allotted additional units without any payment on the basis of holding such units on such date;
- (c) such person sells or transfers all or any of the units referred to in (a) above within a period of 9 months after such date, while continuing to hold all or any of the additional units referred to in (b), then –
 - (i) the loss on sale of original units sold within a period of 9 months after the record date will be ignored and

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- (ii) the amount of such loss will be considered as the cost of purchase or acquisition of the bonus units held by him on the date of such sale or transfer.

For the purposes of this section,-

- (a) "interest" includes a dividend;
- (b) "record date" means such date as may be fixed by a company or a Mutual Fund or the Unit Trust of India for the purposes of entitlement of the holder of the securities or the unit holder, to receive dividend or income, as the case may be; It also includes such date on which a unit holder is allotted or is entitled to additional units without any payment;
- (c) "securities" includes stocks and shares;
- (d) securities shall be deemed to be similar if they entitle their holders to the same rights against the same persons as to capital and interest and the same remedies for the enforcement of those rights, notwithstanding any difference in the total nominal amounts of the respective securities or in the form in which they are held or in the manner in which they can be transferred.

Self-examination questions

1. Discuss the meaning of the term "Arm's length principle" and its significance.
2. What are the practical difficulties in application of arm's length principle?
3. What are the guidelines to be followed while applying the arm's length principle?
4. Discuss the methods for calculating arm's length price, briefing the advantages and limitations of each method.
5. What are the issues involved in applying arm's length principle to -
 - (a) Intangibles
 - (b) Intra-group services.
6. What is the legislative objective of bringing into existence the provisions relating to transfer pricing in India?
7. Discuss the meaning of the following terms -
 - (a) Associated Enterprise
 - (b) International Transaction
8. What is the procedure for making reference to a Transfer Pricing Officer?
9. What are the information and documents prescribed under Rule 10D to be kept and maintained by the assessee?
10. Write short notes on -
 - (a) Bond washing transactions
 - (b) Dividend stripping.

FOREIGN COLLABORATION

17.1 INTRODUCTION

The globalisation of economic reforms throughout the world has led to an increasing degree of inter-dependence between countries in the fields of technology, manpower, finance, etc. The Indian economy too has been and is continuing to be liberalised by successive Governments through the mode of reducing custom duties and of other levies, relaxing foreign exchange regulations and by encouraging boost in exports. The survival and growth of the industrial sector depends to a great extent upon technological advancement. This is possible through collaborations with developed countries to import their expertise and aid. While drafting foreign collaboration agreements both parties have to necessarily take into consideration the tax laws in the respective countries. This is necessary so as to ensure, on the one hand, that the statutory requirements under the various tax laws in India and the other country are met, as also, on the other hand, to minimise the burden of tax which falls on the income, profits and gains arising from the collaboration. The chapter studies the different forms in which foreign collaborations may be made and the tax implications involved therein.

17.2 TAX LIABILITY BASED ON RESIDENTIAL STATUS

17.2.1 Non-resident: Foreign collaborators are generally non-residents in India. In this context, 'non-resident' means a person who is a non-resident as per section 2(30) of the Income-tax Act, 1961. You are already familiar with the concept of residential status as laid down in section 6 of the Income-tax Act. Foreign collaborators are generally companies incorporated outside India. Therefore, they could be regarded as non-resident within the meaning of section 6(3) since, in the case of foreign companies, the whole of the control and management of the affairs of such a company would not be situated in India, the place of carrying on the business and having transactions and operations being immaterial for the purpose. If, however, the foreign collaborator is a partnership firm or an association of persons, it would be regarded as being resident in India in every case where even a negligible portion of the control and management of the affairs of the firm or association is situated in India; in other words, only if the whole of the control and

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management of the affairs of the foreign collaborator, firm or association is situated outside India, the status of non-resident could be claimed for purposes of income-tax in India. Foreign collaborations are generally not brought about between individuals, although there is no prohibition in the law for doing so.

If, however, a foreign collaborator is an individual, the residential status of the foreign collaborator will have to be determined under section 6(1) on the basis of the number of days of his stay in India during the relevant accounting year.

17.2.2 Test for residence: The tests for residence as aforesaid should be applied to determine the residential status of the taxpayer in respect of each assessment year because the assessee who is resident in one year may be regarded as non-resident in another and vice versa. The determination of residential status should, in every case, be made with reference to the previous year followed by the foreign collaborator for his sources of income in India. Thus, in cases where a foreign collaborator is regarded as resident in India in respect of any one of his different sources of income having regard to the previous year followed for that source, in respect of the assessment year in which the income from that source for the relevant previous year would become assessable, the foreign collaborator must be regarded as resident in India although, in respect of his other sources of income and the previous years followed for the purpose, the assessee may not be regarded as resident. The fact that the taxpayer has been assessed as a resident in an earlier year would not preclude him from claiming the status of a non-resident in the subsequent year if the status for that year is really that of a non-resident.

It must be noted that before the amendment by the Finance Act, 2003, under clause (6) of section 6, a person is said to be "not ordinarily resident" in India in any previous year if such person is an individual who has not been resident in India in nine out of ten previous years preceding that year, or has not during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, seven hundred and thirty days or more.

The status of 'not-ordinarily resident' was incorporated in the statute book as an incentive for non-residents to bring their savings to India at the time of permanent settlement. By this provision their global income would not suffer tax for a period of nine years after they settled in India. However, it has been found that this provision was used by many wealthy resident Indians to avoid tax on income arising outside India. The Gujarat High Court in *Pradip J Mehta v. CIT (2002) 256 ITR 647 (Guj.)* held that where the assessee was a resident in India in 8 out of 10 previous years preceding that year and during last 7 previous years he had stayed in India for a period of 1402 days he could not be treated as 'not ordinarily resident' but his status would be that of resident.

The old definition has been substituted with a new definition by the Finance Act, 2003, to provide that a person would be "not ordinarily resident" in India in any previous year if such person is an individual who has been non-resident in India in nine out of the ten previous years preceding that year, or has during the seven previous years preceding that

year been in India for a period of, or periods amounting in all to, seven hundred and twenty-nine days or less.

Thus, this amendment has the effect of restricting the benefit of the status of 'not ordinarily resident' in the case of a non-resident Indian coming back to India or foreign citizens working in India to only a period of 2 years as against the earlier benefit of 9 years. Hence, a non-resident coming back to India will have to pay tax on their global income after a period of 2 years. Similarly, foreign citizens working in India will be required to pay tax on their global income if they continue to be resident in India beyond a period of 2 years.

This amendment may, however, have a negative impact on the inflow of funds through the medium of non-residents.

17.2.3 Scope of income chargeable: As already discussed in earlier chapters, the scope of income chargeable to tax in the case of a non-resident is laid down in section 5(2) of the Act.

According to this provision, the total income of any previous year of any person who is non-resident must be taken to include all income from whatever source derived which – (i) is received or deemed to be received in India in such year by or on behalf of the non-resident; or (ii) accrues or arises or is deemed to accrue or arise to the non-resident in India during the previous year.

Explanation 1 to section 5 seeks to clarify that income accruing or arising outside India would not be deemed to be received in India for purposes of determination of the total income of the assessee under section 5 merely by reason of the fact that it has been taken into account in a balance sheet prepared in India. In other words, for determining whether a particular income accrues or arises in India or outside, one should not be guided by the entries in the books of accounts and disclosure thereof in the final accounts; it is, therefore, essential to determine the place of actual accrual of the income for purposes of inclusion or exclusion of the same within the scope of total income assessable to tax. *Explanation 2* to section 5 further clarifies that income which has been included in the total income of a taxpayer on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him, should not be again so included on the basis of its actual or deemed receipt in India either by the assessee or on his behalf.

Exemption available to non-residents: Apart from the scope of tax liability being less in the case of non-residents, there are other concessions available to persons who are resident but not ordinarily resident. They are entitled to concessional rates of tax in respect of their income chargeable to tax in India.

Interest on fixed deposits with banks abroad would be taxable in India if such income by way of interest is received in India or the right to receive the same is exercised by the individual in India. Interest on non-resident external non-repatriable deposits as well as Non-resident External Rupee Deposits in the banks in India would be exempt under

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section 10(4) of the Income-tax Act subject, however, to the limits and conditions specified therein. In respect of assets acquired by investment through foreign exchange remittances the concessional rates of income tax would continue to be available to non-resident Indians in respect of their investment income including capital gains under section 115C read with sections 115D, 115E and 115H.

17.2.4 Choice of residential status: An assessee can change his residential status by changing the place of control and management of the affairs of the business (in the case of persons other than individuals) or by increasing or decreasing the number of days of stay in India (in the case of individuals). This may be done from the point of view of what is beneficial to him. In this context it may be kept in mind that if the foreign collaborator is incurring losses outside India, a change in status from non-resident to resident would allow the losses incurred outside India to be set off against income earned in India.

17.3 CHOICE OF PLACE WHERE INCOME IS TO BE RECEIVED

The scope of liability to tax of the non-resident should be clearly identified in the foreign collaboration agreement in every case as part of the process of tax planning by foreign collaborators. Under section 5(2) of the Income-tax Act, a non-resident is chargeable to tax in respect of income on two grounds, namely (i) receipt of income, whether actual or deemed, by or on behalf of the assessee; and (ii) accrual of such income, whether actual or deemed, in India to the assessee. The efforts at tax planning should, in every case, ensure that wherever practicable, the income of a non-resident which accrues or arises outside India and is not deemed to accrue or arise in India, is not first received in India. This is because of the fact that the mere receipt of income by or on behalf of the non-resident in India would attract liability to tax regardless of the question whether the income is due to be received in India or not and also whether it is received in cash or in kind.

When once it is established that income has been received as such, outside India, the mere remittance thereof to India would not attract any tax in India for the simple reason that the same income cannot be received more than once as was held by the Supreme Court in the case of *Banaras State Bank Ltd. v. CIT* (1970) 75 ITR 167 (SC).

Another important point to be kept in mind is whether the amount to be received is in the nature of a capital sum not being a capital gain. Receipts of a capital nature may be received in India without attracting any tax liability. Further, the Apex Court has ruled that wherever the receipt of income is in some form other than cash and liability to tax is attracted thereon, the market value of the items received should be determined and that along should be taken as the amount of income assessable to tax. [*CIT v. Central India Industries Ltd.* (1871) 82 ITR 555 (SC).]

In the case of payments made by cheque, the general principle for determining the place of receipt of income by cheque is that the income is received at the place where the bank on which the cheque is drawn is situated; if, however, the cheque is encashed by the

foreign collaborator by discounting the same in the foreign country with his bank situated outside India, the income must be regarded as having been received at the place where the money attributable to the cheque is credited and withdrawn. Wherever it is the intention of the parties to secure that the foreign collaborator does not receive the moneys due to him under the agreement within India, the amount can be sent by a demand draft payable in the foreign country by the branch of a bank which is located at the place or near the place of office or residence of the foreign collaborator. Thus, the making of payment by drafts instead of cheques would help to shift the place of receipt of income by the foreign collaborator.

17.4 CHOICE OF METHOD OF ACCOUNTING

Under section 145 of the Income-tax Act read with sections 28 and 56 thereof, the determination of the liability to tax in India depends not only upon the receipt of accrual of income but also upon the method of accounting followed by the assessee. The foreign collaborator can choose whether to follow the cash system or the mercantile system of accounting.

Thus, in a case where the foreign collaborator adopts the cash system of accounting, the receipt of income during a particular accounting year would make him chargeable to tax in respect of the moneys received as income. On the other hand, if the accounts of the foreign collaborator are maintained on mercantile basis, the income would be taxable immediately when the right to receive the same has accrued or arisen, the actual receipt being immaterial. Where the income has first accrued or is deemed to have accrued in India and is taxable because of the assessee adopting the mercantile system of accounting for that source, its subsequent receipt would be immaterial because the income having already been taxed on the basis of accrual, it cannot again be taxed on the basis of receipt in view of the express provisions of *Explanation 2* to section 5.

However, it must be kept in mind that once a particular method of accounting has been opted for, it cannot be changed without sufficient reason.

17.5 CHOICE OF FORM OF BUSINESS ORGANISATION

While embarking on any joint venture project in a foreign country, it is most essential to identify and pre-determine the form of business organisation which would be most appropriate to carry on the joint venture activities in the foreign country.

The income-tax law in India impose liability to tax based purely on the residential status of the taxpayer and the tests for ascertaining whether a particular taxpayer is resident or non-resident in India have to be determined by applying different criteria prescribed for different categories of taxpayers. It is for the assessee in India as well as the other party in the foreign country to identify and decide in advance that form of business organisation which would be advantageous from the tax angle.

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The joint venture may be in the form of incorporating a new company or may be in the form of a partnership firm. A third form is the establishment of an association of persons or body of individuals such as a society or a trust. Though there is no restriction for an individual or HUF to carry on joint ventures outside India, it becomes practically rather difficult and uncertain in terms of accountability and permanency.

In the case of a company, the test of residence specified in section 6 of the Income-tax Act requires that for the company to be regarded as resident in India, the company must be either an Indian company within the meaning of section 2(26) or a company the control and management of which is wholly situated in India. If, therefore, the control and management of the affairs of the company is carried out even to a very negligible extent from outside India, the company would be regarded as non-resident and would accordingly be liable to tax in India only on the income which accrues or arises or is deemed to accrue or arise to it in India. Although a non-resident company is subject to tax at higher rates of income-tax as compared to a resident company, the tax base for a non-resident company is confined to its Indian income and, therefore, its foreign income would not suffer tax in India. It is to take advantage of this scheme of income-tax law that one should consider the establishment of a foreign company in the country where the foreign project has to be carried out so that the income by way of profits or losses arising from or attributable to that foreign project is kept outside the purview of Indian tax laws.

On the other hand, if the foreign project in the form of a joint venture is established as a partnership firm, the test applicable for residence would be exactly opposite and materially different. This is because of the fact that in the case of a partnership firm, it is considered to be resident in India within the meaning of section 6 of the Income Tax Act in every case where even a negligible portion of the control and management of the affairs of the firm is carried out from India. If it is desirable to have a taxable entity which would be in a position to claim set off of foreign losses against the Indian income or Indian losses against the foreign income, it would be advisable for the assessee to do so having regard to the facts and circumstances of the case and a reasonable estimation which one could make by proper financial analysis and project planning of the profits and losses of the taxpayers concerned in India and outside.

The other forms of organisations such as trusts, co-operative societies or societies of a general nature and other associations of persons or bodies of individuals could also be thought of to suit the convenience of the parties because even in the case of those associations, bodies or societies, the criteria for determining the residential status would be the same as the one followed in the case of the partnership firms.

But the advantage is that these kinds of entities would also keep the taxpayers free from the difficult circumstances or problems arising from the assessments of partnership firms and their partners to income-tax in India resulting in considerable uncertainties in this regard both for the firms and for the partners.

Depending upon the form of business organisation chosen, the assessee could also shift the place of control and management of the affairs of that organisation to India or outside, whether wholly or partly, to secure that the assessee in question is a resident or non-resident in India for the relevant depending upon what is beneficial from the income-tax angle.

Since each year is a separate and self contained period, it is permissible for the assessee to be resident in one year and to become non-resident in another and such a change can, however, be contemplated or brought about only if the form of organisation is properly thought out. The tax base and consequently the burden of tax, particularly in India would, therefore, be dependent upon the choice made in this regard not only at the beginning but also from year to year.

17.6 TAXABILITY OF DIFFERENT KINDS OF INCOME

17.6.1 Interest income: Under section 2(28A) 'interest' means interest payable in any manner in respect of any moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation) and includes any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised. The definition of interest also includes any service fee or other charges in respect of loans, debts, deposits, etc. as well as commitment charges on non-utilised portion of credit facilities.

Section 9(i)(v) provides that income by way of interest payable by the Government, or by a person who is resident or by a person who is a non-resident, shall be income deemed to accrue or arise in India. However, the following exceptions have been provided:

- (i) interest payable by a resident in respect of any debt incurred or any moneys borrowed and used for the purposes of a business or profession carried on by him outside India;
- (ii) interest payable by a resident in respect of any debt incurred or any moneys borrowed and used for the purpose of making or earning any income from any source outside India;
- (iii) interest payable by a non-resident in respect of any debt incurred or money borrowed and used for the purpose of a business or profession carried on by him in India.

In other words, in the above situations, the income would not be deemed to accrue or arise. For instance, if 'X', a non-resident, borrows from 'Y', another non-resident, and invests the amount as a deposit in an Indian company, the interest payable by 'X' to 'Y' would not be deemed to accrue in India; but the interest receivable by 'X' from the Indian company is taxable in India as it actually accrues in India under section 5(1)(c). Likewise, if a lead bank obtains loans outside India from a consortium of foreign banks and lends the same to an Indian concern, the interest paid by the lead bank to the members of the consortium would not be deemed to accrue in India as has been clarified in the CBDT Circular No. 202 dated 5.7.1976.

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17.6.2 Royalty: Royalty has been defined in Explanation 2 to section 9(1)(vi) to mean the consideration (including any lump sum consideration but excluding any consideration which would be the income of the recipient chargeable under the head 'capital gains') for –

- (i) the transfer of all or any rights (including the granting of a licence) in respect of a patent, invention, model, design, secret formula or process or trade mark or similar property;
- (ii) the imparting of any information concerning the working of or the use of patent, invention, model, design, secret formula or process or trade mark or similar property;
- (iii) the use of any patent, invention, model, secret formula or process or trade mark or similar property;
- (iv) the imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;
- (v) the transfer of all or any rights including the granting of a licence in respect of any copyright, literary, artistic or scientific work including films or video tapes for use in connection with television or tapes for use in connection with radio broadcasting but not including consideration for the sale, distribution or exhibition of cinematographic films; or
- (vi) the rendering of any service in connection with the activities referred to in (i) to (v) above.

Further, CBDT Circular No. 202 dated 5.7.1976 has clarified that 'royalty' would include both industrial royalties and copyright royalties.

Section 9(1)(vi) deems income by way of royalty as accruing or arising in India in the following three cases:

- (i) Royalty payable by the Central Government or any State Government must be deemed to accrue in India regardless of who is the payee and what is the amount of royalty and also irrespective of the purpose of the payment;
- (ii) Royalty payable by any resident taxpayer to any person, whether resident or non-resident, would be deemed to accrue in India in every case except where the payment is relatable to a business or profession carried on by the resident outside India or to any other source of his income outside India; and
- (iii) Royalty payable even by a non-resident would be deemed to accrue in India in cases where the payment is relatable to any business or profession carried on by the non-resident in India or to any other sources of the non-resident's income in India.

However, the definition excludes any income which might otherwise be chargeable as capital gains. Thus, a receipt of a capital nature for the total change in ownership of the patents, invention, model, design, drawings, specifications, trade mark, secret formula or process, data, documentation, etc. representing technical know-how provided by foreign

collaborators to Indian taxpayers would not give rise to income by way of royalty while the authority given under the collaboration agreement to the Indian taxpayer to use for the purpose of his business the drawings, designs, patents, etc., representing technical know-how which would continue to belong to the foreign collaborator would come within the purview of royalty for purposes of deeming the same accruing in India, thus, making the non-resident liable to tax under this provision. For this purpose, it is immaterial whether the royalty is paid as a lump sum or as a recurring payment; it is also immaterial whether the royalty is described as such under the collaboration agreement or is known as licence fees, copyright charges or by any other name.

Under section 115A (1)(b)(A), royalty income is taxable in the hands of non-corporate non-residents and foreign companies at the rate of 10% if it is received in pursuance of an agreement made after 31st May, 2005, 20% if it is received in pursuance of an agreement made after 31st May, 1997 but before 1st June, 2005, and at the rate of 30% if such agreement is made on or before 31st May, 1997. The conditions attached to this provision are as follows:

- (i) The recipient of the royalty should be a foreign company or a non-corporate non-resident.
- (ii) The royalty may be received from the Government or an Indian concern.
- (iii) The royalty should be received in pursuance of an agreement made by the foreign company with the Government or the Indian concern after 31st March, 1976.
- (iv) Where the agreement is with an Indian concern, it should be approved by the Central Government.
- (v) Where the agreement relates to a matter included in the industrial policy (prevailing at that time) of the Central Government, the agreement should be in accordance with that policy.
- (vi) The conditions (iv) and (v) shall not apply where the royalty is received in consideration for the transfer to an Indian concern, all or any rights in respect of copyright in any book, or for the transfer to a person resident in India, any computer software.
- (vii) In computing the royalty income, no deduction shall be allowed under sections 28 to 44C and section 57.

It is to be noted that section 115A is not applicable in respect of royalty income covered under section 44DA (1).

17.6.3 Fees for technical services: For the purpose of taxation, technical services fees are treated similarly as royalty income.

Explanation 2 to section 9(1)(vii) defines 'fees for technical services' as any consideration (including lump sum consideration) for the rendering of any managerial, technical or

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consultancy services (including the provision of services of technical or other personnel) but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient.

Further, any income of the recipient chargeable under the head “salaries” will also not form part of fees for technical services.

The taxability of fees received for technical services is on similar lines as royalty income. Under section 115A(1)(b)(B), income-tax shall be charged at 10% if the technical fees has been received in pursuance of an agreement made after 31st May, 2005, at 20% if such fees are received in pursuance of an agreement made after 31st May, 1997 but before 1st June, 2005, and at 30% if the said agreement was made on or before 31st May 1997. No deduction shall be allowed under sections 28 to 44C and section 57 in respect of any expenditure or allowance, for the purpose of computing the aforesaid income. In this regard, the following issues are relevant. When a foreign collaboration agreement provides for technical know-how, engineering and allied services to the company in India and out of the total fee payable, a specified amount is identified as cost of supervision of the work of erection and commissioning of the plant, only that amount of money which is paid to the employer for technical services would be regarded as fees for technical service. The balance would be treated as royalty. [*CIT vs. Krebs & Co. (1998) 229 ITR 615 (MP)*].

Section 115A, however, does not apply in respect of fees for technical services covered under section 44DA (1).

17.6.4 Transfer of know-how: Royalty payments may be in exchange for something in addition to the mere use of the invention. Usually the licence contracts include “know-how” provisions. In other words, the licensor not only grants the right to use the invention but also undertakes to supply the licensee with technical ‘know-how’. The Madras High Court in *Fenner Woodroffe & Co., vs. CIT (1976) 102 ITR 665 (Mad.)* has explained that know-how may be taken as comprehending within it the fund of knowledge or experience gained by a manufacturer during the long number of years in which they had been manufacturing on the formulae, the engineering drawings and specifications, mechanical details or processes and general knowledge that is associated with the production and development which is in the exclusive knowledge of the trade.

Know-how is also referred to as a manufacturing technique. It is an intangible asset. The House of Lords in *Moriarty vs. Evans Medical Supply Ltd. (1959) 35 ITR 707* laid down the criteria to be applied to determine whether the transaction involving dealings in know-how would constitute a receipt of payment of a capital or revenue nature. If the assessee sells its know-how and realises the price for the same, the money realised for providing the know-how would be a receipt of a capital nature. On the other hand, in a case where the assessee who owns the know-how continues to own it and allows the other person only the right of use of such know-how the payments received towards the use of the know-how by another person would be a revenue receipt liable to tax. The question whether the

transaction involved is one of purchase or sale of know-how or is that of allowing the other person the right to use it will have to be determined with reference to the facts and circumstances of the case. Where the receipt is of a capital nature, it would be wholly outside the purview of tax under section 9(1)(vi) as royalty. Further, receipts of a capital nature which would otherwise have been liable to tax under the head "capital gains" (e.g. on transfer of patents, designs, drawings, secret formula, etc. forming part of the know-how) would not be liable to tax in the hands of the collaborator in India particularly when the transfer does not take place in India. Therefore, only if the transfer takes place in India, the non-resident collaborator would attract liability to capital gains tax in respect of the transfer of know-how, but not otherwise.

17.6.5 Export of goods from India by non-residents: Clause (b) of the Explanation to section 9(1)(i) of the Act provides that in the case of every non-resident, no income should be regarded as being deemed to accrue or arise to him in India through or from operations which are confined to the purchase of goods in India for the purpose of export. Thus, even in cases where the non-resident has an agency or office in India but the agent or branch office in India does nothing more than the purchase of the goods for their export, there would be no question of income accruing to the non-resident under the deeming provisions although in effect the non-resident may derive income outside India from the goods so exported ultimately on their sale outside India and the profits arising from such export are traceable to the business connection in India through the agency, branch or office. The exemption is, however, subject to the non-resident taking precaution to ensure that even a negligible part of the goods manufactured are not sold in India and the whole of the goods manufactured are only exported. The country to which the export is made is immaterial for the purpose. In the context of expanding the scope for diversification of the business of Indian enterprises particularly in cases where the market for the products manufactured is quite good outside India, it would be advisable for the non-residents to set up branch offices, agencies, etc. in India for manufacturing the export goods so that the whole of the income arising from such foreign collaboration to the non-resident does not attract liability to income-tax in India. Of course, care should be taken in every case to secure that no part of the sale proceeds for the goods exported is received directly or indirectly, in cash or in kind in India by or on behalf of the non-resident. In view of this benefit of total exemption from income-tax without any monetary or other limits and conditions, every possible export should be made by foreign collaborators and their Indian counterparts to secure that the benefit of exemption under clause (b) of the Explanation to section 9(1)(i) is obtained, wherever practicable.

17.6.6 Tax liability of Foreign Telecasting Companies (FTCs): The genuine interest evinced in the broadcasting media both by Indian and by foreign governments as well as enterprises gave rise to closer projections and this, in turn, led to the foreign telecasting companies through the satellite media to beam advertisements of foreign products in India and of Indian products abroad. The foreign telecasting companies have opted to function from abroad without having a permanent establishment in India and the question whether

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they are liable to tax in India on the moneys by way of advertisement received or receivable from Indian enterprises has been examined by the Central Board of Direct Taxes in pursuance of representations from foreign telecasting companies.

Circular No. 6 of 2001, dt. 5.3.2001 issued by CBDT explains the governmental stand as under:

1. The Central Board of Direct Taxes vide Circular No. 742 dated 2.5.1996 [(1996) 132 ITR (ST) 9] had laid down certain guidelines for the computation of profits of FTCs from advertisement payments received by them from India. These guidelines were extended till further orders by Circular No. 765 dated 15.4.1998 [(1998) 146 CTR (ST) 5]. The Central Board of Direct Taxes hereby withdraws the above circular with effect from 31.3.2001.
2. The total income of FTCs from advertisements, hitherto computed on a presumptive basis shall now be determined by the Assessing Officers in accordance with the other provisions of the Income-tax Act, 1961, in relation to assessment year 2002-2003 and subsequent assessment years. In case, accounts for Indian operations are not available, the provisions of rule 10 of the Income-tax Rules, 1962 may be invoked. Where an FTC is a resident of a country with whom India has a Double Taxation Avoidance Agreement (DTAA), its business income (including receipts from advertisement) can be taxed only if it has a Permanent Establishment in India. Therefore, the taxability of an FTC in this regard shall be determined on the facts and circumstances of each case. Taxation of FTCs who are residents or countries with whom India does not have a DTAA, shall be governed by the provisions of section 5 read with section 9 of the Income-tax Act, 1961.
3. It may be reiterated that the guidelines for computation of profits of FTCs Circular Nos. 742 and 765 were applicable only to the income stream from advertising. Other kinds of income like subscription charges receivable from cable operators in respect of pay channels and income from the sale or lease of decoders etc. shall continue to be taxed in accordance with the paragraph 2 above.

[F. No. 500/50/1996-FTD – From Central Board of Direct Taxes]

17.7 TAX TREATMENT OF PAYMENTS MADE FOR EXPENSES, ETC.

The carrying on of a business in India by different categories of taxpayers involves a variety of expenses being incurred by them both in India and outside. The nature and amount of the expenses would, however, depend on the nature of the business, the purpose of incurring the expenditure and the stage at which it is incurred. Of these, a substantial portion of the expenditure is incurred after the business of the taxpayer in India is actually set up. The expenses incurred prior to the setting up of the business do not qualify for any allowance or deduction in computing the taxable profits of the business in India since the previous year of the business cannot be regarded as having commenced

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until the business is actually set up. Therefore, expenses which are incurred prior to the setting up of business and which are directly related to the acquisition of capital assets including their installation, whichever necessary, have to be capitalised and the assessee would become entitled to claim depreciation allowance and investment allowance in respect thereof from the time the business commences its normal operations by virtue of the commercial production being started. An important guiding factor for deciding in favour of or against the foreign collaboration agreement would be the admissibility or otherwise of the expenses incurred in the form of payments made to the foreign collaborator in computing the business profits of the taxpayer in India.

Wherever the expenditure is disallowable because of the restrictions under section 37(1) read with section 28 of the Income-tax Act, the Indian taxpayers will have to be extremely careful to examine, before entering into the foreign collaboration agreement whether the scheme of foreign collaboration could be modified suitably to secure that such a disallowance is not attracted. This is because of the fact that the incurring of any expenditure which is disallowable would effectively mean that the Indian taxpayers' financial position would be substantially weakened by virtue of the agreement under which the disallowable expenditure becomes liable to be incurred. The reason for this is not far to seek. Under the scheme of the Income-tax law in India, any expenditure which is incurred by a taxpayer carrying on business and which is disallowed in computing the taxable profits would result in an addition to the real income of the assessee to the extent of the disallowed expenditure. Consequently, the taxpayer in India will not only be having the commitment of paying the amount of expenditure but also be faced with the problem of having to pay a sizeable amount towards income-tax with interest on the amount of notional income attributable to the disallowed expenditure in his income-tax assessment.

Section 37(1) of the Income-tax Act would be the primary guiding provision for the purpose of determining the admissibility or otherwise of the expenditure incurred by the Indian taxpayer. Under this section, it is obligatory for the assessee to establish, for the purpose of obtaining an allowance in respect of the expenditure incurred by him, that the expenditure is of a revenue nature and has been incurred wholly and exclusively for the purpose of the business or profession carried on during the previous year, the income of which is assessable to tax in India.

The criteria for deciding the nature of the expenditure to ascertain whether it is capital or revenue is not one of universal application and the decision in each case will have to depend on the facts and circumstances of the case. The question whether a particular expenditure is capital or revenue in nature and is accordingly deductible or not for purpose of computing the taxable profits is essentially a mixed question of law and fact.

The broad principles for making a distinction between capital and revenue expenditure were outlined by the Andhra Pradesh High Court in *Hylam Ltd. v. CIT* (1973) 87 ITR 310 after a perusal of a number of judicial pronouncements of the courts in India and abroad on this issue. These are quoted below:

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1. If the expenditure is for the initial outlay or for acquiring or bringing into existence an asset or advantage of an enduring benefit to the business that is being carried on or for the extension of the business that is going on or for substantial replacement of an existing business asset, it would be capital expenditure.
2. If, on the other hand, the expenditure, although for the purpose of acquiring an asset or advantage is for running the business or for working out that asset with a view to producing profit, it would be revenue expenditure.
3. If the outgoing is related to the carrying on or the conduct of the business that it may be regarded as an integral part of the profit earning process or operations and not for acquisition of an of an asset of a permanent character, possession of which is a condition precedent for the running of the business, then it would be expenditure of a revenue nature.
4. Special knowledge or technical knowledge or a patent or a trademark is an asset and if it is acquired for payment for use and exploitation for a limited period and what is acquired is not an asset or advantage of an enduring nature and at the end of the agreed period that advantage or asset reverts back intact to the giver of the special knowledge or the owner of the patents or trademarks, it would be expenditure of a revenue nature.
5. If it is intrinsically a capital asset, it is immaterial whether the price of it is paid once and for all or periodically or whether it is paid out of the capital or income or linked up with net sales; the outgoing in such a case would be of the nature of capital expenditure.
6. If the amount paid for the acquisition of an asset of an enduring nature is settled for the mere fact that the amount so settled is chalked out into various small amounts or periodic installments, the capital nature of the expenditure would not cease to be so or be altered it into the nature of a revenue expenditure.
7. A lump sum amount for liquidating recurring claims would not cease to be revenue expenditure or get converted into capital expenditure merely because its payment is spread over a number of years. It is the intention and object with which the asset is acquired that determines the nature of the expenditure incurred over it and not the method or the manner in which the payment is made or the source of such payment.
8. If the expenditure is recurring and is incurred during the course of business or manufacture, it would be revenue expenditure.
9. An asset or advantage of an enduring nature does not mean that it should last for ever. If the capital asset is in its nature a short-lived one, the expenditure incurred over it does not for that reason cease to be a capital expenditure.
10. It is not the law that if an enduring advantage is obtained the expenditure for securing it must always be treated as capital expenditure. If the advantage acquired

is to get any stock-in-trade of the business then it would be revenue expenditure. But if what is acquired is not the advantage of getting any stock-in-trade directly but of something which has to be dressed up or processed before it is converted into stock-in-trade, the expenditure incurred over it would be capital expenditure”.

17.8 OTHER FACTORS

17.8.1 Drafting of agreement: Special care is required in regard to the terms of the agreement. Since the facts and circumstances of each case differ from one another, it would be difficult to lay down a uniform guideline or principle by which the nature of the expenditure could be indicated as being capital or revenue in nature much in advance of incurring the expenditure itself. Therefore, having regard to the broad principles laid down by the Supreme Court case and also the High Courts in various cases one should, as far as practicable, plan the terms of the agreement in such a manner as to ensure that the amount payable to the foreign collaborator qualifies for deduction either as a revenue expenditure under section 37(1) when it is incurred or as capital expenditure qualifying for amortisation by way of depreciation admissible thereon.

In many cases, the problem of allocation of expenditure between capital and revenue and also the determination of the amount of royalties or fees for technical services or other consideration for the transfer of patents, copyrights, etc. outside India poses a considerable advantage both for the taxpayers and for the tax authorities. The solution to this problem lies in proper planning whereby under the terms of the agreement it is expressly indicated as to what is the amount of payment attributable to each type of service provided or asset given by the collaborator to the Indian taxpayer. To prescribe one composite amount of consideration for covering all the different types of services is to the disadvantage of both the Indian taxpayer and the foreign collaborator. It would be most advisable to have separate agreements for collaboration between the Indian company and the foreign collaborator for each of the technical services besides ensuring that the transfer of capital assets, wherever contemplated, is made by the collaborator to the Indian assessee outside India in every case. The agreement should also provide the amount of consideration for each type of service rendered or asset given, indicating also the manner in which the payment to the collaborator should be calculated. In other words, every care should be taken to secure that there is no ambiguity in terms of the agreement as a result of which the tax authorities might interpret the same to the disadvantage of the assessee. If it is not convenient to have separate agreements for different types of technical services because of the difficulties involved in obtaining the approval of the Central Government/CBDT to the agreements individually in each case coupled also with the formalities involved in obtaining the permission required under the Foreign Exchange Management Act from the different authorities, the Indian company may enter into one single collaboration agreement but the agreement should spell out in clear terms the different types of technical services and the amount of consideration payable for each one of them. By doing so, the Indian assessee and the foreign collaborator would be in a

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position to secure that the tax authorities do not have any authority to ignore the consideration specified under the agreement and substitute/allocate or even apportion the amount of consideration to the different items in the manner they find to be beneficial to the revenue.

Expenditure incurred towards professional fees for drafting of agreement in connection with the investments, collaboration, etc. would be expenditure of a revenue nature [*CIT v. Century Spg. & Mfg. Co. Ltd.* (1994) 210 ITR 783 (Bom)]

17.8.2 Termination of Agreement: The Bombay High Court in *Dorr-Oliver India Ltd. v. CIT* (1998) 234 ITR 723 has held that in the case of a collaboration agreement, the liability of the Indian company to make payment under the agreement to the non-resident would continue only so long as the agreement remains operative. When once the Government of India and the Reserve Bank do not approve the agreement or direct the assessee to terminate the Agreement by a specified period, the moneys paid/payable after the date of termination of the agreement would not qualify for deduction as a business expenditure. This is because a termination of the agreement brings about cession of the liability and hence the question of deduction for a non-existing liability does not arise; for this purpose it is immaterial that the collaboration agreement initially entered into had stipulated that it would be operative for specified period and came to be terminated as per the orders of the Government or the Reserve Bank earlier than the duration of the agreement.

17.9 ASSESSMENT OF FOREIGN COLLABORATORS

The Income-tax Act contains special provision for making assessments on representative assessee of non-resident foreign collaborators. Sections 160(1)(i), 161, 162 and 163 read with sections 166 and 167 govern the scheme of assessment of non-residents through their agents.

17.9.1 Meaning of 'representative assessee': Section 160(1)(i) defines the expression 'representative assessee' for all purposes of assessment to income-tax to mean the agent of a non-resident in respect of the income of the non-resident which is deemed to accrue or arise to him in India under section 9(1) of the Income-tax Act. The expression 'agent', in this context, must also be taken to include a person who is treated or deemed to be an agent by the Assessing Officer for the purposes of making assessment on him under section 263 of the Income-tax Act.

Section 2(7) also defines the term 'assessee' to include a representative assessee within its scope. The Assessing Officer is statutorily empowered to issue notice under section 163 to any person to deem him as the agent of the non-resident foreign collaborator. The term 'agent' should, for this purpose, be taken to include:

- (i) any person in India who is employed by or on behalf of the non-resident; or

- (ii) any person in India who has any business connection with the non-resident within the meaning of section 9(1)(i); or
- (iii) any person in India from or through whom the non-resident is in receipt of any income, whether directly or indirectly; or
- (iv) any person in India who is the trustee of the non-resident; or
- (v) any person in India who, whether resident or non-resident, has acquired by means of a transfer, a capital asset in India.

However, a broker in India who in respect of any transaction does not deal directly with or on behalf of a non-resident principal but deals with or through a non-resident broker should not be deemed to be an agent under section 163(1) in respect of the income attributable to those transactions provided both the following conditions are fulfilled:

- (a) the transactions must be carried on in the ordinary course of business through the first mentioned broker; and
- (b) the non-resident broker must be one who carries on such transactions in the ordinary course of his business and not as a principal.

17.9.2 Liabilities of a representative assessee: It is essential that a person who is sought to be assessed as the agent of the non-resident must be given an opportunity of being heard before the assessing officer treats him as the agent and imposes on him the vicarious liability to income-tax on behalf of the non-resident.

In order to be assessed as the agent of a non-resident it is not essential that the agent, who is regarded as the representative assessee under section 160(1)(i), must be actually in receipt of or is entitled to receive the income of the non-resident.

The representative assessee is not liable to be assessed under section 161 in his own name in respect of that income but the assessment made on him must, for all purposes be deemed to have been made upon him only in his representative capacity. The tax determined on assessment shall be levied upon and recovered from the representative assessee in the like manner and to the same extent as it would be leviable upon and recoverable from the foreign collaborator for whom he is the representative assessee. It may so happen that a person who is in India may have business connections with different non-residents and may also be a trustee in a number of trusts besides being a director of a number of companies. In such cases, there can be a large number of assessments on the very person as the representative assessee of each one of the non-residents with whom he has business connections, (as the representative assessee of the trusts) of which he is a trustee and these assessments in the representative capacity shall be made over and above his own assessment to income-tax and wealth-tax as an individual. Even if the representative assessee so desires, the income assessable in his hands in his representative capacity cannot be added to determine his total income assessable under the Income-tax Act in his individual capacity or in any other representative capacity.

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17.9.3 Protective assessment: The Supreme Court has also pointed out in *Lalji Haridas v. ITO (1961) 43 ITR 387 (SC)* that “in cases where it appears to the income-tax authorities that certain income has been received during the relevant assessment year but it is not clear who has received that income and prima facie it appears that the income may have been received either by A or by B or by both together, it would be open to the relevant income-tax authorities to determine the said question by taking appropriate proceedings both against A and B.” It is also expressly provided by section 16(2) that in every case where assessment has to be made on any person as representative assessee he should not be in respect of that income be assessed under any other provision of the Income Tax Act; in other words, the status of the assessee in his representative capacity for the non-resident cannot be ignored and the income of the non-resident cannot just be added to the other income of the representative assessee which may be made on him in his individual or other representative capacity.

17.9.4 Rights of a representative assessee

Right to recover tax: Section 162 grants to every representative assessee the right to over the tax paid by him as a result of such assessments. Accordingly, every representative assessee who pays any sum (which would include not only the tax but also the interest, fine and/or penalty, if any,) is statutorily entitled to recover the amount paid by him from the person/s on whose behalf the payment is made by him in his representative capacity. He is also entitled, if it is necessary to do so, to retain out of any moneys that may be in his possession or may come to him in his representative capacity the amount equal to the payment of tax or other sum made by him. In the event of any disagreement between the principal and the representative assessee in regard to the amount to be so retained, the representative assessee is entitled to apply to the assessing officer to secure a certificate from him specifying the amount to be so retained pending the final settlement of his liability to tax.

Right to agitate assessment as agent: The question whether, in any particular case, the taxpayer in India could be assessed as the agent of a non-resident or not is essentially a question of law. Thus, the liability to be assessed arbitrarily or unreasonably, could be challenged in the court through a writ or other appellate proceedings.

Quite often the Indian company is treated as the representative assessee for the foreign technicians of the collaborators who visit India and such a situation becomes necessary by the fact that before the technicians leave India they have to discharge the liability to tax in India and obtain tax clearance certificate from the income-tax authorities. Often it becomes difficult for them to fulfil all the obligations and the tax authorities also find it difficult to quantify the liability which has to be discharged by the technicians before they leave India. In such cases the Indian enterprise executes a guarantee bond in favour of the income-tax department undertaking to discharge the liability to tax which may be found to become due from the employee leaving India. While executing such a guarantee the Indian company also refunds in certain cases the amount of tax which might have

been already deducted at source to the foreign technicians in the assessment of the technicians. Consequently, if the Assessing Officer takes a view that the exemption was not assessable and he in turn passes an order of assessment raising a demand against the foreign technician by treating the Indian company as the representative assessee of the foreign technician, the Indian enterprise becomes liable to pay the tax demanded from it.

Criteria for assessment as agent: The assessment can be made either on the representative assessee or the non-resident principal to him. The CBDT, in its Circular No.157 dated 26.12.1974, has clarified that “once the choice is made by the department to tax either the trustee or the beneficiary, it is no more open to the department to go behind it and assess the other at the same time.”

17.10 DEDUCTION OF TAX AT SOURCE FROM NON-RESIDENT'S INCOME

The provision of sections 192 to 206B contained in Part B of Chapter XVII of the Income-tax Act, 1961 regulate the manner in which and the extent to which the tax on the income liable to income-tax in India should be recovered by way of deduction of the tax at source by the person who makes the payment or from whom the non-resident collaborator becomes entitled to receive the same.

17.10.1 Salaries : If the non-resident renders technical services in the capacity of an employee to the Indian enterprise and the payment for such technical services becomes liable to be taxed in India under the head ‘salaries’, the tax payable thereon should be deducted at source by the Indian enterprise before making the payment of remuneration or crediting the amount thereof to the account of the non-resident under section 192.

Failure on the part of the Indian enterprise to deduct the tax at source would disentitle it to claim the remuneration paid or payable to the non-resident employee as an expenditure in computing its taxable income because of the mandatory provisions for disallowance contained in section 40(a)(iii) of the Income-tax Act. Further, the Indian enterprise would also attract liability for prosecution besides the liability to penalty and fine over and above the obligation to pay the amount of tax which ought to have been deducted, with interest, to the government. For this purpose all the provisions for collection and recovery of tax would be applicable since the employer in India would be deemed in such a case to be the assessee in default.

17.10.2 Other payments to non-residents : According to section 195(1) any person who is responsible for paying to a non-resident any interest or any other sum (not being salaries) chargeable to income-tax under the Income-tax Act must, at the time of credit of such income to the account of the payee or at the time of making the payment, thereof in cash or by the issue of a cheque or draft or any mode, whichever is earlier, deduct income-tax payable thereon at the rates in force.

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Sub-section (2) to section 195 provides that in cases where the person is responsible for paying any sum chargeable to income-tax in India to a non-resident and he considers that the whole of the amount of payment may not be income assessable to tax in the hands of the recipient, he may make an application to the Assessing Officer to determine, by a general or special order, the appropriate proportion of the sum payable as being chargeable to tax and thereby obtain an advance ruling from the Assessing Officer with regard to the income assessable and the tax payable thereon. If that is done, the tax shall be deducted under section 195(1) only in that proportion in which the payment to the non-resident becomes taxable in India.

In this context, it may be noted that section 40(a)(i) provides for disallowance of any interest, royalty, fees for technical services or other sum chargeable under this Act, which is payable, -

- (a) outside India;
- (b) in India to a non-resident, not being a company or to a foreign company,

on which tax is deductible at source under Chapter XVIIB and such tax has not been deducted or, after deduction, has not been paid during the previous year, or in the subsequent year before the expiry of the time prescribed under section 200(1). It is also provided that where in respect of any such sum, where tax has been deducted in any subsequent year, or has been deducted in the previous year but paid in any subsequent year after the expiry of the time prescribed under section 200(1), such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Self-examination questions

1. Discuss the taxability of the following income in the hands of a non-resident -
 - (a) Interest income;
 - (b) Royalty;
 - (c) Fees for technical services.
2. Who are representative assesseees? Discuss the rights and liabilities of a representative assessee.
3. Discuss the different forms in which foreign collaboration may be made and the tax implications involved therein.
4. Explain what is meant by "Protective Assessment".
5. Discuss the employer's liability to deduct tax at source from the salary paid to a non-resident employee and the consequences, if any, for failure to deduct tax at source.

18.1 INTRODUCTION

One of the dictionary meanings of the word “restructuring” is “rearrangement”. Thus, business restructuring refers to a rearrangement of the corporate structure. In today’s world, along with increasing focus on globalisation and liberalization, there is free competition amongst businesses. As a result, corporates are trying to identify opportunities so that they can command a presence in the market. They are redefining their strategies, looking at core competency and trying to create a value for the shareholder in a competitive business environment. This has given rise to business restructuring.

18.2 FORMS OF BUSINESS RESTRUCTURING

Business restructuring can be done through mergers, acquisitions, strategic alliances, etc. The following are the methods by which businesses are redefining their affairs:

1. Amalgamation/merger
2. Demerger and spin off
3. Conversion of sole proprietary business into a company
4. Conversion of partnership firm into a company
5. Slump sale of business
6. Buy back of shares
7. Capital reduction
8. Redemption of preference shares
9. Conversion of debentures into shares

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These are discussed in the subsequent paragraphs.

18.3 AMALGAMATION

18.3.1 Definition : In the context of taxation, amalgamation includes not only the merger of one existing company with another existing company but also the merger of two or more existing companies to form a third company.

The Income-tax Act, 1961 defines amalgamation in section 2(1B) as a merger of one or more companies with another company, or the merger of two or more companies to form one company, in such a manner that:

- a. all the properties of the amalgamating company or companies immediately before the amalgamation, become the properties of the amalgamated company by virtue of the amalgamation;
- b. all the liabilities of the amalgamating company or companies immediately before the amalgamation, become the liabilities of the amalgamated company by virtue of the amalgamation; and
- c. shareholders holding not less than 75% in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee, for the amalgamated company or its subsidiary) become shareholders of the amalgamated company.

18.3.2 Effective date: Amalgamation is assumed to take effect on the date on which it is approved by the High Court. Once amalgamation is approved, it should be treated as relating back to the appointed date with reference to which the accounts of both the amalgamating and amalgamated companies are made up.

18.3.3 Exemptions available under the Income-tax Act, 1961:

Exemption from capital gains in the hands of the amalgamating companies:

Under section 47(vi) of the Income-tax Act, capital gains arising from the transfer of assets by the amalgamating companies to the Indian amalgamated company is exempt from tax.

Exemption from capital gains for the shareholders of the amalgamating companies: Under section 47(vii) of the Income-tax Act, capital gains arising from the transfer of shares by a shareholder of the amalgamating companies are exempt from tax, if:

- a. The transfer is made in consideration of the allotment to him of shares in the amalgamated company; and
- b. The amalgamated company is an Indian company.

The issue of exemption from capital gains is not free from doubt where the transaction is not structured as a share for share exchange and the consideration is paid in other forms. There are two contrary High Court judgments in this regard.

In the case of *CIT vs. Gautam Sarabhai Trust* [1988] 173 ITR 216, the Gujarat High Court held that to qualify for exemption u/s 47(vii) of the IT Act, the shareholder should receive the entire consideration in the form of shares of the amalgamated company alone. In other words, if besides the share or shares in the amalgamated company, the shareholders of the amalgamating company is allotted something more, namely, bonds or debentures in consideration of the transfer of his share or shares in the amalgamating company, he cannot get the benefit of Section 47(vii).

The other view is based on the judgment in the case of *CIT vs. M.C.T.M Corporation Private Ltd.* [1996] 221 ITR 525. In this case, the Madras High Court held that in as much as shares and debentures are allotted to the assessee on account of the amalgamation of the two companies and in view of the fact that the identity of the transferor company got lost in the amalgamation, there was no transfer or extinguishments of any right in allotting the shares and debentures in favour of the assessee under the provisions of Section 2(47) of the Act. Even if there was a transfer, the gains arising therefrom, were entitled to exemption under section 47(vii) of the Act.

Exemption from capital gains in case of international restructuring : Under section 47(via), in case of amalgamation of foreign companies, transfer of shares held in Indian company by amalgamating foreign company to amalgamated foreign company is exempt from tax, if the following two conditions are satisfied:

- a. At least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and
- b. The amalgamation is tax-free in the foreign company.

18.3.4 Carry forward and set-off of accumulated loss and unabsorbed depreciation in certain cases of amalgamation: Sub-section (1) provides that where there is an amalgamation of a company, owning an industrial undertaking or a ship or a hotel with another company or the amalgamation of a banking company with a specified bank, then the accumulated loss and unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or allowance for depreciation of the amalgamated company for the previous year in which the amalgamation was effected and other provisions of the Act shall apply accordingly.

The “specified bank” means the State Bank of India constituted under the State Bank of India Act, 1955 or a subsidiary bank as defined in the State Bank of India (Subsidiary Banks) Act, 1959 or a corresponding new bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 or under section 3 of the

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Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980.

Conditions: However, sub-section (2) lays down the following conditions for admissibility of set-off and carry forward in hands of the amalgamated company:

Conditions to be fulfilled by the amalgamating company

- (i) The amalgamating company should have been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for three or more years.
- (ii) The amalgamating company has held continuously as on the date of amalgamation at least three-fourths of the book value of the fixed assets held by it, two years prior to the date of amalgamation.

Conditions to be fulfilled by the amalgamated company

- (i) the amalgamated company holds continuously for a minimum period of 5 years from the date of amalgamation at least 75% in the book value of fixed assets of the amalgamating company acquired in a scheme of amalgamation;
- (ii) the amalgamated company continues the business of the amalgamating company for a minimum period of 5 years from the date of amalgamation;
- (iii) the amalgamated company fulfills such other conditions as may be prescribed to ensure the revival of the business of the amalgamated company or to ensure that the amalgamation is for genuine business interest.

Withdrawal of deduction or allowance: Sub-section (3) provides that where any of the conditions laid down in sub-section (2) are not complied with, the set off or allowance for depreciation made in any previous year in the hands of the amalgamated company shall be deemed to be the income of the amalgamating company chargeable to tax for the year in which such conditions are not complied with.

Meaning of “Industrial undertaking”: “Industrial undertaking” means any undertaking which is engaged in:

- (i) the manufacture or processing of goods; or
- (ii) the manufacture a computer software; or
- (iii) the business of generation or distribution of electricity or any other form of power; or
- (iv) the business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite service, network of trunking, broadband network and internet services; or

- (v) mining; or
- (vi) the construction of ships, aircrafts or rail systems.”

18.3.5 Power of Central Government to prescribe other conditions: Section 72A(2)(iii) empowers the Central Government to prescribe other conditions to ensure that the amalgamation is for “genuine business purpose” or for the purpose of revival of the business of amalgamating company.

Rule 9C prescribes that the amalgamated company should achieve the level of production of at least 50% of the installed capacity of the said undertaking before the end of 4 years from the date of amalgamation and maintain the said minimum level till the end of 5 years from the date of amalgamation. The assessee is required to obtain a report also which is as per Form No.62 as given in the rules.

An issue arises that the above condition prescribed vide the above notification cannot be satisfied in case where the installed capacity is not there. Examples could be software companies, units engaged in assembly/processing activities etc.

18.3.6 Other benefits: Apart from carrying forward unabsorbed business loss and unabsorbed depreciation, the amalgamated company shall also be entitled to carry forward and set off the following unabsorbed expenditures of the amalgamating company:

- (a) Capital expenditure on Scientific Research u/s 35;
- (b) Expenditure in connection with amalgamation u/s 35DD;
- (c) Expenditure for obtaining licence to operate telecommunication services u/s 35ABB;
- (d) Preliminary expenses u/s 35D;
- (e) Deduction for expenditure on prospecting etc. for minerals u/s 35E.

Similarly, the provisions of 41(1) shall be applied for the amalgamated company.

18.4 DEMERGER

The concept of demerger was introduced in the context of taxation by Finance Act, 1999. The objective was to enable corporate undertakings to undertake business restructuring in a tax neutral form.

18.4.1 Definition: Section 2(19AA) of the Income tax Act, 1961 defines demerger in relation to companies, as the transfer, pursuant to a scheme of arrangement u/s 391 to 394 of the Companies Act, 1956, by the demerged company of one or more of its undertakings to any resulting company in such manner that:

- (a) all the property and liabilities of the undertaking which is being transferred by the demerged company become the property and liabilities of the resulting company by virtue of the demerger;

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- (b) the property and liabilities of the undertakings being transferred by the demerged company are transferred at their book values immediately before the demerger;
- (c) in consideration of the demerger, the resulting company issues shares to the shareholders of the demerged company on a proportionate basis;
- (d) shareholders holding not less than 75% in value of the shares in the demerged company (other than shares already held therein immediately before the demerger by the resulting company or by a nominee of the resulting company or its subsidiary) becomes shareholders of the resulting company by virtue of the demerger;
- (e) the transfer of the undertaking is on a going concern basis;
- (f) the demerger is in accordance with the conditions, if any, notified by the Central Government u/s 71A(5) of the Act.

For this purpose, the following points need to be noted:

- (i) An 'undertaking' shall include any part of an undertaking, or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets or liabilities or any combination thereof not constituting a business activity.
- (ii) 'Liabilities' shall mean the following:
 - (a) those which arise out of the activities or operations of the undertaking;
 - (b) the specific loans or borrowings (including debentures) raised, incurred and utilized solely for the activities or operations of the undertaking;
 - (c) so much of the general or multipurpose borrowings of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of the demerged company immediately before the demerger.
- (iii) For determining the value of the property, any change in the value of assets consequent to their revaluation shall be ignored.
- (iv) Demerged company means the company whose undertaking is transferred pursuant to demerger, to the resulting company.
- (v) The splitting up or the reconstruction of any authority or a body constituted or established under a Central, State or Provincial Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies, as the case may be, shall be deemed to be a demerger if such split up or reconstruction fulfils the conditions specified by the Central Government.

'Resulting company' means one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and against which the resulting company issues shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger.

18.4.2 Exemption and benefits : A demerger transaction fulfilling the conditions of section 2(19AA) is free from capital gains tax, both with respect to the transfer of assets as well with respect to issue of shares to the shareholders.

Section 2(22) of the Income-tax Act has been amended to provide that the issue of shares directly to the shareholder pursuant to the demerger of an undertaking will not constitute deemed dividend.

Further, in respect of international demergers, provisions similar to amalgamation of foreign companies have been made. Transfer of shares of an Indian company pursuant to the demerger of a foreign company is exempt provided the following two conditions are satisfied.

At least 75% of the shareholders in the demerged foreign company continue to be shareholders in the resulting company;

Such transfer should not attract capital gains tax in the foreign company.

18.4.3 Accumulated losses and depreciation : Accumulated losses and depreciation relating to the undertaking being transferred in a scheme of demerger is allowed to be carried forward and set off in the hands of the resulting company.

In case such past losses cannot be directly attributed to the undertaking being transferred, the IT Act provides for the apportionment of the same between the demerged company and the resulting company in the same proportion in which the value of the assets have been transferred.

Depreciation in the hands of the resulting company : The depreciable assets base for tax purposes in the hands of the resulting company would be tax written down value in the hands of the demerged company.

Reduction from book value of assets in the hands of the demerged company : The tax depreciable assets base for the demerged company will be reduced by the tax written down value of the assets transferred in the demerger process.

Cost of acquisition of shares in the resulting company : In a demerger transaction, the shareholders of the demerged company are allotted shares in the resulting company by virtue of the demerger.

The cost of acquisition of the shares of the demerged company in the hands of the shareholders will be calculated by apportioning the cost of acquisition of the shares of the demerged company in the ratio of net assets transferred (to the resulting company) to the net worth of the demerged company.

18.4.4 Deductibility of statutory payments under section 43B of the Income-tax Act in the hands of the demerged company: Another issue that is relevant in the connection

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is the deductibility of statutory payments in the hands of the demerged company made after the appointed date by the resulting company. On the basis of the decision of the Cochin Tribunal in *CIT v Diza Electrical*, it may be possible to adopt a position that deduction should be made available to the demerged company. Reliance may also be placed on the Supreme Court judgment in the case of *T. Veerbhadra Rao*. This would also be in accordance with the principles of natural justice that must form the basis of the interpretation of any fiscal statute.

18.5 CONVERSION OF SOLE PROPRIETARY BUSINESS INTO COMPANY

Where a sole proprietary concern is converted into a company and as a result of such conversion, the sole proprietary concern transfers any capital asset (whether tangible or intangible) to the company, such transfer will not be charged to capital gains tax if the following conditions are complied with:

- (i) all the assets and liabilities of the sole proprietary concern immediately before its succession should become the assets and liabilities of the company;
- (ii) the shareholding of the sole proprietor in the company is not less than 50% of the total voting power in the company and his shareholding continues to remain so for a period of 5 years from the date of succession;
- (iii) the sole proprietor does not receive any consideration or benefit (whether directly or indirectly) other than the shares allotted to him by the company section 47(xiv).

18.6 CONVERSION OF PARTNERSHIP FIRM INTO COMPANY

Where a firm is converted into a company and as a result of such conversion, the firm transfers any capital asset (whether tangible or intangible) to the company, such transfer will not be charged to capital gains tax if the following conditions are complied with:

- (i) all the assets and liabilities of the firm immediately before its succession should become the assets and liabilities of the company;
- (ii) all the partners of the firm immediately before its succession become the shareholders of the company in the same proportion in which their capital accounts stood before such succession;
- (iii) the partners of the firm do not receive any consideration or benefit (whether direct or indirect) other than the shares allotted to them by the company;
- (iv) the partners' aggregate shareholding in the company is not less than 50% of the total voting power in the company and their shareholding should continue to remain so for a period of 5 years from the date of succession – section 47 (xiii).

Carry forward of loss and unabsorbed depreciation in case of re-organisation of business : If a firm or a proprietary concern is succeeded by a company fulfilling the conditions laid down in sections 47(xiii) and 47(xiv), then the accumulated loss and the unabsorbed depreciation of the predecessor firm or the proprietary concern shall be allowed to be carried forward and set off by the successor company.

If any of the conditions laid down in clause (xiii) or clause (xiv) are not complied with in any subsequent year, the set-off of loss or allowance for depreciation made in any previous year in the hands of the successor company shall be deemed to be the income of the company chargeable to tax in the year in which such conditions are not complied with.

Will the firm be liable to pay tax on depreciable assets?

If the transfer is on a going concern basis, even though no specific exemption is spelt out, the firm shall not be taxable since there can be no inference of a sale of any specific item comprised therein.

18.7 SLUMP SALE

18.7.1 Definition: 'Slump sale' means the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales. If value of an asset or liability is determined for the sole purpose of payment of stamp duty, registration fees or other similar taxes or fees, that should not be regarded as assignment of values to individual assets and liabilities.

One question that arises in this context is whether in a situation where an undertaking is transferred against the allotment of shares in the acquiring company, the transaction would qualify as "slump sale" under the Income-tax Act. One view in this regard is that the transfer must necessarily be effected against a monetary consideration and a transfer against allotment of share is merely an "exchange" which will not qualify as a "sale". However, a more reasonable view seems to be that the allotment of shares is merely a manner of discharge of consideration and the transaction would still qualify as a slump sale if other conditions are satisfied.

18.7.2 Chargeability: Any profits arising from the slump sale effected in the previous year shall be chargeable to tax as capital gains and shall be deemed to be the income of the previous year which the transfer took place. In relation to a capital asset being an undertaking or division transferred by way of such sale, the 'net worth' of the undertaking or the division shall be deemed to be the cost of acquisition and cost of improvement for the purposes of sections 48 and 49. The benefit of indexation shall not be allowed. If the undertaking is owned and held by the assessee for not more than 36 months, it shall be taken as short-term capital asset.

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The Supreme Court in the case of *R.C. Cooper vs. UOI: AIR 1970 SC 564 (610)* held that the undertaking is distinct from the various assets which comprise the undertaking. The aforesaid principle has now been statutorily recognised.

“Undertaking” is defined to include any part of an undertaking or a unit or division of an undertaking or a business activity as a whole, but does not include individual assets or liabilities or any combination thereof not constituting business activity. [Section 2(42C)].

In case of a slump sale, every assessee shall furnish in the prescribed form along with the return of income, a report of a Chartered Accountant indicating the computation of net worth of the undertaking or division, as the case may be, and certifying that the net worth of the undertaking or division has been correctly arrived at in accordance with the provisions of this section.

‘Net worth’ shall be the aggregate value of total assets of the undertaking or division as reduced by the value of liabilities of such undertaking or division as appearing in its books of account. Change in value of assets on account of revaluation shall be ignored. The value of depreciable assets shall be the written down value of block of assets determined in accordance with section 43(6)(c). *The value of capital assets in respect of which the whole of the expenditure has been allowed or is allowable as a deduction under section 35AD would be Nil.* The value of all other assets would be the book value.

The auditor of the company is required to give a certificate in Form No.3CEA (Rule 6H) relating to the computation of capital gains in case of slump sale. This certificate should be filed along with the return of income duly accompanied by copies of the Profit & Loss Account and Balance Sheet in accordance with the provisions of section 139 of the Income-tax Act, 1961.

18.8 BUY BACK OF SHARES

Section 77A was inserted in the Companies Act, 1956 by the Companies (Amendment) Ordinance, 1998. The section allows a company to purchase its own shares subject to certain conditions. The shares bought back have to be extinguished and physically destroyed and the company is precluded from making any further issue of securities within a period of 24 months from such buyback.

Thereafter, a clause was inserted in section 2(22) of the Income-tax Act, 1961 to provide that dividend does not include any payment made by a company on purchase of its own shares in accordance with the provisions of the Companies Act, 1956. Further, section 46A was also inserted in the Act to provide that the difference between any consideration received by a shareholder or a holder of other specified securities from any company on purchase of its own shares or other specified securities and the cost of the shares/securities shall be deemed to be capital gains arising to such shareholder or the

holder of other specified securities in the year in which such shares or other specified securities were purchased by the company.

18.9 CAPITAL REDUCTION

Sale of a capital asset is not a pre-condition for capital gains. As a result of reduction in the face value of the shares, the share capital balance is reduced. It also extinguishes the right of the preference shareholder to receive dividend on the shares held and the right to share in the distribution of the net assets on liquidation in proportion to the extent of reduction in the capital. Such reduction in shareholder's right would amount to a transfer within the meaning of section 2(47) of the Act. *Kartikeya V. Sarabhai vs. CIT (1997) 228 ITR 163 (SC)*.

18.10 REDEMPTION OF PREFERENCE SHARES

When a preference share is redeemed by a company, what the shareholder does in effect is to sell the share to the company. The company redeems its preference shares only by paying the preference shareholders the value of the shares and taking back the preference shares. In effect, the company buys back the preference shares from the shareholders. The redemption of preference shares by the company, therefore, is a sale and squarely comes within the phrase 'sale, exchange or relinquishment' of an asset. *Anarkali Sarabhai vs. CIT (1997) 224 ITR 422*.

Acquisition of irredeemable preference shares of a company in exchange of equity shares consequent to capital restructuring scheme of the company cannot be exchange of one kind of shares against another kind of shares having different rights and liabilities. Where the assessee sells the preference shares within 6 months of their acquisition, the capital gain/loss shall be short-term in nature. *CIT vs. Santosh L. Chowgule (Bombay)*.

18.11 CONVERSION OF DEBENTURES INTO SHARES

Any transfer by way of conversion of bonds or debentures, debenture stock or deposit certificates in any form, of a company into shares or debentures of that company is not regarded as transfer u/s 47(x). Hence, if any amount is paid in cash etc., the entire transaction will attract capital gains tax.

Sub-section (2A) of section 49 states that where the capital asset, being a share or debenture in a company became the property of the assessee in consideration of a transfer referred to in clause (x) of section 47, the cost of acquisition of the asset to the assessee shall be deemed to be that part of the cost of debenture, debenture-stock or deposit certificates in relation to which such asset is acquired by the assessee.

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Self-examination questions

1. What is meant by “business restructuring”? What are the various forms of business restructuring?
2. What are the tax benefits available on amalgamation of one company with another? What are the conditions required to be fulfilled by the amalgamating and amalgamated company for availing such tax benefits?
3. Define demerger. What are the tax benefits available to the resulting company on account of demerger?
4. Write short notes on -
 - (a) Redemption of preference shares
 - (b) Conversion of debentures into shares.
5. What are the tax effects on conversion of -
 - (a) a sole proprietary business into a company; and
 - (b) a partnership firm into a company.
6. What is meant by “Slump sale”? Discuss the provisions of the Income-tax Act relating to slump sales.
7. Write short notes on -
 - (a) Buyback of shares
 - (b) Capital reduction

TAXATION OF E-COMMERCE TRANSACTIONS

19.1 WHAT IS E-COMMERCE

E-commerce or electronic commerce, in its widest sense, means consumer and business transactions conducted over a network, using computers and telecommunications. In other words, e-commerce refers to the exchange of goods or services for value on the internet. It includes, *inter alia*, on-line shopping, on-line trading of goods and services, electronic fund transfers, electronic data exchanges and on-line trading of financial instruments.

The OECD defines e-commerce in a somewhat more restricted manner as commercial transactions between individuals and organisations, based on the processing or transmission of digitised data units, sound, and visual images, which are carried out over open networks (like internet) or over closed networks (like minitel) with a gateway to open networks. This more specific definition would therefore exclude electronic data interchange (EDI), carried out over closed networks, if such EDIs are being used by themselves, without access to an open network (e.g. credit cards used over a closed network, connecting specified merchants with a card organisation).

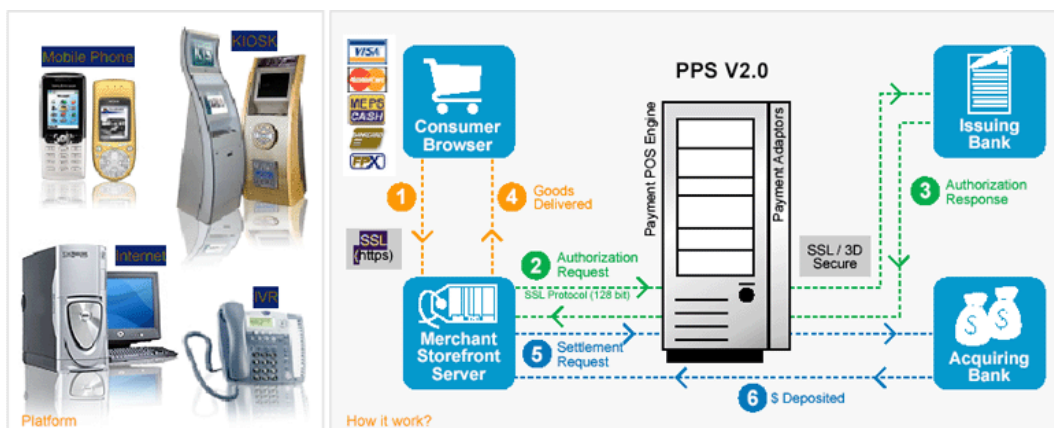


Figure 19.1.1 illustrates an e-commerce transaction. Source: www.ocsb.com.my/ePayment.htm

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Whatever be the definition, this method of carrying on a business is widely different from the traditional practice of business. Whereas traditional businesses have rested squarely on the physical presence and delivery of goods, in doing business via the internet, as is the case in e-commerce transactions, physical presence of goods is not required at all. Consequently, geographical boundaries between nations hold no significance. Secondly, in such type of transactions, physical delivery of goods is not necessary. Where the goods and services are available in digital form, e.g. computer software, music, magazines, drawings etc. physical transactions are replaced by transfer of bytes. Thirdly, e-commerce transactions can be completed almost instantaneously across the world and irrespective of the time of the day.

19.2 ISSUES AND PROBLEMS IN TAXING E-COMMERCE TRANSACTIONS

Due to absence of national boundaries, physical presence of goods and non-requirement of physical delivery, taxation of e-commerce transactions raises several issues. They have to be understood in the light of international taxation. International taxation arises from cross border transactions for the reason that the author of the transactions arises in one country (called the Home State) and the sites of the transactions is in the other country (Host State).

Income arising out of such transaction is subject to tax in both countries by virtue of 'personal attachment' to the transfer (in the Home State) and again by virtue of 'economic attachment' to the income itself (in the Host State). Thus, this gives rise to double taxation of the same income. This problem is generally solved by a Double Taxation Avoidance Agreement (DTAA) between the two countries concerned. The problematic issues arising in respect of e-commerce transactions are as follows :

19.2.1 How to determine 'economic attachment': In order to determine economic attachment, the situs of the transactions should be clearly determined. In a traditional commerce transaction, the situs of the transaction is clearly known, because of the physical presence and the physical delivery. Therefore the Source Rule as laid down in section 9 of the Income-tax Act, 1961 can be clearly applied to effect Host State taxation. Section 9 provides that income is deemed to accrue or arise in Indian taxable territory if there is a business connection. In E-commerce situations, with transactions being completed in cyberspace, it is often not clear as to the place where the transaction is effected, giving rise thereby to difficulties in implementing Source Rule taxation.

19.2.2 How to determine existence of a permanent establishment : Under most bilateral double tax treaties, a country will seek to tax corporate business profits if they can be applied to a 'permanent establishment' in that country. The basic requirement is, therefore, that there must be a place of business and it must have some permanence.

The major taxation problem of e-commerce is that no establishment is necessary across the border to carry on business. With regard to tangible property, the source can be traced, as the delivery has to cross the other territory through the customs or postal barrier. The destination also will be known from the shipping address. Where the seller is located in a tax-haven country, it becomes difficult to enforce tax laws on the non-resident business. In such cases, the natural option should be to tax the resident as the agent, especially where the non-resident cannot be reached. The difficulty is not so much in taxing those who are assessed and who maintain accounts but in taxing others who do business and there is no record of their transactions, like the persons liable to pay the 'use tax' in US. With the development of WAP (Wireless Application Protocol) which integrates mobile telephony with the Internet, e-commerce will be taken over by M-commerce (Mobile Commerce). This makes the place of origin of business invisible thus adding complication to the existing scenario and is a real challenge to domestic jurisprudence.

Further, how such income is to be attributed to the permanent establishment is also a significant matter. This is relevant to determine whether income from sales can be taxed on host country soil. For instance, if a particular income is classified as royalties or fees for technical services, or dividends or interests, then irrespective of the existence of a permanent establishment, the income will be liable to host country taxation under section 115A of the Income-tax Act. On the other hand, if the income is classified as income from sales, then unless there is a permanent establishment, there can be no taxation in the host country. And if there is a permanent establishment, how much income is to be taxable will be determined by how much of the income is to be attributed to the permanent establishment.

19.2.3 Legal difficulty: Till now all cross-border commercial transactions have to cross the customs barrier or the postal barrier. All trade and commerce are operated in a physical world and in terms of tangible goods. Hence, there is a check on these transactions, though smuggling remains outside the scope of any control. Even in the present situation, the tax authorities are unable to fully grapple with the problem of myriad ways of tax evasion. In e-commerce transactions, the contracting parties are in two different states and, therefore, the question would arise as to which state law would be applied.

19.2.4 Nature of contract: A contract need not necessarily be in writing unless, the statute requires it to be so. It can be oral. This will create problems relating to the law that will be applicable in case of dispute. In a contract, generally the parties are free to choose the law applicable to the contract and the same can be expressed or implied in the terms of the contract. In some cases, the principal place of business is relevant in

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deciding the law applicable. In some other case, the place where the buyer normally resides decides the law to be applied. Where there is a clause for retention of title until the buyer performs some act, then the matter of which *lex situs* will govern the validity clause is open to question. In answering this, the Rome Convention says that if the contract accords with the rules of anyone of the States, its validity cannot be questioned. This would be the most satisfactory solution and can be followed. All these problems arise mostly regarding transactions relating to movables and those relating to immovable properties are less difficult. There are many areas where the present domestic laws including international laws would be inadequate to deal with the emerging new field of e-commerce.

19.2.5 Taxable jurisdiction: The taxable jurisdiction of any country covers its national boundary. Besides this the territorial jurisdiction includes territorial sea and airspace above as per the territorial waters, continental shelf, exclusive economic zone and other Maritime Zones Act, 1976. Each one extends to specified nautical miles from the base line. The following are the limits indicated therein:

- (i) Territorial Water -12 nautical miles from the nearest point of appropriate base line.
- (ii) Contiguous Zone - 24 nautical miles beyond and adjacent to the territorial waters from the base line.
- (iii) Continental Shelf - 200 nautical miles from the base line.
- (iv) Exclusive Economic Zone is an area beyond and adjacent to the territorial waters extending to 200 nautical miles from the base line.

But electronic commerce takes place through satellite and the server can be in any part of the globe. It can in all probability be in a tax-haven country. Another condition for taxing the income arising or accruing beyond the taxable territories in the physical residence of the taxpayer for 182 days or more. This becomes meaningless with the Internet access. The information highway provides numerous visits to another jurisdiction outside the control of border mechanism.

19.3 HOW BUSINESS IS TRANSACTED THROUGH E-COMMERCE

E-commerce is but a method of conducting business transactions and not a business transaction by itself. Therefore, the contents of a business transaction done through e-commerce are no different from that of a business transaction carried out through traditional means.

Divergence however arises in two dimensions - the business methods and the business concepts. The first area, which is very different, viz. the means of doing business, is

analysed. In e-commerce there are three distinct means of doing business : electronic advertising, electronic sales and electronic delivery. The presence of anyone or more of these is sufficient to characterise the business as e-commerce.

These are separately discussed below :

19.3.1 Electronic advertising: Advertising is done on the open networks, through websites. Potential customers access the websites and obtain the information they need which enables them thereafter to proceed with the transaction in suitable cases. If the e-commerce business is restricted to putting up a website alone, then the rest of the transaction is completed through traditional means; i.e. the placing of orders by telephone or mail, the making of payment by cheque and credit card and the delivery of goods through a carrier, the telephone etc. being referred to as intermediaries.

19.3.2 Electronic sales: This is done through 'smart' resources which enable the potential customer to place an order on the internet. The payment is effected through a closed network by means of credit cards.

19.3.3 Electronic delivery: This is of course possible only for goods and services that can be fully digitised, but this range is quite wide and ever expanding. Texts, visual materials, audio materials and computer software are digitised. Therefore products like journals, books, music, plans, designs, drawings and games to mention a few, would be goods available in digitised form. Besides goods, services like diagnostic services, could also be available in digitised form. Therefore a whole host of goods and services could be delivered electronically.

One way of classifying E-commerce is based on parties involved in transactions. Major types are mentioned below:

1. Business to Customers (B2C)
2. Business to Business (B2B)
3. Government to Customers (G2C)
4. Government to Business (G2B)
5. Customer to Customer (C2C)

The name of a type indicates the parties involved in that type of E-commerce transaction.

19.3.4 The Committee of Fiscal Affairs of the OECD has been actively working on taxation issues relating to e-commerce. The committee has developed the taxation framework conditions setting forth the governing principles in relation to e-commerce. The key conclusion was that the taxation principles that guide Governments in relation to conventional commerce, should also guide them in relation to e-commerce. It was

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postulated that this would be possible only by adapting and adopting the existing principles to e-commerce situations.

For adapting and adopting the existing principles, the following key areas in the context of international tax were identified :

- (1) the extent to which a website or a server can constitute a permanent establishment and how income may be attributed to it; and
- (2) the manner in which payments for digitised products are to be characterised.

19.4 PERMANENT ESTABLISHMENT IN E-COMMERCE SITUATIONS

We now discuss different situations which arise in an e-commerce environment and consider whether these situations would constitute a permanent establishment.

19.4.1 Situation 1 - Existence of a website on host country soil : A website may be defined as a set of web documents belonging to a particular organisation. It consists of data and programmes in digitised form which is stored on a server of the internet service provider. On the other hand, a permanent establishment, as the name itself suggests, is a fixed place of some permanence from where a business is carried on. Therefore, the existence of a website, by itself, would not constitute a permanent establishment.

19.4.2 Situation 2 - Server on host country soil: A server is a system which carries out activities initiated by an end-user's computer. The question whether a server can be considered as a permanent establishment is more complicated. It is possible that the enterprise that operates the server may be different from the enterprise that carries on business through the website. The use of a particular internet service provider (ISP) does not give website owner the right of control over the server's operation. The server's location is not at that enterprise's disposal. The server could easily be removed to other locations.

In such a situation, the server's location cannot be considered to be the place of business.

On the other hand, if the enterprise itself owns or leases and operates the server, and the computer equipment is fixed, and business is carried on through the server, it could be construed to be a permanent establishment. Therefore what is essential to be considered in this issue, is not merely whether a server exists or host country soil, but also what the value as well as extent of its operations are. As the permanent establishment concept deals not only with permanence and a geographical link with the host soil, but also with the actual carrying on of the business, the values and extent of the operations carried out by the server becomes important. We now consider separately the above points.

Nature of operation - The nature of operations could have a very wide range. The range could profess from being a mere provider of information, to being a forwarding address to acting as a warehouse for digitised goods, to contributing directly to productivity and value creation, thereby realising profits. In a situation where the server acts as a mere provider of information it cannot be considered to be a permanent establishment. At the other end, where it contributes to productivity, the server will become a permanent establishment for distinctions which falls in between there two entrances, it would be necessary to go to the next step of examining the extent of operations.

Extent of operations- In the extent of operations, as well, there could be a wide range of activities. A server could be simply located on host country soil with skeletal support services, or it could be a server with multiple services, or it could be a server which carries on the complete set of operations. In the last situation, there would clearly be a permanent establishment.

19.4.3 Situation 3 - Server functioning as agent: It is possible that a server on host country soil could be construed to be a dependent agent of the foreign enterprise. Such a situation will apply in the case of 'Smart' servers. 'Smart' servers are programmed to not only provide information but also to take and process orders from persons who make a 'hit' 'n the website. Such a server has the power to contract on behalf of the foreign enterprise and habitually exercises this power. It is possible to argue that since such a server is a dependent agent of the foreign enterprise, it may be considered to be a permanent establishment. However, a contrary and more logical view would be that the website together with the server that hosts it can only constitute the medium through which orders are placed. The time acceptance of the order is not done by the machine itself but by the person or corporation which inserted into the machine a programme capable of performing these tasks. Therefore, the website and the server would not constitute a permanent establishment.

According to the principles of international taxation, business income cannot be taxed on Host State soil, unless there is a permanent establishment in the Host State. If there is such a permanent establishment, then the only income which the Host State is entitled to tax is the income attributable to the permanent establishment. Such attributable income is determined by imagining the permanent establishment to be an entity independent of the foreign enterprise, and dealing with the foreign enterprise at arm's length price. The issue therefore translates to one of determining the transfer price between the foreign enterprise and permanent establishment, and rewriting the transaction between the two, at arm's length.

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19.5 DETERMINATION OF THE NATURE OF INCOME

The manner of taxation in income arising from e-commerce transactions, as it also the case in conventional commercial transactions, depends on the characterisation of the income. The characterisation of income is relevant because different types of income are taxed differently. Once this is identified, the existing rules may be adopted and adapted to the e-commerce transactions.

In conventional commerce, when all rights in a property are transferred it would amount to a sale giving rise therefore to business income. On the other hand, when only limited rights in a property are transferred, the transferor retaining substantial rights therein, the income therefrom would be classified either as a royalty in the case of intellectual properties, or a lease rent in the case of tangible properties. Thirdly, if the ultimate results of the transaction is the rendering of services, the income would have to be characterised either as fees for professional services.

Similarly, in an e-commerce situation, if licensing of a know-how is done, the payment for this would clearly be characterised as a royalty income in terms of most double taxation avoidance agreements and this would be so irrespective of whether this is done by physical transfer of information or by transfer of digitised information. If on the other hand, practically all rights in a design are transferred, whether physically or through electronic transfer of digitised information, with no rights being retained by the transferor, under most double taxation avoidance agreements, the transaction would be considered to be one which is more in the nature of outright sale of the design rather than a licence thereof. The payment for this would then be characterised as a sale consideration rather than as a royalty.

The principles of adopting and adapting postulated by the OECD and the US treasury unable a proper determination of the character of income in most cases. However, the problem arises in the case of transactions involving software. This is discussed below:

Transactions involving software: The process of adopting and adapting existing rules to e-commerce transactions becomes complicated in the case of transactions involving software. For instance, where a packaged product like Windows 98 is sold, we normally refer to it as buying a product. Moreover, this sale in reality, not a sale but an agreement or a licence to use the software. The product comes in a transparent shrink wrap packaging through which the licence agreement can be read.

When the buyer tears open the packaging, this act is tantamount to his signing the agreement or licence. By doing so, the buyer (licensee) accepts the terms of the licence, i.e. he agrees to use the software only at that one work station, to not make copies except

for archival purposes, to not alter the contents, etc. other than a licence. When it comes to taxation of such transactions the characterisation of the income would become extremely relevant. If for instance the transactions were to be treated as a sale transaction, and the title is transferred outside the buyer's country, the transaction would not be subject to host country taxation in the buyer's State; this is because there would be no permanent establishment of the 'seller' of the software in the buyer's State, and therefore no subjection to Host State taxation. If on the other than the transactions were to be treated as one of licensing, irrespective of the fact that there might be no permanent establishment in the buyer's State, the amount paid by the buyer would, (according to most double taxation avoidance agreements and most domestic tax laws), be considered not as a sale consideration, but as a licence fee constituting a royalty and this would therefore be subject to Host State taxation on the basis of the Source Rule, the payer of the consideration being a resident of the Host State.

Let us now examine this issue in the context of Indian law.

Section 14 of the Copyright Act, 1957, as amended by the Copyright (Amendment) Act, 1999, defines "copyright" to mean the exclusive right to do or authorise the doing of any of the following acts, in respect of a work or any substantial part thereof

- a) in the case of a literary, dramatic or musical work, not being a computer programme,-
 - i) to reproduce the work in any material form including the storing of it in any medium by electronic means;
 - ii) to issue copies of the work to the public not being copies already in circulation;
 - iii) to perform the work in public; or communicate it to the public;
 - iv) to make any cinematograph film or sound recording in respect of the work;
 - v) to make any translation of the work;
 - vi) to make any adaptation of the work;
 - vii) to do, in relation to a translation or an adaptation of the work, any of the acts specified in relation to the work in sub-clause (i) to (vi);
- b) in the case of a computer programme, -
 - i) to do any of the acts specified in clause (a);
 - ii) to sell or give on commercial rental or offer for sale or for commercial rental any copy of the computer programme.

However, such commercial rental does not apply in respect of computer programme where the programme itself is not the essential object of the rental.

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It is therefore abundantly clear that computer programmes, including software would clearly be considered to be covered by copyright. Therefore if software is licensed or its use is permitted in any manner, in accordance with Explanation 2 to section 9(1)(vi) of the Income-tax Act, the income would be royalty in nature. The income would therefore be deemed to arise in India in accordance with section 9(1)(vi)(b) when the payer of the same is an Indian resident, unless it could be established that the software is used in a business outside India. When therefore purchase consideration in respect of any software to be used in India is paid to a non resident who has exported software, the payment will be construed as income deemed to arise or accrue within India, in terms of section 9(1)(vi); it would become income of the non resident subject to Indian tax in terms of section 5(2); and consequently tax would require to be deducted by the buyer of the software in terms of section 195. In terms of most double taxation agreements entered into by India with other countries, again the amount would be considered royalty income accruing or arising within India, and therefore subject to Indian withholding tax.

Therefore, what is most important in this context is the underlying concept of copyright.

US Revenue Regulations Approach: The US Revenue Regulations clearly use a two stage approach. In the first stage, the distinguishing done is whether the transfer is of a copyright article or of a copyright right. Thereafter, at the second stage, two different parameters are used for copyright articles and for copyright rights, but these parameters are rational and not arbitrary.

In the case of a copyrighted article, the source code is generally not given, which means that it is only use of the copyrighted article, that is possible. Nothing beyond the use of the copyrighted article would be possible, if the only transfer effected is on the copyrighted article. On the other hand, if there is a transfer of the copyright right (as contrasted to transfer of right merely in the copyright article) all the underlying rights in the intellectual property are also transferred. The source code is most available, with the result that it would be possible to delete, add, modify, adopt and use in all possible manners, the software in which the rights are transferred.

If the transfer in a copyright article is that of significant benefits and burdens of ownership, then the income imbedded in the transaction is considered to be sales income. If on the other hand, only insignificant benefits and burdens of ownership have been transferred, then this is treated as a rental income.

When it comes to copyright rights a different parameter is used viz. Whether all substantial rights are transferred or not. If the transfer is of all substantial rights, the transaction is considered to be one of sales, and the income therefrom is therefore business profits. On the other hand, if there is no transfer of all substantial rights, the

transaction is one of licensing and the income therefrom is royalty income.

Therefore, according to the guidelines set out in the US Revenue Regulations for the income to constitute sales income, significant benefits and burdens of ownership in a copyright article or transfer of all substantial right in copy right rights should be effected. If this is not done, then the income arising from a copyright right is considered to be royalty and that from a copyright article to be rental income.

The OECD has sought to distinguish a software product transaction, from a software copyright transaction. Therefore they have sought to distinguish the transfer of a programme copy on the one hand (which is a software product transaction), from the transfer of copyright right on the other hand (which is a software copyright transaction). When the transfer is only of a programme copy, then this being only a software product transaction, the nature of the receipt would be a sale consideration received for a product, and therefore the income embedded therein would be a business profit. This therefore overcomes the hyper technicality of considering the transaction as one of a licence, and accepts it for the commercial reality of what is actually is, namely a sale transaction. The income therefrom will then be considered business profits.

On the other hand, when it comes to the transfer of a copyright right, this is then recognised as a software copyright transaction, and it is only at the next phase, that this approach requires determination of whether what is transferred is a complete right or a partial right. If what is transferred is a complete right, then the transaction is one of a sale and income imbedded therein is business profit. If on the other hand, the transfer is only of partial right, then the transaction is one of licensing and not of sale, and the income imbedded therein is clearly a royalty.

Therefore, in essence both the approaches are along similar lines.

19.6 CONCLUSION

Despite the divergence of method between traditional commercial transaction and e-commerce transactions, it is essential to conform to the tenets of neutrality of taxation.

On account of the characteristics of e-commerce namely that transactions are completed in cyberspace, thereby making national boundaries meaningless, and considering the level of dis-intermediation and untraceability of the path of the transactions, traditional Source Rules of taxation become increasingly difficult to apply.

As techniques of e-commerce progress, the situations become more complex with increasing dis-intermediation. Instances of these could be where traditional transfer pricing rules cannot be applied to multiple servers which switch signals depending on their work loads. This could give rise to increasing emphasis on Residence Rule taxation

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whenever Source Rule taxation becomes difficult to apply. Such a situation could spell diminishing revenues for developing countries, particularly in situations of technology transfers, where Host States are generally developing countries.

Self-examination questions

1. Explain what is meant by “e-commerce”.
2. Discuss the issues and problems in taxing e-commerce transactions.
3. Explain how businesses are transacted through e-commerce.
4. How is existence of a permanent establishment determined in e-commerce situations?
5. Explain in detail the manner of taxation of income arising from e-commerce transactions.

INCOME-TAX AUTHORITIES

20.1 APPOINTMENT AND CONTROL [SECTIONS 116 TO 119]

The following are the classes of income-tax authorities :

- (i) The Central Board of Direct Taxes.
- (ii) Directors General of Income-tax or Chief Commissioners of Income-tax.
- (iii) Directors of Income-tax or Commissioners of Income-tax or Commissioners of Income-tax (Appeals).
- (iv) Additional Directors of Income-tax or Additional Commissioners of Income-tax or Additional Commissioners of Income-tax (Appeals).
- (v) Joint Directors or Joint Commissioners of Income-tax
- (vi) Deputy Directors of Income-tax or Deputy Commissioners of Income-tax.
- (vii) Assistant Directors of Income-tax or Assistant Commissioners of Income-tax.
- (viii) Income-tax Officers.
- (ix) Tax Recovery Officers.
- (x) Inspectors of Income-tax.

20.1.1 Assessing Officer

In this connection, it may be noted that under section 2(7A), the term 'Assessing Officer' means –

- (a) the Assistant Commissioner or Deputy Commissioner or Assistant Director or Deputy Director; or
- (b) the Income-tax Officer who is vested with the relevant jurisdiction by virtue of directions or orders issued under section 120(1) or (2) or any other provision of the Act; and
- (c) the Additional Commissioner or Additional Director or Joint Commissioner or Joint Director who is directed under section 120(4)(b) to exercise or perform all or any of the powers and functions conferred on, or assigned to, an Assessing Officer.

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20.1.2 Central Board of Direct Taxes (CBDT)

The Central Board of Direct Taxes is a statutory body constituted under the Central Board of Revenue Act, 1963. It consists of a number of members appointed by the Central Government for the performance of such duties, as may be entrusted to the Board from time to time. It is functioning under the jurisdiction of the Ministry of Finance. The Central Board of Direct Taxes, besides being the highest executive authority, exercises control and supervision over all officers of the Income-tax Department and is authorised to exercise certain powers conferred upon it by the Income-tax Act. In particular, it has the powers, subject to the control and approval of the Central Government to make any rules, from time to time for the proper administration of the provisions of the Income-tax Act.

All the rules under the Act are framed by the Board under section 295 and placed before the Parliament. In addition to the general power of making rules and of superintendence, the Board has been given specific powers on several matters.

The Board has been empowered under section 119 to issue instructions and circulars to its subordinates for the proper administration of the Act. It is obligatory for the various authorities and all other persons employed in the execution of the Act to observe and follow such orders, instructions and directions of the Board. However, the Board is not empowered to issue orders, instructions or directions in such a way as to (i) require any income-tax authority to make the assessment of a particular case in a particular manner or (ii) interfere with the discretion of the Appellate Assistant Commissioner in the exercise of his appellate functions. Further, the Board may, if it considers necessary or expedient to do so, for the purpose of proper and effective management of the work of assessment and collection of revenue, issue general or special orders from time to time in respect of any class of incomes or fringe benefits or class of cases setting forth directions and instructions not being prejudicial to the assessee. In appropriate cases, the Board may relax the provisions of sections 115P, 115S, 139, 143, 144, 147, 148, 154, 155, 234A, 234B, 271 and 273. The Board can exercise its powers to remove difficulties in the matter of sections 201(1A), 210, 211 and 234C. The following table gives a brief glimpse of what these sections relate to –

Section	Particulars of section
115P	Interest payable for non-payment of tax by domestic companies
115S	Interest payable for non-payment of tax on distributed income to unit-holders
139	Return of income
143	Assessment of income
144	Best Judgment Assessment of income

- 147 Income escaping assessment
- 148 Issue of notice where income has escaped assessment
- 154 Rectification of mistake apparent on record
- 155 Other amendments relating to assessment of income
- 201(1A) Interest for non-deduction of tax or non-payment of tax after deduction by such person/principal officer/company, as the case may be.
- 210 Payment of advance tax by the assessee of his own accord or in pursuance of order of Assessing Officer.
- 211 Installments of advance tax and due dates
- 234A Interest for default in furnishing return of income
- 234B Interest for default in payment of advance tax
- 234C Interest for deferment of advance tax
- 271 Penalty for failure to furnish returns, comply with notices, concealment of income etc.
- 273 Penalty for false estimate of, or failure to pay, advance tax

The Central Government may appoint such persons as it thinks fit to be Income-tax authorities. It may also authorise the Board or a Director General, a Chief Commissioner or a Director or a Commissioner to appoint Income-tax authorities below the rank of an Assistant Commissioner. An Income-tax authority authorised by the Board may appoint such executive or ministerial staff as may be necessary to assist it in the execution of its functions. The Board may also direct that any Income-tax authority or authorities shall be subordinate to such other income-tax authority as may be specified.

20.2 JURISDICTION OF INCOME-TAX AUTHORITIES

The Income-tax authorities shall exercise all or any of the powers and perform all or any of the functions conferred on, or assigned to, such authorities in accordance with the directions issued by the CBDT for the exercise of such powers and performance of the functions by all or any of those authorities [Section 120(1)].

Any income-tax authority, being an authority higher in rank, may exercise the powers and perform the functions of the income-tax authority lower in rank, if so directed by the CBDT. Such direction issued by the CBDT shall be deemed to be a direction issued under the said section 120(1).

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In issuing such directions the Board may have regard to the following criteria:

- (a) Territorial area.
- (b) Persons or classes of persons.
- (c) Incomes or classes of incomes.
- (d) Cases or classes of cases.

The CBDT can authorise any Director General or Director of Income-tax to perform such functions of any other Income-tax authority.

The CBDT can empower the Director General or Chief Commissioner or Commissioner to issue orders in writing to the effect that the powers and functions conferred on or assigned to the Assessing Officer can be exercised or performed by a Joint Commissioner or Joint Director.

Further, the powers and functions conferred on or assigned to the Assessing Officer may also be exercised or performed by an Additional Commissioner and Additional Director, on issue of order in writing to that effect by the Director General, Chief Commissioner or Commissioner.

The CBDT or any other authority authorised in this behalf can confer jurisdiction with more than one Income-tax authority in relation to any case.

20.2.1 Jurisdiction of Assessing Officers [Section 124]

- (i) Where the Assessing Officer has been vested with jurisdiction over any area within the limits of such area he shall have jurisdiction in respect of any person carrying on business or profession within that area and in respect of any other person residing within the area.
- (ii) Where a question arises under this section as to whether an Assessing Officer has jurisdiction to assess any person the question shall be determined by the Director General or the Chief Commissioners or Commissioner.
- (iii) Section 124(3)(a) provides that no person shall be entitled to call in question the jurisdiction of an Assessing Officer where such person has made a return of income under section 139(1), after the expiry of one month from the date on which he was served with a notice under section 142(1) or section 143(2) or after the completion of the assessment, whichever is earlier.
- (iv) Section 124(3)(b) provides that the jurisdiction of the Assessing Officer shall not be called in question where no return has been made, after the expiry of the time allowed by the notice under section 142(1) or under section 148 for the making of the return or by the notice under section 144, whichever is earlier.

- (v) Where the assessee questions the jurisdiction of an Assessing Officer, then, the Assessing Officer shall, if not satisfied with the correctness of the claim refer the matter for determination under (ii) above before the assessment is made.

20.2.2 Power to transfer cases [Section 127]

- (i) The power to transfer a case from one Assessing Officer to another subordinate Assessing Officer is vested with the Director General or Chief Commissioner or Commissioner of Income-tax. However, this power can be exercised only after giving the assessee a reasonable opportunity of being heard, wherever possible.
- (ii) There may be situations where the Assessing Officer from whom the case is transferred and the Assessing Officer to whom the case is transferred do not fall under the control of the same Director General or Chief Commissioner or Commissioner of Income-tax. In such cases, the Director General or Chief Commissioner or Commissioner of Income-tax from whose jurisdiction the case is transferred shall pass an order, if such concerned higher authorities mutually agree for such transfer.
- (iii) If the higher authorities are not in agreement about the transfer, then, the Board or any such authority authorized by the Board may pass the order.
- (iv) If the case is transferred between Assessing Officers within the same city or locality or place, then, it is not necessary to give the assessee an opportunity of being heard.
- (v) The transfer of a case may be made at any stage of the proceedings and it is not necessary to reissue any notice already issued.

20.2.3 Change of Income-Tax Authority [Section 129]

- (i) In cases where an income-tax authority succeeds another income-tax authority, who ceases to exercise jurisdiction, then, the succeeding income-tax authority may continue the proceedings from the stage at which the proceedings was left by his predecessor.
- (ii) The assessee concerned can demand that before continuance of proceedings as in (1) above, the previous proceedings or any part thereof be reopened or be reheard before passing of any assessment order.

20.3 POWERS OF INCOME-TAX AUTHORITIES [SECTIONS 131 TO 136]

20.3.1 Discovery, production of evidence etc. [Section 131]: The Assessing Officer, Deputy Commissioner (Appeals), Joint Commissioner, Commissioner (Appeals), the Chief Commissioner *and the Dispute Resolution Panel referred to in section 144C* have the powers vested in a Civil Court under the Code of Civil Procedure, 1908 while dealing with the following matters:

- (i) discovery and inspection;

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- (ii) enforcing the attendance of any person and examining him on oath;
- (iii) compelling the production of books of account and documents; and
- (iv) issuing commissions.

The powers aforementioned are normally those exercisable by a Court when it is trying a suit. While exercising these powers the authorities act in a quasi-judicial capacity and ought to conform to the principles of judicial procedure.

Further, the said Income-tax authority is vested with the power to impound or retain in its custody for such period as it may think fit, any books of account or other documents produced before it in any proceeding under this Act. The powers are unrestricted in the case of all the authorities except the Assessing Officer or an Assistant Director or Deputy Director whose powers are subjected to two restrictions; (i) he must record his reasons for impounding books of account or other documents; and (ii) if he desires to retain in his custody any such books or documents for a period exceeding fifteen days (excluding holidays), he must obtain the prior approval of the Chief Commissioner or Director General for the purpose.

20.3.2 Search and seizure [Section 132]: Under this section wide powers of search and seizure are conferred on the income-tax authorities. The important points relating to this provision have been briefly summarised below :

The provisions of the Criminal Procedure Code relating to searches and seizure would, as far as possible, apply to the searches and seizures under this Act. Contravention of the orders issued under this section would be punishable with imprisonment and fine under section 275A.

(i) Search and seizure can be authorised by Director General or Director or the Chief Commissioner or Commissioner or any such Joint Director or Joint Commissioner as may be empowered by the Board. A Director General or Director or the Chief Commissioner or Commissioner may authorise any Joint Director, Joint Commissioner, Assistant Director, or Deputy Director, Assistant Commissioner or Deputy Commissioner or Income-tax Officer. A Joint Director or Joint Commissioner can authorise Assistant Director or Deputy Director or Assistant Commissioner or Deputy Commissioner or Income-tax Officer.

Thus, under section 132(1), the income-tax authorities listed above are empowered to authorise other income-tax authorities to conduct search and seizure operations.

The authorities empowered to issue authorization are:

- (1) *Director General or Chief Commissioner;*
- (2) *Director or Commissioner; and*
- (3) *such Joint Director or Joint Commissioner as are empowered by the CBDT to do so.*

Sections 2(28C) and 2(28D) define Joint Commissioner and Joint Director, respectively, to include Additional Commissioner and Additional Director. Accordingly, Additional Directors and Additional Commissioners have been issuing warrant of authorisation since 1st June, 1994. However, there have been Court rulings holding that Joint Directors or Joint Commissioners referred to in section 132 Act does not include Additional Director or Additional Commissioner and, consequently, the warrants of authorisation issued by the latter are illegal. As a result, all search and seizure operations have been declared to be illegal.

Therefore, a clarificatory amendment has been made in section 132 to provide explicitly that Additional Director and Additional Commissioner always had the power to issue warrant of authorisation under the said provisions, whether or not specifically empowered by the CBDT to do so. Further, it has also been clarified that Joint Commissioner and Joint Director always had the power to issue warrant of authorization, whether or not specifically empowered by the CBDT to do so.

Thus, in effect, the warrants of authorization issued by Additional Director/Additional Commissioner/Joint Director/Joint Commissioner upto 30th September, 2009 are valid, whether or not they have been specifically empowered by the CBDT to issue such warrants. However, with effect from 1st October, 2009, an Additional Director/Additional Commissioner/Joint Director/Joint Commissioner can issue warrant of authorization only if he has been specifically empowered to do so by the CBDT.

(ii) Such authorisation could take place if the authority believes, on the basis of information in his possession:

- (a) that the person to whom a summons was issued to produce books of account or other documents has omitted or failed to do so; or
- (b) that a person to whom a summons or a notice has been or might be issued, does not or would not produce any books of account or other documents called for or which will be useful or relevant to any proceeding under the Income-tax Act; or
- (c) that a person who is in possession of any articles or things, including money, bullion or jewellery etc. (which has not been disclosed by him) or that such property would not be disclosed by the person concerned for income-tax purposes in future.

(iii) Such an authorisation can empower the authorised officer to enter any building or place or vehicle, vessel or aircraft where he has reasons to suspect that such books of account, documents, articles including money, jewellery, valuables etc. are kept and in case they are found, he may seize them, place marks of identification on them or make a note or inventory thereof for the purpose. However, any bullion, jewellery or other valuable article or thing, which is in the nature of stock-in-trade of the business, found as a result of search shall not be seized but the authorised officer shall make a note or inventory of such stock-in-trade of the business. The person who is in possession or control of books of account or other documents maintained in the form of electronic

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records, shall be required to afford the necessary facility to authorised officer to inspect all such books of account or other documents.

Electronic record as defined in clause (t) of sub-section (1) of section 2 of the Information Technology Act, 2000 means data, record or data generated, image or sound stored, received or sent in an electronic form or microfilm or computer generated microfile.

In the discharge of such a duty, he is authorised to break open the locks in case keys are not readily available. But the books of account and other documents seized should be returned within a period of 30 days from the date of the order of assessment under section 153A or section 158BC(c), unless the reasons for retaining the same are recorded and approved by the Chief Commissioner or Commissioner or Director General or Director. The books or other records cannot be retained for a period exceeding 30 days after the assessment proceedings for the relevant year are over. The persons from whose custody any books of account or other documents have been seized may make copies thereof or take extracts therefrom.

(iv) The Authorised Officer is empowered to search any person in or about the building or place in respect of which a search has been authorised, if he has reason to suspect that any article for which the search is being made is concealed about his person. This Authorised Officer is also entitled to search any person who has got out of or is able to get into or is in the building, place, vessel, vehicle or aircraft in respect of which a search has been authorised, if he has reason to suspect that such person has secreted about his person any books of account or other documents, money, bullion, jewellery or other valuable articles for which the search is being made.

(v) The Commissioner of Income-tax has the power to authorise the search of any building, place, vessel, vehicle, aircraft etc., within his territorial jurisdiction and also in cases where he has no jurisdiction over the persons concerned, if he has reason to believe that any delay in obtaining authorisation from the Commissioner having jurisdiction over the person would be prejudicial to the interests of revenue.

(vi) Where a search for any books of account or other documents or assets has been authorised by any authority who is competent to do so, and the Commissioner has reason to suspect that such books of account or the documents of the assessee are kept in any building, place, vessel, vehicle or aircraft not specified in the search warrant, he may authorise the authorised officer to search such other building, place, vessel, vehicle or aircraft. Accordingly if a search warrant is issued by the Commissioner of Income-tax, Bombay, authorising the search of a premises in Madras and the Authorised Officer finds that the books of account or other documents and/or assets have been secreted in a building or place not specified in the search warrant, he could request any of the local Commissioners to authorise him to search that building or place.

(vii) Now there is a rebuttable presumption to the effect that the books of account or other

documents and assets found in the possession of any person in the course of a search belong to such person and also that the contents of such books of account and other documents are true and that the signature and every other part of such books of account and other documents are in hand-writing of the persons who can reasonably be assumed to have signed or written the books of account or other documents.

(viii) Where the Authorised Officer has no jurisdiction over the person concerned, he is required to hand over the books of account etc., seized by him to the Assessing Officer within a period of 60 days from the date on which the last of the authorisations for search was executed; and thereafter, the powers and function of the Authorised Officer under sections 132(8) and (9) would be exercised by the Assessing Officer.

(ix) Where it is not possible or practicable to take physical possession of any valuable article or thing and remove it to a safe place due to its volume, weight or other physical characteristics or due to its being of a dangerous nature, the authorised Officer may serve an order on the owner or the person who is in immediate possession thereof that he shall not remove, part with or otherwise deal with it except with the previous permission of such authorised officer and such action of the authorised Officer shall be deemed to be seizure of such valuable article or thing. This is called a restraint order. However, such a deeming seizure would not apply to stock-in-trade of the business.

(x) The examination of any person may be not merely in respect of any books of account, other documents or assets found as a result of the search but also in respect of all matters relevant for the purposes of any investigation under the Act.

(xi) An order under sub-section (3) shall not be in force for a period exceeding 60 days from the date of the order [Section 132(8A)].

(xii) The person from whose custody any books of account or other documents are seized under sub-section(1) or sub-section(1A) may make copies thereof, or take extracts therefrom, in the presence of the authorized officer or any other person empowered by him in this behalf, at such place and time as the authorized officer may appoint in this behalf [Section 132(9)].

(xiii) Where the authorized officer has no jurisdiction over the person referred to in clause (a) or clause (b) or clause (c) of sub-section(1), the books of account or other documents, or any money, bullion, jewellery or other valuable article or thing seized under that sub-section shall be handed over by the authorized officer to the Assessing Officer having jurisdiction over such person within a period of 60 days from the date of which the last of the authorizations for search was executed and thereupon the powers exercisable by the authorized officer under sub-section (8) or sub-section (9) shall be exercisable by such Assessing Officer [Section 132(9A)].

20.3.3 Power to requisition books of account etc. [Section 132A]: Where any books of account or other documents and assets have been taken into custody by the Officer or

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authority under any other law (e.g.) by the Collector of Customs, the Sales-tax Commissioner etc., the Director General or Director or the Chief Commissioner or Commissioner of Income-tax may, in such circumstances as are covered by section 132 for search and seizure, authorise any *Additional Director, Additional Commissioner, Joint Director, Assistant Commissioner, Assistant Director* or the Income-tax Officer to require such Assistant Commissioner, Assistant Director or the Income-tax Officer to require such Officer or authority to deliver to him such books of account or other documents and assets. In case where such a requisition is made the officer or the authority concerned would be required to deliver the books of account or other documents and assets. In case where such a requisition is made the officer or the authority concerned would be required to deliver the books of account or other document and assets to the requisitioning Officer either forthwith or, when such officer or the authority is of the opinion that it is no longer necessary to retain the same in his custody. Rule 112D of the Income-tax Rules is also relevant.

20.3.4 Application of retained assets [Section 132B]: This section provides that the seized assets can be appropriated against all tax liabilities of the assessee. However, if the nature of source of acquisition of seized assets is explained satisfactorily by the assessee, then, such assets are required to be released within a period of 120 days from the date on which last of the authorisations for search under section 132 is executed after meeting any existing liabilities. For this purpose, it has been provided that the assessee should make an application to the assessing officer within a period of 30 days from the end of the month in which the asset was seized. The assessee shall be entitled to simple interest at $\frac{1}{2}\%$ per month or part of a month, if the amount of assets seized exceeds the liabilities eventually, for the period immediately following the expiry of 120 days from the date on which the last of the authorisations for search under section 132 or requisition under section 132A was executed to the date of completion of the assessment under section 153A or under Chapter XIV-B.

20.3.5 Power to call for information and Registers of Companies [Sections 133, 134]: The Assessing Officer, the Deputy Commissioner (Appeals), the Joint Commissioner or the Commissioner (Appeals) can call for a variety of information from the assessee and their business associates as well as those with whom they have had dealings in some capacity or the other. They are also authorised to take out copies of any register of members, debenture-holders or mortgages and charges etc., of any company or of any entry in such a register under section 184.

Under the existing provisions of section 133(6) the prescribed authorities have the power to call for any information from any person which will be useful for or relevant to any proceedings under the Act. The amendment by Finance Act, 1995 w.e.f. 1-7-1995 in sub-section 6 empowers the prescribed authorities to call for information for the purpose of any enquiry under this Act. However, an income-tax authority below the rank of Director or Commissioner, can exercise the said power in respect of an enquiry only with the prior approval of the Director or Commissioner.

20.3.6 Power of Survey [Section 133A]: An income-tax authority may enter any place within the limits of the area assigned to him or any place occupied by any person in respect of whom he exercises jurisdiction, at which a business or profession is carried on and require any proprietor, employee or any other person/s, who may at that time/place be attending in any manner to or helping him to carry on any such business or profession. This power may be exercised:

- (i) to afford him the necessary facility to inspect such books of account or other documents as he may require and which may be available at such place;
- (ii) to afford him the necessary facility to check or verify the cash, stock or other valuable articles or things which may be found therein; and
- (iii) to furnish such information as he may require as to any matter which may be useful for or relevant to any proceeding under the Income-tax Act.

This power may be exercised in respect of any place with which the assessee is connected, whether or not such place is the principal place of business or profession. It will also include any other place, whether any business or profession is carried on therein or not, in which the person carrying on the business or profession states that any of his books of account or other valuable article or thing relating to his business or profession is kept. The Income-tax authority may enter any place of business or profession mentioned above only during the hours at which such place is/or open for the conduct of business or profession and in the case of any other place, only after sunrise and before sunset.

The Income-tax authority exercising this power of survey may:

- (i) place marks of identification, if he finds it necessary, on the books of account or other documents inspected by him and make or cause to be made extracts or copies therefrom;
- (ii) impound and retain in his custody for such period as he thinks fit any book of account or other documents inspected by him after recording reasons for doing so.

However, the income tax authority cannot retain in his custody such books of account etc. for a period exceeding 10 days (excluding holidays) without obtaining the approval of the Chief Commissioner or Director General therefor, as the case may be.

- (iii) make an inventory of any cash, stock or valuable article or thing checked or verified by him; and
- (iv) record the statements of any person which may be useful for or relevant to any proceedings under the Income-tax Act.

However, the income-tax authority cannot remove or cause to be removed from the place where he has entered, any cash, stock or other valuable article or thing.

The Income-tax authorities would also have the power to collect information and record

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the statements of any of the persons concerned at any time after any function, ceremony or event even before the stage of commencement of assessment proceedings for the following year for which the information may be relevant, if they are of the opinion that having due regard to the nature, scale and extent of the expenditure incurred, it is necessary to do so. This provision is intended to help in collecting evidence about ostentatious expenditure immediately after the event to be used at the time of the assessment.

If any person who is required to provide facility to the income-tax authority to inspect the books of account or the other documents or to check or verify any cash, stock or other valuable articles or to furnish any information or to have his statement recorded, either refuses or evades to do so, the Income-tax authority would be entitled to use all the powers vested in it under section 131(1) for enforcing proper compliance with the requirements. However, no action under sub-section (1) shall be taken by the Assistant Director or a Deputy Director or an Assessing Officer or a Tax Recovery Officer or an Inspector of Income-tax except with the prior approval of the Joint Director or the Joint Commissioner, as the case may be.

20.3.7 Power to collect certain information [Section 133B]: (i) Under the section an Income-tax authority may enter any building or place (at which a business or profession is carried on) within its jurisdiction or any building or place (at which a business or profession is carried on) which is occupied by any person in respect of whom the said authority exercises jurisdiction for the purpose of collecting any information which may be useful for or relevant for the purposes of the Act. It is not necessary that such a place should be the principal place of the business or profession.

(ii) The authority may require any proprietor, employee or any other person who may at the time and place be attending in any manner to or helping in carrying on such business or profession to furnish such information as may be prescribed.

(iii) An Income-tax authority may enter any place of business or profession referred to above only during the hours at which such place is open for business.

(iv) Such authority shall on no account remove or cause to be removed from the building or place wherein he has entered any books of account or other valuable articles or things.

(v) In this section Income-tax authority means a Joint Commissioner, an Assistant Director or Deputy Director or an Assessing Officer, and includes an Inspector of Income-tax who has been authorised by the Assessing Officer to exercise the power conferred under this section in relation to the area in respect of which the Assessing Officer exercises jurisdiction or any part thereof.

20.3.8 Other powers [Sections 135 and 136]: The Director General or Director, the Chief Commissioner or Commissioner and the Joint Commissioner are competent to make

any enquiry under section 135 and for all purposes they shall have the powers vested in an Assessing Officer in relation to the making of enquiries.

If the Investigating officer is denied entry into the premises, the Assessing Officer shall have all the powers vested in him under sections 131(1) and (2). All the proceedings before Income-tax authorities are judicial proceedings for purposes of section 96 of the Indian Penal Code and fall within the meaning of sections 193 and 228 of the Code.

An income-tax authority shall be deemed to be a Civil Court for the purposes of section 195 of the criminal procedure code.

20.3.9 Disclosure of information regarding assesseees [Section 138]: If a person makes an application in accordance with Rule 113 of the Income-tax Rules, 1962 to the Chief Commissioner or the Commissioner of Income-tax in the prescribed form for obtaining any information relating to any assessee in respect of any assessment year, the commissioner may, if he is satisfied that it is in the public interest, furnish the information. His decision in this regard cannot be called into question. Nevertheless the Government may, having regard to practice and usage customary or otherwise, and any other relevant factors, direct that no information or documents shall be furnished or produced by a public servant in respect of such matters relating to a particular class or classes of assesseees except to certain authorities which may be specified. It would be observed that, under section 138, the Commissioner can make a disclosure on the basis of an application made to him; he cannot volunteer to give the information.

Further, the Board has been empowered to furnish or cause to be furnished any information relating to any assessee in respect of assessment under the Income-tax Act to any office or authority or body performing any function under any law relating to the imposition of any tax, duty or cess or dealings in foreign exchange in all cases where the Board considers such information necessary for the purpose of enabling the officer, authority or body to perform his or its functions under that law. This power of disclosure of information can as well be exercised by any other Income-tax authority specified by the Board by general or special order in this behalf. It will also be open to the Central Government to notify any officer, authority or body performing functions under any other law and on such notification, the Board or any other Income-tax authority may furnish or cause to be furnished similar information relating to any assessee to the officer, authority or body concerned.

Self-examination questions

1. An income-tax authority, in the course of exercise of powers of survey under section 133A, serves a summon on the assessee and impounds the books of account and

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other documents found in the premises visited. Discuss the legality of the action.

2. Certain assets were seized in the course of search on 4.5.2009. State the procedure laid down to deal with such assets seized under the Act.
3. What are the presumptions which can be made if any books of account, document, money, bullion, jewellery is found in possession of a person in the course of a search?
4. What are the circumstances under which an authorization under section 132 can be issued?
5. Is it possible to retain seized books and other documents beyond a period of 30 days? If so, what are the conditions to be fulfilled in this regard?
6. Explain the manner of utilization of the assets seized.
7. Write short notes on the following powers of an income-tax authority -
 - (a) Power to call for information
 - (b) Power to make enquiry
8. The Director of Income Tax received information that Mr. X has unaccounted cash exceeding Rs.50 lakh. Can the Director pass orders for seizure of the cash invoking his powers under section 131(1A)? Does the Director have any other course open to him for the seizure of cash?
9. The assessment of ABC Ltd. was completed under section 143(3). The assessing authority subsequently reopened the assessment by relying upon the circular issued by the CBDT in which the Board had given a direction to subordinate authorities to treat the ex-gratia amounts paid by the company to its employees under the Voluntary Retirement Scheme (VRS) as capital expenditure. On writ, ABC Ltd. contended that the circular issued was contrary to the provisions of the Act and also that it was beyond the powers of the CBDT to issue such a circular against the interest of the assessee. Discuss the correctness or otherwise of ABC Ltd.'s contention.
10. Is the CBDT competent to permit admission of an application for refund under section 237 even after the expiry of the period prescribed under section 239 for avoiding genuine hardship in any case or class of cases?

Answers

8. The powers under section 131(1A) deal with power of discovery and production of evidence. They do not confer the power of seizure of cash or any asset. The

Director, for purposes of making an enquiry or investigation relating to any income concealed or likely to be concealed by any person or class of persons within his jurisdiction shall be competent to exercise powers conferred under section 131(1), which confine to discovery and inspection, enforcing attendance, compelling the production of books of accounts and other documents and issuing commissions. Thus, the power of seizure of unaccounted cash is not one of the powers conferred on the Director under section 131(1A).

However, under section 132(1), the Director has the power to authorise any Assistant Director, Deputy Director, Assistant Commissioner or Deputy Commissioner or Income-tax Officer to seize money found as a result of search [Clause (iii) of section 132(1)], if he has reason to believe that any person is in possession of any money which represents wholly or partly income which has not been disclosed [Clause (c) of section 132(1)]. Therefore, the proper course open to the Director is to exercise his power under section 132(1) and authorise the officers concerned to enter the premises in which the cash is kept and seize the unaccounted cash.

9. This issue came up before the Madras High Court in *Madura Coats v. Dy. CIT (2005) 145 Taxman 226 / 273 ITR 0032*. The High Court held that under section 119(2), the CBDT is given the power to issue instructions to subordinate authorities for the purpose of proper and efficient management of the work of assessment and collection of revenue, provided that such instructions are not prejudicial to the assessee. Therefore, any instruction to be issued should not affect the interests of the assessee. If such directions are issued, they have to be held ultra vires the scope of section 119(2). The reason behind the statutory bar under section 119(2) to issue any instruction contrary to the interests of the assessee is that a subordinate official is bound to comply with the directions/opinion of a superior authority. Any such instruction to an authority discharging the functions of a quasi-judicial nature would be impermissible. In the instant case, there was a positive direction to the assessing authorities to treat the ex-gratia amount as capital expenditure, which direction was certainly adverse to the assessee. Therefore, to the extent the circular was against the interests of the assessee, the same was liable to be held ultra vires.

Therefore, in this case, the contention of ABC Ltd. is correct.

10. This question was taken up by the Full Bench of the Punjab & Haryana High Court in *Jaswant Singh Bambha v. CBDT (2005) 142 Taxman 528*. The High Court observed that under section 239, no power has been conferred on the Assessing Officer to entertain a claim for refund after the period prescribed thereunder. However, section

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5 of the Limitation Act, 1963 permits the admission of an application beyond the period of limitation, if the applicant satisfies the Court that he had sufficient cause for not making the application within such period. This provision has general application.

Section 29(2) of the Limitation Act provides that section 5 of the Limitation Act shall apply in cases of special or local laws to the extent to which it is not expressly excluded by such special or local laws. In other words, section 5 of the Limitation Act cannot be resorted to only when it is expressly excluded by such special or local law.

Section 239 has not expressly excluded the application of section 5 of the Limitation Act, 1963. In fact, a conjoint reading of sections 239 and 119(2) clearly shows that the application of section 5 of the Limitation Act, 1963 to the claims of refund has been specifically included in the Act. Thus, the power given to the Board under section 119(2) to entertain a belated claim is nothing but incorporation of the provisions of section 5 of the Limitation Act. Therefore, by virtue of power conferred on the CBDT under section 119(2), it is competent to permit admission of an application for refund even after the expiry of the period prescribed under section 239 for avoiding genuine hardship in any case or class of cases.

21.1 RETURN OF INCOME

The Income-tax Act contains provisions for filing of return of income. Return of income is the format in which the assessee furnishes information as to his total income and tax payable. The format for filing of returns by different assesseees is notified by the CBDT. The particulars of income earned under different heads, gross total income, deductions from gross total income, total income and tax payable by the assessee are generally required to be furnished in a return of income. In short, a return of income is the declaration of income by the assessee in the prescribed format.

21.2 COMPULSORY FILING OF RETURN OF INCOME [SECTION 139(1)]

(1) As per section 139(1), it is compulsory for companies and firms to file a return of income or loss for every previous year on or before the due date in the prescribed form.

(2) In case of a person other than a company or a firm, filing of return of income on or before the due date is mandatory, if his total income or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeds the basic exemption limit.

(3) Such persons should, on or before the due date, furnish a return of his income or the income of such other person during the previous year in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed.

(4) Further, every person, being an individual or a HUF or an AOP or BOI or an artificial juridical person -

whose total income or the total income of any other person in respect of which he is assessable under this Act during the previous year

without giving effect to the provisions of section 10A or 10B or Chapter VI-A

exceeded the basic exemption limit

is required to file a return of his income or income of such other person on or before the

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due date in the prescribed form and manner and setting forth the prescribed particulars.

For the A.Y.2010-11, the basic exemption limit is Rs.1,60,000 for individuals/HUFs/AOPs/BOIs and artificial juridical persons, Rs.1,90,000 for women assesseees below the age of 65 years and Rs.2,40,000 for assesseees of the age of 65 years or more at any time during the previous year. These amounts denote the level of total income, which is arrived at after claiming the admissible deductions under sections 10A, 10B and Chapter VI-A. However, the level of total income to be considered for the purpose of filing return of income is the income before claiming the admissible deductions under sections 10A, 10B and Chapter VI-A.

(5) 'Due date' means -

- (a) 30th September of the assessment year, where the assessee is -
 - (i) a company; or
 - (ii) a person (other than a company) whose accounts are required to be audited under the Income-tax Act, 1961 or any other law in force; or
 - (iii) a working partner of a firm whose accounts are required to be audited under the Income-tax Act, 1961 or any other law for the time being in force.
- (b) 31st July of the assessment year, in the case of any other assessee.

21.3 INTEREST FOR DEFAULT IN FURNISHING RETURN OF INCOME [SECTION 234A]

(1) Interest under section 234A is attracted for failure to file a return of income on or before the due date mentioned above i.e. interest is payable where an assessee furnishes the return of income after the due date or does not furnish the return of income.

(2) Simple interest @1% per month or part of the month is payable for the period commencing from the date immediately following the due date and ending on the following dates -

Circumstances	Ending on the following dates
Where the return is furnished after due date	the date of furnishing of the return
Where no return is furnished	the date of completion of assessment

(3) The interest has to be calculated on the amount of tax on total income as determined under section 143(1) or on regular assessment as reduced by the advance tax paid and any tax deducted or collected at source.

Note – Section 143(1) provides that if any tax or interest is found due on the basis of a return of income after adjustment of advance tax, tax deducted at source and self-assessment tax, an intimation would be sent to the assessee and such intimation is deemed to be a notice of demand issued under section 156. If any refund is due on the

basis of the return, it shall be granted to the assessee and an intimation to this effect would be sent to the assessee. Where no tax or refund is due, the acknowledgement of the return is deemed to be an intimation under section 156.

21.4 OPTION TO FURNISH RETURN OF INCOME TO EMPLOYER [SECTION 139(1A)]

(1) This section gives an option to a person, being an individual who is in receipt of income chargeable under the head "Salaries", to furnish a return of his income for any previous year to his employer, in accordance with such scheme as may be notified by the CBDT and subject to such conditions as may be specified therein.

(2) Such employer shall furnish all returns of income received by him on or before the due date, in such form (including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media) and manner as may be specified in that scheme.

(3) In such a case, any employee who has filed a return of his income to his employer shall be deemed to have furnished a return of income under sub-section (1).

21.5 INCOME-TAX RETURN THROUGH COMPUTER READABLE MEDIA [SECTION 139(1B)]

(1) This sub-section enables the taxpayer to file his return of income in computer readable media, without interface with the department.

(2) It provides an option to a person (both corporate and non-corporate) required to furnish a return of his income.

(3) Such person may, on or before the due date, furnish a return of income in accordance with such scheme as may be notified by the CBDT, in such form (including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media) and manner as may be specified in that scheme.

(4) Such return shall be deemed to be a return furnished under section 139(1).

21.6 RETURN OF LOSS [SECTION 139(3)]

(1) This section requires the assessee to file a return of loss in the same manner as in the case of return of income within the time allowed under section 139(1).

(2) Under section 80, an assessee cannot carry forward or set off his loss against income in the same or subsequent year unless he has filed a return of loss in accordance with the provisions of section 139(3).

(3) A return of loss has to be filed by the assessee in his own interest and the non-receipt of a notice from the Assessing Officer requiring him to file the return cannot be a valid excuse under any circumstances for the non-filing of such return.

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(4) In particular, a return of loss must be filed by an assessee who has incurred a loss under the heads "Profits and gains from business or profession", "Capital gains", and income from the activity of owning and maintaining race horses taxable under the head "Income from other sources".

(5) However, loss under the head "Income from house property" under section 71B and unabsorbed depreciation under section 32 can be carried forward for set-off even though return of loss has not been filed before the due date.

21.7 BELATED RETURN [SECTION 139(4)]

(1) Any person who has not furnished a return within the time allowed to him under section 139(1) or within the time allowed under a notice issued under section 142(1) may furnish the return for any previous year at any time -

- (i) before the expiry of one year from the end of the relevant assessment year; or
 - (ii) before the completion of the assessment,
- whichever is earlier.

(2) A belated return cannot be revised. It has been held in *Kumar Jagdish Chandra Sinha v. CIT [1996] 86 Taxman 122 (SC)* that only a return furnished under section 139(1) or in pursuance of a notice under section 142(1) can be revised. A belated return under section 139(4) cannot be revised.

Note – Notice under section 142(1) is served by the Assessing Officer for the purpose of making an assessment -

- (i) on any person who has filed a return under section 139(1) to -
 - (a) produce or cause to be produced such accounts or documents as may be required by the Assessing Officer; or
 - (b) to furnish in writing information in the prescribed form on such points or matters as required by the Assessing Officer.
- (ii) on a person who has not filed his return within the time allowed under section 139(1) or before the end of the relevant assessment year to -
 - (a) furnish a return of his income or the income of any other person in respect of which he is assessable under the Act, in the prescribed form containing the prescribed particulars;
 - (b) produce or cause to be produced such accounts or documents as may be required by the Assessing Officer; or
 - (c) to furnish in writing information in the prescribed form on such points or matters as required by the Assessing Officer.

21.8 RETURN OF INCOME OF CHARITABLE TRUSTS AND INSTITUTIONS [SECTION 139(4A)]

- (1) Every person in receipt of income -
 - (i) derived from property held under a trust or any other legal obligation wholly or partly for charitable or religious purpose; or
 - (ii) by way of voluntary contributions on behalf of such trust or institutionmust furnish a return of income if the total income in respect of which he is assessable as a representative assessee (computed before allowing any exemption under sections 11 and 12) exceeds the basic exemption limit.
- (2) Such persons should furnish the return in the prescribed form and verified in the prescribed manner containing all the particulars prescribed for this purpose.
- (3) This return must be filed by the representative-assessee voluntarily within the time limit. Any failure on the part of the assessee would attract liability to pay interest and penalty.

21.9 RETURN OF INCOME OF POLITICAL PARTIES [SECTION 139(4B)]

- (1) Under this section, a political party is required to file a return of income if, before claiming exemption under section 13A, the party has taxable income.
- (2) The grant of exemption from income-tax to any political party under section 13A is subject to the condition that the political party submits a return of its total income within the time limit prescribed under section 139(1).
- (3) The chief executive officer of the political party is statutorily required to furnish a return of income of the party for the relevant assessment year, if the amount of total income of the previous year exceeds the basic exemption limit before claiming exemption under section 13A.
- (4) The return must be filed in the prescribed form and verified in the prescribed manner setting forth such other particulars as may be prescribed by the CBDT.
- (5) The provisions of the Act would apply as if it were a return required to be furnished under section 139(1).

21.10 MANDATORY FILING OF RETURNS BY SCIENTIFIC RESEARCH ASSOCIATIONS, NEWS AGENCY, TRADE UNIONS, ETC. [SECTION 139(4C)]

- (1) It will be mandatory for the following institutions/associations etc. to file the return of income if their total income without giving effect to exemption under section 10, exceeds the basic exemption limit –

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Institution/Association etc.	Applicable section
(a) scientific research association	10(21)
(b) news agency	10(22B)
(c) association or institution	10(23A)
(d) Institution	10(23B)
(e) Fund or institution	10(23C)(iv)
(f) Trust or institution	10(23C)(v)
(g) University or other educational institution	10(23C)(vi)/(iiiad)
(h) Hospital or other medical institution	10(23C)(via)/(iiiiae)
(i) Trade union	10(24)(b)

(2) Such return of income should be in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed.

(3) Then, the provisions of the Act would apply as if it were a return required to be furnished under section 139(1).

21.11 MANDATORY FILING OF RETURNS BY UNIVERSITIES, COLLEGES ETC. [SECTION 139(4D)]

(1) It will be mandatory for every university, college or other institution referred to in clause (ii) and clause (iii) of section 35(1), which is not required to furnish its return of income or loss under any other provision of section 139, to furnish its return in respect of its income or loss in every previous year.

(2) All the provisions of the Income-tax Act, 1961 shall apply to such return as if it were a return under section 139(1).

21.12 REVISED RETURN [SECTION 139(5)]

(1) If any person having furnished a return under section 139(1) or in pursuance of a notice issued under section 142(1), discovers any omission or any wrong statement therein, he may furnish a revised return at any time before the expiry of one year from the end of the relevant assessment year or before completion of assessment, whichever is earlier.

(2) It may be noted that a belated return cannot be revised. It has been held in *Kumar Jagdish Chandra Sinha v. CIT* [1996] 86 Taxman 122 (SC) that only a return furnished under section 139(1) or in pursuance of a notice under section 142(1) can be revised. A belated return furnished under section 139(4), therefore, cannot be revised.

21.13 PARTICULARS REQUIRED TO BE FURNISHED WITH THE RETURN [SECTION 139(6)]

The prescribed form of the return shall, in certain specified cases, require the assessee to furnish the particulars of -

- (i) income exempt from tax
- (ii) assets of the prescribed nature and value and belonging to him
- (iii) his bank account and credit card held by him
- (iv) expenditure exceeding the prescribed limits incurred by him under prescribed heads
- (v) such other outgoings as may be prescribed.

21.14 PARTICULARS TO BE FURNISHED WITH RETURN OF INCOME IN THE CASE OF AN ASSESSEE ENGAGED IN BUSINESS OR PROFESSION [SECTION 139(6A)]

The prescribed form of the return shall, in the case of an assessee engaged in any business or profession also require him to furnish -

- (i) the report of any audit referred to in section 44AB.
- (ii) the particulars of the location and style of the principal place where he carries on the business or profession and all the branches thereof.
- (iii) the names and addresses of his partners, if any, in such business or profession.
- (iv) if he is a member of an association or body of individuals,
 - (a) the names of the other members of the association or the body of individuals; and
 - (b) the extent of the share of the assessee and the shares of all such partners or members, as the case may be, in the profits of the business or profession.

21.15 DEFECTIVE RETURN [SECTION 139(9)]

(1) Under this sub-section, the Assessing Officer has the power to call upon the assessee to rectify a defective return.

(2) Where the Assessing Officer considers that the return of income furnished by the assessee is defective, he may intimate the defect to the assessee and give him an opportunity to rectify the defect within a period of 15 days from the date of such intimation. The Assessing Officer has the discretion to extend the time period beyond 15 days, on an application made by the assessee.

(3) If the defect is not rectified within the period of 15 days or such further extended period, then the return would be treated as an invalid return. The consequential effect would be the same as if the assessee had failed to furnish the return.

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(4) Where, however, the assessee rectifies the defect after the expiry of the period of 15 days or the further extended period, but before assessment is made, the Assessing Officer can condone the delay and treat the return as a valid return.

(5) A return of income shall be regarded as defective unless all the following conditions are fulfilled, namely:

(a) The annexures, statements and columns in the return of income relating to computation of income chargeable under each head of income, computations of gross total income and total income have been duly filled in.

(b) The return of income is accompanied by the following, namely:

(i) a statement showing the computation of the tax payable on the basis of the return.

(ii) the report of the audit obtained under section 44AB (If such report has been furnished prior to furnishing the return of income, a copy of such report and the proof of furnishing the report should be attached).

(iii) the proof regarding the tax, if any, claimed to have been deducted or collected at source and the advance tax and tax on self-assessment, if any, claimed to have been paid. (However, the return will not be regarded as defective if (a) a certificate for tax deducted or collected was not furnished under section 203 or section 206C to the person furnishing his return of income, (b) such certificate is produced within a period of 2 years).

(iv) the proof of the amount of compulsory deposit, if any, claimed to have been paid under the Compulsory Deposit Scheme (Income-tax Payers) Act, 1974;

(c) Where regular books of account are maintained by an assessee, the return of income is accompanied by the following -

(i) copies of manufacturing account, trading account, profit and loss account or income and expenditure account, or any other similar account and balance sheet;

(ii) the personal accounts as detailed below -

(1)	Proprietary business or profession	the personal account of the proprietor
(2)	Firm, association of persons or body of individuals	personal accounts of partners or members
(3)	Partner or member of a firm, association of persons or body of individuals	partner's personal account in firm member's personal account in the association of persons or body of individuals

- (d) Where the accounts of the assessee have been audited, the return should be accompanied by copies of the audited profit and loss account and balance sheet and the auditor's report.
- (e) Where the cost accounts of an assessee have been audited under section 233B of Companies Act, 1956, the return should be accompanied by such report.
- (f) Where regular books of account are not maintained by the assessee, the return should be accompanied by -
 - (i) a statement indicating -
 - (1) the amount of turnover or gross receipts,
 - (2) gross profit,
 - (3) expenses and
 - (4) net profitof the business or profession;
 - (ii) the basis on which such amounts mentioned in (1) above have been computed,
 - (iii) the amounts of total sundry debtors, sundry creditors, stock-in-trade and cash balance as at the end of the previous year.

21.16 PERMANENT ACCOUNT NUMBER (PAN) [SECTION 139A]

(1) Sub-section (1) requires the following persons, who have not been allotted a permanent account number (PAN), to apply to the Assessing Officer within the prescribed time for the allotment of a PAN -

- (i) Every person whose total income or the total income of any other person in respect of which he is assessable under this Act during any previous year exceeded the basic exemption limit; or
- (ii) Every person carrying on any business or profession whose total sales, turnover or gross receipts exceeds or is likely to exceed Rs.5 lakh in any previous year; or
- (iii) Every person who is required to furnish a return of income under section 139(4A).

[Sub-section (1)].

(2) A person who has already been allotted a PAN under sub-clauses (i), (ii) or (iii) of sub-section (1), is not required to obtain another PAN under sub-clause (iv). The PAN already allotted to him shall be deemed to be the PAN in relation to fringe benefit tax.

(3) The Central Government is empowered to specify, by notification in the Official Gazette, any class or classes of persons by whom tax is payable under the Act or any tax or duty is payable under any other law for the time being in force. Such persons are required to apply within such time as may be mentioned in that notification to the

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Assessing Officer for the allotment of a PAN [Sub-section (1A)].

(4) For the purpose of collecting any information which may be useful for or relevant to the purposes of the Act, the Central Government may notify any class or classes of persons, and such persons shall within the prescribed time, apply to the Assessing Officer for allotment of a PAN [Sub-section (1B)].

(5) The Assessing Officer, having regard to the nature of transactions as may be prescribed, may also allot a PAN to any other person (whether any tax is payable by him or not) in the manner and in accordance with the procedure as may be prescribed [Sub-section (2)].

(6) Any person, other than the persons mentioned in (1) to (5) above, may apply to the Assessing Officer for the allotment of a PAN and the Assessing Officer shall allot a PAN to such person immediately.

(7) The CBDT had introduced a new scheme of allotment of computerized 10 digit PAN. Such PAN comprises of 10 alphanumeric characters and is issued in the form of a laminated card.

(8) All persons who were allotted PAN (Old PAN) earlier and all those persons who were not so allotted but were required to apply for PAN, shall apply to the Assessing Officer for a new series PAN within specified time.

(9) Once the new series PAN is allotted to any person, the old PAN shall cease to have effect. No person who has obtained the new series PAN shall apply, obtain or process another PAN.

(10) Quoting of PAN is mandatory in all documents pertaining to the following prescribed transactions :

- (a) in all returns to, or correspondence with, any income-tax authority ;
- (b) in all challans for the payment of any sum due under the Act;
- (c) in all documents pertaining to such transactions entered into by him, as may be prescribed by the CBDT in the interests of revenue. In this connection, CBDT has notified the following transactions, namely:
 - (i) sale or purchase of any immovable property valued at Rs.5 lakh or more;
 - (ii) sale or purchase of motor vehicle or other vehicle (other than two wheeled motor vehicle) which requires registration under section 2(28) of the Motor Vehicle Act, 1988;
 - (iii) a time deposit exceeding Rs.50,000 with a banking company;
 - (iv) a deposit exceeding Rs.50,000 in any account with Post Office Savings Bank;
 - (v) a contract for sale or purchase of securities exceeding value of Rs.1 lakh;

- (vi) opening a bank account;

However, in case the person making the application is a minor who does not have any income chargeable to tax, he is required to quote the PAN of his father or mother or guardian, as the case may be.

- (vii) making an application for installation of telephone connection (including cellular telephone connection);
- (viii) bill payments to hotels and restaurants exceeding Rs.25,000 at any one time;
- (ix) payment in cash for purchase of bank drafts/pay orders/banker's cheque from a banking company for an amount aggregating Rs.50,000 or more during any one day;
- (x) cash deposit aggregating Rs.50,000 or more with a banking company during any one day;
- (xi) cash payment in excess of Rs.25,000 in connection with travel to any foreign country at any one time. Such payment includes cash payment made towards fare, or to a travel agent or a tour operator, or for the purchase of foreign currency. However, travel to any foreign country does not include travel to the neighbouring countries or to such places of pilgrimage as may be specified by the CBDT under *Explanation 3* to section 139(1);
- (xii) making an application to any bank or banking institution or company or any institution for issue of a credit card;
- (xiii) making an application for the following purposes involving payment of an amount exceeding Rs.50,000 -
 - (a) for purchase of units of a mutual fund;
 - (b) for acquiring shares of a company through public issue;
 - (c) for acquiring debentures of a company or institution;
 - (d) for acquiring bonds of Reserve Bank of India.

(11) Every person who receives any document relating to any transaction cited above shall ensure that the PAN is duly quoted in the document.

(12) If there is a change in the address or in the name and nature of the business of a person, on the basis of which PAN was allotted to him, he should intimate such change to the Assessing Officer.

(13) Every person who receives any amount from which tax has been deducted at source shall intimate his PAN to the person responsible for deducting such tax.

(14) Where any amount has been paid after deducting tax at source, the person deducting

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tax shall quote the PAN of the person to whom the amount was paid in the following documents:

- (i) in the statement furnished under section 192(2C) giving particulars of perquisites or profits in lieu of salary provided to any employee;
- (ii) in all certificates for tax deducted issued to the person to whom payment is made;
- (iii) in all returns made to the prescribed income-tax authority under section 206;
- (iv) in all statements prepared and delivered or caused to be delivered in accordance with the provisions of section 200(3)[Sub-section (5B)].

(15) The above sub-sections (5A) and (5B) shall not apply to a person who –

- (i) does not have taxable income or
- (ii) who is not required to obtain PAN

if such person furnishes a declaration under section 197A in the prescribed form and manner that the tax on his estimated total income for that previous year will be nil.

(16) The CBDT is empowered to make rules with regard to the following:

- (a) the form and manner in which an application for PAN may be made and the particulars to be given there;
- (b) the categories of transactions in relation to which PAN is required to be quoted on the related documents;
- (c) the categories of documents pertaining to business or profession in which PAN shall be quoted by every person;
- (d) the class or classes of persons to whom the provisions of this section shall not apply;

The following classes of persons are exempt from the provisions of section 139A:

- (i) persons who have agricultural income and are not in receipt of any other taxable income;
 - (ii) non-residents under the Act, provided that any non-resident entering into any of the prescribed transactions shall furnish a copy of his passport.
- (e) the form and manner in which a person who has not been allotted a PAN shall make a declaration;
 - (f) the manner in which PAN shall be quoted for transactions cited in (b) above;
 - (g) the time and manner in which such transactions shall be intimated to the prescribed authority.

21.17 SCHEME FOR SUBMISSION OF RETURNS THROUGH TAX RETURN PREPARERS [SECTION 139B]

- (1) This section provides that, for the purpose of enabling any specified class or classes of persons to prepare and furnish their returns of income, the CBDT may notify a Scheme to provide that such persons may furnish their returns of income through a Tax Return Preparer authorised to act as such under the Scheme.
- (2) The Tax Return Preparer shall assist the persons furnishing the return in a manner that will be specified in the Scheme, and shall also affix his signature on such return.
- (3) A Tax Return Preparer can be an individual, other than
 - (i) any officer of a scheduled bank with which the assessee maintains a current account or has other regular dealings.
 - (ii) any legal practitioner who is entitled to practice in any civil court in India.
 - (iii) a chartered accountant.
 - (iv) an employee of the 'specified class or classes of persons'.
- (4) The "specified class or classes of persons" for this purpose means any person other than a company or a person whose accounts are required to be audited under section 44AB (tax audit) or under any other existing law, who is required to furnish a return of income under the Act.
- (5) The Scheme notified under the said section may provide for the following -
 - (i) the manner in which and the period for which the Tax Return Preparers shall be authorised,
 - (ii) the educational and other qualifications to be possessed, and the training and other conditions required to be fulfilled, by a person to act as a Tax Return Preparer,
 - (iii) the code of conduct for the Tax Return Preparers,
 - (iv) the duties and obligations of the Tax Return Preparers,
 - (v) the circumstances under which the authorisation given to a Tax Return Preparer may be withdrawn, and
 - (vi) any other relevant matter as may be specified by the Scheme.
- (6) Every Scheme framed by the CBDT under this section shall be laid before each House of Parliament while it is in session to make the same effective.
- (7) If both the houses decide in making any modification of Scheme, then the Scheme will have effect only in such modified form.
- (8) Similarly, if both the Houses decide that any Scheme should not be framed, then

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such Scheme will thereafter be of no effect.

(9) However, such modification or annulment should be without prejudice to the validity of anything previously done under that scheme.

(10) Accordingly, the CBDT has, in exercise of the powers conferred by this section, framed the Tax Return Preparer Scheme, 2006, which came into force from 1.12.2006.

As per this scheme, Tax Return Preparer means any individual who has been issued a Tax Return Preparer Certificate and a unique identification number by the Partner Organisation to carry on the profession of preparing the returns of income in accordance with the provisions of this Scheme. However, the following persons are not eligible to act as a Tax Return Preparer -

- (i) any person referred to in clause (ii) or clause (iii) or clause (iv) of sub-section (2) of section 288, namely, any officer of a Scheduled Bank with which the assessee maintains a current account or has other regular dealings, any legal practitioner who is entitled to practice in any civil court in India and an accountant.
- (ii) any person who is in employment and income from which is chargeable to income-tax under the head salaries

Educational qualification for Tax Return Preparers

Any individual who holds a graduation degree from a recognized Indian University in the fields of Business Administration or Management or Commerce or Economics or Law or Mathematics or Statistics shall be eligible to act as Tax Return Preparer.

21.18 POWER OF CBDT TO DISPENSE WITH FURNISHING DOCUMENTS ETC. WITH THE RETURN AND FILING OF RETURN IN ELECTRONIC FORM [SECTIONS 139C & 139D]

- (i) Section 139C provides that the CBDT may make rules providing for a class or classes of persons who may not be required to furnish documents, statements, receipts, certificate, reports of audit or any other documents, which are otherwise required to be furnished along with the return under any other provisions of this Act.
- (ii) However, on demand, the said documents, statements, receipts, certificate, reports of audit or any other documents have to be produced before the Assessing Officer.
- (iii) Section 139D empowers the CBDT to make rules providing for –
 - (a) the class or classes of persons who shall be required to furnish the return of income in electronic form;
 - (b) the form and the manner in which the return of income in electronic form may be furnished;
 - (c) the documents, statements, receipts, certificates or audited reports which may not be furnished along with the return of income in electronic form but have to be

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produced before the Assessing Officer on demand;

- (d) the computer resource or the electronic record to which the return of income in electronic form may be transmitted.

21.19 AUTHORISED SIGNATORIES TO THE RETURN OF INCOME [SECTION 140]

This section specifies the persons who are authorized to sign and verify the return of income under section 139 of the Act.

	Assessee	Circumstance	Authorised signatory
1.	Individual	(i) In circumstances not covered under (ii), (iii) & (iv) below	- the individual himself
		(ii) where he is absent from India	- the individual himself; or - any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
		(iii) where he is mentally incapacitated from attending to his affairs	- his guardian; or - any other person competent to act on his behalf
		(iv) where, for any other reason, it is not possible for the individual to sign the return	- any person duly authorised by him in this behalf holding a valid power of attorney from the individual (Such power of attorney should be attached to the return of income)
2.	Hindu Undivided Family	(i) in circumstances not covered under (ii) and (iii) below	- the karta
		(ii) where the karta is absent from India	- any other adult member of the HUF
		(iii) where the karta is mentally incapacitated from attending to his affairs	- any other adult member of the HUF
3.	Company	(i) in circumstances not covered under (ii) to (v) below	- the managing director of the company

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		(ii) (a) where for any unavoidable reason such managing director is not able to sign and verify the return; or (b) where there is no managing director	- any director of the company - any director of the company
		(iii) where the company is not resident in India	- a person who holds a valid power of attorney from such company to do so (such power of attorney should be attached to the return).
		(iv) (a) Where the company is being wound up (whether under the orders of a court or otherwise); or (b) where any person has been appointed as the receiver of any assets of the company	- Liquidator - Liquidator
		(v) Where the management of the company has been taken over by the Central Government or any State Government under any law	- the principal officer of the company
4.	Firm	(i) in circumstances not covered under (ii) below	- the managing partner of the firm
		(ii) (a) where for any unavoidable reason such managing partner is not able to sign and verify the return; or (b) where there is no managing partner.	- any partner of the firm, not being a minor - any partner of the firm, not being a minor
5.	LLP	(i) in circumstances not covered under (ii) below	Designated partner

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		<i>(ii)</i> <i>(a) where for any unavoidable reason such designated partner is not able to sign and verify the return; or</i> <i>(b) where there is no designated partner.</i>	- any partner of the LLP - any partner of the LLP
6.	Local authority	-	- the principal officer
7.	Political party [referred to in section 139(4B)]	-	- the chief executive officer of such party (whether he is known as secretary or by any other designation)
8.	Any other association	-	- any member of the association or the principal officer of such association
9.	Any other person	-	- that person or some other person competent to act on his behalf.

21.20 SELF-ASSESSMENT [SECTION 140A]

- (i) Where any tax is payable on the basis of any return required to be furnished under section 139 or section 142 or section 148 or section 153A, after taking into account -
- (1) the amount of tax, already paid,
 - (2) the tax deducted or collected at source
 - (3) relief of tax claimed under section 90 or 90A
 - (4) deduction of tax claimed under section 91
 - (5) any tax credit claimed to be set-off in accordance with the provisions of section 115JAA.

the assessee shall be liable to pay such tax together with interest payable under any provision of this Act for any delay in furnishing the return or any default or delay in payment of advance tax before furnishing the return and the return shall be accompanied by the proof of payment of such tax and interest.

- (ii) Where the amount paid by the assessee under section 140A(1) falls short of the aggregate of the tax and interest as aforesaid, the amount so paid shall first be adjusted towards the interest payable and the balance shall be adjusted towards the tax payable.

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- (iii) For the above purpose, interest payable under section 234A shall be computed on the amount of tax on the total income as declared in the return, as reduced by the amount of -
 - (1) advance tax paid, if any;
 - (2) any tax deducted or collected at source;
 - (3) relief of tax claimed under section 90 or 90A;
 - (4) deduction of tax claimed under section 91;
 - (5) any tax credit claimed to be set-off in accordance with the provisions of section 115JAA.
- (iv) Interest payable under section 234B shall be computed on the assessed tax or on the amount by which the advance tax paid falls short of the assessed tax. For this purpose “assessed tax” means the tax on total income declared in the return as reduced by the amount of -
 - (1) tax deducted or collected at source on any income which forms part of the total income;
 - (2) relief of tax claimed under section 90 or 90A
 - (3) deduction of tax claimed under section 91
 - (4) any tax credit claimed to be set-off in accordance with the provisions of section 115JAA [Sub-section (1B)].
- (v) After the regular assessment under section 143 or section 144 or an assessment under section 153A has been made, any amount paid under sub-section (1) shall be deemed to have been paid towards such regular assessment or assessment, as the case may be.
- (vi) If any assessee fails to pay the whole of tax and interest he shall be deemed to be an assessee in default in respect of the tax and interest and all the provisions of this Act shall apply accordingly.

21.21 INQUIRY BEFORE ASSESSMENT [SECTION 142]

For the purpose of making an assessment, the Assessing Officer may serve on any person who has made a return under section 139 or in whose case the time allowed under section 139(1) for furnishing the return has expired, a notice requiring him:

- (i) To furnish a return of his income or the income of such other person in respect of which he is assessable, in the prescribed form and verified in the prescribed manner and setting-forth such other particulars as may be prescribed [This is in a case where such person has not made a return within the time allowed under section 139(1) or before the

end of the relevant assessment year]

Further, where any notice has been served on or after April 1, 1990 under the aforesaid provision after the end of the relevant assessment year to any person who has not made a return of his income within the time allowed under section 139(1) or before the end of the relevant assessment year, such notice shall be deemed to be a notice served in accordance with the provisions of section 142(1). This provision is applicable retrospectively from April 1, 1990.

Now, the department can issue notice either under section 142(1) or under section 148. Notice under section 142(1) saves the department from the requirement of having to record reasons for the belief that income chargeable to tax has escaped assessment.

It may be noted that the time-limit for completion of assessment under section 153(1) is 24 months (21 months under the amended provisions) from the end of the assessment year in which the income was first assessable. Therefore, since assessment has to be completed within the said period of 24/21 months, it appears that notice under section 142(1) should also be issued within that period.

(ii) To produce, or cause to be produced, such accounts or documents as the Assessing Officer may require.

(iii) To furnish in writing and verified in the prescribed manner information in such form and on such points or matters (including a statement of all assets and liabilities of the assessee, whether included in the accounts or not) as the Assessing Officer may require.

However, the previous approval of the Joint Commissioner has to be obtained before requiring the assessee to furnish the statement of all assets and liabilities not included in the accounts.

Further, the Assessing Officer shall not require the production of any accounts relating to a period more than 3 years prior to the previous year.

Where the business is carried on in several places the assessment of the total profits must be made by the Assessing Officer having jurisdiction at the principal place of business. He can call for the accounts pertaining to any Branch office even if independent inquiries have already been made and the accounts have been examined by the Assessment Officer exercising jurisdiction at the Branch. Similarly the Assessing Officer has power to call for the account books of a foreign business carried on abroad provided that such books are in the possession or control of the assessee.

21.22 AUDIT UNDER SECTION 142

Sub-sections (2A), (2B), (2C), and (2D), of section 142 contain the statutory provisions relating to the conduct of audit. Students may note that the audit envisaged under this provision is different from the Compulsory Tax Audit under section 44AB. A summary of these provisions is given below:

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1. The 'Assessing Officer' has got the power to direct the assessee to get his accounts audited by an accountant if, at any stage of the proceedings before him, he is of the opinion that it is necessary for him to get the accounts audited. The opinion of the Assessing Officer on the basis of which a direction for getting the audit done should be arrived at after having due regard to the nature and complexity of the account of the assessee and the interest of the revenue. Before giving any direction to the assessee for getting the audit done, the Assessing Officer must obtain the approval of the Chief Commissioner or Commissioner of Income-tax.

The expression 'accountant' for this purpose means a 'chartered accountant' within the meaning of the Chartered Accountants Act, 1949 and includes, in relation to any State, any person who, by virtue of the provisions of section 226(2) of the Companies Act, 1956 is entitled to be appointed to act as an auditor of companies registered in that State.

2. The auditor by whom the audit should be carried out would be nominated by the Commissioner of Income-tax specifically for the purpose and the auditor is required to furnish the report of his audit in the prescribed form duly signed and verified by him and setting forth such other particulars as may be prescribed and also giving details in regard to such additional particulars as the Assessing Officer may require in respect of each individual case. The report of the auditor should be furnished in Form No.6B prescribed under Rule 14A of the Income-tax Rules, 1962. The auditor appointed for carrying out the audit becomes liable to carry out the requirements of audit as directed by Assessing Officer and it is the Commissioner and not the assessee who would be his client for this purpose.

3. The Supreme Court in *Rajesh Kumar & Ors. v. DCIT (2006) 287 ITR 91* observed that the order under section 142(2A) is a quasi judicial order. Therefore, the principles of natural justice have to be applied and the assessee has to be given an opportunity of being heard before directing the special audit. The principles of natural justice are based on two principles, namely, (i) nobody shall be condemned unheard; (ii) nobody shall be a judge of his own cause. Once it is held that the assessee suffers civil consequences and any order passed would be prejudicial to him, the principles of natural justice must be held to be implicit. If the principles of natural justice were to be excluded, the Parliament could have said so expressly.

Accordingly, to give effect to the observation of the Supreme Court, the Finance Act, 2007 has provided that the Assessing Officer is now required to give the assessee an opportunity of being heard before issuing directions for special audit under section 142(2A).

4. The Assessing Officer is empowered to direct the audit to be carried out in the case of any particular assessee even if the accounts of the assessee have already been audited under any other law for the time being in force or otherwise.

5. The report of the auditor after conducting the audit must be furnished to Assessing Officer by the assessee within the period specified by the Assessing Officer in his order. The Assessing Officer is, however, entitled, *suo motu* on receipt of an application made in

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this behalf by the assessee for any good any sufficient reason to extend the time-limit by such further period or periods as he deems fit. Further, the aggregate of the period originally fixed and the period or periods so extended should not exceed 180 days in any case. This time of 180 days must be reckoned from the date on which the Assessing Officer's direction to get the accounts audited is received by the assessee.

6. Where the direction for special audit is issued by the Assessing Officer on or after 1.6.2007, the expenses of, and incidental to, such special audit, including remuneration of the Accountant, shall be determined by the Chief Commissioner or Commissioner in accordance with the prescribed guidelines. The expenses so determined shall be paid by the Central Government.

Rule 14B lays down the guidelines for the purposes of determining expenses for audit under section 142(2A). The said Rule is applicable when the audit under section 142(2A) is directed by an Assessing Officer on or after 1st June, 2007. The expenses of, and incidental to, audit (including the remuneration of the accountant, qualified assistants, semi-qualified and other assistants who may be engaged by such Accountant) should not be less than Rs.3750 and not more than Rs.7500 for every hour of the period as specified by the Assessing Officer under section 142(2C). Such period shall be specified in terms of the number of hours required for completing the report.

7. The assessee should, however, be given an opportunity of being heard in respect of any material gathered on the basis of –

- (i) any inquiry under section 142(2); or
- (ii) any audit under section 142(2A)

which is proposed to be utilized for the purposes of the assessment. If, however, the assessment is in nature of a best judgment assessment under section 144, it is not obligatory for the Assessing Officer to give the assessee an opportunity to be heard, before passing the assessment order on the basis of the report of the auditor.

8. In any case, where the assessee is directed to get audit done and the assessee fails to do so, the Assessing Officer is entitled to make a best judgment assessment under section 144 in addition to imposing penalty or taking such steps as may be necessary under the law.

21.23 POWER OF ASSESSING OFFICER TO MAKE A REFERENCE TO THE VALUATION OFFICER [SECTION 142A]

- (i) For determining the cost of construction of properties, an Assessing Officer has been taking the assistance of a Valuation Officer by exercising the power vested in him under section 131 of the Income-tax Act.

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- (ii) Section 131 provides that the Assessing Officer shall have the same powers as are vested in a Court under the Code of Civil Procedure, 1908, when trying a suit.
- (iii) One such power is that of an “issuing commission” provided under section 131(1)(d) which, *inter-alia*, empowers the court “to make a local investigation” and also “to hold a scientific, technical or expert investigation”.
- (iv) The authority of Valuation Officer was created under the Wealth-tax Act by Taxation Laws (Amendment) Act, 1972 with effect from 15.11.1972.
- (v) The scope of power under section 131 vested in an Assessing Officer to make a reference to the Valuation Officer for estimating the cost of construction of properties has been a matter attracting different legal interpretations.
- (vi) Therefore, with a view to remove any doubt in this regard, section 142A has been inserted by the Finance (No.2) Act, 2004, with retrospective effect from 15.11.1972, to clarify that Assessing Officer has and always had the power to make a reference to the Valuation Officer.
- (vii) Sub-section (1) provides that where an estimate of the value of any – (1) investment referred to in section 69 or section 69B or (2) bullion, jewellery or other valuable article referred to in section 69A or section 69B
is required for the purposes of making any assessment or re-assessment, the Assessing Officer may require the Valuation Officer to make an estimate of the same and report to the Assessing Officer.
- (viii) Sub-section (2) provides that the Valuation Officer to whom such a reference is made under sub-section (1) shall, for the purpose of dealing with such reference, have all the powers that he has under section 38A of the Wealth-tax Act, 1957.
- (ix) Sub-section (3) provides that on receipt of the report from the Valuation Officer, the Assessing Officer may after giving the assessee an opportunity of being heard, take into account such report in making such assessment or reassessment.
- (x) However, the provisions of the section will not apply in respect of an assessment made on or before 30th September, 2004, where such assessment has become final and conclusive on or before that date.
- (xi) The *Explanation* to the section provides that the definition of the expression “Valuation Officer” will have the same meaning as in section 2(r) of the Wealth-tax Act, 1957 i.e. a person appointed as a Valuation Officer under section 12A, and includes a Regional Valuation Officer, a District Valuation Officer, and an Assistant Valuation Officer.

21.24 ASSESSMENT [SECTION 143]

Where a return has been made under section 139 or in response to a notice under section 142(1), if any tax or interest is found due an intimation should be sent to the assessee which will be deemed to be a demand notice. If any refund is due to the assessee it shall be granted.

21.24.1 Summary assessment [Section 143(1)/(1A)/(1B)/(1C)]

- (i) Section 143(1) provides for computation of the total income of an assessee after making the following adjustments to the returned income:-
 - (a) any arithmetical error in the return; or
 - (b) an incorrect claim, if such incorrect claim is apparent from any information in the return.
- (ii) The term “an incorrect claim apparent from any information in the return” shall mean such claim on the basis of an entry, in the return, –
 - (a) of an item, which is inconsistent with another entry of the same or some other item in such return;
 - (b) in respect of which, information required to be furnished to substantiate such entry, has not been furnished under this Act; or
 - (c) in respect of a deduction, where such deduction exceeds specified statutory limit which may have been expressed as monetary amount or percentage or ratio or fraction.
- (iii) Tax and interest should be computed on the basis of the total income computed after making the adjustments in (i) above.
- (iv) The sum payable by, or the amount of refund due to, the assessee shall be determined after adjustment of such tax and interest, if any, so computed by any tax deducted at source, any tax collected at source, any advance tax paid, any relief allowable under an agreement under section 90 or section 90A, or any relief allowable under section 91 any tax paid on self-assessment and any amount paid otherwise by way of tax or interest.
- (v) Based on the above adjustments, an intimation shall be prepared or generated and sent to the assessee within a period of one year from the end of the financial year in which the return was made. The intimation shall specify the sum determined to be payable by, or the amount of refund due to, the assessee.
- (vi) If any amount of refund is due to the assessee, the same shall be granted to the assessee.
- (vii) An intimation shall also be sent to the assessee in a case where the loss declared in the return by the assessee is adjusted but no tax or interest is payable by, or no refund is due to, him.
- (viii) On the other hand, where there is neither any adjustment nor any tax due from or refund

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payable to the assessee, the acknowledgement of the return shall be deemed to be the intimation under section 143(1).

- (ix) The scheme contemplates avoiding human interface and therefore, provides for computerised processing of returns for making the above adjustments i.e., the software will be designed to detect arithmetical inaccuracies and internal inconsistencies and make appropriate adjustments in the computation of the total income/fringe benefits.
- (x) For this purpose, the Department is in the process of establishing a system for Centralised Processing of Returns. To facilitate the Department in establishing this system –
 - (a) the Board may formulate a scheme with a view to expeditiously determine the tax payable by, or refund due to, the assessee;
 - (b) the Central Government may issue a notification in the Official Gazette, directing that any of the provisions of this Act relating to processing of returns shall not apply or shall apply with such exceptions, modifications and adaptations as may be specified in the notification. However, such direction shall not be issued after *31st March, 2010*.
 - (c) every notification shall be laid before each House of Parliament as soon as such notification is issued. Along with the notification, the scheme referred above is also required to be laid before each House of Parliament.

21.24.2 Regular assessment/Scrutiny assessment

If the Assessing Officer considers it necessary or expedient to ensure that the assessee has not understated his income or has not computed excessive loss or has not underpaid his tax in any manner he can issue a notice for making the assessment in the normal manner as at present. This will be a scrutiny assessment. It may be noted that notice for detailed scrutiny under section 143(2) cannot be issued after the expiry of 6 months from the end of the financial year in which the return of income is furnished. This procedure does not prevent the Assessing Officer to issue intimation u/s 143(1).

It is also obligatory for scientific research associations and other institutions exempt under clauses (21),(22B),(23A),(23B), sub-clauses (iv),(v),(vi) and (via) of clause (23C) of Section 10 to file their returns of income. In these cases, the Assessing Officer cannot make an assessment denying exemption under section 10 without intimating the Central Government or the prescribed authority of the contravention of the provisions of the relevant sections and till the approval granted to these funds, trusts, institutions, universities, educational institutions or hospitals or medical institutions has been withdrawn or notification rescinded. The time period for completing the assessment in such cases will exclude the period between the date on which the Assessing Officer gives the intimation of the default and date on which copy of the order withdrawing the approval is received by the Assessing Officer.

Assessing Officer empowered to send a proposal to the Central Government recommending withdrawal of approval of scientific research association, university, college or other institution approved under section 35(1)(ii) and (iii)

- (i) The guidelines, the manner and the conditions in accordance with which an application made by a scientific research association, university, college or other institution shall be approved under clause (ii) or clause (iii) of sub-section (1) of section 35 have been provided by the Taxation Laws (Amendment) Act, 2006. Also, the amendment provides for grant of one time approval, which means the approval is to remain in force unless it is withdrawn.
- (ii) Therefore, the Assessing Officer is now required to satisfy himself as to the activities of the university, college or other institution referred to in clause (ii) or clause (iii) of section 35(1).
- (iii) If the activities are not being carried out in accordance with all or any of the conditions subject to which any of the said entities had been approved, the Assessing Officer may, after giving a reasonable opportunity of showing cause to the concerned entity, send a proposal to the Central Government recommending withdrawal of approval.
- (iv) The Central Government may, by order, withdraw the approval and forward a copy of the order to the concerned university, college or other institution and to the Assessing Officer.

21.24.3 Best judgment assessment [Section 144]

If any person:

- (a) fails to make the return required under section 139(1) and has not made a return or a revised return under sub-section (4) or sub-section (5) of section 139 or
- (b) fails to comply with all the terms of a notice issued under section 142(1) or fails to comply with the direction issued under section 142(2A) or
- (c) having made a return, fails to comply with all the terms of a notice issued under section 143(2) the Assessing Officer shall make a best judgment assessment.

Before making such assessment the Assessing Officer can take into account all relevant material which he has gathered. The assessee must be given an opportunity of being heard. Such opportunity shall be given by an Assessing Officer by serving a notice calling upon the assessee to show cause on a date and time to be specified in the notice, why the assessment should not be completed to the best of his judgment. There after, the Assessing Officer shall make the assessment of total income or loss to the best of his judgement and determine the sum payable on the basis of such assessment. It may be noted that no refund can be granted under section 144.

However, where a notice under section 142(1) has been issued prior to the making of an

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assessment under this section, it is not necessary to give such opportunity.

In all the three cases stated above it is mandatory for the Assessing Officer to make best judgment assessment and he has no discretion to make or not to make such assessment. These three cases are alternative and not cumulative for the purpose of making on ex parte assessment.

In a case where a Chief Commissioner or Commissioner issued instructions under section 142(2A) nominated a Chartered Accountant for auditing the assessee's accounts and though the concerned assessee was willing to produce the records the concerned Chartered Accountant refused to audit the accounts, the question arose as to whether there was a failure on the assessee's part to comply with the directions under section 142(2A) and consequently the best judgement assessment could be made under section 144(b).

The Supreme Court held that if for a frivolous reason the Chartered Accountant declined to undertake the audit of the assessee's accounts the assessee could not be held responsible. In such a case there was no default or failure to comply with the direction issued under section 142(2A) on the assessee's part so as to attract the provisions of section 144(b). The best judgement made by the assessing officer was set aside with the directions to appoint another Chartered Accountant within one month to get the accounts audited. [*Swadesh Polytex Ltd. v. ITO* [1983] 15 Taxman 19(SC)].

21.25 POWER OF JOINT COMMISSIONER TO ISSUE DIRECTIONS IN CERTAIN CASES [SECTION 144A]

- (i) A Joint Commissioner may on his own motion or on a reference being made to him by the Assessing Officer or on the application of an assessee, call for and examine the record of any proceeding in which an assessment is pending and if he considers that, having regard to the nature of the case or the amount involved or for any other reason it is necessary so to do, he may issue such direction as he thinks fit for the guidance of the Assessing Officer to enable him to complete the assessment. Such directions shall be binding on the Assessing Officer.
- (ii) No directions which are prejudicial to the assessee shall be issued before an opportunity is given to the assessee to be heard.

21.26 PROVISION FOR CONSTITUTION OF ALTERNATE DISPUTE RESOLUTION MECHANISM [SECTION 144C]

An alternate dispute resolution mechanism which will aid speedy resolution of disputes on a fast track basis has now been provided for under the Income-tax Act. The significant features of the alternate dispute resolution mechanism are briefed hereunder –

- (1) *The Assessing Officer shall, forward a draft order of assessment to the eligible assessee if he proposes to make, on or after 1st October, 2009, any variation in the income or loss*

returned which is prejudicial to the interest of such assessee.

“Eligible assessee” means,-

- (i) any person in whose case such variation arises as a consequence of the order of the Transfer Pricing Officer passed under sub-section (3) of section 92CA; and*
 - (ii) any foreign company.*
- (2) The eligible assessee shall, within thirty days of the receipt by him of the draft order,-*
- (a) file his acceptance of the variations to the Assessing Officer; or*
 - (b) file his objections, if any, to such variation with,—*
 - (i) The Dispute Resolution Panel; and*
 - (ii) The Assessing Officer.*

“Dispute Resolution Panel” means a collegium comprising of three commissioners of Income-tax constituted by the CBDT for this purpose.

- (3) The Assessing Officer has to complete the assessment on the basis of the draft order, if —*
- (a) the assessee intimates the acceptance of the variation to the Assessing Officer; or*
 - (b) no objections are received within the period of 30 days specified in (2) above.*
- (4) The Assessing Officer shall, notwithstanding anything contained in section 153, pass the assessment order within one month from the end of the month in which,—*
- (a) the acceptance is received; or*
 - (b) the period of filing of objections expires.*
- (5) The Dispute Resolution Panel shall, in a case where any objections are received, issue such directions, as it thinks fit, for the guidance of the Assessing Officer to enable him to complete the assessment.*
- (6) The Dispute Resolution Panel shall issue such directions, after considering the following, namely:—*
- (a) Draft order;*
 - (b) Objections filed by the assessee;*
 - (c) Evidence furnished by the assessee;*
 - (d) Report, if any, of the Assessing Officer, Valuation Officer or Transfer Pricing Officer or any other authority;*
 - (e) Records relating to the draft order;*
 - (f) Evidence collected by, or caused to be collected by, it; and*
 - (g) Result of any enquiry made by, or caused to be made by it.*
- (7) The Dispute Resolution Panel may, before issuing any such directions -*
- (a) make such further enquiry, as it thinks fit; or*

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- (b) cause any further enquiry to be made by any income tax authority and report the result of the same to it.*
- (8) The Dispute Resolution Panel may confirm, reduce or enhance the variations proposed in the draft order. However, it cannot set aside any proposed variation or issue any direction as mentioned in (5) above, for further enquiry and passing of the assessment order.*
- (9) If the members of the Dispute Resolution Panel differ in opinion on any point, the point shall be decided according to the opinion of the majority of the members.*
- (10) Every direction issued by the Dispute Resolution Panel shall be binding on the Assessing Officer.*
- (11) If any direction is prejudicial to the interest of the assessee or the interest of the revenue, then, the same can be issued only after an opportunity of being heard is given to the assessee or the Assessing Officer, as the case may be.*
- (12) Such direction has to be issued within nine months from the end of the month in which the draft order is forwarded to the eligible assessee.*
- (13) Upon receipt of such direction, the Assessing Officer has to complete the assessment in accordance with the same, within one month from the end of the month in which the direction is received. There is no requirement of providing any further opportunity of being heard to the assessee,*
- (14) The CBDT is empowered to make rules for the efficient functioning of the Dispute Resolution Panel and speedy resolution of the objections filed by the eligible assessee.*

21.27 VALUATION OF INVENTORY [SECTION 145A]

The valuation of purchase and sale of goods and inventory for the purpose of determining the income chargeable under the head 'Profits and gains of business or profession' shall be in accordance with the method of accounting regularly followed by the assessee. Such value will be arrived at after being adjusted to include the amount of any tax, duty, cess or fee (by whatever name called), actually paid or incurred by the assessee to bring the goods to their present location and condition.

Further, for the purpose of valuation, any entitlement to rebate or set-off, etc. therefrom should not be considered. In this context, the following points may be noted:

This section applies irrespective of section 145 of the Act laying down method of accounting to be followed, to determine Business Income.

It applies only in respect of valuation of purchase and sale of goods and inventory (opening as well as closing stock).

Otherwise, business income should be computed in accordance with method of accounting regularly employed.

In valuation of sale and purchase of goods as well as inventory, any amount actually

paid or incurred on any tax, duty, cess or fees, ("duty etc." in relation to purchase and sale of goods) shall be included.

Duty, etc., must have been actually paid or incurred to bring the goods to the place of its location and condition, as on the date of valuation.

The amount of duty, etc., included in value of inventory, should not take into account any right arising as a consequence of payment, meaning any credit or set-off or rebate etc.

21.28 INCOME ESCAPING ASSESSMENT [SECTION 147]

21.28.1 Applicability

1. If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of sections 148 to 153 assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the relevant assessment year.

2. Where an assessment under section 143(3) or 147 has been made for the relevant assessment year, no action shall be taken under this section after the expiry of four years from the end of the relevant assessment year unless any income chargeable to tax has escaped assessment for such assessment year by reason of the failure on the part of the assessee to make a return under section 139, or in response to a notice issued under section 142(1) or section 148 or to disclose fully and truly all material facts necessary for his assessment for that assessment year.

The Assessing Officer must have 'reason to believe' that income chargeable to tax had escaped assessment. The belief which prompts an Income-tax Officer to apply section 147 to any particular case must be that of an honest and reasonable person based upon reasonable grounds, and that the Assessing Officer may act under this section on direct or circumstantial evidence but not on a mere suspicion, gossip or rumour. The powers of the Assessing Officer are wide, but not plenary in nature. Care must be taken to note that the words used in the section are "reason to believe" and not 'reason to suspect'. The expression 'reason to believe' does not, however, mean a purely subjective satisfaction on the part of the Assessing Officer. The belief must be held in good faith. It cannot be a mere pretence. It is open to the Court to examine whether the reasons for the belief have a rational connection or a relevant bearing to the formation of the belief and are not extraneous or irrelevant to the purpose of the section. There is no requirement in any of the provisions of the Act or under any section laying down as a condition for the initiation of the proceeding that the reasons which induced the Assessing Officer, to issue the notice must also be communicated to the assessee. Therefore, the Assessing Officer

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need not communicate to the assessee the reasons, which led him to initiate the proceedings under section 147.

3. The Assessing Officer may assess or reassess an income which is chargeable to tax and has escaped assessment other than the income involving matters which are the subject matter of any appeal, reference or revision.

4. It has been clarified that production before the Assessing Officer of account books or other evidence from which material evidence could have been discovered by the Assessing Officer will not necessarily amount to disclosure.

5. For the purpose of this section, the following shall also be deemed to be cases where income chargeable to tax has escaped assessment :

- (a) Where no return of income has been furnished by the assessee although his total income or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeded the maximum amount which is not chargeable to income tax.
- (b) Where a return of income has been furnished by the assessee but no assessment has been made and it is noticed by the Assessing Officer that the assessee has understated the income or has claimed excessive loss, deduction, allowance or relief in the return.
- (c) Where an assessment has been made but:
 - (i) income chargeable to tax has been under-assessed
 - (ii) such income has been assessed at too low a rate
 - (iii) such income has been made the subject of excessive relief under this Act
 - (iv) excessive loss or depreciation or any other allowance under this Act has been computed.

6. *Explanation 3 to section 147 provides that the Assessing Officer may assess or reassess the income in respect of any issue (which has escaped assessment) which comes to his notice subsequently in the course of proceedings under this section, even though the reason for such issue does not form part of the reasons recorded under section 148(2).*

21.28.2 Issue of notice where income has escaped assessment [Section 148]

1. Before making the assessment, reassessment or recomputation under section 147, the Assessing Officer shall serve on the assessee, a notice requiring him to furnish a return within such period as may be specified in the notice, a return of his income or the income of any other person for whom he is assessable under the Act, during the previous year corresponding to the relevant assessment year in the prescribed form and verified in the prescribed manner and setting forth such other particulars may be prescribed. The provisions of this Act shall apply accordingly as if such return were a return required to be

furnished under section 139.

In case of income escaping assessment, where the return of income has been furnished during the period between 1.10.91 and 30.9.05 in response to notice under section 148, a notice for scrutiny under section 143(2) served at any time before the expiry of the time limit for making an assessment/re-assessment/re-computation as specified in section 153(2) shall be deemed to be a valid notice. Prior to this amendment, such notice was required to be served on the assessee within a period of 12 months from the end of the month in which the return is furnished.

For instance, where in response to a notice under section 148 served on August 5th, 2002, the taxpayer submits a return for the A.Y.1999-2000 on November 25th, 2002, the scrutiny notice can be issued at any time after November 25th, 2002 (it can be issued even after the expiry of 12 months from the end of the month in which return is submitted, i.e., even after November 30th, 2003). However, since reassessment cannot be completed after March 31, 2004 [as per the time-limit given under section 153(2)], therefore, scrutiny notice cannot be issued in this case after March 31, 2004.

However, these provisions do not apply to any return which has been furnished on or after 1.10.2005 in response to a notice served under section 148.

2. The Assessing Officer shall, before issuing any notice under this section, record his reasons for doing so.

21.28.3 Reassessment - Notice Period

Under section 148 of the Act, an assessment can be reopened and for the purpose a notice can be issued to an assessee for filing a return of his income within a specified period, not being less than thirty days. At present in the printed form of notice under section 148, the assessee is required to furnish a return of his income 'within thirty days'.

Sub-section (2A) of this section lays down certain time limits in cases where fresh assessment has to be made.

Accordingly, an order of fresh assessment in pursuance of an order under section 250 or 254 or 263 or 264. Setting aside or canceling an assessment, may be made at any time before the expiry of one year from the end of the financial year in which the order under section 250 or 254 is received by the Chief Commissioner or Commissioner, or the order under section 263 or 264 is passed by the Chief Commissioner or Commissioner.

21.28.4 Time limit for notice [Section 149] - Notice under section 148 must be issued within the following time limit:

- (a) Where the income which has escaped assessment amounts to or is likely to amount to Rs.1 lakh or more, the notice under section 148 shall be issued within six years from the end of the relevant assessment year.
- (b) In other cases, the notice shall be issued within four years from the end of the relevant assessment year.

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21.29 SANCTION FOR ISSUE OF NOTICE [SECTION 151]

(1) In a case where an assessment under section 143(3) or section 147 has been made for the relevant assessment year no notice shall be issued under section 148 except by an Assessing Officer of the rank of Assistant Commissioner or Deputy Commissioner, unless the Joint Commissioner is satisfied on the reasons recorded by the Assessing Officer that it is a fit case for issue of notice.

(2) After the expiry of four years from the end of the relevant assessment year no such notice shall be issued unless the Chief Commissioner or Commissioner is satisfied on the reasons recorded by the Assessing Officer aforesaid thereof it is a fit case for the issue of such notice.

(3) In all other cases (*i.e.* non-scrutiny cases) no notice shall be issued under section 148 by an Assessing Officer who is below the rank of Joint Commissioner after the expiry of four years from the end of the relevant assessment year unless the Joint Commissioner is satisfied on the reasons recorded by such Assessing Officer that it is a fit case for the issue of such notice.

(4) The Joint Commissioner, the Commissioner or the Chief Commissioner, as the case may be, on being satisfied with the reasons recorded by the Assessing Officer about the fitness of a case for the issue of notice under section 148, need not issue the notice himself. Thus, where the approval of the Joint Commissioner/Chief Commissioner/Commissioner/ Commissioner is required for issue of notice under section 148, it is not necessary that such notice should be issued by the Joint Commissioner/Chief Commissioner/ Commissioner himself. It would be sufficient if the Assessing Officer issues the notice.

21.30 TIME LIMIT FOR COMPLETION OF ASSESSMENTS AND REASSESSMENTS [SECTION 153]

1. No order of assessment shall be made under section 143 or 144 at any time after the expiry of 21 months from the end of the assessment year in which the income was first assessable.

2. No order of assessment, reassessment or recomputation shall be made under section 147 after the expiry of 9 months from the end of the financial year in which the notice under section 148 was served [Section 153(2)].

3. Sub-section (2A) of this section lays down certain time limits in cases where fresh assessment has to be made.

Accordingly, an order of fresh assessment in pursuance of an order under section 250 or 254 or 263 or 264, setting aside or canceling an assessment, may be made at any time before the expiry of 9 months from the end of the financial year in which the order under section 250 or 254 is received by the Chief Commissioner or Commissioner, or the order under section 263 or 264 is passed by the Chief Commissioner or Commissioner. This is notwithstanding anything contained in sub-sections (1), (1A), (1B) and (2) of section 153.

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Where immediately after the exclusion of the time mentioned in the explanation, the period of limitation available to the Assessing Officer for making orders under sections 153(1), (1A), (1B), (2), (2A), (4) is less than 60 days, the remaining period shall be extended to 60 days and the aforesaid period of limitation shall be deemed to be extended accordingly.

4. **No time limit** – The provisions of sub-sections (1), (1A), (1B) and (2) shall not apply to the following classes of assessments, reassessments and recomputations:

(i) Where the assessment or reassessment is made on the assessee or any other person in consequence of or to give effect to any finding or direction contained in any order under sections 250, 254, 260, 262, 263 or 264 (in appeal, reference, revision) or an order by a Court in a proceeding otherwise than by way of appeal or reference under this Act.

(ii) where in the case of a firm an assessment is made on a partner of the firm in the case of a firm an assessment of the escaped income is made on the firm under section 147 [Sub-section 3].

5. Section 153A(2) provides for revival of abated assessments/reassessments, where the assessment order or reassessment order has been annulled in any appeal or legal proceeding. The time limit for completion of such assessment or reassessment shall be one year from the end of the month in which the abated assessment revives or within the period already specified in section 153 or in sub-section (1) of section 153B, whichever is later [Sub-section (4)].

6. **Exclusion of period** - In computing the period of limitation for the purposes of section 153 the following time periods shall be excluded.

- (a) The time taken in reopening the whole or any part of the proceedings in giving an opportunity to the assessee to be reheard when there is a change in the incumbency of the office under section 129.
- (b) Any time during which the assessment proceeding is stayed by an order of a court.
- (c) the period commencing from the date on which the Assessing Officer, under clause (i) of the proviso to section 143(3), intimates the Central Government or the prescribed authority, the contravention of the provisions of clause (21) or clause (22B) or clause (23A) or clause (23B) of section 10 or sub-clause (iv) or (v) or (vi) or (via) of section 10(23C), and ending with the date on which the copy of the order withdrawing the approval or rescinding the notification, as the case may be, under those clauses is received by the Assessing Officer.
- (d) Time taken for completion of special tax audit of the accounts of the assessee under section 142(2A) beginning with the date on which the Assessing Officer directs the assessee to get his accounts audited and ending with the last date by which the assessee is required to furnish the audit report.

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- (e) Where a declaration under section 158A is made by an assessee commencing from the date on which the Assessing Officer received the declaration and ending with the date on which an order under section 158A(3) is made by the Assessing Officer. However the period cannot exceed 60 days.
- (f) In a case where an application for settlement of case has been rejected or is not allowed to be proceeded with, the period commencing from the date on which such application is made and ending with the date on which the order of the Settlement Commission is received by the Commissioner.
- (g) The period commencing from the date on which an application is made before the Authority for Advance Rulings under section 245Q(1) and ending with the date on which the advance ruling pronounced by it or the order rejecting the application is received by the Commissioner under section 245R(7)/(3).

Explanation 1 to section 153 provides for exclusion of certain periods as specified therein in computing the period of limitation for the purposes of section 153. If after exclusion of such time period, the period of limitation available to the Assessing Officer is less than 60 days, such remaining period shall be extended to 60 days and the period of limitation shall be deemed to be extended accordingly.

7. In a case where a proceeding before the Settlement Commission abates under 245HA, the period of limitation available under this section to the Assessing Officer for making an order of assessment , reassessment or recomputation as the case may be , shall , after the exclusion of the period under sub section (4) of section 245HA , be not less than one year ; and where such period of limitation is less than one year , it shall be deemed to have extended to one year: and for the purpose of determining the period of limitation under sections 149, 153B, 154, 155, 158BE and 231 and for the purpose of payment of interest under section 243 or section 244 or , as the case may be , section 244A, this provision shall also apply.

8. Where by an order in appeal reference or revision any income is excluded from the total income of the assessee for any assessment year, the assessment of such income for another assessment year shall, for the purpose of sections 150 and 153 be deemed to be one made in consequence of or to give effect to any finding or direction contained in the appellate order.

9. Where by an order in appeal, reference or revision, any income is excluded from the total income of one person and held to be the income of another person then an assessment of such income on such other person shall, for the purpose of section 150 and 153 be deemed to be one made in consequence of or to give effect to any finding or direction contained in the appellate order. The other person must be given an opportunity of being heard before the order of assessment is passed.

21.31 LIMITATION PERIOD FOR COMPLETION OF ASSESSMENTS AND REASSESSMENTS

Section 153 of the Act lays down the time limit for making an order of assessment i.e. any time before expiry of 21 months from the end of the assessment year in which the income was first assessable. Also, *Explanation 1* below section 153 of the Act sets out certain circumstances in which certain periods as specified are excluded from the period of limitation.

In a case where an audit under section 142(2A) is ordered, the assessee is required to furnish a report of such audit within the prescribed time. In such a case, the period commencing from the date on which the Assessing Officer directs the assessee to get his accounts audited under section 142(2A) and ending with the last date on which the assessee is required to furnish a report of such audit is excluded while reckoning the period of limitation for completion of the assessment, as per *Explanation 1 (iii)* below section 153.

This would enable extension of the limitation period, at least, by the time permitted although the audit reports not furnished.

21.32 ASSESSMENT PROCEDURE IN CASE OF SEARCH OR REQUISITION [SECTION 153A/153B/153C]

The block assessment procedure introduced in 1995 and in operation since then for 8 years with various amendments from time to time has been abolished in respect of search carried out after 31st May, 2003. In the place of the block assessment, a new scheme of reassessment has been introduced by inserting three new sections 153A, 153B and 153C of the Income-tax Act w.e.f. 1.6.03 for assessment in case of search or making requisition.

Procedure for assessment where search is initiated under section 132 or books of account etc. are requisitioned under section 132A [Section 153A]

- (a) The provisions of section 153A prescribing a procedure for assessment in the case of search or requisition will apply notwithstanding anything contained in sections 139/147/148/149/151 and 153.
- (b) This section provides for the procedure for completion of assessment where a search is initiated under section 132 or books of account, other documents or any assets are requisitioned under section 132A after 31st May, 2003.
- (c) In such cases, the Assessing Officer shall issue notice to such person. Such a person has to furnish a return of income within such period as may be specified in the notice setting forth such other particulars as may be prescribed.
- (d) Such a return should be filed in respect of six assessment years immediately preceding the assessment year relevant to the previous year in which the search was conducted under section 132 or requisition was made under section 132A.

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- (e) The Assessing Officer shall assess or reassess the total income of each of these six assessment years.
- (f) The assessment or reassessment, if any, relating to any assessment year falling within the above period of six assessment years, pending on the date of the initiation of the search under section 132 or requisition under section 132A, as the case may be, shall abate. In other words, they will cease to be applicable.
- (g) If any proceeding initiated under section 153A or any order of assessment or reassessment made under section 153A(1) has been annulled in any appeal or other legal proceeding, the abated assessment or reassessment relating to any assessment year shall stand revived with effect from the date of receipt of the order of such annulment by the Commissioner. If the order of annulment is set aside, such revival shall cease to have effect.
- (h) Unless section 153A, section 153B and section 153C provide otherwise, all other provisions of the Income-tax Act shall apply to the assessment or reassessment made in respect of assessment year under this section.
- (i) The tax shall be chargeable at the rate or rates as applicable to such assessment year.

Time-limit for completion of search assessments [Section 153B]

- (a) Section 153B provides for the time-limit for completion of search assessments.
- (b) An assessment or reassessment order in respect of each assessment year falling within six assessment years under section 153A, should be made within a period of two years from the end of the financial year in which the last of the authorisations for search under section 132 or requisition under section 132A was executed.
- (c) The section also provides the time limit for completion of assessment in respect of the assessment year relevant to the previous year in which the search is conducted under section 132 or requisition is made under section 132A within a period of 21 months from the end of the financial year in which the last of the authorisations for search under section 132 or for requisition under section 132A, as the case may be, was executed.
- (d) In case of any other person referred to in section 153C, the time limit for making assessment or reassessment of total income of the assessment years referred to in clause (b) and clause (c) above, shall be the either 21 months from the end of the financial year in which the last of authorisations for search under section 132 or for requisition under section 132A was executed or 9 months from the end of the financial year in which books of account or documents or assets seized or requisitioned are handed over under section 153C to the Assessing Officer having jurisdiction over such other person, whichever is later.

Time limit for completion of assessment/reassessment where a reference is made to the Transfer Pricing Officer

The time limit for completion of assessment/re-assessment where a reference is made to the Transfer Pricing Officer under section 92CA(1) (on or after 1.6.2007 or before that date but the order is yet to be passed as on that date) has been increased by 12 months i.e.

Section	Particulars	Time-limit
Second Proviso to section 153(1)	Completion of assessment under section 143 or section 144 for the A.Y. 2005-06 onwards.	33 months from the end of the assessment year in which the income was first assessable.
Third proviso to section 153(2)	Completion of assessment/ reassessment/recomputation under section 147 if notice is served under section 148 on or after April 1, 2006.	21 months from the end of the financial year in which notice under section 148 is served.
Third proviso to section 153(2A)	Fresh assessment in pursuance of an order under section 254 (received by the Chief Commissioner / Commissioner on or after April 1, 2006) or an order passed by the Commissioner under sections 263 and 264 on or after April 1, 2006.	21 months from the end of the financial year in which such order is received by the Chief Commissioner / Commissioner or passed by the Commissioner, as the case may be.
Third Proviso to section 153B(1)	Completion of assessment in cases where the last of the authorizations for search under section 132 or for requisition under section 132A was executed during F.Y.2005-06 or thereafter.	33 months from the end of the financial year in which the last of the authorizations for search under section 132 or requisition under section 132A was executed.
Fourth Proviso to section 153B(1)	Completion of assessment/ reassessment in case of other person referred to in section 153C in cases where the last of the authorizations for search under section 132 or for requisition under section 132A was executed during F.Y.2005-06 or thereafter.	33 months from the end of the financial year in which the last of the authorizations for search under section 132 or for requisition under section 132A was executed or 21 months from the end of the financial year in which the books of account or documents or assets seized or requisitioned are handed over under section 153C to the Assessing Officer having jurisdiction over such other person, whichever is later.

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Exclusions while computing period of limitation [Explanation to Section 153B]

In computing the period of limitation for completion of assessment or reassessment, the following periods should be excluded -

1. **Stay or injunction** - The period during which the assessment proceeding is stayed by an order or injunction of any court; or
2. **Audit under section 142(2A)** - The period commencing from the day on which the Assessing Officer directs the assessee to get his accounts audited under section 142(2A) and ending on the day on which the assessee is required to furnish a report of such audit under that section; or
3. **Re-hearing under section 129** - The time taken in reopening the whole or any part of the proceeding or giving an opportunity to the assessee of being re-heard under the proviso to section 129; or
4. **Settlement** - In a case where an application made before the Settlement Commission under section 245C is rejected by it or is not allowed to be proceeded with by it, the period commencing on the date on which such application is made and ending with the date on which the order under section 245D(1) is received by the Commissioner under section 245D(2); or
5. **Advance Ruling** - The period commencing from the date on which an application is made before the Authority for Advance Ruling under section 245Q(1) and ending with the date on which the order rejecting the application is received by the Commissioner under section 245R(3); or
6. **Advance Ruling** - The period commencing from the date on which an application is made before the Authority for Advance Ruling under section 245Q(1) and ending with the date on which the advance ruling pronounced by it is received by the Commissioner under section 245R(7) or
7. **Setting aside of order of annulment** - The period commencing from the date of annulment of a proceeding or order of assessment or reassessment referred to in sub-section (2) of section 153A till the date of the receipt of the order setting aside the order of such annulments by the Commissioner.

If, after the exclusion of the aforesaid period, the period of limitation available to the Assessing Officer for making an order of assessment or reassessment, as the case may be, is less than sixty days, such remaining period shall be extended to sixty days and the period of limitation shall be deemed to be extended accordingly.

Assessment or reassessment of income of any other person [Section 153C]

- (a) Section 153C provides for assessment or reassessment of income of any other person.
- (b) Where the Assessing Officer is satisfied that any money, bullion, jewellery or other

valuable article or thing or books of account or documents seized or requisitioned belong or belongs to a person other than the person referred to in section 153A, then the books of account, or documents or assets seized or requisitioned shall be handed over to the Assessing Officer having jurisdiction over such other person. [Section 153C(1)]

- (c) That Assessing Officer shall proceed against such other person and issue such other person notice and assess or reassess income of such other person in accordance with the provisions of section 153A. [Section 153C(1)]
- (d) The assessment or reassessment, if any, relating to any assessment year falling within the period of six assessment years referred to in the said section pending on the date of initiation of the search under section 132 or on the date of making of requisition under section 132A, as the case may be, shall abate.
- (e) In case of such other person, the reference to the date of initiation of the search under section 132 or making of requisition under section 132A in the second proviso to section 153A shall be construed as reference to the date of receiving the books of account or documents or assets seized or requisitioned by the Assessing Officer having the jurisdiction over such other person [Section 153C(1)].
- (f) In respect of the assessment year relevant to the previous year in which search is conducted under section 132 or requisition is made under section 132A, in case of such other person, where -
 - (i) no return of income has been furnished by such person and no notice under sub-section (1) of section 142 has been issued to him, or
 - (ii) a return of income has been furnished by such person but no notice under sub-section (2) of section 143 has been served and limitation of serving the notice under sub-section (2) of section 143 has expired, or
 - (iii) assessment or reassessment, if any, has been made,before the date of receiving of books of account or documents or assets seized or requisitioned by the Assessing Officer having jurisdiction over such other person, such Assessing Officer shall issue the notice and assess or reassess total income of such other person for such assessment year in the manner provided in section 153A. [Section 153C(2)].
- (g) The provisions of sub-section (2) would apply where books of account or documents or assets seized or requisitioned referred to in sub-section (1) has been received by the Assessing Officer having jurisdiction over such other person after the due date for furnishing the return of income for the assessment year relevant to the previous year in which search is conducted under section 132 or requisition is made under section 132A.

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Prior approval of Joint Commissioner required for assessment or reassessment in respect of search cases [Section 153D]]

Section 153D has been inserted to provide that assessment or reassessment of search cases in respect of each assessment year referred to in section 153A(b) or the assessment year referred to in 153B(1)(b) shall not be made by an Assessing Officer below the rank of Joint Commissioner without the previous approval of the Joint Commissioner.

21.33 RECTIFICATION OF MISTAKES [SECTION 154]

With a view to rectifying any mistake apparent from the record an income tax authority referred to in section 116 may:

- (a) amend any order passed by it under the provisions of this Act;
- (b) amend any intimation or deemed intimation under section 143(1).

The jurisdiction of any authority under the Act to make an order under section 154 depends upon the existence of a mistake apparent on the face of the record. It may be a mistake of fact as well as mistake of law. For instance, the treatment of a non-agricultural income as agricultural income and granting exemption in respect of such income is an obvious mistake of law which could be rectified under section 154. However, a mere change of opinion cannot be the basis on which the same or the successor Assessing Officer can treat a case as one of rectification of mistake. A mistake is one apparent from the record in case, where it is a glaring, obvious, patent or self-evident. Mistake, which has to be discovered by a long drawn process of reasoning or examination or arguments on points, where there may be two opinions, cannot be said to be mistake or error apparent from the record. A mistake arising as a result of subsequent interpretation of law by the Supreme Court would also constitute error apparent from the record. Retrospective amendment of law could also lead to rectification if an order is plainly and obviously inconsistent with the specific and clear provision, as amended retrospectively.

Where any matter has been considered and decided in any proceeding by way of appeal or revision relating to a rectifiable order the authority passing such order may, amend the order in relation to any matter other than the matter which has been so considered and decided.

The concerned authority may make an amendment of its own motion.

However he should mandatorily make the amendment for rectifying any such mistake which has been brought to its notice by the assessee. Where the authority concerned is the Deputy Commissioner (Appeals) or the Commissioner (appeals) the mistake can be printed out by the Assessing Officer also.

An amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee, shall not be made unless the authority concerned has given notice to the assessee of its intention so to do and has allowed the

assessee a reasonable opportunity of being heard.

Where an amendment is made under this section, an order shall be passed in writing by the authority concerned. Where any such amendment has the effect of reducing the assessment, the Assessing Officer shall make any refund due to assessee. However, this is subject to the provisions of section 241 under which the Assessing Officer has to power to withhold the refund in certain cases. Where any such amendment has the effect of enhancing the assessment or reducing the refund already made, the Assessing Officer shall serve the assessee with a notice of demand in the prescribed form specifying the sum payable. Except in cases which are specifically covered by section 155 or section 186(4) dealing with cancellation or registration no amendment under this section shall be made after the expiry of four years from the date of the order sought to be amended.

It is further provided that with effect from 1st June, 2001, where an application for amendment is made by the assessee on or after 1st June, 2001, the income-tax authority shall pass an order within six months from the end of the month in which the order is received, either making the amendment or refusing the claim.

21.34 OTHER AMENDMENTS [SECTION 155]

Where any assessment made in respect of any assessment year is required to be amended on account of any specific provisions in the Act mentioned hereunder, such an amending order can be passed at any time within 4 years from the end of the year in which such provision is attracted.

1. Where a partner is assessed in respect of any remuneration from a firm under section 28(v) and later in the assessment of the firm, such remuneration is found not deductible under section 40(b), the assessment order of the partner shall be amended to exclude such remuneration which is not deductible in the firm's case. This is in view of the proviso to clause (v) of section 28 which states that the remuneration disallowed in the firm's case cannot be charged to tax in the partner's case [Sub-section (1A)].
2. The amendment of the assessment of a member of an association of persons (AOP) consequent upon the assessment or reassessment or any enhancement or reduction in the income of the AOP as a result of an order in appeal, reference, revision or rectification or as a result of an order made by the Settlement Commission [Sub-section (2)].
3. Amendments resulting from any proceedings initiated under section 147 on account of recomputation of total income, where excessive loss or depreciation allowance had been allowed or losses had been set off and carried forward under the different heads [Sub-section (4)].
4. Recomputation of the total income of the assessee consequent upon deduction allowed in excess of expenditure actually incurred on approved programme of scientific research (Such deduction originally allowed to him but consequently withdrawn on the ground that the prescribed conditions have not been complied with) [Sub-section (5B)].

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5. Under the provisions of section 47A, capital gains which were not charged to tax by virtue of section 47(iv) or (v) may be deemed to be chargeable in certain circumstances. The Assessing Officer may accordingly make an order of amendment at any time before the expiry of four years from the end of the previous year in which the relevant capital asset was converted into or treated as stock in trade or as the case may be the parent company ceasing to hold the entire share capital of the subsidiary company before 8 years from the date of transfer [Sub-section (7B)].

6. Sub-section (11A) provides that where in the assessment for any year, the deduction under section 10A or section 10B has not been allowed on the ground that such income -

- (1) has not been received in convertible foreign exchange in India, or
- (2) having been received in convertible foreign exchange outside India, or having been converted into convertible foreign exchange outside India, has not been brought into India, by or on behalf of the assessee with the approval of the Reserve Bank of India or such other approved authority and

subsequently such income or part thereof has been or is received in, or brought into, India in the manner aforesaid, the Assessing Officer shall amend the order of assessment so as to allow deduction under section 10A or section 10B, as the case may be, in respect of such income or part thereof as is so received in, or brought into, India.

7. Under section 155(13), the Assessing Officer has power to rectify an assessment order to allow deduction under sections 80HBB, 80HHC, 80HHD, 80HHE, 80R, 80-O etc. (which was earlier denied on the ground that such income had not been received in convertible foreign exchange in India), when such income is subsequently received or brought into India with the approval of the competent authority.

8. Where TDS/TCS certificates are not furnished alongwith the return of income and such certificates are produced before the Assessing Officer within two years from the end of the Assessment year in which the income covered by the TDS/TCS certificate is assessable [Sub-section (14)].

However, such rectification under section 155(14) is possible only if the income from which tax has been deducted or the income on which tax has been collected has been disclosed in the return of income filed by the assessee for the relevant assessment year.

9. Where the assessing officer adopts stamp duty as full value of consideration under section 50C and later, such value is revised in any appeal or revision or reference [Sub-section (15)].

10. Where capital gains is recomputed on account of any reduction of any compensation in a compulsory acquisition by any Court, Tribunal, or any other authority, the Assessing Officer shall revise the assessment [Sub-section (16)].

11. Where deduction under section 80RRB is allowed and subsequent to the allowance of such deduction in respect of any patent, the Controller or the High Court passes an

order under the Patents Act, 1970 revoking the patent or excluding the name of the assessee from the Patents Register as patentee in respect of that patent [Sub-section (17)].

Note – For the purpose of amending the order under any of the sub-sections (1A), (7B) or (16) or (17) of section 155, the time permissible is four years from the end of the year in which the event giving necessity to such amendment occurs.

21.35 NOTICE OF DEMAND [SECTION 156]

When any tax, interest, penalty or fine or any other sum is payable consequent to any order passed under this Act, the Assessing Officer shall serve upon the assessee a notice of demand in the prescribed form, specifying the sum so payable.

The Apex Court in *Sri Mohan Wahi v. CIT*, 248 ITR 799 has held that failure to serve notice of demand renders the recovery proceedings invalid.

An intimation under section 143(1) would be deemed to be a notice of demand for the purpose of section 156, where any sum is determined to be payable by the assessee under section 143(1).

21.36 INTIMATION OF LOSS [SECTION 157]

When, in the course of the assessment of total income of any assessee, it is established that a loss has taken place which the assessee is entitled to have carried forward and set-off under the provisions of section 72(1) or 73(2) or 74(1) or 74(3) or 74A(3), the Assessing Officer shall notify the assessee by an order in writing the amount of the loss as computed by him for this purpose.

Self-examination questions

1. Filing of return of income on or before due date is necessary for carry forward of all losses - Discuss the correctness of this statement.
2. Who are the persons authorised to sign the return of income in the case of -
 - a) Hindu Undivided Family
 - b) Company
 - c) Partnership firm
3. What are the circumstances when a return of income can be treated as defective?
4. List ten transactions for which quoting of permanent account number is mandatory.
5. Write short notes on -
 - a) Regular assessment

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- b) Best judgement assessment
- 6. Write short notes on -
 - a) Valuation of inventory for tax purposes
 - b) Tax Return Preparers
- 7. Does the Assessing Officer have power to make a reference to the Valuation Officer? If so, under what circumstances can he exercise such power?
- 8. (i) Discuss the procedure for assessment in search cases under section 153A of the Income-tax Act, 1961?
(ii) What is the time limit for completion of such search assessments?
- 9. Is it necessary that the Assessing Officer should record his reasons in writing for exercising the power to reduce the period for making the payment specified in the notice of demand?
- 10. Anirudh filed return of income for A.Y. 2009-10 claiming a refund of Rs.37,500. The said refund was granted and paid to the assessee on 1st March, 2010 after processing the return under section 143(1). Later on, the case was taken up for regular assessment by issue of notice under section 143(2) and the said assessment was completed on 7th September, 2010 resulting in demand of Rs.6,300. Is the assessee liable to pay interest on the amount of refund already granted to him and if so, what is the amount of such interest?
- 11. Rallis Ltd. filed its original return for the previous year 2007-08 on 30th October, 2008 declaring loss of Rs.16.25 lakhs. Thereafter, it filed a revised return on 28th February, 2010 declaring loss of Rs.19.3 lakhs. The assessment of Rallis Ltd. was not completed at that point of time. The Assessing Officer opined that the loss indicated in the original return alone can be carried forward for set-off in the subsequent years, since section 80 does not contemplate that a revised return can be filed. Is the contention of the Assessing Officer correct? Discuss.
- 12. Can intimation under section 143(1)(a) be issued after notice for regular assessment is issued under section 143(2)?

Answers

- 9. The Delhi High Court, in *Agricultural Produce Marketing Committee v. Union of India* (2006) 155 Taxman 186, observed that the legal position regarding the competence of the Assessing Officer to reduce the period for payment of the outstanding dues is clearly stated in section 220. A plain reading of the proviso to section 220(1) makes it clear that while the assessing authority has the power to reduce the period for making the payment specified in the notice of demand under section 156, such reduction must be supported by valid reasons to be recorded in writing. Therefore,

whenever the competent authority invokes its powers of reducing the period stipulated under section 220, it must take care not only to pass a proper order but also to support the same by cogent reasons.

In this case, the High Court has built in the principles of natural justice into the provisions of section 220(1), by interpreting that the “reason to believe” as required by the proviso to section 220(1), implies that such reasons should be cogent and should be recorded in writing.

10. As per section 234D, where any refund is granted to the assessee after processing the return u/s 143(1) and later on, in the regular assessment there is no refund due or the amount refunded exceeds the amount refundable, the assessee shall be liable to pay simple interest at $\frac{1}{2}\%$ for every month or part of a month from the date of grant of refund to the date of such regular assessment on the whole or the excess amount so refunded.

The assessee was granted refund on 1.3.2010 after processing the return u/s 143(1). The regular assessment u/s 143(3) was completed on 7.9.2010 and resulted in tax payable of Rs.6,300. Therefore, no refund was due on regular assessment. Accordingly, the assessee is liable to pay interest u/s. 234D on Rs.37,500 at $\frac{1}{2}\%$ for 7 months (i.e. from 1st March, 2009 to 7th September 2010; part of a month is to be considered as full month).

Interest payable by the assessee u/s 234D works out to Rs.1,313 (i.e. $\text{Rs.37,500} \times \frac{1}{2}\% \times 7 \text{ months}$).

11. Rallis Ltd. had filed its original return under section 139(3) before the time allowed under section 139(1) i.e. before 31st October, 2008. It has also filed its revised return within the time allowed under section 139(5) i.e. before the expiry of one year from the end of the relevant assessment year or before completion of assessment, whichever is earlier. In this case, the assessment was yet to be completed and one year from the end of the relevant assessment year expires on 31.3.2010. Since Rallis Ltd. has filed its revised return on 28.2.2010, it was within the time allowed under section 139(5).

A perusal of section 139(3) makes it clear that a return of loss filed under section 139(3) may be filed within the time allowed under section 139(1). Once such a return is filed, all the provisions of the Act shall apply as if such return has been filed under section 139(1). In other words, a return filed under section 139(3) is deemed to be a return filed under section 139(1). The provision contained in section 139(3) makes it clear that all the provisions of the Act shall apply to such a return as if it were a return under section 139(1). In view of such a specific provision, there is no further necessity in section 80 to refer to such provision. Hence, there is no reason to exclude the applicability of section 139(5) to a return filed under section 139(3).

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Therefore, a loss return filed under section 139(3) can be revised by filing a revised return under section 139(5) within the time allowed. Such loss as per the revised return can be carried forward, even though section 80 does not specifically provide for carry-forward of loss which has been determined in pursuance of return filed under section 139(5).

This principle has been supported by the Madras High Court in *CIT v. Periyar District Co-op. Milk Producers Union Ltd.* (2004) 137 Taxman 364 (Mad.)

The contention of the Assessing Officer is, therefore, incorrect.

12. The Apex Court, in *CIT v. Gujarat Electricity Board* (2003) 260 ITR 0084, opined that once regular assessment proceedings have commenced under section 143(2) of the Income-tax Act, 1961, it is a limitation on the jurisdiction of the Assessing Officer to commence proceedings under section 143(1)(a) of the Act. Section 143(1)(a) of the Act enacts a summary procedure for quick collection of tax and quick refunds. Under the scheme, if there is a serious objection to any of the orders made by the Assessing Officer determining the income, it is open to the assessee to ask for rectification under section 154. It is not open to the Revenue to issue intimation under section 143(1)(a) of the Income-tax Act, 1961, after notice for regular assessment is issued under section 143(2). The Legislature intended that where the summary procedure under section 143(1) has been adopted, there should be scope available for the Revenue, either *suo moto* or at the instance of the assessee, to make a regular assessment under section 143(2). The converse is not available : a regular assessment proceeding having been commenced under section 143(2), there is no need for a summary proceeding under section 143(1)(a).

SETTLEMENT OF TAX CASES

22.1 SETTLEMENT COMMISSION

Introduction : The Wanchoo Committee felt that in the administration of fiscal laws, where the primary objective is to raise revenue, there has to be room for compromise and settlement. A rigid attitude would not only inhibit a one-time tax evader or an unintending defaulter from making a clean breast of his affairs but would also unnecessarily strain the investigational resources of the Department in cases of doubtful benefit to revenue, while needlessly proliferating litigation and holding up collections. Even in the United Kingdom, the 'confession' method has been in vogue since 1923. In the U.S. Law also, there is a provision for compromise with the tax payer as to his tax liabilities. A provision of this type facilitating settlement in individual cases will have this advantage over general disclosure schemes. Hence the Committee recommended the setting up of a high level settlement machinery. Accordingly, Chapter XIXA incorporating the recommendations of the Wanchoo Committee was enacted by Taxation Laws (Amendment) Act, 1975 with effect from April 1, 1976. The provisions relating to settlement commission are discussed below.

1. The Central Government has constituted a Settlement Commission. It shall consist of a Chairman and as many Vice-Chairmen and other members as the Central Government thinks fit. Where a member of the Central Board of Direct Taxes is appointed as the chairman or a member of the commission, he ceases to be a member of the Board.
2. The Chairman, Vice-Chairman and other members of the Settlement Commission are to be appointed by the Central Government from amongst persons of integrity and outstanding ability, having special knowledge of, and experience in, problems relating to direct taxes and business accounts.
3. The Commission functions within the Department of Revenue and Banking of the Central Government.

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22.2 DEFINITION OF 'CASE' [SECTION 245A(b)]

For the purpose of settlement of cases, the term 'case' has been defined to mean any proceeding for assessment under the Income-tax Act 1961, of any person in respect of any assessment year or years which may be pending before an Assessing Officer on the date on which an application under section 245C(1) is made.

Henceforth, application cannot be made to the Settlement Commission where -

- notice for assessment/reassessment/recomputation under section 147 has been issued under section 148.
- search has been initiated under section 132 or requisition has been made under section 132A followed by assessments under section 153A(b)/153B(1)(b).
- fresh assessment has been directed on account of the original assessment being set aside by the Commissioner(Appeals)/Appellate Tribunal under sections 263/264/254.

Therefore, no such proceedings, except original assessment proceedings, should be pending at the time of making an application to the Settlement Commission.

22.3 APPLICATION FOR SETTLEMENT OF CASES [SECTION 245C]

1. An assessee may, at any stage of a case relating to him, make an application in the prescribed form and manner, containing a full and true disclosure of his income which has not been disclosed before the Assessing Officer [Sub-section (1)].
2. He should also disclose the following to the Settlement Commission for settlement of his case –
 - (i) the manner in which such income has been derived,
 - (ii) the additional amount of income-tax payable on such income and
 - (iii) other particulars as may be prescribed [Sub-section (1)].
3. Further, the additional amount of income-tax offered should exceed Rs.3 lakh and the additional tax offered and interest thereon should be paid before filing the application and proof of payment should be attached with the application [Proviso to sub-section (1)].
4. The additional amount of income-tax has to be calculated in the following manner as provided in the sub-section (1B) read with the sub-section (1C), in a case where the income disclosed in the application relates to only one previous year–

(i)	If the applicant has not furnished a return in respect of the total income of that year.	Tax should be calculated on the income disclosed in the application as if such income is the total income. Such tax represents the additional amount of income-tax.
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(ii)	If the applicant has furnished a return in respect of the total income of that year.	The tax should be calculated on the aggregate of total income returned and the income disclosed in the application i.e. as if the aggregate represents the total income. The additional amount of income-tax is the amount calculated on such aggregate as reduced by the amount of tax calculated on the total income returned for that year.
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5. Where the income disclosed in the application relates to more than one previous year, then the above procedure is to be adopted in respect of each previous year and the aggregate of tax payable is to be calculated [Sub-section (1D)].

6. Every settlement application made under sub-section (1) should be accompanied by the prescribed fees of Rs.500 [Sub-section (2)].

7. The settlement application made under sub-section (1) cannot be withdrawn by the applicant [Sub-section (3)].

8. The assessee should also intimate to the Assessing Officer in the prescribed manner that he has made an application to the Settlement Commission. Such intimation should be made on the same date when he makes an application to the Settlement Commission [Sub-section (4)].

22.4 PROCEDURE ON RECEIPT OF APPLICATION [SECTION 245D]

(1) Admission of Petition [Sub-section (1)]

(i) On receipt of the settlement application, the Settlement Commission shall issue a notice to the applicant within 7 days from the date of receipt of application.

(ii) After hearing the applicant, the Settlement Commission shall pass an order either rejecting or allowing the application to be proceeded with within 14 days from the date of application.

(iii) Application not disposed off within 14 days shall be treated as admitted.

(2) Copy of every order under section 245D(1) has to be sent to the applicant and to the Commissioner [Sub-section (2)].

(3) Deemed date of admission/disposal of Settlement applications made before 1.6.2007 [Sub-section (2A)]

(i) Settlement applications made prior to 1.6.2007, if not disposed off by 31st May, 2007, shall be deemed to be admitted, if the additional tax on the income disclosed in such application and the interest thereon is paid on or before 31.7.2007.

(ii) 31.7.07 shall also be deemed to be the date of the order of rejection or admission for such applications.

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(4) Time limit for furnishing report by Commissioner and passing order by the Settlement Commission [Sub-sections (2B) & (2C)]

- (i) The Settlement Commission shall call for a report from the Commissioner within the time limit specified below –

(i)	In respect of an application admitted under section 245D(1)	Within 30 days from the date of application
(ii)	In respect of an application deemed to have been admitted under section 245D(2A)	On or before 7.8.2007

- (ii) The Commissioner is required to furnish the report within 30 days from the receipt of communication from the Settlement Commission.
- (iii) The Settlement Commission can also pass an order declaring the application as invalid on the basis of the report of the Commissioner.
- (iv) Such order should be passed in writing within 15 days of the receipt of report after giving the applicant an opportunity of being heard.
- (v) A copy of the order should be sent to the applicant and the Commissioner.
- (vi) However, in a case where the Commissioner has not furnished the report within the prescribed time, the Settlement Commission shall proceed further in the matter without the report of the Commissioner.

(5) Status of pending settlement applications as on 1st June 2007, which are already admitted under the old provisions [Sub-section (2D)]

All settlement applications which are admitted under the existing provisions of section 245D(1), but for which an order under section 245D(4) is not passed before 1.6.2007, will not be allowed to be proceeded with further unless the applicant pays the additional tax and interest thereon on or before 31.7.2007.

(6) Proceedings after admission [Sub-section (3)]

- (i) The Settlement Commission may call for records from the Commissioner in respect of an application which has not been declared invalid under sub-section (2C) or an application which has been allowed to be further proceeded with under sub-section (2D).
- (ii) After examination of such records, the Settlement Commission may require the Commissioner to make further enquiry or investigation and furnish a report on the matters covered by the application and any other matter relating to the case.
- (iii) The Commissioner shall furnish the report within a period of 90 days of the receipt of communication from the Settlement Commission.

- (iv) If the Commissioner fails to furnish the report within the said period of 90 days, the Settlement Commission may proceed to pass an order under sub-section (4) without such report.

(7) Final order of settlement [Sub-sections (4) and (4A)]

- (i) The Settlement Commission may pass such order as it thinks fit on the matters covered by the application and any other matter relating to the case not covered by the application but referred to in the report of the Commissioner.
- (ii) Such order should be passed by the Settlement Commission after –
- (1) examining the records and report of the Commissioner, if any, received at the time of admission or on investigation or enquiry conducted as per the instructions of the Settlement Commission;
 - (2) giving an opportunity of being heard to the applicant and the Commissioner;
 - (3) examining such further evidence as may be placed before it or obtained by it.
- (iii) The time limit for passing such order is –

(1)	In respect of an application made on or after 1.6.2007	Within 12 months from the end of the month in which the application was made.
(2)	In respect of an application filed before 1.6.2007 [under sub-section (2A) or (2D)]	On or before 31.3.2008

- (8) Before passing any order and subject to the provisions dealing with the jurisdiction of Settlement Commission, the various materials brought on record before the Settlement Commission must be considered by the members of the concerned Bench and in cases where there is any difference of opinion among the members, the opinion of the majority shall prevail and the order of the Settlement Commission must also be expressed in terms of the views of the majority [Sub-section (5)].

- (9) All the orders passed by the Settlement Commission under section 245D(4) must provide for the terms of the settlement including any demand by way of tax, penalty, the manner in which any amount due as a result of the settlement should be paid and all other matters which are essential to make the settlement of the case effective [Sub-section (6)].

- (10) The order should also provide that the settlement shall be void if it is subsequently found by the Settlement Commission that the settlement order was obtained by fraud or any misrepresentation of facts by the applicant. In cases where the settlement becomes void, the proceeding, in respect of which the settlement order was passed, must be deemed to have been revived from the stage at which the application was allowed to be proceeded with by the Settlement Commission and the Income-tax authority concerned may complete the proceedings for assessment or re-assessment of income or the levy of

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penalty, fine, etc., at any time before the completion of two years from the end of the financial year in which the settlement becomes void [Sub-sections (6) & (7)].

(11) Where the tax payable in pursuance of an order passed by the Settlement Commission is not paid by the assessee within 35 days of receipt of a copy of final order, the assessee shall be liable to pay simple interest @ 1¼% for every month or part of a month on the outstanding amount from the date of expiry of 35 days. Such liability will arise even in cases where the Commission extended the time allowed for such payment or permitted payment by installment [Sub-section (6A)].

(12) The time limit for completion of assessments and re-assessments contained in section 153 shall have no application to any order passed by the Settlement Commission or to any order of assessment or re-assessment or recomputation required to be made by the Assessing Officer in pursuance of any directions contained in an order passed by the Settlement Commission [Sub-section (8)].

22.5 POWER OF SETTLEMENT COMMISSION TO ORDER PROVISIONAL ATTACHMENT TO PROTECT REVENUE [SECTION 245DD]

(i) Under section 245DD, the Settlement Commission is empowered to provisionally attach the property belonging to the applicant for protecting the interest of the revenue. The manner in which such provisional attachment is to be effected is provided in the Second Schedule. Such provisional attachment is valid for a period of 6 months, after which it ceases to have effect.

(ii) The Settlement Commission may, for reasons to be recorded in writing, extend the aforesaid period by such further period or period as it thinks fit.

22.6 RE-OPENING OF COMPLETED PROCEEDINGS [SECTION 245E]

If the Settlement Commission is of the opinion that for the proper disposal of the case pending before it, it is necessary or expedient to reopen any proceeding connected with the case, but which has been completed under Income-tax Act, 1961 by any Income-tax authority before the application of the assessee under Section 245C was made, it may, with the concurrence of the applicant, reopen such proceedings and pass such orders thereon as it deems fit as if the case in relation to which the application for the settlement had been made by the applicant covered by the proceedings for reopening of assessments as well. Before initiating the proceedings for reopening of assessment in any case, the reasons for arriving at the opinion for such reopening of the assessment must be recorded by the Settlement Commission. However no proceeding shall be reopened by the Settlement Commission under this section if the period between the end of the assessment year to which such a proceeding relates and the date of application for settlement exceeds nine years.

However, the Settlement Commission shall not have any power to reopen the proceedings in respect of an application made on or after 1.6.2007.

22.7 JURISDICTION AND POWERS OF THE SETTLEMENT COMMISSION

- (a) The jurisdiction, powers and authority of the Settlement Commission may be exercised by benches thereof.
- (b) A bench shall be presided over by the Chairman or a Vice-chairman and shall consist of two other members.
- (c) The bench for which the Chairman is the presiding officer shall be the principal bench and the other benches shall be known as additional benches.
- (d) The Chairman may authorise the Vice-chairman or other Member appointed to one bench to discharge also the functions of the Vice-chairman or other member of another bench.
- (e) Where the presiding officer or other member of a bench is unable to discharge his functions owing to absence, illness or any other cause or where a vacancy occurs in the office of the presiding officer or a member the remaining two persons may function as the bench and if the presiding officer is not one of the members, the senior member will be the presiding officer. However, if it is felt that the case is such that it should be heard by a bench of three members the chairman has powers to transfer the case to such a bench. The chairman for the disposal of a particular case, institute a Special Bench consisting of more than three members.
- (f) The places at which the Principal Bench and the Additional Benches shall ordinarily sit shall be notified by the Central Government. The Central Government has specified that New Delhi is the place where the Principal Bench and Bombay, Calcutta and Madras as the places where Additional Benches of the Settlement Commission shall ordinarily sit.
- (g) The Vice-chairman has been empowered to act as chairman and discharge his functions under certain circumstances as vacancy, death, resignation etc.
- (h) On the application of the assessee or the Commissioner and after notice to them and hearing, the chairman may transfer any case pending before one bench, for disposal, to another bench.
- (i) If the members of a bench differ in opinion on any point the point shall be decided according to the opinion of the majority. If they are equally divided they shall state the point on which they differ and make a reference to the chairman who shall either hear the point himself or refer the point to one or more of the other members and such point shall be decided according to the opinion of the majority of the members who have heard the case including those who first heard it.

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- (j) The Settlement Commission has been vested with all the powers which are vested in an Income-tax authority under the Income-tax Act.
- (k) Accordingly, in cases where an application made by the assessee under section 245C has been allowed by the Settlement Commission to be proceeded with under section 245D, the Settlement Commission is empowered to exercise exclusively the jurisdiction and powers and perform the functions allotted to an Income-tax authority under the Income-tax Act until an order for settlement of the case is passed.
- (l) In respect of an application made under section 245C on or after 1.6.2007, such exclusive jurisdiction would begin with the date of filing of application with the Settlement Commission.
- (m) The exclusive jurisdiction of the Settlement Commission would end on –
 - (a) the date of passing an order under section 245D(4); or
 - (b) the date of passing the order rejecting the application (made on or after 1.6.2007) under section 245D(1); or
 - (c) the date on which the application is not allowed to be proceeded with under section 245D(2A); or
 - (d) the date on which the application is declared invalid under section 245D(2C); or
 - (e) the date on which the application is not allowed to be further proceeded with under section 245D(2D).
- (n) However, in the absence of any express direction to the contrary by the Settlement Commission, the operation of any other provision of the Income-tax Act requiring the applicant to pay the tax on the basis of self-assessment shall continue to be applicable in relation to matters which are before the Settlement Commission for consideration. Further in the absence of any express directions by the Settlement Commission to the contrary, the provisions of sections 245A to 245L would not affect the operation of any other provision of the Income-tax Act insofar as those provisions relate to any matters other than those covered by the case before the Settlement Commission.
- (o) The Commission shall subject to the provisions of this Chapter have power to regulate its own procedure and the procedure of benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions including the places at which the Board shall hold their sittings.
- (p) **Inspection of reports:** According to section 245G, no person is entitled to inspect or obtain copies of any reports made by any Income-tax authority to the Settlement Commission in relation to the case, but, the Settlement Commission may, in its discretion, furnish copies thereof to any person or receipt of an application made to it in this behalf and on payment of the prescribed fee. However, in order to enable any

person whose case is under consideration to rebut any evidence which has been brought on record against him in any such report, the Settlement Commission shall, on receipt of an application in this behalf and on payment of the prescribed fee, furnish to the applicant, a certified copy of any such report or particular thereof which may be relevant for the purpose.

22.8 POWER TO GRANT IMMUNITY FROM PROSECUTION AND PENALTY [SECTION 245H]

- (i) The Settlement Commission may, if it is satisfied that any person who made the application for settlement under Section 245C has co-operated with the Settlement Commission in the conduct of the proceedings before it and has made a true disclosure of his income, and the manner in which such income has been derived, grant to such person immunity from prosecution for any offence under the Income-tax Act or under the Indian Penal Code or under any other Central Act which is for the time being in force.
- (ii) Such an immunity may also be granted in the matter of imposition of any penalty under the Income-tax Act in respect of the case which is covered by the settlement.
- (iii) The Commission can grant partial immunity from imposition of penalty to the applicant.
- (iv) The power of the Settlement Commission to grant immunity from prosecution and the imposition is, however, subject to such conditions as the commission may think fit to impose in the circumstances of the case.
- (v) No such immunity shall be granted by the commission in cases where the proceedings for the prosecution for any such offence have been instituted before the date of receipt of the application for settlement.
- (vi) Under section 245H, the Settlement Commission may grant immunity from prosecution for any offence under the Indian Penal Code, Income-tax Act and any other Central Act. This power has now been restricted in respect of application made under section 245C on or after 1.6.2007. In respect of such cases, the Settlement Commission shall not grant immunity from prosecution for any offence under the Indian Penal Code or under any Central Act other than the Income-tax Act and Wealth-tax Act. However, in respect of applications pending as on 1.6.2007, the Settlement Commission has the power to grant immunity from prosecution for any offence under the Indian Penal Code and other Central Acts also.
- (vii) An immunity granted under this section shall stand withdrawn if such person fails to pay any sum specified in the order of settlement within the time specified in the order or within such further time as may be allowed by the commission or fails to comply with any other condition subject to which the immunity was granted and thereupon the provisions of this Act shall apply as if such immunity had not been granted.

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- (viii) An immunity granted by the Settlement Commission to any person may, at any time, be withdrawn by it in cases where it is satisfied that the person concerned had, in the course of the settlement proceedings concerned may be tried for the offence with respect to which the immunity was granted or for any other offence in respect of which he has been found guilty in connection with the settlement.
- (ix) After the withdrawal of the immunity from prosecution, the person concerned may also become liable to the imposition of the penalty under the Income-tax Act to which he would otherwise have been liable in the absence of the immunity given to him under section 245H.

22.9 ABATEMENT22.9 ABATEMENT OF PROCEEDING BEFORE THE SETTLEMENT COMMISSION [SECTIONS 245HA & 245HAA]

- (i) In the following cases, the proceedings before the Settlement Commission shall abate on the specified date as given below –

Case	Specified date
(1) where an application made to the Settlement Commission on or after 1.6.2007 has been rejected under section 245D(1).	The date on which the application was rejected.
(2) where any application is not allowed to be proceeded with under section 245D(2A) or further proceeded with under section 245D(2D).	31.7.2007
(3) where an application has been declared invalid under section 245D(2C).	The last day of the month in which the application was declared invalid.
(4) Where an order under section 245D(4) has not been passed within the time allowed under section 245D(4A).	The date on which the time or period specified in section 245D(4A) expires.

- (ii) On abatement of proceedings, the case would revert back to the Assessing Officer having jurisdiction or any other income-tax authority before whom the proceedings were pending at the time of making the application. Such income-tax authority shall dispose of the case in accordance with the provisions of the Act.

- (iii) For completing the proceedings, the Assessing Officer or other Income-tax authority shall be entitled to use the material and information produced by the assessee before the Settlement Commission as if such material and information had been produced before the Assessing Officer or other income-tax authority. Similarly, the Assessing Officer or other Income-tax authority shall be entitled to use the results of the inquiry held or evidence recorded by the Settlement Commission in the course of the proceedings before it, as if

such inquiry or evidence had been held or recorded by him in the course of the proceedings before him.

(iv) The period from the date on which the application was made before the Commission up to the date on which proceedings get abated shall be excluded from the time limit for completion of proceedings by the Assessing Officer and for payment of interest under section 243, 244 or 244A.

(v) In case of abatement of settlement proceedings, the Assessing Officer is required to give credit for the tax and interest paid on or before the date of making the application or during the pendency of the case before the Settlement Commission. This has been provided by insertion of section 245HAA.

22.10 ORDER OF SETTLEMENT COMMISSION TO BE CONCLUSIVE [SECTION 245-I]

Section 245-I provides that every order of the Settlement Commission passed under section 245D(4) shall be conclusive in respect of the matters contained therein and consequently no matter covered by the settlement order shall be liable to be reopened in any proceeding under the Income-tax Act or under any other law for the time being in force except, however, in those cases wherein the reopening of the case is specifically provided under section 245D(7).

22.11 RECOVERY OF SETTLED AMOUNT [SECTION 245J]

According to section 245J, any amount specified in an order of settlement passed by the Settlement Commission under section 245D(4), may be recovered and any penalty for default in making the payment may be imposed and recovered from the person concerned in accordance with the provisions of the Income-tax Act. The power for making the recovery if any, as may be specified by the Settlement Commission in the order passed by it. The right of recovery may be exercised by the Assessing Officer having jurisdiction over the person who has made the application for settlement under section 245C.

22.12 BAR ON SUBSEQUENT APPLICATION FOR SETTLEMENT [SECTION 245K]

- (i) In the event of occurrence of any of the following, the person concerned shall not be entitled to apply for settlement in relation to any other matter –
- (1) the order of settlement passed under section 245D(4) provides for imposition of penalty for concealment of income; or
 - (2) after the passing of order under section 245D(4) in relation to a case, the person is convicted of an offence under Chapter XXII in relation to that case; or
 - (3) the case of such person was sent back to the Assessing Officer by the Settlement Commission on or before 1.6.2002.

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- (ii) Further, with effect from 1.6.2007, the option of going to the Settlement Commission would be available only once in the lifetime of a person. Therefore, where an application for settlement is made on or after 1.6.2007 and such application has been allowed to be proceeded with, then such person will not be subsequently entitled to make any application under section 245C.

22.13 PROCEEDINGS TO BE JUDICIAL PROCEEDINGS [SECTION 245L]

All the proceedings under the Income-tax Act before the Settlement Commission shall be deemed to be judicial proceedings within the meaning of sections 193, 196 and 228 of the Indian Penal Code.

22.14 ORDER TO BE CONCLUSIVE

Every order of settlement passed by the commission shall be conclusive as to the matter stated therein. No matter covered by such order shall be reopened in any proceeding under this Act or under any other law for the time being in force. The only exception is the power given to commission itself to reopen the completed proceedings.

However the Supreme Court has held in *CIT vs. B.N. Bhattacharjee (1979) 118 ITR 461* that Article 136 of the Constitution was wide enough to bring within the Supreme Court's jurisdiction orders passed by the Settlement Commission.

Self-examination questions

1. Define the term "Case" for the purpose of settlement of cases.
2. Discuss the jurisdiction and powers of the Settlement Commission.
3. What is the binding nature of the orders of the Settlement Commission?
4. Pursuant to a search conducted in the premises of Mr. Sriram, certain seizures were made. Mr. Sriram filed an application for settlement in terms of section 245C claiming to have received the amount by way of loan from several persons. The Settlement Commission accepted his statement and made an order under section 245D(4). The CBI, however, conducted enquiry at the request of the Revenue regarding the loans and opined that the alleged lenders had no means or financial capacity to advance such huge loans to the assessee and were mere name lenders. The Commissioner filed an application under section 245D(6) praying for the order to be declared void and for withdrawal of benefit granted. Mr. Sriram, however, contended that the order of the Settlement Commission was final in terms of section 245-I and any fresh analysis would amount to sitting in judgement over an earlier decision, for which the Settlement Commission was not empowered. Discuss the correctness of Mr. Sriram's contention.
5. The Settlement Commission had passed an order under section 245D(4) waiving and/or reducing interest levied on the assessee under sections 234A, 234B and 234C

in accordance with the state of law at the relevant point of time. Thereafter, the Settlement Commission, after a period of less than four years served notice upon the assessee stating that in view of the decision of the Supreme Court in the case of *CIT v. Anjum M.H. Ghaswala (2001) 252 ITR 1*, the aforesaid order required rectification. After considering the reply of the assessee, the Settlement Commission passed an order under section 154 withdrawing the reduction/waiver of interest granted by it earlier. Discuss the following with reference to the facts of the case stated above -

- (a) Is the Settlement Commission vested with the powers of an Income-tax Authority to give effect to the judgment of the Supreme Court?
- (b) Is the scope and ambit of section 245F wide enough to enable the Settlement Commission to rectify an order passed by it under section 245D(4)?

Answers

4. The Apex Court, in *CIT v. Om Prakash Mittal (2005) 143 Taxman 373 / 273 ITR 0326*, observed that a bare reading of section 245D(6) shows that every order passed under sub-section (4) has to provide for the following –

- (i) the terms of settlement and
- (ii) that the settlement would become void if it is subsequently found by the Settlement Commission that it has been obtained by fraud or misrepresentation.

The decision whether the order has been obtained by fraud or misrepresentation is that of the Settlement Commission. However, there is no requirement that the Settlement Commission must *suo motu* initiate the action. The Revenue can move the Settlement Commission for decision on an issue if it has material to show that the order was obtained by fraud or misrepresentation of facts.

The Supreme Court observed that the foundation for settlement is an application which an assessee can file at any stage of a case relating to him in such form and manner as may be prescribed. The fundamental requirement of the application under section 245C is that there must be full and true disclosure of the income along with the manner in which it has been derived. If an order is obtained by fraud or misrepresentation of facts, it cannot be said that there is a full and true disclosure. This is why the Legislature has prescribed the condition relating to declaration of the order void when it is obtained by fraud or misrepresentation of facts.

The Supreme Court held that merely because section 245-I provides that the order of settlement is conclusive, it does not take away the power of the Settlement Commission to decide whether the settlement order has been obtained by fraud or misrepresentation of facts. If the Commissioner is able to establish that the earlier decision was void because of misrepresentation of facts, then it is open for the Settlement Commission to decide the issue. It cannot be called by any stretch of imagination to be a review of the earlier judgment or the subsequent Bench sitting in appeal over the earlier Bench's decision.

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Mr. Sriram's contention is, therefore, not correct.

5. The above questions have been answered by the Gujarat High Court in *Sanjaybhai R. Patel v. Assessing Officer* (2004) 135 *Taxman* 210. In this case, the Gujarat High Court observed that section 245F(1) vests the Settlement Commission with all the powers which are vested in an income-tax authority under the Act, in addition to the powers that the Commission has under Chapter XIX-A.

Section 154 contemplates that the powers of rectification thereunder can be exercised only with a view to rectify a mistake apparent from record and that the said powers can be exercised by an income-tax authority referred to in section 116. Section 154(7) prescribes the time-limit for exercise of such powers and it says that no amendment under this section shall be made after the expiry of 4 years from the end of the financial year in which the order sought to be amended was passed.

In the instant case, the Settlement Commission had waived or reduced the interest under sections 234A, 234B and 234C despite the fact that it had no such power under the Act and it was contrary to the law laid down by the Supreme Court. The High Court took into consideration the decision in *Standard Radiators v. CIT* (1987)165 *ITR* 178 (Guj.) and held that in the instant case, the Settlement Commission had committed an error apparent on the face of the record in reducing/waiving the interest chargeable under sections 234A, 234B and 234C. As far as the issue as to whether the Settlement Commission is an income-tax authority or not is concerned, section 245F(1) specifically states that the Settlement Commission has got all the powers of the income-tax authority, over and above the powers under Chapter XIX-A.

The Settlement Commission cannot issue circulars for which the issuing powers are vested with the CBDT under section 119, but it is certainly an Income-tax authority to confer the benefit available to the assessee under the circular and for this purpose, section 245F can be pressed into service. If such powers are exercised by the Settlement Commission within 4 years from the date of original order passed under section 245D, the same is in accordance with the provisions contained in section 154. Therefore, there was no infirmity in the order passed by the Settlement Commission while exercising the powers under section 154 for the purpose of rectifying the mistake committed by it in the original order under section 245D, which was a mistake apparent from record.

23.1 INTRODUCTION

Chapter XIX-B, consisting of sections 245N to 245V provides a scheme for giving advance rulings in respect of transactions involving non-residents and specified residents with a view to avoiding needless litigation and promoting better tax-payer relations.

23.2 DEFINITIONS

23.2.1 Advance Ruling [Section 245N(a)]: This term means

- (a) a determination by the Authority in relation to a transaction which has been undertaken or is proposed to be undertaken by a non resident applicant and such determination shall include the determination of any question of law or of fact specified in the application; or
- (b) a determination by the Authority in relation to the tax liability of a non-resident arising out of a transaction which has been undertaken or is proposed to be undertaken by a resident applicant with such non-resident.

However, advance rulings pronounced before 14.5.03, being the date on which the Finance Bill, 2003, received the assent of the President, in respect of an application by a resident applicant shall be binding on persons specified in section 245S.

- (c) a determination or decision by the Authority in respect of an issue relating to computation of total income which is pending before any Income-tax Authority or the Appellate Tribunal and such determination or decision shall include the determination or decision on any question of law or fact in relation to such computation of total income specified in the application.

23.2.2 Applicant [Section 245N(b)]: 'Applicant' means any person who –

- (i) is a non-resident referred to in (a) above;
- (ii) is a resident referred to in (b) above;

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- (iii) is a resident falling within such class or category of persons as the Central Government may, by notification in the Official Gazette, specify in this behalf, and
- (iv) makes an application for advance ruling under section 245 Q.

In this connection the Central Government has notified the following class of persons as applicants for the purposes of this Chapter–

- (a) Public sector company as defined under section 2(36A) of the Income-tax Act;
- (b) a person seeking advance ruling in relation to the tax liability of a non-resident arising out of a transaction undertaken by him with a non-resident.

[Notification No.SO 473 (E) dated 21.6.1999]

First proviso to section 245R (2) prohibits an application in respect of the following :

- (i) any question pending before any Income-tax Authority, Appellate Tribunal or Court (except in case of a resident applicant mentioned in para 20.3.01 (a) above);
- (ii) any question that involves determination of fair market value of any property; and
- (iii) any question in relation to a transaction which is designed *prima facie* for the avoidance of income-tax (except in case of a resident applicant mentioned in para 20.3.1(a) above).

Restrictions on Appellate Authority : Section 245RR has been inserted providing that where a resident applicant has made an application to AAR and referred issues therein for decision of AAR, then, any Income-tax Authority or Tribunal should not take any decision in respect of such issues. In other words, a resident assessee cannot pursue both the remedies, i.e. an appeal or revision before Income-tax Authority/Appellate Authority as well as an application for Advance Ruling to AAR, in respect of an issue.

23.3 AUTHORITY FOR ADVANCE RULINGS [SECTION 245-O]

1. The Authority for Advance Rulings shall be constituted by the Central Government.
2. The Authority for Advance Rulings will consist of a Chairman, who will be a retired Judge of the Supreme Court and two other members thereon from the Indian Revenue Service and Indian Legal Service.
3. The headquarters of the authority will be in Delhi.
4. The Central Government shall provide the Authority with such officers and staff as may be necessary for the efficient exercise of the powers of the Authority under this Act.

23.4 VACANCIES, ETC., NOT TO INVALIDATE PROCEEDINGS [SECTION 245P]

No proceeding before, or pronouncement of advance ruling by, the Authority shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the Authority.

23.5 APPLICATION FOR ADVANCE RULING [SECTION 245Q]

Any non-resident desirous of obtaining an advance ruling may make an application in the form and manner to be prescribed by rules along with the payment of a fee of Rs. 2,500. Such an application may be withdrawn within 30 days from the date of application. Rule 44E prescribes Form No. 34C for application for obtaining advance ruling in quadruplicate.

23.6 PROCEDURE ON RECEIPT OF APPLICATION [SECTION 245R]

The Authority on receipt of an application will send a copy to the Commissioner concerned and wherever considered necessary, also call upon the Commissioner to furnish relevant records. Such records will be returned to the Commissioner as soon as possible.

The Authority may either allow or reject an application. However, the Authority shall not allow an application where the question raised in the application:

- (i) is already pending in the case of the applicant either before any income-tax authority, or Appellate Tribunal (except in case of a resident applicant falling within any such class or category of persons as the Central Government may notify in this behalf) or any court.
- (ii) involves the determination of the fair market value of any property;
- (iii) relates to a transaction or issue which is designed *prima facie* for avoidance of income-tax (except in case of a resident applicant falling within any such class or category of persons as the Central Government may notify in this behalf)

However, no application shall be rejected unless an opportunity has been given to the applicant. Further, where an application is rejected the reason for rejection shall be given in the order.

An applicant on request can appear either in person or can be represented through a duly authorised representative.

The authority will pronounce the advance ruling within 6 months from the receipt of application by the authority.

23.7 APPLICABILITY OF ADVANCE RULING [SECTION 245S]

The advance ruling shall be binding only on the applicant who has sought it and in respect of the specific transaction in relation to which advance ruling was sought. It will also be binding on the Commissioner and the Income-tax Authorities subordinate to the Commissioner who are having jurisdiction over the applicant.

The advance ruling will continue to remain in force unless there is a change either in law or in fact on the basis of which the advance ruling was pronounced.

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23.8 ADVANCE RULING TO BE VOID IN CERTAIN CIRCUMSTANCES [SECTION 245T]

Where an advance ruling has been obtained by the applicant by fraud or misrepresentation of facts, the Authority may, by order, declare such ruling to be void *ab initio*. The provisions of the Act shall apply (excluding the period beginning with the date of such advance ruling and ending with the date of order under this section) to the applicant as if such advance ruling had never been made. A copy of this order shall be sent to the applicant and the Commissioner.

23.9 POWERS OF THE AUTHORITY [SECTION 245U]

The authority will have all the powers of the Civil Court in respect of discovery and inspection, enforcing the attendance of any person, including any officer of a banking company and examining on oath, issuing commissions and compelling the production of books of accounts and other record. It will also have the power to regulate its own procedure in all matters arising out of exercise of its powers under the Act. The authority would be deemed to be a Civil Court for the purposes of section 195 of the Code of Criminal Procedure, 1973 and every proceeding before the authority shall be deemed to be a judicial proceeding under certain provisions of the Indian Penal Code.

23.10 PROCEDURE OF AUTHORITY [SECTION 245V]

The Authority shall, subject to the provisions of this Chapter, have power to regulate its own procedure in all matters arising out of the exercise of its powers under the Act.

Self-examination questions

1. Define the following terms under the Income-tax Act, 1961 -
 - (a) Advance Ruling
 - (b) Applicant
2. What is the eligibility for being appointed as members of the Authority for Advance Rulings?
3. What is the procedure to be followed by the Authority for Advance Rulings on receipt of an application under section 245Q?
4. What are the restrictions on the applicability of an advance ruling pronounced by the Authority?
5. When can an advance ruling pronounced by the Authority for Advance Rulings be declared void?
6. Can a person resident in India seek advance ruling from the Authority for Advance ruling?

APPEALS AND REVISION

The assessee is given a right of appeal by the Act where he feels aggrieved by the order of the assessing authority. But the assessee has no inherent right of appeal unless the statute specifically provides that a particular order is appealable. There are four stages of appeal under the Income-tax Act, as shown hereunder –

Assessment Order

First Appeal

Commissioner (Appeals)

Second Appeal

Appellate Tribunal

Third Appeal

High Court

Final Appeal

Supreme Court

24.1 APPEALABLE ORDERS BEFORE COMMISSIONER (APPEALS) [SECTION 246A]

24.1.1 An assessee aggrieved by any of the following orders may appeal to the Commissioner (Appeals) against such orders under section 246A -

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- (a) an order passed by a Joint Commissioner under section 115VP(3)(ii) or an order against the assessee where the assessee denies his liability to be assessed under this Act or an intimation under section 143(1)/(1B), where the assessee objects to the making of adjustments, or any order of assessment under section 143(3) (*except an order passed in pursuance of the directions of Dispute Resolution Panel*) or section 144, to the income assessed, or to the amount of tax determined, or to the amount of loss computed, or to the status under which he is assessed;
- (b) an order of assessment, reassessment or recomputation under section 147 (*except an order passed in pursuance of the directions of Dispute Resolution Panel*) or section 150;
- (c) an order of assessment or reassessment under section 153A;
- (d) an order made under section 154 or section 155 having the effect of enhancing the assessment or reducing a refund or an order refusing to allow the claim made by the assessee under either of the said sections;
- (e) an order made under section 163 treating the assessee as the agent of a non-resident;
- (f) an order made under section 170(2)/(3);
- (g) an order made under section 171;
- (h) an order made under section 201;
- (i) an order made under section 206C(6A) [Right of appeal by a person deemed to be an assessee in default for failure to collect or pay tax. Also, an appeal filed by an assessee in default against an order made under section 206C(6A) on or after 1st April, 2007 but before 1st June, 2007 shall be deemed to have been filed before the Commissioner (Appeals)];
- (j) an order made under section 237;
- (k) an order imposing a penalty under
 - (i) Section 221; or
 - (ii) Section 271, section 271A, section 271AA, 271AAA, section 271F, 271FB or section 272BB;
- (l) an order of assessment made by an Assessing Officer under section 158BC(c), in respect of search initiated under section 132 or books of account, other documents or any assets requisitioned under section 132A on or after 1st January, 1997;
- (m) an order imposing penalty under section 271B or section 271BB;
- (n) an order made by a Deputy Commissioner imposing a penalty under section 271C,

section 271CA, section 271D, or section 271E;

- (o) an order made by a Deputy Commissioner or a Deputy Director imposing a penalty under section 272A;
- (p) an order made by a Deputy Commissioner imposing a penalty under section 272AA;
- (q) an order imposing or enhancing penalty under section 275(1A);
- (r) an order imposing a penalty under Chapter XXI;
- (s) an order made by an Assessing Officer other than a Deputy Commissioner under the provisions of this Act in the case of such person or class of persons, as the Board may, having regard to the nature of the cases, the complexities involved and other relevant considerations direct.

It is also provided that the aforesaid provision will apply to all orders whether made before or after the appointed date which has been defined in the section as “the day appointed by the Central Government by notification in the Official Gazette.”

It is further provided that every appeal which is pending before the appointed day before the Deputy Commissioner (Appeals) and any matter arising out of or connected with such appeal and which is so pending shall stand transferred on that day to the Commissioner (Appeals) and the Commissioner (Appeals) may proceed with such appeal or matter from the stage in which it was on that day.

It is also provided that an appellant may demand that before proceeding further with the appeal and the matter, the previous proceedings or any part thereof be re-opened or the appellant be re-heard.

24.1.2 Appeal by person denying liability to deduct tax under section 195 [Section 248]

This section provides that where under an agreement or other arrangement, the tax deductible on any income, other than interest, under section 195 is to be borne by the person by whom the income is payable, and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, he may appeal to the Commissioner (Appeals) for a declaration that no tax was deductible on such income.

This section restricts the eligibility of filing an appeal only to cases where the tax is borne by the assessee. Therefore, the cases where the tax is to be borne by the non-resident is outside the scope of section 248 and no appeal can be filed in such cases.

24.1.3 Form of appeal and prescribed fees [Section 249(1)]

Every appeal shall be in the prescribed form and shall be verified in the prescribed manner.

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Prescribed fees - In case of an appeal made to the Commissioner (Appeals) on or after 1-10-1998, irrespective of the date of initiation of the assessment proceedings, the appeal shall be accompanied by a fee of:

- (i) where the total income of the assessee as computed by the Assessing Officer is Rs.1,00,000 or less
Rs.250
- (ii) where the total income of the assessee computed as above is more than Rs.1,00,000 but not more than Rs.2,00,000
Rs.500
- (iii) where the total income of the assessee computed as above is more than Rs.2,00,000
Rs.1,000
- (iv) in any case other than (i), (ii) and (iii) above
Rs.250

24.1.4 Time limit [Section 249(2) & (3)] - An appeal to the Commissioner (Appeals) against any order which is appealable is to be presented within 30 days from the dates specified below in the particular cases. However, the Commissioner (Appeals) may admit an appeal even after the expiry of the said period of thirty days, if he is satisfied that the appellant had sufficient cause for not presenting the appeal within the specified time. The dates from which the limitation period of 30 days has to be reckoned are as follows:

<i>Appeal relating to</i>	<i>30 days to be reckoned from</i>
1. Section 248	Date of payment of tax
2. Assessment/penalty	Date of service of notice of demand
3. Any other case	Date on which intimation of the order sought to be appealed against is served.

24.1.5 Exemption in respect of tax to be paid at the time of filing the appeal [Section 249(4)] - No appeal to the Commissioner (Appeals) shall be admitted for consideration unless, at the time of filing the appeal, the assessee has paid the tax on the amount of income returned by him in cases where a return has been filed by the assessee. If, however, no return has been filed by the assessee and an assessment has been made on him by the Assessing Officer, then the assessee must pay an amount equal to the amount of advance tax which was payable by him before filing the appeal. The Commissioner (Appeals) is, however, empowered to exempt an appellant from the operation of the requirement in regard to advance tax on receipt of an application from the appellant made specifically for this purpose, giving the reasons for the non-payment of the tax. The concerned authority is also required to pass an order in writing while granting the exemption indicating also the reasons on account of which the exemption is granted to the assessee.

24.1.6 Procedure in appeal [Section 250] - On account of an appeal the Commissioner (Appeals) shall fix a day and place for the hearing of the appeal and shall give notice of the same to the assessee and the Assessing Officer against whose order the appeal is made. Both the assessee and the Assessing Officer have the right to be heard at the hearing of the appeal either in person or by an authorised representative.

The Commissioner (Appeals), before passing an order on an appeal, may make such further enquiries as he thinks fit or direct the Assessing Officer to make further enquiries and report the same to him. He may also allow the appellant to go into any grounds of appeal not specified previously by the appellant if he is satisfied that the omission of that ground was not wilful or unreasonable.

The order of the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision. On disposal of the appeal the Commissioner (Appeals) must communicate the order passed by him to the assessee as well as the Commissioner.

In every appeal the Commissioner (Appeals), where it is possible, may hear and decide such appeal within a period of one year from the end of the financial year in which such appeal is filed under sub-section (1) of section 246A.

24.1.7 Powers of the Commissioner (Appeals) [Section 251] - While disposing of an appeal the Commissioner (Appeals) is vested with the following powers viz.,

- (i) In an appeal against an order of assessment, he may confirm, reduce, enhance or annul the assessment.
- (ii) In an appeal against the assessment order in respect of which the proceeding before the Settlement Commission abates under section 245HA, to confirm, reduce, enhance or annul the assessment after taking into consideration the following -
 - (1) all the material and other information produced by the assessee before the Settlement Commission;
 - (2) the results of the inquiry held by the Settlement Commission;
 - (3) the evidence recorded by the Settlement Commission in the course of the proceeding before it; and
 - (4) such other material as may be brought on his record.
- (iii) In an appeal against an order imposing a penalty he may confirm or cancel such order or vary it in such a way as to enhance or reduce the penalty.
- (iv) In any other case the Commissioner (Appeals) may pass such orders in the appeal as he deems fit.

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The Commissioner (Appeals), however, is not empowered to enhance an assessment or a penalty or to reduce a refund due to the assessee without giving the assessee a reasonable opportunity of showing cause against such an enhancement or reduction. In disposing of an appeal, the Commissioner (Appeals) may consider and decide any matter arising out of the proceedings in which the order appealed against was passed even if such matters were not raised before the Commissioner (Appeals) by the appellant.

24.2 APPEALS TO THE APPELLATE TRIBUNAL [SECTIONS 252 TO 255]

24.2.1 Constitution - The Central Government shall constitute an Appellate Tribunal consisting of judicial and accountant members to exercise the powers and discharge the functions conferred on the Tribunal by the Act.

Judicial Member - qualification

1. Must have held at least for 10 years a judicial office in the territory of India; or
2. Must have been a member of the Indian Legal Service in Grade II or any equivalent or higher post for at least three years; or
3. Must have been an advocate for at least 10 years.

Accountant Member - qualification

1. Minimum 10 years in the practice of accountancy as a Chartered Accountant; or
2. Must have been a member of the Indian Income-tax Service, Group A and must have held the post of Additional Commissioner of Income-tax or any equivalent or higher post for at least three years.

The Central Government shall ordinarily appoint a Senior Vice President or one of the Vice Presidents of the Tribunal to be the President thereof. The Government may appoint one or more members of the Tribunal to be the Vice-President or Vice-Presidents thereof. The Central Government may appoint one of the Vice-Presidents to be the Senior Vice-President. The Senior Vice-President or a Vice-President shall exercise such of the powers and perform such of the functions of the President as may be delegated to him by the President in writing.

24.2.2 Orders appealable before the Appellate Tribunal [Section 253]

Section 253(1) provides that an assessee aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order -

Order passed by	Section	Particulars
1. Assessing Officer	115VZC(1)	Power of Assessing Officer to exclude a tonnage tax company from the tonnage tax scheme if such company is a party to

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		any transaction or arrangement which amounts to an abuse of such scheme.
	143(3)/147	<i>An order of assessment passed by an Assessing Officer in pursuance of the directions of Dispute Resolution Panel or an order passed under section 154 in respect of such order</i>
2. Commissioner (Appeals)	154	Order rectifying a mistake
	250	Order of the Commissioner (Appeals) disposing of the appeal
	271	Order imposing penalty for failure to furnish return, comply with notices, concealment of income etc.
	271A	Order imposing penalty for failure to keep, maintain or retain books of account, documents etc.
3. Commissioner	12AA	Order refusing/canceling registration of trust or institution
	80G(5)(vi)	Refusal to grant approval to the Institutions or Fund
	263	Revision of erroneous order passed by Assessing Officer
	271	Order imposing penalty for failure to furnish return, comply with notices, concealment of income etc.
	272A	Order imposing penalty for failure to answer questions, sign statements, furnish information returns or statements, allow inspections etc.
	154	Amending the order passed under section 263.
4. Chief Commissioner or Director General or Director	272A	Order imposing penalty for failure to answer questions, sign statements, furnish information returns or statements, allow inspections etc.

Section 253(2) provides that the Commissioner may, if he objects to any order passed by the Commissioner (Appeals) under section 154 or section 250, direct the Assessing Officer to appeal to the Appellate Tribunal against such order.

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24.2.3 Time limit, cross objections etc. - An assessee can appeal to the Tribunal. The Commissioner, if he objects to any order passed by a Commissioner (Appeals) under section 154 or 250 may direct the Assessing Officer to file an appeal to the Tribunal. Every appeal to the Appellate Tribunal has to be filed within sixty days from the date on which the order sought to be appealed against is communicated to the assessee or the Commissioner, as the case may be. However, the Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross objection even after the expiry of the said period of 60 days, if he is satisfied that there was sufficient cause for not presenting it within that period. The Act vests in the respondents in every appeal filed before the Tribunal a right to file a memorandum of cross objections against any part of the order of the Commissioner (Appeals) within thirty days of the notice of the appeal and such memorandum is to be disposed of by the Appellate Tribunal as if it were an appeal. The appeal and the memorandum of cross objections to the Tribunal are to be in the prescribed form, and verified in the prescribed manner.

24.2.4 Fees

- (1) Where the total income of the assessee as computed by the Assessing Officer in the case to which the appeal relates is Rs.1,00,000 or less: **Rs.500**
- (2) Where the total income exceeds Rs.1,00,000 but is not more than Rs.2,00,000 : **Rs.1,500.**
- (3) Where the total income is more than Rs.2,00,000 : **1% of the assessed income subject to a maximum of Rs.10,000.**
- (4) No fee need be paid by a Commissioner or in the case of filing of memorandum of cross-objections.
- (5) An application for stay of demand shall be accompanied by a fee of Rs.500.
- (6) A fee of Rs.500 will be payable in any case other than those mentioned in (1) to (5) above.

The Appellate Tribunal may, after giving both the parties to the appeal a reasonable opportunity of being heard, pass such orders on any appeal as it thinks fit. Such orders passed by the Appellate Tribunal shall be final unless appeal is made to the High Court under section 260A **upto the date when the National Tax Tribunal is constituted. Thereafter, such orders passed by the Appellate Tribunal shall be final unless appeal is made to the National Tax Tribunal (NTT) under section 15 of the National Tax Tribunal Act, 2005.**

24.2.5 Rectification - The Appellate Tribunal may, at any time within 4 years from the date of the order, with a view to rectifying any mistake apparent from records, amend any order passed by it. However, if the mistake is brought to its notice by the assessee or the Assessing Officer, the Tribunal is bound to rectify the same. In cases where the

amendment has the effect of enhancing the assessment or reducing a refund or otherwise increasing the liability of the assessee, the Tribunal shall not pass any order of amendment unless it has given notice to the assessee of its intention to do so and has allowed him a reasonable opportunity of being heard. The Tribunal must send a copy of any orders passed by it to the assessee and to the Commissioner.

24.2.6 Fees for rectification - Any application for rectification filed by the assessee on or after 1-10-1998 shall be accompanied by a fee of Rs.50.

24.2.7 Time limit - In every appeal, the Appellate Tribunal, where it is possible, may hear and decide such appeal within a period of four years from the end of the financial year in which such appeal is filed under sub-section (1) or (2) of section 253 [Sub-section (2A)].

Under section 254(2A), the Appellate Tribunal can grant stay of demand of tax which can extend only up to 180 days from the date of granting such stay. If the appeal is not disposed of within 180 days, the stay order shall stand vacated after the expiry of the said period.

Where an order of stay has been passed and the appeal has not been disposed of within the specified period of 180 days from the date of such order, the Appellate Tribunal may extend the period of stay or pass an order of stay for a further period or periods, as it thinks fit, on an application made in this behalf by the assessee and on being satisfied that the delay in disposing of the appeal is not attributable to the assessee.

However, the aggregate of the period originally allowed and the period or periods so extended or allowed shall not, in any case, exceed 365 days, even if the delay in disposing of the appeal is not attributable to the assessee. If the appeal is not disposed of within such period or periods, the order of stay shall stand vacated after the expiry of such period or periods.

24.2.8 Cost of appeal - The cost of any appeal to the Appellate Tribunal shall be at the discretion of that Tribunal. [Sub-section (2B)]

24.2.9 Final authority on facts - On all questions of fact the orders passed by the Appellate Tribunal on appeal shall be final and binding on the assessee as well as the Department [Section 255].

24.2.10 Benches - The powers and functions of the Appellate Tribunal may be exercised and discharged by Benches constituted by the President of Tribunal from amongst the members thereof. Ordinarily, a Bench shall consist of one judicial member and one accountant member. However, the President or any other member of the Appellate Tribunal authorised in this behalf by the Central Government may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member and which pertains to an assessee whose total income as computed by the Assessing Officer in the case does not exceed Rs.5,00,000. The President may, for the disposal of any particular

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case constitute a special Bench consisting of three or more members, one of whom must necessarily be a judicial member and one an accountant member.

Where members differ - If the member of a Bench differ in opinion on any point the point shall be decided according to the opinion of the majority, if there is a majority. But if the members are equally divided they should state the points on which they differ and the case shall be referred by the President of the Tribunal for hearing on such point by one or more of the other members of the Tribunal: then, such points shall be decided according to the opinion of the majority of the members of the Tribunal who have heard the case, including those who first heard it.

Regulating power - The Appellate Tribunal is empowered to regulate its own procedure and the procedure of its Benches in all matters arising out of the exercise of its power of the discharge of its functions, including the places at which the Benches shall hold their sittings. The Tribunal is vested with all the powers which are exercisable by Income-tax authorities under section 131 for the purpose of discharging its functions. Any proceeding before the Appellate Tribunal shall be deemed to be a judicial proceeding for the purpose of the Income-tax Act and the Indian Penal Code and that Appellate Tribunal shall be deemed to be a Civil Court for all the purposes of the Income-tax Act and the Code of Criminal Procedure, 1898.

24.3 EFFECT TO THE DECISION OF SUPREME COURT AND OF THE NTT [SECTION 260]

(i) Sub-section (1) provides that the Supreme Court upon hearing any reference made to it by the Appellate Tribunal under section 257 shall decide the question of law raised therein, and shall deliver its judgment thereon containing the grounds on which such decision is founded.

[Note - Section 257 provides for direct reference by the Appellate Tribunal to the Supreme Court against an application made by the assessee or the Commissioner under section 256 for reference to the High Court, where there is a conflict in the decisions of the High Courts in respect of any particular question of law. It may be noted that an application under section 256 can be made only against order passed by the Appellate Tribunal before 1.10.98]

(ii) A copy of the judgment shall be sent under the seal of the Court and the signature of the Registrar to the Appellate Tribunal.

(iii) The Appellate Tribunal shall pass such orders as are necessary to dispose of the case conforming to such judgment.

(iv) Sub-section (2) provides that where the National Tax Tribunal delivers a judgment in an appeal filed before it or in any matter transferred to it under the National Tax Tribunal Act, 2005, effect shall be given to the order of that Tribunal by the Assessing Officer on the basis of a certified copy of the judgment.

(v) Sub-section (3) provides that the cost of any reference to the Supreme Court (which shall not include the fee for making the reference) shall be at the discretion of the Court.

Note – This section would come into force only from the date on which the National Tax Tribunal is constituted [See Note at the end of the chapter].

24.4 APPEAL TO HIGH COURT [SECTION 260A]

Section 260A provides for direct appeal to the High Court against the orders of the Appellate Tribunal.

(i) Appeal - Section 260A(1) provides that an appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal **up to the date of establishment of the NTT**, if the High Court is satisfied that the case involves a substantial question of law. If the High Court is so satisfied, it shall formulate that question. **After the establishment of the NTT, the appeal shall lie to the NTT.**

The Chief Commissioner or the Commissioner or an assessee aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court under this section.

(ii) Form for appeal - The appeal shall be in the form of a memorandum of appeal, precisely stating in it the substantial question of law involved.

(iii) Time limit for appeal - The appeal shall be filed within 120 days from the date on which the order appealed against is received by the assessee, or the Chief Commissioner or Commissioner.

(iv) Matters on which appeal can be heard - The appeal shall be heard only on the question formulated. However, the respondent shall at the hearing of appeal, be allowed to argue that the case does not involve such question. Further, the Court shall also have power to hear the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question. However, such power shall be exercised by the Court only after recording the reasons for hearing such other question.

Further, the High Court may determine any issue which -

- (a) has not been determined by the Appellate Tribunal; or
- (b) has been wrongly determined by the Appellate Tribunal, by reason of a decision on such question of law as is referred to in section 260A(1).

(v) Delivery of judgment - After the appeal is heard the High Court shall decide the question of law so formulated and deliver such judgment thereon, but such judgment should contain the grounds on which such decision is founded.

(vi) Award of costs - The High Court is empowered to award such costs as it deems fit.

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(vii) Code of Civil Procedure - Unless otherwise provided in this Act, the Code of Civil Procedure, 1908, relating to appeals to the High Court, shall apply to appeals under this section.

Case before High Court to be heard by not less than two judges [Section 260B]

Strength of the bench hearing the appeal - The appeal shall be heard by a bench of not less than 2 judges of the High Court.

Decision of the majority - The appeal shall be decided in accordance with the opinion of the judges or the majority, if any.

Where there is no such majority, the point of law upon which the judges differ shall be referred to one or more of the other judges of the High Court and such point shall be decided according to the opinion of the majority of the Judges who have heard the case, including those who first heard it.

24.5 APPEAL TO THE SUPREME COURT [SECTION 261]

According to section 261, an appeal shall lie to the Supreme Court from any judgment of the High Court **delivered before the establishment of the NTT**, in a case which the High Court certifies to be a fit one for appeal to the Supreme Court. **Thereafter, an appeal shall lie to the Supreme Court from any judgment of the NTT as per the provisions of the National Tax Tribunal Act, 2005.**

The provisions of the Code of Civil Procedure, 1908 in regard to appeal shall apply in the case of all appeals to the Supreme Court in the same manner as in the case of all appeals from decrees of a High Court. The cost of appeal shall be decided at the discretion of the Supreme Court. Where the judgment of a High Court is varied in the appeal, effect should be given to the order of the Supreme Court in the same manner as provided in the case of a judgment of the High Court.

24.6 PROVISION FOR AVOIDING REPETITIVE APPEALS [SECTION 158A]

(1) Section 158A makes provision for avoiding repetitive appeals when identical question of law is pending before High Court or Supreme Court. This is applicable to a situation where an assessee claims that any question of law arising in his case for an assessment year which is pending before the Assessing Officer or any appellate authority is identical with a question of law arising in his case for another assessment year which is pending before the High Court on an appeal under section 260A before the High Court or in appeal under section 261 before the Supreme Court. In such a situation, notwithstanding anything contained in the Act, the assessee may furnish a declaration in Form No.8 that if the Assessing Officer or the appellate authority, as the case may be, agrees to apply in the present case, the final decision passed on the other case, he (the assessee) shall not raise again the same question of law in appeal before any appellate authority or in appeal

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before the High Court under Section 260A or in appeal before the Supreme Court under section 261.

(2) Where such a declaration is furnished by the assessee to an appellate authority, the appellate authority shall call for a report from the Assessing Officer on the correctness of the claim. Where the Assessing Officer makes a request to the appellate authority to give him an opportunity of being heard, it shall allow him such opportunity.

(3) The Assessing Officer or the appellate authority, as the case may be, may, by order in writing –

(i) admit the claim if satisfied that the question of law is identical in the present as well as the other case; or

(ii) reject the claim, if not so satisfied.

(4) Where a claim is admitted, -

(i) the Assessing Officer or appellate authority, as the case may be, may make an order disposing of the present case without waiting for the final decision on the other case.

(ii) the assessee shall then not be entitled to raise in relation to the relevant case, such question of law in appeal before any appellate authority or in appeal before the High Court under section 260A or the Supreme Court under section 261.

(5) When the final decision on the question of law is passed in the other case, the Assessing Officer or the appellate authority, as the case may be shall apply it to the present case and amend the order passed, if necessary, in order to conform to such decision.

(6) An order under sub-section (3) above admitting or rejecting the claim of the assessee, as the case may be, shall be final and cannot be called in question in any proceeding by way of appeal, reference, revision under the Act.

(7) For the purposes of this section –

(i) “Appellate authority” means the Deputy Commissioner (Appeals), the Commissioner (Appeals) or the Appellate Tribunal.

(ii) “Case” means any proceeding under the act for assessment of the total income of the assessee or for the imposition of any penalty or fine on him.

24.7 REVISION BY THE COMMISSIONER [SECTIONS 263 AND 264]

24.7.1 Revision of Orders prejudicial to the Revenue [Section 263]

(i) The Commissioner may call for and examine the record of any proceeding under the Act. If he considers that any order passed by the Assessing Officer is erroneous in so far as it is prejudicial to the interests of the revenue, he may, after giving the

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assessee an opportunity of being heard and after making or causing to be made such inquiry as may be necessary, pass a suitable order.

- (ii) He can enhance, modify or cancel an assessment. He can also direct that a fresh assessment should be made.
- (iii) The term 'record' shall include and shall be deemed always to have included all records relating to any proceedings under the Act available at the time of examination by the Commissioner.
- (iv) Where any order referred to in section 263(1) passed by the Assessing Officer had been the subject-matter of any appeal, the powers of the Commissioner under section 263(1) shall extend and shall be deemed always to have extended to such matters as had not been considered and decided in such appeal.
- (v) No order shall be made after the expiry of 2 years from the end of the financial year in which the order sought to be revised was passed.
- (vi) In computing the period of 2 years, the time taken in giving an opportunity to the assessee to be reheard under section 129 and any period during which the revision proceeding is stayed by an order or injunction of any court shall be excluded.
- (vii) The time limit, however, does not apply in case where the Commissioner has to give effect to a finding or direction contained in the order of the Appellate Tribunal, High Court or the Supreme Court.

24.7.2 Revision of other orders [Section 264] - In the case of any other order (not being an order prejudicial to the Revenue) passed by any subordinate authority including the Deputy Commissioner (Appeals) the Commissioner may either on his own motion or on receipt of an application from the assessee, call for the record of any proceedings under the Act in the course of which the order was passed. After making such enquiries as may be necessary the Commissioner may pass such order as he thinks fit. The Commissioner is not empowered to revise any order on his own motion if a period of more than one year has expired from the date of the order sought to be revised. If the application for revision is made by the assessee, it must be made within one year from the date on which the order in question was communicated to him or the date on which he otherwise comes to know of it, whichever is later. However, the Commissioner may admit an application even after the expiry of one year, if he is satisfied that the assessee was prevented by sufficient cause from making the application within that period. The application to the Commissioner for revision must be accompanied by a fee of Rs.500. If an order is passed by the Commissioner declining to interfere in any proceeding, it shall not be deemed to be an order prejudicial to the assessee. However, the Commissioner is

not empowered to revise any order in the following cases, viz.,

- (i) where an appeal against the order lies to the A.A.C., or the Commissioner (Appeals) or the Tribunal but has not been made and the time within which the appeal may be made has not expired or in the case of an appeal to the Tribunal the assessee has not waived his right of appeal;
- (ii) where the order is pending on an appeal before the Deputy Commissioner (Appeals);
- (iii) where the order has been made subject to an appeal to the Commissioner (Appeals) or the Appellate Tribunal.

24.7.3 Limitation of time for revision of orders by Commissioner of Income-tax under section 264

Under section 264, the Commissioner of Income-tax is empowered to revise an order passed by the subordinate authority where no appeal has been filed. There is a limitation of one year for filing the application but there was no time limit for the Commissioner to dispose of the application. Section 264 has now been amended to provide as follows:

- (a) In respect of an application made on or after 1-10-1998, it shall be obligatory on the Commissioner to pass an order within a period of one year from the end of financial year in which such application is made by the assessee for revision.
- (b) In computing the above referred period of limitation, the time taken in giving an opportunity to the assessee to be re-heard under the proviso to section 129 and any period during which any proceeding under this section is stayed by an order or injunction of any Court shall be excluded [Explanation to section 264(6)].
- (c) The aforesaid time limit shall not apply to any order which has been passed in consequence of or to give effect to any finding or direction contained in an order of the Appellate Tribunal, NTT, High Court or the Supreme Court.

The assessee is bound to pay the tax due from him in accordance with the assessment made on him irrespective of the fact that a reference to the High Court or an appeal to the Supreme Court has been made to him [Section 265]. The High Court may, on a petition made to it for the execution of the order to the Supreme Court in respect of any costs awarded, thereby transmit the order for execution to any Court subordinate to it [Section 266]. Where as a result of an appeal under section 246 or section 246A or section 253, any change is made in the assessment of a body of individuals or an association of persons or a new assessment of a body of individuals or an association of persons is ordered to be made, the Commissioner (Appeals) or the Appellate Tribunal, as the case may be, shall pass an order authorizing the Assessing Officer either to amend the

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assessment made on any member of the body or association or make a fresh assessment on any member of the body or association [Section 267].

Section 268 - In computing the period of limitation prescribed for an appeal under this Act, the day on which the order complained of was served and, if the assessee was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order, should be excluded.

24.7.4 Consequence of non-filing of appeal in respect of cases where the tax effect is less than the prescribed monetary limit [Section 268A]

- (i) As per section 268A(1), the CBDT is empowered to issue orders, instructions or directions to other income tax authorities, fixing such monetary limits as it may deem fit. Such fixing of monetary limit is for the purpose of regulating filing of appeal or application for reference by any income tax authority.
- (ii) Where an income-tax authority has not filed any appeal or application for reference on any issue in the case of an assessee for any assessment year, due to abovementioned order/instruction/direction of the CBDT, such authority shall not be precluded from filing an appeal or application for reference on the same issue in the case of –
 - (1) the same assessee for any other assessment year; or
 - (2) any other assessee for the same or any other assessment year.
- (iii) Further, in such a case, it shall not be lawful for an assessee to contend that the income-tax authority has acquiesced in the decision on the disputed issue by not filing an appeal or application for reference in any case.
- (iv) The Appellate Tribunal or Court should take into consideration the above mentioned orders/instructions/directions of the CBDT and the circumstances under which such appeal or application for reference was filed or not filed in respect of any case.
- (v) Every order/instruction/direction which has been issued by the CBDT fixing monetary limits for filing an appeal or application for reference shall be deemed to have been issued under sub-section (1) of this section and all the provisions of this section shall apply accordingly.

Note

National Tax Tribunal (NTT) means the National Tax Tribunal established under section 3 of the National Tax Tribunal Act, 2005. The National Tax Tribunal Act, 2005 has been enacted by the Parliament in pursuance of Article 323B of the Constitution. It came into

force with effect from December 28th, 2005. The notified date of establishment of the National Tax Tribunal by the Central Government is 6th January, 2006.

The objective behind the enactment of the National Tax Tribunal Act, 2005 is to modify the present system of appeals under the Income-tax Act by substituting the National Tax Tribunal for the High Court, for facilitating quick adjudication of disputes under direct and indirect tax laws and achieve uniformity in the interpretation of central legislation.

This Act provides that, on establishment of the National Tax Tribunal, High Courts will not have appellate jurisdiction in matters of direct and indirect taxes. This Act vests jurisdiction in NTT to decide direct and indirect tax disputes on appeal from the decision of the respective Appellate Tribunals. Appeal to NTT can be filed both by the assessee and the revenue, from an order passed by the ITAT or CESTAT, on a substantial question of law. Appeal to NTT will lie only if the NTT is satisfied that the case involves a substantial question of law. The NTT shall formulate the substantial question of law for the purpose of hearing of appeal by it.

A party to an appeal, other than the Government, may either appear in person or authorize one or more chartered accountants or legal practitioners or any person duly authorized by him or it to present the case before the NTT. The Government may authorize one or more legal practitioners or any of its officers to present its case before the NTT. It may be noted that the Act does not permit chartered accountants to present the case of the Government before the NTT.

The Act provides that any person, including any department of the Government, aggrieved by any decision or order of NTT may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order of the NTT to him. The Supreme Court can allow filing of the appeal beyond 60 days, if the appellant was prevented by sufficient cause from filing the appeal within the said period of 60 days.

However, the Bombay High Court, in P.C.Joshi vs. Union of India (2006) 152 Taxman 285, has passed an ad-interim order restraining the Government from constituting the NTT and transferring the matters pending in the High Court to the NTT. Therefore, the constitution of the NTT will take effect only after the stay is vacated.

Self-examination questions

1. Explain briefly the four stages of appeal under the Income-tax Act.
2. List ten orders appealable before the Commissioner (Appeals).
3. What are the powers which can be exercised by the Commissioner (Appeals) while disposing of an appeal?

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4. Write short notes on the following -
 - (a) Constitution of Appellate Tribunal
 - (b) Time limit for disposing appeals.
5. Which are the orders against which an aggrieved assessee can file an appeal to the Appellate Tribunal?
6. Write short notes on -
 - (a) Appeal to the Supreme Court
 - (b) Provision for avoiding repetitive appeals
7. Discuss the Commissioner's powers to revise an order prejudicial to the interests of Revenue.
8. Explain the Commissioner's powers under section 264 to revise other orders.
9. The assessee, Mr. Ram, declared the cost of construction of cinema theatre at Rs.10.53 lakh, based on the registered valuer's report. The Assessing Officer accepted the value of the theatre as declared by the assessee and completed the assessment. However, the CIT, on enquiry, found that the assessee had availed a loan of Rs.17 lakh from a leasing company declaring the value of the theatre at Rs.27.40 lakh. Therefore, the CIT, after giving the assessee an opportunity of being heard, set aside the order of assessment and directed the Assessing Officer to make fresh assessment after verification and enquiry. On appeal before the Tribunal, the assessee questioned the order of the CIT by contending that the invocation of the provision under section 263 is not sustainable in law, since there was no information relating to any proceedings under the Income-tax Act available before the Assessing Officer which show that the assessment was erroneous and prejudicial to the Revenue. Discuss the correctness of the assessee's contention.
10. "It is necessary for a substantial question of law to be formulated at the time of admission of appeal itself, in the absence of which the High Court is not empowered to decide an appeal under section 260A' – Elucidate the above statement. What are the tests laid down by the Supreme Court to determine whether there is a substantial question of law?

Answers

9. This issue was resolved by the Madras High Court in *CIT v. Dr. K. Ramachandran (2004) 139 Taxman 320*. The High Court observed that the *Explanation* to section 263 provides that the term "record" shall include and shall be deemed always to have

included all records relating to any proceeding under the Act available at the time of the examination by the CIT. In *CIT v. Shree Manjunathesware Packing Products & Camphor Works (1998) 231 ITR 53(SC)*, the Apex Court made it clear that section 263 enables the CIT to call for and examine the records of any proceedings under the Act and pass such orders thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment or canceling the assessment and directing a fresh assessment, if he considers that the order passed by the Assessing Officer is erroneous and prejudicial to the interest of the Revenue. For this purpose, record would include not only record which was available to the Assessing Officer at the time of passing the assessment order, but would include the records available with the CIT at the time of passing of the order by the CIT.

The High Court also relied on its earlier decision in the case of *CIT v. M.N. Sulaiman (1999) 238 ITR 139*, wherein it followed the above decision of the Supreme Court. The High Court further held that the *Explanation* added to section 263(1) in the year 1988 has to be regarded as declaratory.

Therefore, since the term “record” includes all records available at the time of passing of order under section 263 by the CIT and is not restricted to information available to the Assessing Officer at the time of passing the assessment order, the assessee’s contention is not correct.

10. The Supreme Court, in *M. Janardhana Rao v. Jt. CIT (2005) 142 Taxman 722*, observed that an appeal to the High Court lies only when a substantial question of law is involved. It is essential for the High Court to first formulate question of law and thereafter, proceed in the matter. Without insisting on the statement of substantial question of law in the memorandum of appeal and formulating the same at the time of admission, the High Court is not empowered to decide the appeal under section 260A without adhering to the procedure prescribed in that section. Further, the High Court must make every effort to distinguish between a question of law and a substantial question of law. An appeal under section 260A can be only in respect of a ‘substantial question of law’. The expression ‘substantial question of law’ has not been defined anywhere in the statute. But it has acquired a definite connotation through various judicial pronouncements. There is no scope for interference by the High Court with a finding recorded when such finding could be treated to be a finding of fact.

Thus, in the above case, the Apex Court has reiterated that it is necessary for a substantial question of law to be formulated at the time of admission of appeal itself,

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in the absence of which the High Court is not empowered to decide an appeal under section 260A.

In order to determine whether there is a substantial question law, the Apex Court laid down the following tests in *Sir Chunilal V. Mehta & Sons Ltd v. Century Spinning & Mfg. Co. Ltd. AIR 1962 SC 1314* –

- (1) whether directly or indirectly it affects substantial rights of the parties; or
- (2) the question is of general public importance; or
- (3) whether it is an open question in the sense that issue is not settled by pronouncement of the Supreme Court or Privy Council or by the Federal Court; or
- (4) the issue is not free from difficulty, and
- (5) it calls for a discussion for alternative view.

25.1 INTRODUCTION

The Income-tax Act provides for the imposition of a penalty on an assessee who wilfully commits any offence under the provisions of the Act. Penalty is levied over and above the amount of any tax or interest payable by the assessee and thus, penalty is distinct and different from the tax payable. Penalty proceedings, however, are a part of the assessment proceedings. The authority concerned is entitled to levy penalty only if he is satisfied in the course of any proceedings under the Act that a person has been found guilty of any default in complying with the provisions of the Act. If the order of the penalty is set aside in appeal on the ground the assessee was not given a reasonable opportunity of being heard, the Assessing Officer would be entitled to levy a penalty again after rectifying the mistakes in proceedings. The penalty to be levied on an assessee is to be based upon the law as it stood at the time the default was committed and not the law as it stands in the financial year for which the assessment is made.

25.2 PENALTIES

The various sections prescribe the minimum and the maximum penalty that can be levied in certain cases though the Commissioner is empowered to waive or reduce the penalty in some cases. The authority concerned has been given the discretion to levy or not to levy a penalty. But if a penalty is levied, it cannot be less than the prescribed minimum nor can it exceed the maximum amount prescribed by the Act. The quantum of penalty levied by a lower authority can be modified by a higher authority on appeal, reference or revision. The various defaults in respect of which penalty can be levied under the Act are discussed as follows:

Section	Nature of Default	Penalty Leviable	Remarks
221(1)	Default in making payment of tax u/s 220	As directed by Assessing Officer. Total amount of penalty cannot exceed the amount of tax in arrears.	1. This is in addition to arrears and interest payable u/s 220 (2) 2. Where the assessee

25.2 Income Tax

			proves to the satisfaction of Assessing Officer that the default was for good and sufficient reasons, no penalty is leviable
			3. Even if tax is paid after default it makes no difference
271(1)(b)	Failure to comply with a notice u/s 142(1)/143(2) or direction u/s 142(2A).	Rs.10,000 for each such failure.	This will be in addition to tax, if any, payable
271(1)(c)	Concealment of particulars of income or furnishing of inaccurate particulars of income	Minimum 100% Maximum 300% of tax sought to be evaded - in addition to tax, if any, payable.	Explanations to section 271(1) extend the scope of concealed income (see after Table for details)
271(4)	Where profits of registered firm are distributed otherwise than in accordance with partnership deed and consequently the partner has not disclosed his correct income in his return.	Minimum as per Assessing Officer's discretion- Maximum 150% of tax on assessed income less tax on returned income. This will be in addition to tax, if any, payable by him.	

Penalties 25.3

271A	Failure to keep or maintain or retain books of account, documents etc. as required u/s 44A	Rs.25,000
271AA	Failure to keep and maintain any information and document as required under sub-section (1) or (2) of section 92D	2% of the value of each international transaction entered into by such person
271AAA	Undisclosed income of the specified previous year in respect of searches initiated under section 132 on or after 1.6.2007 [See para 25.5 for details]	10% of undisclosed income
271B	Failure to get accounts audited or obtain audit report under section 44AB or to furnish the report of such auditor with return of income.	$\frac{1}{2}\%$ of total sales turnover or gross receipts of business/gross receipts of profession or Rs.1,00,000 whichever is less.
271BA	Failure to furnish audit report as required under section 92E	Rs.1,00,000

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271C	Failure to deduct tax at source as per chapter XVII-B or to pay any part of the tax as required by - (i) Section 115-O(2) or (ii) the proviso to section 194B.	A sum equal to the amount of tax which he failed to deduct or pay.	With effect from 1.10.1998, penalty under sections 271C/271CA/271D/271E shall be imposed by the Joint Commissioner.
271CA	Failure to collect the whole or any part of the tax as required by or under the provisions of Chapter XVII-BB	The sum equal to the amount of tax not collected	
271D	Failure to comply with the provisions of Sections 269SS.	Penalty of a fixed sum equal to amount of loan or deposit taken.	
271E	Failure to comply with the provisions of Section 269T	A sum equal to the amount of deposit or loan so repaid.	
271F	Failure to furnish return under section 139(1) or by the proviso to that section before the end of the relevant assessment year.	Penalty of Rs.5,000.	
271FA	Failure to furnish Annual Information Return within the prescribed time.	A sum of Rs.100 for every day during which failure continues.	

271G	Failure to furnish information or document under section 92D	2% of the value of the international transaction for each such failure	
272A(1)	-Refusal to answer questions put by income tax authority. -Refusal to sign statements made in the course of income tax proceedings. -Non-compliance with summons issued under Section 131(1) to give evidence or produce books of accounts.	Rs.10,000 for each such default or failure	
272A(2)	Failure to comply with notice u/s 94(6) To give notice of discontinuance of business/ profession u/s 176(3) To furnish in due time returns statements mentioned in sections 133,206, 206C or 285B. To allow inspection of register referred in section 134 To furnish returns of income u/s 139(4A) or 139(4C) To deliver or cause to be delivered copy of the declaration u/s 197A	Rs.100 for everyday during which default continues.	Section 272A(3) specifies that for the default committed u/s 272(A)(1) and (2), the penalty can be imposed by an income-tax authority not lower in rank than a Joint Director or a Joint Commissioner. Section 272A(4) provides for grant of hearing before imposition of penalty under this provision.
		The amount of penalty for failure in relation to a declaration under	

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	To furnish a certificate as required in section 203 or 206C	section 197A, certificate as required u/s 203, and returns
	To deduct and pay tax u/s 226(2)	u/s 206 and 206C and statements u/s 200(3) or
	To furnish a statement as required by section 192(2C)	proviso to section 206C(3) shall not exceed the
	To deliver or cause to be delivered in due time a copy of the declaration referred to in section 206C(1A)	amount of tax deductible or collectible, as the case may be.
	To deliver or cause to be delivered a copy of the statement within the time specified in section 200(3) or the proviso to section 206C(3)	
	To deliver or cause to be delivered the statements within the time specified in section 206A(1).	
272AA	Failure to comply with the provision of section 133B	Any amount upto Rs.1,000
272B	Failure to comply with the provisions of section 139A (w.e.f. 1.6.2002)	Rs.10,000
	Failure to quote/intimate PAN u/s 139A(5A) or 139A(5C) or quoting / intimating false PAN	
272BB	Failure to comply with the provisions of section 203A	Rs.10,000

Quoting false TAN
willfully in challans/
certificates/statements/
other documents referred
to in section 203A(2)

No order shall be passed under sections 272A, 272AA, 272B, 272BB and 272BBB unless the person on whom the penalty is proposed to be imposed is given an opportunity of being heard in the matter.

25.3 PENALTY NOT LEVIABLE IN CERTAIN CASES [SECTION 273B]

No penalty is leviable under sections 271(1)(b), 271A, 271AA, 271B, 271BA, 271BB, 271C, 271CA, 271D, 271E, 271F, 271FA, 271FB, 271G, 272A(1)(c) or 272(A)(1)(d), 272A(2), 272AA(1), 272B, 272BB(1) & (1A), 272BBB(1), 273(1)(b), 273(2)(b) or 273(2)(c) if the assessee proves that there was reasonable cause for the said failure.

25.4 EXTENSION OF SCOPE OF CONCEALED INCOME

Penalty under section 271(1)(c) - If the Assessing Officer or the Commissioner (Appeals) in the course of proceedings under the Act, is satisfied that any person has concealed the particulars of his income or furnished inaccurate particulars of income, then, he may direct that such person shall pay penalty which shall not be less than the tax sought to be evaded, but which shall not exceed three times the amount of tax sought to be evaded. The penalty is in addition to the tax, if any, payable by the assessee. Therefore, section 271(1)(c) is attracted where (a) any person has concealed the particulars of his income, or (b) has furnished inaccurate particulars of such income.

The Explanations to section 271(1) extend the scope of the provisions relating to levy of penalty.

25.4.1 Explanation 1 : For the purpose of levy of penalty for concealment of income the assessee would be deemed to have concealed the particulars of his income or to have furnished false or inaccurate particulars thereof in cases where, in respect of any facts material to the computation of the taxable income of the assessee:

- (i) he has failed to offer a satisfactory explanation or the explanation offered by him is found by the Assessing Officer or the Commissioner (Appeals) or the Commissioner to be false; or
- (ii) the assessee offers an explanation which he is not able to substantiate and fails to prove that such Explanation is *bonafide* and that all the facts relating to the same and material to the computation of his total income have been disclosed by him.

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Under these circumstances the amount added or disallowed in the computation of the taxable income as a result of the unsatisfactory or the false statement of the assessee would be deemed to represent concealed income in respect of which fake particulars had been furnished by the assessee.

Students may note that the burden to prove that his explanation is *bonafide* etc. has been specifically placed upon the assessee.

25.4.2 Explanation 2 : In case where the source of any receipt, deposit or outgoing or investment in any assessment year is claimed by any assessee to be an amount which had been added in computing his taxable income or deducted in computing the assessable loss in his assessment for any earlier assessment year/years, but in respect of which no penalty under section 271(1)(c)(iii) had been levied, then, that part of the amount which had been so added or deducted in the earlier assessment year immediately preceding the year in which the receipt, deposit, outgoing or investment appears, which is sufficient to cover the amount represented by such receipts, or outgoings or the value of such investments (otherwise known as the utilised amount or value) must be treated as the income of the assessee the particulars of which had been concealed or inaccurate particulars whereof had been furnished for the first preceding year. Where the amount so added or deducted in the first preceding year is not sufficient to cover the utilised amount then, that part of the sum added or deducted in the year immediately preceding the first preceding year which is sufficient to cover such part of the utilised amount as is not so covered must be treated as the income of the assessee which had been concealed for the year immediately preceding the first preceding year, and so on, until the entire utilised amount is covered by the amount so added to the income or deducted from the loss of such earlier assessment year or years.

Where any penalty is imposable by virtue of this *Explanation*, proceedings for imposition of penalty may be initiated even if the proceedings in the course of which penalty proceedings could have been initiated have been completed. This is provided for in section 271(1A).

25.4.3 Explanation 3 : Where any person fails without reasonable cause to furnish within the period specified in section 153(1), a return of his income which he is required to furnish under section 139 in respect of any assessment year commencing on or after the 1st April 1989 and until the expiry of the period aforesaid no notice has been issued to him under section 142(1) or 148 and the Assessing Officer or Commissioner (Appeals) is satisfied that in respect of such assessment year such person has taxable income such person shall be deemed to have concealed the particulars of his income notwithstanding that such person furnishes a return of income at any time after the expiry of the period aforesaid in pursuance of a notice under section 148.

25.4.4 Explanation 4 : This seeks to define the meaning and scope of the expression “the amount of tax sought to be evaded” which is the basis for levying penalty for

concealment of income. Accordingly, the meaning of the expression will have to be taken as follows:

1. In cases where the amount of income, in respect of which particulars have been concealed or inaccurate particulars have been furnished has the effect of reducing the loss declared in the return or converting that loss into income, means the tax that would have been chargeable on the income in respect of which particulars have been concealed or inaccurate particulars have been furnished had such income been the total income.
2. In cases where the provisions of Explanation 3 apply, the amount of tax sought to be evaded by the assessee would mean the tax on the total income assessed as reduced by the amount of advance tax, TDS, TCS and self-assessment tax paid before the issue of notice under section 148.
3. In any other case, the amount of tax sought to be evaded must be taken to mean the amount of difference between the tax on the total income actually assessed and the tax that would have been chargeable had such total income been reduced by the amount of income in respect of which particulars had been concealed or false particulars had been furnished.

25.4.5 Explanation 5: Where in the course of a search initiated under section 132 before 1.6.2007, the assessee is found to be the owner of any money, bullion, jewelry or other article or thing and he claims that such assets have been acquired by him by utilizing, wholly or in part his income of:

- (a) any previous year which has ended before the date of search, but the return of that year has not been furnished or such income has not been declared in any return furnished before the said date; or
- (b) any previous year which ends on or after the date of search then notwithstanding the fact that such income is declared by him in any return of income furnished on or after the date of search, he shall be deemed to have concealed the particulars of such income for the purpose of imposition of penalty. However, if unless such income is/or the transactions resulting in such income are recorded before such search in the books of accounts if any or such income otherwise disclosed before such search before the Commissioner, the above deeming provisions will not apply.

If the assessee in the course of the search makes a statement under Sub-section (4) of Section 132 that any money, bullion, jewelry or other valuable article or thing found in his possession or under his control has been acquired out of his income which has not been disclosed so far in his return of income to be furnished before the expiry of time specified in Section 139(1)(a) or (b) and also specifies in the statement the manner in which such income has been derived and pays the tax together with interest in respect of such income then also the deeming explanation will not be applicable.

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25.4.6 Explanation 5A: Explanation 5A would be applicable in respect of searches conducted on or after 1st June, 2007. This Explanation provides that where an assessee is found to be the owner of any -

- asset and he claims that such assets have been acquired by him by utilizing his income for any previous year; or
- income based on any entry in the books of account or documents or transactions and he claims that such entry represents his income for any previous year,

which has ended before the date of the search and the due date for filing of the return has expired and return has not been filed, such income would be deemed to be concealed income, even if such income is declared in the return of income filed on or after the date of search.

The scope of Explanation 5A has been expanded retrospectively w.e.f. 1st June, 2007 to cover cases where the assessee has filed the return of income for any previous year before the date of search and the income found during the course of search relating the such previous year is not disclosed in the return of income. In such cases also, the assessee would be deemed to have concealed the particulars of income and would be liable for penalty under section 271.

25.4.7 Explanation 6: Penalty for concealment of income shall not be imposed on so much of the income on which additional income tax has been charged under section 143(1)(a).

25.4.8 Explanation 7: In the case of an assessee who has entered into an international transaction under section 92B, if any amount is added or disallowed in computing the total income under section 92C(4), then the amount so added or disallowed shall be deemed to be income in respect of which particulars have been concealed or inaccurate particulars have been furnished unless the assessee proves to the satisfaction of the Assessing Officer or Commissioner (Appeals) or the Commissioner that the price charged or paid in such transaction was computed in accordance with the provisions of section 92C in the prescribed manner under that section, in good faith and with due diligence.

Section 271(1B) clarifies that where any amount is added or disallowed in computing the total income or loss of an assessee in any order of assessment or reassessment, and such order contains a direction for initiation of penalty proceedings under section 271(1)(c), such an order of assessment or reassessment shall be deemed to constitute satisfaction of the Assessing Officer for initiation of the penalty proceedings.

Any reference in section 271 to income shall be construed as a reference to the income or fringe benefits, as the case may be, and the provisions of this section, to the extent relevant, shall also apply in relation to any assessment in respect of fringe benefits also. [Section 271(6)].

25.5 PENALTY IN RESPECT OF SEARCHES INITIATED UNDER SECTION 132 ON OR AFTER 1.6.2007 [SECTION 271AAA]

- (i) Section 271AAA provides for imposition of penalty at 10% of undisclosed income of the specified previous year, in respect of searches initiated under section 132 on or after 1.6.2007.
- (ii) Undisclosed income means -
 - (a) any income represented by any asset or entry in the books of accounts or other documents or transactions found in the course of search under section 132 which has -
 - (1) not been recorded in the regular books of accounts or documents on or before the date of search; or
 - (2) otherwise not been disclosed to the Chief Commissioner or Commissioner before the date of search.
 - (b) any income represented by any entry in respect of an expense recorded in regular books of accounts or documents, which is found to be false as a result of search.
- (iii) Specified previous year means –
 - (i) the previous year which has ended before the date of search, but the due date of filing the return of income under section 139(1) has not expired before the date of search; or
 - (ii) the previous year in which the search was conducted.
- (iv) Therefore, this section covers the previous year for which the due date of filing the return has not expired on the date of search and the year of search.
- (v) No penalty under section 271(1)(c) is leviable in respect of such undisclosed income.
- (vi) This section grants immunity from imposition of penalty, if:
 - (1) the assessee admits undisclosed income in a statement under section 132(4) during the course of search and,
 - (2) specifies the manner in which such income has been derived;
 - (3) substantiates the manner in which the undisclosed income was derived; and
 - (4) pays the tax, together with interest, if any, in respect of the undisclosed income.
- (vii) The provisions of section 274 relating to the procedure for levying penalty and section 275 relating to bar of limitation for imposing penalties shall, to the extent relevant, be applicable to the penalty referred to in this section.

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(viii) The provisions of penalty in respect of search initiated on or after 1.6.2007 is summarized in the table below –

Section	Relevant previous year	Penalty
Explanation 5A to section 271(1)	P.Y. which has ended before the date of search, in respect of which the due date has expired, but the return has not been furnished. For example, in respect of P.Y.2009-10, if the date of search is 15.11.2010, then the P.Y. has ended before that date (i.e., on 31.3.2010) and the due date of filing return (31.7.2010/30.9.2010, as the case may be) has also expired, but the return has not been furnished. In such a case, penalty would be attracted under this section.	100% to 300% of the tax sought to be evaded.
Explanation 5A to section 271(1)	P.Y. which has ended before the date of search, in respect of which return has been furnished, but income found during the search has not been disclosed in the return. In such a case also, penalty would be attracted under this section.	100% to 300% of the tax sought to be evaded.
271AAA	(i) P.Y. which has ended before the date of search, but the due date for filing return has not expired before the date of search, and the return has not been furnished. For example, in respect of P.Y.2009-10, if the date of search is 15.5.2010, then the P.Y. has ended before the date of search, but the due date of filing the return has not expired. (ii) P.Y. in which the search is conducted.	10% of the undisclosed income. However, no penalty is leviable if disclosure is made under section 132(4), manner of earning is disclosed and tax and interest is paid.

25.6 PENALTY IN THE CASE OF FIRM [SECTION 271(2)]

In all the above cases where the person liable to pay penalty in a registered firm or an unregistered firm which is assessed as registered under section 183(b) then, the penalty

imposable on the firm shall be the same amount as would be imposable on that firm it were unregistered.

25.7 PROCEDURE FOR ASSESSMENT OF PENALTIES [SECTION 274]

Section 274 provides that no order imposing a penalty exceeding Rs.10,000 shall be made by an Assessing Officer. Where the penalty exceeds Rs.25,000, the Deputy Commissioner (Appeals) has to get the prior approval of the Joint Commissioner.

In all cases before a penalty is imposed, the assessee should be given a reasonable opportunity of being heard.

Further, where the authority imposing penalty is not the Assessing Officer, a copy of the penalty order should be sent to the Assessing Officer.

25.8 REDUCTION OR WAIVER OF PENALTY AND INTEREST

25.8.1 Reduction or waiver of penalty [Section 273A] : Section 273A authorises the Commissioner of Income-tax to reduce or waive the amount of penalty payable by an assessee. The exercise of this power by the Commissioner is purely at his discretion and may be done either on his own motion or otherwise, that is on receipt of an application from the assessee.

The Commissioner would be entitled to reduce or waive the penalty payable by any person only if the following conditions are satisfied:-

- (i) In cases where penalty is levied or leviable on an assessee for concealment of income, the reduction or waiver by the Commissioner would be permissible only, if, prior to the detection of the concealment by the Assessing Officer, the assessee has made a full and true disclosure of all the particulars in respect of his income and, that, too voluntarily and in good faith.
- (ii) Further, it is essential that the assessee must have co-operated with the department in any enquiry relating to the assessment of his income and he must also have either paid or made satisfactory arrangements for the payment of any tax or interest, which may become payable in consequence of any order passed under the Income-tax Act in respect of the assessment year.
- (iii) For purposes of waiver of the penalty, a person must be deemed to have made a full and true disclosure of his income or of all the particulars relating thereto in any case where the excess of income assessed over the income returned is of such a nature as not to attract the imposition of any penalty under section 271(l)(c). In other words in every case where there is the scope for levying penalty on an assessee for having concealed his income liable to tax or for having furnished false or inaccurate particulars of such income, the assessee would not be deemed to have made a full and true disclosure of his income.

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(iv) However, the Commissioner of Income-tax would be entitled to exercise his power only after getting the previous approval of the Chief Commissioner or Director General in the following case:

In a case falling under section 271(1)(c) the amount of income in respect of which the penalty is imposed or imposable for the relevant assessment year or where such disclosure relates to more than one assessment year, the aggregate amount of such income for those years exceeds Rs.5,00,000.

(v) While exercising the powers of reduction or waiver of penalty the Commissioner is required to pass an order in writing and also to record his reasons for so doing. These powers could be exercised by the Commissioner either on his own motion or on receipt of an application from the assessee or from anyone else, he is also entitled to stay or compound any proceedings for the recovery of any penalty which might have been levied on the assessee in cases where he satisfied that:

- (i) to do otherwise would cause genuine hardship to the assessee having due regard to all the facts and circumstances of the case; and
- (ii) the assessee has co-operated in any enquiry relating to the assessment or any proceeding for the recovery of any amount due from him.

The Commissioner's order for reduction or waiver of penalty is final and cannot be challenged in any court or before any authority.

25.8.2 Reduction or waiver of penal interest [Notification No.F.No.400/234/95 I.T (B) dated 23.5.1996] : 1. The Central Board of Direct Taxes has authorised the Chief Commissioners and Directors and Directors-General (Investigation) to reduce or waive penal interest charged under section 234A/234B/234C in the following circumstances, namely:

- (i) Where, in the course of search and seizure operation, books of accounts have been taken over by the Department and were not available to the taxpayer to prepare his return of income;
- (ii) Where, in the course of search and seizure operation, cash had been seized which was not permitted to be adjusted against arrears of tax or payment of advance tax instalments falling due after the date of the search.
- (iii) Any income other than "capital gains" which was received or accrued after the date of first or subsequent instalment of advance tax, which was neither anticipated nor contemplated by the taxpayers and on which advance tax was paid by the tax payer after the receipt of such income;
- (iv) Where, as a result of any retrospective amendment of law or the decision of the Supreme Court after the end of the relevant previous year, Certain receipts which

were hitherto treated as exempt, become taxable. Since no advance tax would normally be paid in respect of such receipts during the relevant financial year, penal interest is levied for the default in payment of advance tax;

- (v) Where return of income is filed voluntarily without detection by the Income-tax Department and due to circumstances beyond control of the taxpayer such return of income was not filed within the stipulated time-limit or advance tax was not paid at the relevant time.

However, no reduction or waiver of such interest shall be ordered unless the assessee has filed the return of income for the relevant assessment year and paid the entire tax due on the income as assessed except the amount of interest for which reduction or waiver has been requested for. The Chief Commissioner of Income-tax or the Director-General of Income-tax may also impose any other conditions deemed fit for the said reduction or waiver of interest.

2. The class of income of cases in which the reduction or waiver of interest under section 243A or section 234B or, as the case may be, section 234C can be considered, are as follows:

- (a) Where during the course of proceedings for search and seizure under section 132 or otherwise, the books of account and other incriminating documents have been seized and for reasons beyond the control of the assessee, he has been unable to furnish the return of income for the previous year during which the action under section 132 has taken place, within the time specified in this behalf and the Chief Commissioner or, as the case may be, Director-General is satisfied having regard to the facts circumstances of the case that the delay in furnishing such return of income cannot reasonably be attributed to the assessee.
- (b) Where during the course of search and seizure operation under section 132, cash is seized which is not allowed to be utilised for payment of advance tax instalments as they fall due after the seizure of cash and the assessee has not paid fully or partly advance tax on the current income and the Chief Commissioner or the Director-General is satisfied that the assessee is unable to pay the advance tax.
- (c) Where any income chargeable to income-tax under any head of income, other than 'Capital Gains' is received or accrues after the due date of payment of the first or subsequent instalments of advance tax which was neither anticipated nor was in the contemplation of the assessee and the advance tax on such income is paid in the remaining instalment(s) and the Chief Commissioner/Director-General is satisfied that this is a fit case for reduction or waiver of interest chargeable under section 234C.
- (d) Where any income which was not chargeable to income-tax on the basis of any High Court order passed in the case of an assessee, and as a result, he did not pay

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income-tax in relation to such income in any previous year and subsequently after the end of the previous year, in consequence of any retrospective amendment of law or, as the case may be, the decision of the supreme court in his own case, in any assessment or reassessment proceedings the advance tax paid by the assessee during the financial year immediately preceding the relevant assessment year is found to be less than the amount of advance tax payable on his current income, the assessee is chargeable to interest under section 234B or section 234C and the Chief Commissioner or Director-General is satisfied that this is a fit case for reduction or waiver of such interest.

- (e) Where a return of income could not be filed by the assessee due to unavoidable circumstances and such return of income is filed voluntarily by the assessee or his legal heirs without detection by the Assessing Officer.

3. The Chief Commissioner of Income-tax/Director General of Income-tax may order the waiver or reduction of interest under sections 234A, 234B and 234C but shall not so reduce or waive penal interest in those cases where waiver or reduction of such interest has been rejected in the past on the merits of the case.

25.9 POWER OF COMMISSIONER TO GRANT IMMUNITY FROM PENALTY [SECTION 273AA]

Section 273AA empowers the Commissioner to grant immunity from penalty.

- (i) The application for the immunity has to be made by the assessee (person whose case has been abated under section 245HA) to the Commissioner of Income-tax.
- (ii) Where penalty was levied before or during the pendency of settlement proceedings, then the assessee can approach the Commissioner for immunity at any time.
- (iii) However, if no penalty was levied till the time of abatement of proceedings before Settlement Commission, then the assessee must make an application for immunity before the imposition of penalty by the Income-tax authority.
- (iv) The Commissioner can grant immunity, subject to such conditions as he may think fit to impose, on being satisfied that the assessee has –
 - (i) co-operated in the proceedings after abatement; and
 - (ii) made a full and true disclosure of his income and the manner in which such income has been derived.
- (v) The immunity granted shall stand withdrawn, if such assessee fails to comply with any condition subject to which the immunity was granted.
- (vi) The immunity granted to a person may, at any time, be withdrawn by the Commissioner, if he is satisfied that such person had, in the course of any proceedings, after abatement, -

- (i) concealed any particulars material to the assessment from the income-tax authority; or
- (ii) given false evidence.

Consequently, such person would become liable to the imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

25.10 TIME LIMITS FOR IMPOSITION OF PENALTY [SECTION 275]

- (i) Section 275(1) provides the time limit for imposing penalty under Chapter XXI of the Income-tax Act, 1961, as under -
 - (1) In a case where the relevant assessment or other order is the subject matter of an appeal to the Commissioner (Appeals) under section 246 or section 246A or an appeal to the Appellate Tribunal under section 253, an order imposing a penalty shall not be passed –
 - (a) after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty has been initiated, are completed; or
 - (b) six months from the end of the month in which the order of the Commissioner (Appeals) or, as the case may be, the Appellate Tribunal is received by the Chief Commissioner or Commissioner,whichever period expires later.
 - (2) However, this limitation is applicable only if the Commissioner (Appeals) passed the order before 1st June, 2003 disposing of the appeal made to him.
 - (3) In a case where the relevant assessment or other order is the subject matter of an appeal to the Commissioner (Appeals) under section 246 or section 246A, and the Commissioner (Appeals) passes the order on or after 1st June, 2003 disposing of such appeal, an order imposing penalty shall be passed –
 - (a) before the expiry of the financial year in which the proceedings, in the course of which action for imposition of penalty has been initiated, are completed; or
 - (b) within one year from the end of the financial year in which the order of the Commissioner (Appeals) is received by the Chief Commissioner or Commissioner,whichever is later.

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- (4) In a case where the relevant assessment or other order is the subject matter of revision under section 263 or section 264, an order imposing penalty shall not be passed after the expiry of six months from the end of the month in which such order of revision is passed;
 - (5) In any other case, an order imposing penalty shall not be passed after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty has been initiated, are completed, or six months from the end of the month in which action for imposition of penalty is initiated, whichever period expires later.
- (ii) Sub-section (1A) facilitates the revision of an order for the imposition of penalty or dropping the proceedings for the imposition of penalty, on the basis of subsequent revision of assessment by Commissioner (Appeals) or Appellate Tribunal or High Court or Supreme Court or by the Commissioner under section 263 or section 264.
- (iii) It has been provided that in a case where the relevant assessment or other order is the subject-matter of -
 - (1) an appeal to the Commissioner(Appeals) under section 246 or section 246A; or
 - (2) an appeal to the Appellate Tribunal under section 253; or
 - (3) an appeal to the High Court under section 260A; or
 - (4) an appeal to the Supreme Court under section 261; or
 - (5) revision under section 263 or section 264and an order imposing or enhancing or reducing penalty or dropping the proceedings for the imposition of penalty is passed before the order of –
 - (1) the Commissioner(Appeals); or
 - (2) the Appellate Tribunal; or
 - (3) the High Court; or
 - (4) the Supreme Court

is received by the Chief Commissioner or the Commissioner, or the order of revision under section 263 or 264 is passed, an order imposing or enhancing or reducing penalty or dropping the proceedings for the imposition of penalty may be passed on the basis of assessment as revised by giving effect to such order of the Commissioner (Appeals) or, the Appellate Tribunal or, the High Court, or the Supreme Court or order of revision under section 263 or 264. A revision order under this sub-section can again be revised under this sub-section.

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- (iv) It has also been provided that no such order imposing or enhancing or reducing or canceling penalty or dropping the proceedings shall be passed without hearing the assessee or giving him a reasonable opportunity of being heard.
- (v) Further, no such order can be passed after the expiry of six months from the end of the month in which -
 - (1) the order of the Commissioner (Appeals) or the Appellate Tribunal or the High Court or the Supreme Court is received by the Chief Commissioner or the Commissioner; or
 - (2) the order of revision under section 263 or section 264 is passed.
- (vi) Also, it has been provided that the provisions of section 274(2) shall apply in respect of such order imposing or enhancing or reducing penalty.

Note - Section 274(2) provides that for passing an order imposing penalty exceeding Rs.10,000, the Income-tax authority has to take the prior approval of the Joint Commissioner. Also, for passing an order imposing penalty exceeding Rs.20,000, the Assistant Commissioner or the Deputy Commissioner should take the prior approval of the Joint Commissioner.

- (vii) In computing the period of limitation, the time taken to give the assessee a reasonable opportunity of being heard or reheard under section 129 and any period during which the proceedings for the levy of the penalty are stayed by an order or injunction of the Court or any period during which the immunity granted under section 245H received in force will be excluded.

Self-examination questions

1. What is the penalty leviable under the Income-tax Act for -
 - (a) failure to keep or maintain or retain books of account as required under section 44A.
 - (b) failure to furnish audit report as required under section 92E;
 - (c) failure to furnish annual information report within the prescribed time.
2. Discuss the provisions under the Income-tax Act, 1961 which authorise the reduction or waiver of penalty by the Commissioner of Income-tax.
3. What is the period of limitation for levy of penalty under Chapter XXI?
4. Discuss the provisions for levy of penalty on undisclosed income arising consequent to a search initiated under section 132 on or after 1.6.2007.
5. Does the Commissioner have power to grant immunity from penalty? Discuss.
6. Can penalty be levied where a return is filed belatedly under section 139(4)?

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Answer

6. Penalty is attracted under section 271F for failure to furnish return of income as required under section 139(1) before the end of the relevant assessment year. The time allowed for filing a belated return is up to one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier. If the belated return under section 139(4) is filed before the end of the relevant assessment year, penalty under section 271F is not attracted. However, if the same is filed after the end of the relevant assessment year, penalty under section 271F is attracted.

OFFENCES AND PROSECUTION

26.1 SUMMARY OF OFFENCES AND PROSECUTION

While penalties may be imposed by the Income-tax authorities, the imposition of a fine or the launching of prosecution for any offence under the Act can be made only by the Magistrate of a Court under sections 275A to 280. In respect of the same default of an assessee, penalty may be imposed and a prosecution also may be launched against him.

Section	Nature of default	Rigorous imprisonment	Fine
275A	Contravention of order made under the second proviso to sub-section (1) or sub-section (3) of section 132 regarding search and seizure	Upto 2 Years	No limit specified
275B	Failure to afford the authorized officer the necessary facility to inspect the books of account or other documents as required under section 132(1)(iib)	Upto 2 years	No limit specified
276	Removal, concealment, transfer or delivery of property to thwart tax recovery	Upto 2 years	No limit specified
276A	Failure to comply with the provisions of section 178(1) and (3) regarding company in liquidation or parting with any of the assets of the company or the properties in his hands in contravention of the provision of section 276A	6 months to 2 years	-
276AB	Failure to comply with the provisions of section 269UC or 269UE or 269UL relating surrendering of property to Central Government	6 months to 2 years	-

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276B	Failure to pay to the Central Government, tax deducted under the provisions of Chapter XVII-B or the tax payable by him, as required by (i) section 115-O(2); or (ii) Second proviso to section 194B	3 months to 7 years	No limit specified
276BB	Failure to pay to the Central Government tax collected under section 206C	3 months to 7 years	No limit specified
276C(1)	Wilful attempt to evade tax, penalty or interest.	Evaded tax exceeding 1 lakh: 6 months to 7 years Other cases : 3 months to 3 years	No limit specified
276C(2)	Wilful attempt to evade payment of tax, penalty or interest.	3 months to 3 years	No limit specified
276CC	Wilful failure to furnish in due time a return of income u/s 139(1) or u/s 142(1)(i) or 148 or 153A. Note: If return of income under section 139(1) is furnished before expiry of the assessment year or the tax payable by him on the total income determined on regular assessment reduced by advance tax and TDS does not exceed Rs.3000 - No prosecution.	Evaded tax exceeding 1 lakh : 6 months to 7 years Other cases: 3 months to 3 years	No limit specified
276D	Willful failure to produce accounts and documents under section 142(1)/ 142(2A)	Up to one year	Rs.4 to Rs.10 for every day of default.
277	False statements in verification.	Evaded tax exceeding 1 lakh: 6 months to 7 years In other cases: 3 months to 3 years	No limit specified

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277A	Falsification of books or documents, etc. to induce or abet any person to evade any tax, penalty or interest chargeable or imposable under the Act. It is not necessary to prove that the other person has actually evaded any tax, penalty or interest chargeable or imposable under the Act for the purpose of establishing the charge under this section.	Imprisonment of 3 months to 3 years.	No limit specified
278	Abetment of false return etc. (relating to any income chargeable to tax)	Evaded tax exceeding 1 lakh: 6 months to 7 years In other cases: 3 months to 3 years	No limit specified
278A	Second and subsequent offences under section 276B, 276C(1), 276CC, 276DD, 276E, 277, 278.	6 months to 7 years for every subsequent offence	No limit specified
280(1)	Disclosure of particulars by public servants in contravention of Section 138(2). Prosecution after previous sanction of Central Government under section 280(2).	Up to 6 months	No limit specified

Section 278AA provides that where a reasonable cause for the failure is proved, punishment shall not be imposed for offences specified in sections 276A, 276AB and 276B.

For the purposes of offences and prosecutions, the following individuals will be deemed to be guilty of the offence committed by the respective person

Person	Section	Individual
Company	278B	Every person in charge of affairs; Director, Manager, Secretary and every officer who is guilty of offence
Firm	278B	Partner
AOP/BOI	278B	Members controlling the affairs
HUF	278C	Karta or member either by acquiescence or negligence.

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Section 278B(3) provides that if an offence under the Act has been committed by a person being a company, it shall be punished with fine. Every other person who was in charge of and was responsible for the conduct of business of the company, or any director, manager, secretary or other officer of the company (with whose consent or connivance or due to whose neglect the offence was committed) would be liable for punishment of imprisonment and fine wherever so provided.

26.2 POWER OF COMMISSIONER TO GRANT IMMUNITY FROM PROSECUTION [SECTION 278AB]

Section 278AB empowers the Commissioner to grant immunity from prosecution -

- (i) The application for the immunity must be made by the assessee (person whose case has been abated under section 245HA) to the Commissioner of Income-tax before institution of the prosecution proceedings after abatement.
- (ii) The assessee can approach the Commissioner for immunity any time if prosecution proceedings were instituted before or during the pendency of settlement proceedings. However, if the assessee has received any notice etc. from the Income-tax authority for institution of prosecution, then he must apply to the Commissioner for immunity, before actual institution of prosecution.
- (iii) The Commissioner can grant immunity, subject to such conditions as he may think fit to impose, on being satisfied that the assessee has –
 - (a) co-operated in the proceedings after abatement; and
 - (b) made a full and true disclosure of his income and the manner in which such income has been derived.
- (iv) Where application for settlement under section 245C had been made before the 1st June, 2007, the Commissioner can also grant immunity from prosecution for any offence under this Act or under the Indian Penal Code or under any other Central Act.
- (v) If the assessee fails to comply with any condition subject to which the immunity was granted, the same would be withdrawn.
- (vi) The immunity granted to a person may, at any time, be withdrawn by the Commissioner, if he is satisfied that such person had, in the course of any proceedings, after abatement, -
 - (a) concealed any particulars material to the assessment from the income-tax

authority; or

(b) given false evidence.

Consequently, the person may be tried for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the proceedings.

26.3 PRESUMPTION WITH REGARD TO ASSETS, BOOKS OF ACCOUNTS [SECTION 278D]

Section 278D provides that in case where, during the course of any search made under section 132, any money, bullion, jewelry or other valuable articles or things or any books of account or other documents had been found in the possession or control of any person and such assets or books of account or other documents are tendered by the prosecution in evidence against such person and/or against any person who is convicted of an offence under section 278, the provisions of section 132(4A) would apply, in relation to all such books of account and other documents. Accordingly, it would be presumed that such books of account or other documents and assets belong to the person in whose control or possession they were found, at the time of search and also that the contents of such books of account and other documents are true.

Similarly, in cases where any books of accounts or other documents and assets are taken into custody from the possession or control of any person by the officer or authority specified in section 132A(1)(a) or (c) and these are delivered to the requisitioning officer under section 132A(2), it would be presumed that the presumption similar to the one mentioned earlier would operate in these cases as well. It would be for assessee to rebut the presumption wherever necessary by producing cogent and reliable evidence.

26.4 PRESUMPTION AS TO CULPABLE MENTAL STATE

Section 278E provides as follows:

1. In any prosecution for any offence under this Act which requires a culpable mental state on the part of the accused, the court shall presume the existence of such mental state but it shall be a defence for the accused to prove the fact that he had no such mental state with respect to the act charged as an offence in that prosecution.
2. 'Culpable mental state' includes intention, motive or knowledge of a fact or belief in, or reason to believe, a fact.

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3. For the purposes of this section a fact is said to be proved only when the court believes it to exist beyond reasonable doubt and not merely when its existence is established by a preponderance of probability.

Students may note that penalty proceedings being quasi-criminal in nature, it has been judicially held in the context of various penalty and prosecution proceedings, that the burden is on the department to establish that the assessee concealed the particulars of his income or deliberately furnished inaccurate particulars thereof and it is not enough for the revenue merely to show that a certain amount was received by the assessee. Section 278E has clearly overruled this view and has specifically placed the burden of proof on the assessee.

It specifically provided that where any prosecution requires a culpable mental state (*mens rea*) the court shall presume the existence of such mental state but the assessee is entitled to prove that he had no such mental state with respect to the act charged with. Thus, the burden to prove the non-existence of *mens rea* has been effectively placed on the assessee.

26.5 PROSECUTION TO BE MADE AT THE INSTANCE OF THE CHIEF COMMISSIONER OR COMMISSIONER [SECTION 279 AND 279A]

Section 279(1) provides that the proceedings to punish a person for an offence under Sections 275A, 275B, 276, 276A, 276B, 276BB, 276C, 276CC, 276D, 277, 277A and 278 can be initiated only after previous sanction of the Commissioner or the Commissioner (Appeals) or the appropriate authority. However, the Chief Commissioner or the Director General may issue such instructions or directions to the said authorities for institution of proceedings under section 279(1). An offence may either before or after the institution of prosecution proceedings be compounded by the concerned authorities under Section 279(2). If a person is proceeded against under any of the provisions of Sections 275A to 278, then a statement made or account or documents produced before any authority under Act shall not be inadmissible as evidence for purpose of the prosecution proceedings merely on the ground that such account or document was produced or statement was made in the belief that the penalty imposable would be reduced or waived under Section 273A or that the offence would be compounded.

Section 279A provides that offences punishable under Sections 276B, 276C, 276CC, 277 and 278 shall be deemed to be non-cognizable offences. Section 279B, deals with proof of entries in record or other documents in the custody of income-tax authority. Section 280 deals with disclosure of particulars by public servants.

26.6 PROOF OF ENTRIES IN RECORDS OR DOCUMENTS [SECTION 279B]

Entries in the records or other documents in the custody of an income-tax authority shall be admitted in evidence in any proceedings for the prosecution of any person for an offence under this Chapter, and all such entries may be proved either by the production of the records or other documents in the custody of the income-tax authority containing such entries, or by the production of a copy of the entries certified by the income-tax authority having custody of the records or other documents under its signature and stating that it is a true copy of the original entries and that such original entries are contained in the records or other documents in its custody.

26.7 DISCLOSURE OF PARTICULARS BY PUBLIC SERVANTS [SECTION 280]

If a public servant furnishes any information or produces any document in contravention of section 138(2), he shall be punishable with imprisonment which may extend to 6 months and shall also be liable to pay fine.

However, no prosecution shall be instituted under this section except with the previous sanction of the Central Government.

Self-examination questions

1. Is prosecution attracted in respect of the following offences? If so, what is the period of imprisonment?
 - (a) Removal, concealment, transfer or delivery of property to thwart tax recovery;
 - (b) Failure to pay to the Central Government, tax collected under section 206C;
 - (c) Wilful attempt to evade tax, penalty or interest;
 - (d) Wilful failure to produce accounts and documents under section 142(1);
 - (e) Abetment of false return of income.
2. Write short notes on the following -
 - (a) Offences by companies
 - (b) Presumption as to culpable mental state
3. Enlist the offences which are deemed to be non-cognizable offences.
4. Discuss the correctness or otherwise of the following statement – “Prosecution proceedings can be initiated only after the previous sanction of the Chief Commissioner or Commissioner”.
5. Discuss the power of the Commissioner to grant immunity from prosecution.

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6. Can the Department launch prosecution in a case where they have accepted the revised return filed by the assessee, rectifying a mistake in the original return of income?

Answer

6. This question came up before the Karnataka High Court in *K.E. Sunil Babu, Asst. CIT v. Steel Processors and Others* (2006) 286 ITR 315. The High Court observed that since the Department had accepted the revised returns filed under section 139(5), it was clear that there was a bona fide mistake in the original return and there was no element of *mens rea*. Therefore, the High Court held that the Department cannot launch prosecution under sections 276C, 277 and 278.

MISCELLANEOUS PROVISIONS

27.1 MODE OF TAKING OR ACCEPTING CERTAIN LOANS AND DEPOSITS [SECTION 269SS]

Section 269SS provides that no person shall accept any loan of Rs.20,000 or more from any other person except by account payee cheque or account payee bank draft. This requirement also applies in cases where on the date of taking or accepting a loan or deposit from a person, any earlier loan or deposit taken or accepted from the same person and remaining unpaid on that date, is twenty thousand rupees or more. The requirement also applies if the aggregate amount of such earlier loan or deposit and to amount of loan or deposit proposed to be taken or accepted from that person is twenty thousand rupees or more.

The requirement will not however, apply to loan or deposit taken or accepted from, or any loan or deposit taken from or accepted by Government, any banking company, post office saving bank or any cooperative bank, any corporation established by a Central, State or Provincial Act: or any Government company as defined in section 617 of the Companies Act, 1956. The provisions of this section will also not apply to any loan or deposit taken, or accepted from, or any loan or deposit taken from or accepted by, any institution, association or body which the Central Government may, for reasons to be recorded in writing in this behalf notify in the Official Gazette. This requirement will not apply to those cases where the persons involved in the transaction derive income only from agriculture or where neither of them has any income chargeable to tax under the Act.

The expression “loan or deposit” in this section will mean any loan or deposit of money.

Section 271D provides for penalty for failure to comply with the provisions of section 269SS – If a person takes or accepts any loan or deposit in contravention of the provisions of section 269SS, he shall be liable to pay, by way of penalty, a sum of equal to the amount of the loan or deposit taken or accepted. Such penalty shall be imposed by the Joint Commissioner.

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27.2 MODE OF REPAYMENT OF CERTAIN DEPOSITS [SECTION 269T]

Section 269T provides that no branch of the banking company or a co-operative bank or any other company or co-operative society or a firm or other person, shall repay any loan or deposit made with it otherwise than by account payee cheque or account payee bank draft, drawn in the name of the person who has made the loan or deposit if the amount of loan or deposit together with interest, if any, payable thereon or the aggregate amount of such loans or deposits held by such person with the branch or the banking company or cooperative bank or as the case may be, the other company or cooperative society or the firm, or any other person either-in his own name or jointly with any other person on the date of such repayment, together with the interest if any payable on such loan or deposit is Rs.20,000 or more. However, if the repayment is made by a branch of bank or a cooperative bank, such repayment could be made by crediting the amount of such loan or deposit to the saving bank account or the current account, if any, with such branch of the person to whom such loan or deposit has to be repaid.

However, the provisions of this section shall not apply in case of repayment of any loan or deposit taken or accepted from -

- (i) Government;
- (ii) any banking company, post office savings bank or co-operative bank;
- (iii) any corporation established by a Central, State or Provincial Act;
- (iv) any Government company as defined in section 617 of the Companies Act, 1956;
- (v) such other institution, association or body or class of institutions, associations or bodies which the Central Government may, for reasons to be recorded in writing, notify in this behalf in the Official Gazette.

For the purposes of this section and 269SS, the expression “banking company” will mean a company to which the Banking Regulation Act, 1949 applies and includes any bank or banking institution referred to in section 51 of that Act. The expression “co-operative bank” will have the meaning assigned to it in Part V of the Banking Regulation Act, 1949.

‘Loan or Deposit’ means any loan or deposit of money which is repayable after notice or repayable after a period. In the case of any person other than a company, loan or deposit of any nature will be covered by this section.

27.3 SPECIAL BEARER BONDS [SECTION 269TT]

Section 269TT, similarly, provides that the amount payable on redemption of Special Bearer Bonds, 1991 shall be paid only by an account payee cheque or account payee bank draft drawn in the name of the person to whom such repayment is to be made.

27.4 TRANSFERS TO DEFRAUD REVENUE VOID [SECTION 281]

As a safeguard against non-realisation of revenue due to fraudulent transference of assets by a defaulting assessee it is provided under this Section that, certain transfers specified therein are deemed to be void for purpose of income-tax. Accordingly, in cases where, during the pendency of any proceeding under the Income-tax Act or after the completion thereof, but before the service of notice by the Tax Recovery Officer any assessee creates a charge on, or parts with, the property by way of sale, mortgage, gift, exchange, or any other mode of transfer whatsoever of any of his assets in favour of any other person such a charge or transfer must be deemed to be void as against any claim in respect of any tax, penalty, interest or fine payable by the assessee as a result of the completion of the proceedings or otherwise. However, the charge or transfer made by the assessee would not be void in case where it is made.

- (a) for adequate consideration and without any notice of the pendency of such proceeding or, as the case may be, without any notice of such tax or other monies remaining payable by the assessee; or
- (b) with the previous permission of the Assessing Officer.

This provision applies to all cases where the amount of tax or other sum of money which is payable or likely to be payable exceeds Rs.5,000 and the assets which are charged or transferred by the assessee exceeds Rs.10,000 in value, in the aggregate. For this purpose, the term 'assets' should be taken to mean land, buildings, machinery, plant, shares, securities and fixed deposits in bank to the extent to which any of these assets do not form part of the stock-in-trade of the business carried on by the assessee. In other words, if these items of Properties represent the stock-in-trade of the assessee's business, their transfer would not be treated as void.

27.5 PROVISIONAL ATTACHMENT TO PROTECT THE INTEREST OF THE REVENUE [SECTION 281B]

According to this section, cases where, during the pendency of any proceeding for the assessment of any income or for the assessment or reassessment of any income which has escaped assessment, the Assessing Officer is of the opinion that, for the purpose of protecting the interest of the Revenue, it is necessary to do so, he may, by an order in writing, attach provisionally any property belonging to the assessee. However, before passing an order, the Assessing Officer is required to take the prior permission of the Chief Commissioner, Commissioner, Director General or Director of Income-tax. The attachment in all such cases should be in the same manner as is provided under the rules laid down in the Second Schedule in the Income-tax Act. Every provisional attachment would cease to be effective after the expiry of a period of six months from the date on which order for the attachment is passed by the Assessing Officer. However, the Chief

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Commissioner or Commissioner is entitled, for reasons to be recorded in writing, to extend the validity of the period during which the order for attachment would be operative by such further period or periods as he deems fit. But, in no case shall the total period of provisional attachment of the property exceed two years from the date of the original order of the Assessing Officer.

Where an application for settlement under section 245C is made, the period commencing from the date on which such application is made and ending with the date on which the order under section 245D(1) is made shall be excluded for computing the period of 2 years.

In several cases, the assesseees have filed writ petitions in High Courts and Supreme Court and have obtained stay of the assessment proceedings. Generally, such stay remains in force for several years during which the validity of provisional attachment order expires. Therefore, it has now been provided w.r.e.f. A.Y.1988-89, that the period during which the proceedings for assessment or reassessment are stayed by an order or injunction of any Court, shall also be excluded in calculating the period of 2 years specified above.

27.6 SERVICE OF NOTICE [SECTIONS 282, 283 & 284]

As per section 282, a notice or requisition under the Act may be served on the person named therein either by post or as if it were a summons issued by a court. Hereafter, with effect from 1st October, 2009, such notice or requisition can be served by electronic mail also.

Accordingly, this section has now been substituted w.e.f. 1.10.2009 to provide that the service of notice or summon or requisition or order or any other communication under this Act may be made by delivering or transmitting a copy thereof to the person named therein -

- (1) by post or such courier services as approved by the CBDT; or*
- (2) in such manner as provided in the Code of Civil Procedure, 1908 for the purposes of service of summons; or*
- (3) in the form of any electronic record as provided in Chapter IV of the Information Technology Act, 2000; or*
- (4) by any other means of transmission as may be provided by rules made by the CBDT in this behalf.*

The CBDT is empowered to make rules providing for the addresses (including the address for electronic mail or electronic mail message) to which such communication may be delivered or transmitted to the person named therein.

Following is a list of persons on whom notice should be served and such a notice will be notice to the corresponding assessee mentioned.

Assessee	Addressee
(i) An existing firm	Any member of the firm
(ii) An existing H.U.F.	The Manager or any adult member of the family.
(iii) A Company	The Principal Officer thereof
(iv) Local authority	The Principal Officer thereof
(v) An existing association or body of individuals	The Principal Officer or any member thereof
(vi) An individual	The individual himself
(vii) Any other person	The person incharge of the management and control of his affairs.
(viii) A dissolved firm	Any adult person who was a partner immediately before dissolution.
(ix) A partitioned H.U.F.	The last manager of the family; if he is dead, all adults who were members immediately before the partition.
(x) A dissolved association of persons	Any person who was a member immediately before dissolution
(xi) A discontinued business	The assessee; In the case of a firm or an association of persons, any person who was a member at the time of discontinuance; In the case of a company, its Principal Officer.

27.7 AUTHENTICATION OF NOTICES AND OTHER DOCUMENTS [SECTION 282A]

- (i) Section 282A provides that where any notice or other document is required to be issued by any income-tax authority, such notice or other document should be signed in manuscript by that authority.
- (ii) Every notice or other document required to be issued, served or given for the purposes of this Act by any income-tax authority, shall be deemed to be authenticated if the name and office of a designated income-tax authority is printed, stamped or otherwise written thereon.

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- (iii) A designated income-tax authority means any income-tax authority authorised by the CBDT to issue, serve or give such notice or other document after authentication in the manner as provided in (ii) above.

27.8 ALLOTMENT OF DOCUMENT IDENTIFICATION NUMBER [NEW SECTION 282B]

- (i) *In order to improve the standards of service and transparency in the functioning of the Income-tax Department, a computer based system of allotment and quoting of Document Identification Number (DIN) in each correspondence sent or received by the Income-tax Department has been introduced to facilitate tracking of documents and alleviate the taxpayers grievances.*
- (ii) *Accordingly, a new section 282B has been inserted, w.e.f. 1.10.2010, to provide that every income tax authority shall allot a computer generated Document Identification Number in respect of every notice, order, letter or any correspondence issued by him to any other income-tax authority or assessee or any other person and such number shall be quoted thereon.*
- (iii) *Where the notice, order, letter or any correspondence issued by any income-tax authority does not bear a Document Identification Number, such notice, order, letter or any correspondence shall be treated as invalid and shall be deemed never to have been issued.*
- (iv) *Further, every document, letter or any correspondence, received by an income-tax authority or on behalf of such authority, shall be accepted only after allotting and quoting of a computer generated Document Identification Number.*
- (v) *Where the document, letter or any correspondence received by any income-tax authority or on behalf of such authority does not bear the Document Identification Number, such document, letter or any correspondence shall be treated as invalid and shall be deemed never to have been received.*

27.9 SUBMISSION OF STATEMENTS BY PRODUCERS OF FILMS [SECTION 285B]

This section provides that any person who carries on the production of a cinematograph film during the whole or any part of any financial year is under a statutory obligation, in respect of the period during which such production is carried on by him during the financial year to prepare and deliver or caused to be delivered to the Assessing Officer within 30 days from the end of the financial year or within 30 days from the date of completion of the production of the film, whichever is earlier, a detailed statement in the prescribed form containing the particulars of all the payments exceeding Rs.50,000 in the aggregate made by him or due from him to each person who is was engaged in the production of the firm.

27.10 ANNUAL INFORMATION RETURN [SECTION 285BA]

- (a) Section 285BA provides that any assessee, who enters into any financial transaction, as may be prescribed, with any other person, shall furnish, within the prescribed time, an annual information return in such form and manner, as may be prescribed, in respect of such financial transactions entered into by him during any previous year.
- (b) Sub-section (1) casts responsibility on –
 - an assessee or
 - the prescribed person in the case of an office of Government or
 - certain other authorities,
 - who are responsible for registering or maintaining books of account or other documents containing a record of any specified financial transaction, to furnish an annual information return.
- (c) Such annual information return should be furnished to the prescribed income-tax authority or such other authority or agency as may be prescribed in respect of –
 - (i) such transactions registered or recorded by him during any financial year beginning on or after 1st April, 2004, and
 - (ii) information relating to which is relevant and required for the purposes of this Act
- (d) The annual information return has to be furnished within the prescribed time after the end of such financial year in such form and manner (including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any computer readable media) as may be prescribed.
- (e) The expression “specified financial transaction” has been defined to include the following transactions, which may be prescribed by the CBDT –
 - a. a transaction of purchase, sale or exchange of goods or property or right or interest in a property, or
 - b. a transaction for rendering any service, or
 - c. a transaction under a works contract, or
 - d. a transaction by way of an investment made or an expenditure incurred, or
 - e. a transaction for taking or accepting any loan or deposit
- (f) The CBDT may prescribe different values for different transactions in respect of different persons, having regard to the nature of such transactions.
- (g) The value or the aggregate value of such transactions during a financial year so prescribed referred to above should not be less than fifty thousand rupees.

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- (h) Where the prescribed income-tax authority considers that the annual information return is defective he may intimate such defect to the person who has furnished such return and give him an opportunity to rectify the same within one month or such further period as he may allow in his discretion.
- (i) If the defect is not rectified within such period, such return would be treated as an invalid return and the provisions of the Act would apply as if such person had failed to furnish the annual information return.
- (j) Where a person referred to in sub-section (1) has not furnished the annual information return within the prescribed time, the prescribed income-tax authority may serve a notice requiring him to furnish such return within a period of sixty days from the date of service of such notice. Such person should furnish such return within the time specified in the notice.
- (k) Section 271FA provides a penalty for not furnishing a return as required under section 285BA(1). Penalty of Rs.100 is attracted for every day during which failure continues, if a person who is required to furnish an annual information return fails to furnish such return within the time prescribed.

27.11 PUBLICATION OF INFORMATION [SECTION 287]

The Central Government is empowered to publish the name and address of any assessee and other particular relating to them, if it considers it necessary or expedient in the public interest to do so. But no such publication relating to any penalty or prosecution shall be made until the time for presenting appeal to the Commissioner (Appeals) has expired without an appeal having been presented or until the appeal, if presented, has been disposed of. In the case of a firm, company or other association of persons the names of the partners of the firm, directors or manager of the company or members of the associations, as the case may be may also be published if, in the opinion of the Central Government, the circumstances of the case justify the same.

27.12 APPEARANCE BY REGISTERED VALUERS [SECTION 287A]

Any tax payer who is entitled to or required to attend before any income tax authority or the Appellate Tribunal in connection with any matter relating to the valuation of any asset, otherwise than he is required under Section 131 to attend personally for examination on oath or affirmation, may attend by a registered valuer. For this purpose, a registered valuer means a person who is registered as a valuer [Section 34AB of the Wealth-tax Act, 1957].

27.13 APPEARANCE BY AUTHORISED REPRESENTATIVE

1. Section 288 deals with appearance by authorised representative . Accordingly, any assessee who is entitled or required to attend before any income-tax authority of the Appellate Tribunal in connection with any proceeding under this Act otherwise than

when required under section 131 to attend personally for examination on oath or affirmation, may attend by an authorised representative.

2. For the purpose of this section, “authorised representative” means, a person authorised by the assessee in writing to appear on his behalf. The following persons can be authorised representatives:
 - (a) A person related to the assessee in any manner by a person regularly employed by the assessee
 - (b) any officer of a Scheduled Bank with which the assessee maintains a current account or has other regular dealings
 - (c) any legal practitioner who is entitled to practice in any Civil Court in India
 - (d) an Accountant
 - (e) any person who has passed any accountancy examination recognised in this behalf by the Board. Rule 50 prescribes the accountancy examination recognised for this purpose. They are as follows :
 - (i) The National Diploma in Commerce awarded by the All India Council for Technical Education under the Ministry of Education, New Delhi, provided the diploma-holder has taken Advanced Accountancy and Auditing as an elective subject for the Diploma Examination
 - (ii) Government Diploma in Company Secretaryship awarded by the Department of Company Affairs under the Ministry of Industrial Development and Company Affairs, New Delhi
 - (iii) Final Examination of the Institute of Company Secretaries of India, New Delhi
 - (iv) The Final Examination of the Institute of Cost and Work Accountants of India constituted under the Cost and Works Accountants Act, 1959
 - (v) The Departmental Examination conducted by or on behalf of the Central Board of Direct Taxes for promotion
 - (vi) The Revenue Audit Examination for Section Officers conducted by the Office of the Comptroller and Auditor General of India
 - (f) any person who has acquired such education qualifications as the Board may, prescribe for this purpose. Rule 51 prescribes the concerned educational qualifications as follows:

A degree in Commerce or Law conferred by any of the following Universities:

 - (i) Indian Universities: Any Indian University incorporated by any law for the time being in force.

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- (ii) Rangoon University
 - (iii) English and Welsh Universities: The Universities of Birmingham, Bristol, Cambridge, Durham, Leeds, Liverpool, London, Manchester, Oxford, Reading, Sheffield and Wales
 - (iv) Scottish Universities: The Universities of Aberdeen, Edinburgh, Glasgow and St. Andrews
 - (v) Irish Universities: The Universities of Dublin (Trinity College), the Queen's University, Belfast and the National University of Dublin
 - (vi) Pakistan Universities: Any Pakistan University incorporated by any law for the time being in force.
3. **Accountant:** Accountant means a Chartered Accountant within the meaning of Chartered Accountants Act, 1949 and includes in relation to any State any person, who, by virtue of the provisions of sub-section 2 of section 226 of the Companies Act, 1956 is entitled to be appointed to act as an Auditor of Companies registered in that State.
4. The following persons shall not be qualified to represent an assessee:
- (i) A person who has been dismissed or removed from government service after the first day of April 1938. In this case, he will be disqualified for all times.
 - (ii) A person who has been convicted of an offence connected with any income-tax proceeding or on whom a penalty has been imposed under this Act other than a penalty imposed on him under section 271(10)(ii) - In this case, the person will be disqualified for such time as the Chief Commissioner or the Commissioner may, by order, determine.
 - (iii) A person has become insolvent - In this case, he will be disqualified for a period during which the insolvency continues.
5. If any person is a legal practitioner or an accountant and is found guilty of misconduct in his professional capacity by any authority entitled to institute disciplinary proceedings against him, an order passed by that authority shall have effect in relation to his right to attend before an income-tax authority as it has in relation to his right to practice as a legal practitioner or accountant.
6. If a person is not a legal practitioner or an accountant and is found guilty of misconduct in connection with any income-tax proceedings by the prescribed authority, the prescribed authority, may direct that he shall thenceforth be disqualified to assessee.
7. Before any order or direction of disqualification under sub-section 4(b) or 5(b) is made, the following conditions must be satisfied :

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- (a) No such order or direction shall be made in respect of any person unless he has been given a reasonable opportunity of being heard
 - (b) any person against whom any such order or direction is made, may within one month of the making of the order or direction, may appeal to the Board to have the order or direction cancelled
 - (c) No such order or direction shall take effect until the distrait of one month from the making thereof or where an appeal has been preferred until the disposal of the appeal.
8. A person disqualified to represent an assessee under Indian Income-tax Act, 1922 shall stand disqualified under this Act also.

27.14 ROUNDING OFF OF INCOME, TAX ETC. [SECTIONS 288A AND 288B]

The total income of any assessee shall be rounded off to the nearest ten rupees.

Further, any amount payable, and the amount of refund due, under the provisions of the Income-tax Act, 1961, shall be rounded off to the nearest multiple of ten rupees. For this purpose, any part of a rupee consisting of paise shall be ignored. Thereafter, if such amount is not a multiple of ten, then, if the last figure in that amount is five or more, the amount shall be increased to the next higher amount which is a multiple of ten and if the last figure is less than five, the amount shall be reduced to the next lower amount which is a multiple of ten.

27.15 RECEIPT [SECTION 289]

The Department or the person or authority receiving any money paid by or recovered from the assessee or any other person shall issue a receipt for the same.

27.16 INDEMNITY [SECTION 290]

Every person deducting, retaining or paying any tax in pursuance of this Act in respect of income belonging to another person is entitled to be indemnified for the deduction, retention or payment thereof.

27.17 POWER TO TENDER IMMUNITY FROM PROSECUTION [SECTION 291]

The Central Government is empowered by Section 291 to tender any person immunity from prosecution for any offence under this Act if it is of the opinion that it is necessary or expedient in the public interest to do so for the purpose of obtaining the evidence directly or indirectly concerned in or privy to the concealment of the income or to the evasion of payment to tax on any income taxable under the Act. A tender of immunity made to or accepted by the person concerned shall, to that extent, render him immune from prosecution for any offence in respect of which tender was made or from the imposition of

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any penalty under the Act.

27.18 COGNIZANCE OF OFFENCES AND BAR OF SUITS IN CIVIL COURTS [SECTIONS 292 AND 293]

No suit can be brought in any Civil Court to set aside or modify any order and no prosecution, suit or other proceedings shall lie against any Government Officer for any thing done or intended to be done by him in good faith under the Act. No Court inferior to that of a Presidency Magistrate or a Magistrate of the first class shall try any offence under this Act.

27.19 CERTAIN LAWS NOT TO APPLY [SECTION 292A]

This section provides that the provisions of section 360 of the Code of Criminal Procedure, 1973 or the Probation of Offenders Act, 1958 shall not be applicable to any person who is convicted of an offence under the Income tax Act, unless that person is under 18 years of age.

27.20 RETURN OF INCOME ETC. NOT TO BECOME INVALID [SECTION 292B]

Section 292B provides that no return of income, order of assessment, notice, summons or other proceedings furnished or made or taken or purported to have been furnished or made in pursuance of any of the provisions of the Income-tax Act, shall be invalid or shall be deemed to be invalid merely by reason of any mistake, defect or omission in such return of income, assessment, notice, summons or other proceeding, if they are in substance and effect in conformity with or according to the intent and purposes of the Income-tax Act. The provision, thus, enables tax authorities to accept returns and other documents and tax payers to accept orders, notice, etc., received from tax authorities even in cases where there are a few typographical, arithmetical or other mistakes which do not materially affect the objects with which the document was submitted by the assessee or order was issued by the department [Refer also to section 139(9)].

27.21 NOTICE DEEMED TO BE VALID IN CERTAIN CIRCUMSTANCES [SECTION 292BB]

This section provides that the assessee would be precluded from raising any objection in any proceeding or inquiry that the notice was not served upon him or was not served in time or was served in an improper manner if he had appeared in any proceedings or co-operated in any enquiry relating to assessment or re-assessment.

In short, if the assessee had appeared in any proceedings or co-operated in any enquiry, it shall be deemed that any notice required to be served on him has been duly served upon him in time in accordance with the provisions of the Act. However, such deeming provision would not apply where the assessee has raised an objection (regarding non-

service of notice or non-service of notice in time or improper service of notice) before the completion of such assessment or reassessment.

27.22 PRESUMPTION AS TO ASSETS, BOOKS OF ACCOUNT, ETC. [SECTION 292C]

- (i) Under section 132(4A), it is provided that the books of account, money, bullion, jewellery or other valuable article or thing found in the possession or control of any person in the course of a search under section 132 will be presumed to belong to the said person.
- (ii) It is further provided that it will be presumed that -
 - (1) the contents of such books of account and other documents are true; and
 - (2) the signature and every other part of such books of account and other documents which purport to be in handwriting of any particular person or which may reasonably be assumed to have been signed by, or to be in the handwriting of, any particular person, are in that person's handwriting, and
 - (3) in the case of a document stamped, executed or attested, that it was duly stamped and executed or attested by the person by whom it purports to have been so executed or attested.
- (iii) The Supreme Court, in *P.R. Metrani v. CIT (2006) 287 ITR 209*, held that the aforesaid presumption is not available for framing regular assessment and such presumption is available only in regard to the proceedings for search and seizure under section 132. However, this decision does not reflect the correct intent of law.
- (iv) Therefore, section 292C has been inserted by the Finance Act, 2007 to clarify that presumptions provided in section 132(4A) can be made in any proceeding under this Act.
- (v) This section provides that where any books of account, other documents, money, bullion, jewellery or other valuable article or thing are or is found in the possession or control of any person in the course of a search under section 132 or survey under section 133A, it may, in any proceeding under this Act, be presumed that -
 - (1) such books of account, other documents, money, bullion, jewellery or other valuable article or thing belong or belongs to such person;
 - (2) the contents of such books of account and other documents are true; and
 - (3) the signature and every other part of such books of account and other documents which purport to be in the handwriting of any particular person or which may reasonably be assumed to have been signed by, or to be in the handwriting of, any particular person, are in that person's handwriting;

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- (4) In the case of a document stamped, executed or attested, that it was duly stamped and executed or attested by the person by whom it purports to have been so executed or attested.
- (vi) Further, this presumption has also been extended to books of account, other documents or assets which have been delivered to the requisitioning officer in accordance with the provisions of section 132A. For this purpose, sub-section(2) has been inserted by the Finance Act, 2008 to provide that where any books of accounts, other documents or assets have been delivered to the requisitioning officer in accordance with the provision of section 132A then, the presumption would apply as if such books of accounts, other documents or assets which had been taken into custody from the person referred to in clause (a) or clause (b) or clause(c), as the case may be, of sub- section (1) of section 132A , had been found in the possession or control of that person in the course of a search under section 132.

27.23 CONCESSIONS FOR ENCOURAGING PARTICIPATION IN THE BUSINESS OF PROSPECTING FOR, EXTRACTION ETC., OF MINERAL OILS [SECTION 293A]

With a view to encouraging the foreign companies to participate in the business of oil exploration and production, the Central Government is empowered under Section 293A to make, by a notification in the Official Gazette, an exemption, reduction in rate or other modification in respect of income-tax in favour of any class of persons specified below, if it considers it necessary or expedient so to do in the public interest namely:

- (i) persons with whom the Central Government have entered into agreement for the association or participation of that Government or any person authorised by that Government in any business consisting of prospecting for, or extraction or production of minerals oils;
- (ii) persons providing any services or facilities or supplying any ship, aircraft, machinery or plant (whether by way of sale or hire) in connection with any business consisting of the prospecting for or extraction or production of mineral oils carried on by that Government or any person specified by it in this behalf by notification in the Official Gazette.

The Central Government also has the power to make a modification in regard to the status in which the aforesaid class of persons or members thereof are to be assessed on their income from the said business. The term 'status' has been explained to mean the category under which the assessee is assessed as 'individual', 'Hindu undivided family' and so on.

27.24 AUTHORITY EMPOWERED TO GRANT AN APPROVAL UNDER THE INCOME-TAX ACT DEEMED TO HAVE POWER TO WITHDRAW THE APPROVAL GRANTED [NEW SECTION 293C]

Miscellaneous Provisions 27.15

- (i) *The Central Government, CBDT and income-tax Authorities are empowered under the various provisions of the Income-tax Act to grant approval to the assesseees for availing the benefit of incentives available under the Act.*
- (ii) *However, only some provisions of the Income-tax Act specifically contain provisions for withdrawal of approval. In all other cases, there is no specific power to withdraw the approval granted.*
- (iii) *Therefore, a new section 293C has been inserted w.e.f. 1.10.2009 to provide explicitly, such power to withdraw an approval granted. This section provides that an approval granting authority (i.e. the Central Government, CBDT or income-tax authority, as the case may be) shall also have the powers to withdraw the approval at any time.*
- (iv) *However, such withdrawal can be made only after giving a reasonable opportunity to the concerned assessee of showing cause against the proposed withdrawal. Further, the reasons for withdrawal of the approval should be recorded by the concerned authority.*

27.25 ACT TO HAVE EFFECT PENDING LEGISLATIVE PROVISION FOR CHARGE OF TAX [SECTION 294]

If on the 1st day of April in any assessment year provision has not yet been made by a Central Act for the charging of Income-tax for that assessment year, this Act shall nevertheless have effect until such provision is so made as if the provision in force in the preceding assessment year or the provision proposed in the Bill then before Parliament, whichever is more favourable to the assessee, were actually in force.

27.26 RULES [SECTIONS 295 AND 296]

Section 295 authorises the Central Board of Direct Taxes to make rules for the whole or any part of India for carrying out the purposes and to implement the provisions of the Act. The powers of the Board in this regard are subject to the supervision and control of the Central Government. The rules framed by the Board and approved by the Central Government are required to be placed before each House of the Parliament before enforcing the same. In exercise of the powers conferred on it by this section, the Board with the approval and sanction of the Central Government and the Parliament, has framed the Income-tax Rules, 1962 which have been amended from time to time. This section also enumerates the important matters on which rules may be framed by the Board: the rules framed under this Act have the same force of the section of the Act. The rules must be interpreted in the light of the sections under which they have been made. But the rules should be so framed as not to adversely affect or derogate from the full operative effect of the provisions of the sections. The rules must be within the term of the mandate given to the Board and must be framed in such a way as to be consistent with and supplementary

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to the provisions of the Act.

27.27 SCHEDULES TO THE INCOME-TAX ACT

There are fourteen Schedules to the Income-tax Act, 1962. Briefly they deal with the following matters:

1. Schedule I Method of computing profits and gains of Insurance business
Section 44
2. Schedule II Procedure for Recovery of Tax-Section 222 and 276.
3. Schedule III Procedure for distraint by Assessing Officer or Tax Recovery Officer - Section 226(5)
4. Schedule IV Recognised Provident Funds, approved superannuation funds and approved gratuity funds - Sections 2(38), 10(12), 10(25), 36(1)(iv), 87(1)(d), 111, 192(4).
5. Schedule V List containing certain articles and things in the context of Section 33(1)(b)(B)(i) - Now only of academic importance.
6. Schedule VI Omitted
7. Schedule VII Containing a list of minerals and group of associated minerals in the context of section 35E.
8. Schedule VIII List of Industrially backward States and Union Territories – Section 80IA(2)(iv)(b)
9. Schedule IX Omitted
10. Schedule X Omitted
11. Schedule XI List of articles or things in relation to sections 32A, 32AB, 80CC(3)(a)(i), 80I(2), 80J(4), 88A(3)(a)(i) - now only of academic importance.
12. Schedule XII Processed minerals and ores in the context of Section 80HHC(2)(b)(2).
13. Schedule XIII List of articles or things which an undertaking or enterprise should not manufacture or produce in the context of section 80-IC(2)(a)
14. Schedule XIV List of articles or things which an undertaking or enterprise should manufacture or produce and list of operations which an undertaking or enterprise should commence in the context of section 80-IC(2)(b).

Self-examination questions

1. Discuss the circumstances under which the Assessing Officer can resort to provisional attachment of the property of the assessee. State the period of time for

which such attachment can take place.

2. Explain the validity as well as the consequences of the alienation of assets of a business by an assessee during the pendency of a proceeding under the Income-tax Act.
3. What is an Annual Information Return? Elucidate the provisions of section 285A regarding Annual Information Return.
4. (i) Who are the persons responsible for furnishing an Annual Information Return?
(ii) What is meant by 'specified financial transaction' in the context of Annual Information Return?
5. "Tax Recovery Officer can recover the arrear demands from the assessee in default out of sale proceeds of the property attached after making a proclamation". How can such proclamation be made under the Act?

Answer

5. Movable Property [Rules 38 & 39 of Schedule II to the Income-tax Act, 1961]

Where the Tax Recovery Officer orders sale of movable property, he should issue a proclamation in the language of the district of the intended sale, specifying the time and place of sale and whether the sale is subject to confirmation or not.

The proclamation should be made by beat of drum or other customary mode, -

- (a) in the case of property attached by actual seizure –
 - (i) in the village in which the property was seized, or, if the property was seized in a town or city, then, in the locality in which it was seized; and
 - (ii) at such other places as the Tax Recovery Officer may direct;
- (b) in the case of property attached otherwise than by actual seizure, in such places, if any, as the Tax Recovery Officer may direct.

A copy of the proclamation should also be affixed in a conspicuous part of the office of the Tax Recovery Officer.

Immovable Property [Rule 54 of Schedule II to the Income-tax Act, 1961]

The Tax Recovery Officer shall make a proclamation for sale of immovable property at some place on or near such property by beat of drum or other customary mode. A copy of the proclamation shall be affixed on a conspicuous part of the property and also upon a conspicuous part of the office of the Tax Recovery Officer.

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Where the Tax Recovery Officer directs, such proclamation shall also be published in the Official Gazette or in a local newspaper or both, and the cost of such publication shall be deemed to be cost of the sale.

Where the property to be sold is divided into lots, then it is not necessary to make a separate proclamation for each lot of property, unless in the opinion of the Tax Recovery Officer, proper notice of sale cannot otherwise be given.

DEDUCTION, COLLECTION AND RECOVERY OF TAX

28.1 DEDUCTION AND COLLECTION OF TAX AT SOURCE AND ADVANCE PAYMENT [SECTION 190]

The total income of an assessee for the previous year is taxable in the relevant assessment year. For example, the total income for the P.Y.2009-10 is taxable in the A.Y.2010-11. However, the income-tax is recovered from the assessee in the previous year itself through –

- (1) Tax deduction at source (TDS)
- (2) Tax collection at source (TCS)
- (3) Payment of advance tax

Another mode of recovery of tax is from the employer through tax paid by him under section 192(1A) on the non-monetary perquisites provided to the employee.

These taxes are deductible from the total tax due from the assessee. The assessee, while filing his return of income, has to pay self-assessment tax under section 140A, if tax is due on the total income as per his return of income after adjusting, inter-alia, TDS and advance tax.

28.2 DIRECT PAYMENT [SECTION 191]

Section 191 provides that in the following cases, tax is payable by the assessee directly –

- (1) in the case of income in respect of which tax is not required to be deducted at source; and
- (2) income in respect of which tax is liable to be deducted but is not actually deducted.

In view of these provisions of section 191, the proceedings for recovery of tax necessarily had to be taken against the assessee whose tax was liable to be deducted, but not deducted.

In order to overcome this difficulty, the Explanation to this section provides that if –

28.2 Income Tax

(1) any person, including the principal officer of the company, who is required to deduct tax at source or

(2) an employer paying tax on non-monetary perquisites under section 192(1A),

does not deduct the whole or part of the tax, or after deducting fails to pay such tax deducted, then such person shall be deemed to be an assessee in default.

However, if the assessee himself has paid the tax, this provision will not apply.

28.3 DEDUCTION OF TAX AT SOURCE

28.3.1 Salary [Section 192]

(1) This section casts an obligation on every person responsible for paying any income chargeable to tax under the head 'Salaries' to deduct income-tax on the amount payable.

(2) Such income-tax has to be calculated at the average rate of income-tax computed on the basis of the rates in force for the relevant financial year in which the payment is made, on the estimated total income of the assessee. Therefore, the liability to deduct tax at source in the case of salaries arises only at the time of payment.

(3) Average rate of income-tax means the rate arrived at by dividing the amount of income-tax calculated on the total income, by such total income.

(4) However, deduction at a rate lower than that prescribed may be made if a certificate has been obtained under section 197 from the Assessing Officer.

(5) Every year, the CBDT issues a circular giving details and direction to all employers for the purpose of deduction of tax from salaries payable to the employees during the relevant financial year. These instructions should be followed.

(6) The concept of payment of tax on non-monetary perquisites has been provided in sections 192(1A) and (1B). These sections provide that the employer may pay this tax, at his option, in lieu of deduction of tax at source from salary payable to the employee. Such tax will have to be worked out at the average rate applicable to aggregate salary income of the employee and payment of tax will have to be made every month along with tax deducted at source on monetary payment of salary, allowances etc.

(7) In cases where an assessee is simultaneously employed under more than one employer or the assessee takes up a job with another employer during the financial year after his resignation or retirement from the services of the former employer, he may furnish the details of the income under the head "Salaries" due or received by him from the other employer, the tax deducted therefrom and such other particulars to his current employer. Thereupon, the subsequent employer should take such information into consideration and then deduct the tax remaining payable in respect of the employee's remuneration from both the employers put together for the relevant financial year.

(8) For purposes of deduction of tax out of salaries payable in a foreign currency, the

value of salaries in terms of rupees should be calculated at the prescribed rate of exchange as specified in Rule 26 of the Income-tax Rules.

(9) In respect of salary payments to employees of Government or to employees of companies, co-operative societies, local authorities, universities, institutions, associations or bodies, deduction of tax at source should be made after allowing relief under section 89(1), where eligible.

(10) A tax payer having salary income in addition to other income chargeable to tax for that financial year, may send to the employer the following:

- (i) particulars of such other income
- (ii) particulars of any tax deducted under any other provision
- (iii) loss, if any, under the head 'Income from house property'

The employer shall take the above particulars into account while calculating tax deductible at source.

It is also provided that except in cases where loss from house property has been adjusted against salary income, the tax deductible from salary should not be reduced as a consequence of making the above adjustments.

(11) Sub-section (2C) provides that the employer shall furnish to the employee a statement giving correct and complete particulars of perquisites or profits in lieu of salary provided to him and the value thereof. The statement shall be in the prescribed form (Form 12BA) and manner. This requirement is applicable only where the salary paid/payable to an employee exceeds Rs.1,50,000. For other employees, the particulars of perquisites/profits in lieu of salary shall be given in Form 16 itself.

28.3.2 Interest on securities [Section 193]

(1) This section casts responsibility on every person responsible for paying to a resident any income by way of interest on securities.

(2) Such person is vested with the responsibility to deduct income-tax at the rates in force from the amount of interest payable.

The rate at which tax is deductible under section 193 is 10%, both in the case of domestic companies and resident non-corporate assessees.

(3) Tax should be deducted at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier.

(4) However, no tax deduction is to be made from any interest payable:

- (i) on 4¼% National Defence Bonds 1972, where the bonds are held by an individual not

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being a non-resident;

- (ii) on 4¼% National Defence Loan, 1968 or 4¾% National Defence Loan, 1972, where the interest is payable to an individual;
- (iii) on National Development Bonds;
- (iv) on 7-year National Savings Certificates (IV Issue);
- (v) on debentures issued by any institution or authority or any public sector company or any co-operative society (including a co-operative land mortgage bank or a co-operative land development bank), as notified by the Central Government;
- (vi) on 6½% Gold Bonds, 1977 or 7% Gold Bonds, 1980, where the bonds are held by an individual (other than a non-resident), provided that the holders of the bonds make a written declaration that the total nominal value of the bonds held by him or on his behalf did not in either case exceed Rs.10,000 at any time during the period to which the interest relates;
- (vii) on any security of the Central Government or a State Government;

Note – It may be noted that tax has to be deducted at source in respect of interest payable on 8% Savings (Taxable) Bonds, 2003, if such interest payable exceeds Rs.10,000 during the financial year.

- (viii) on debentures issued by the company in which the public are substantially interested to a resident individual. However:
 - (a) such debentures must be listed in a recognised stock exchange;
 - (b) the interest should be paid by the company by an account payee cheque;
 - (c) the amount of such interest or the aggregate thereof paid or likely to be paid during the financial year to the resident individual should not exceed Rs.2,500.
- (ix) on securities to LIC, GIC, subsidiaries of GIC or any other insurer, provided –
 - (a) the securities are owned by them or
 - (b) they have full beneficial interest in such securities.
- (x) on any security issued by a company, where such security is in dematerialised form and is listed on a recognised stock exchange in India in accordance with the Securities Contracts (Regulation) Act, 1956 and the rules made thereunder.

(5) In all the above cases, the declaration shall be made by the recipient to the person responsible for paying such interest on securities.

(6) If the person entitled to receive interest produces a certificate under section 197 from the Assessing Officer to the effect that his total income is either below the taxable limit or is liable to income-tax at a lower rate, the interest on securities shall be paid without any deduction of tax or after deduction of tax at such lower rate, as the case may be.

(7) Where any income by way of interest on securities is credited to any account in the books of account of the person liable to pay such income, such crediting is deemed to be credit of such income to the account of the payee and tax has to be deducted at source.

(8) The account to which such interest is credited may be called "Interest Payable account" or "Suspense account" or by any other name.

28.3.3 Dividends [Section 194]

(1) Dividends declared, distributed or paid by a domestic company are exempt in the hands of the shareholder under section 10(34). This includes deemed dividend under sections 2(22)(a) to (d). This is because such dividend attracts dividend distribution tax @ 15% in the hands of the company.

(2) The TDS provisions under this section are attracted only in respect of deemed dividend referred to in section 2(22)(e), if such dividend exceeds Rs.2,500 in a year.

(3) The rate of deduction of tax in respect of such dividend is 10%.

(4) Individual shareholders, who are residents in India are entitled to receive their dividends from any domestic company without deduction of tax at source by the company in cases where -

- (i) the amount of dividend income received from the company does not exceed Rs.2500 during the year; and
- (ii) the dividend is paid by an account payee cheque.

The TDS provisions will not apply to dividend receivable by LIC, GIC, its subsidiaries or any other insurer provided the shares are owned by them, or they have full beneficial interest in such shares.

28.3.4 Interest other than interest on securities [Section 194A]

This section deals with the scheme of deduction of tax at source from interest other than interest on securities. The main provisions are the following:

(1) This section applies only to interest, other than "interest on securities", credited or paid by assesseees other than individuals or Hindu undivided families not subject to tax audit under section 44AB in the immediately preceding financial year. In other words, individuals and HUFs subject to tax audit in the immediately preceding financial year, companies, firms, association of persons, local authorities and artificial juridical persons are under a legal obligation to deduct tax at source in respect of the interest other than "interest on securities" paid by them.

(2) These provisions apply only to interest paid or credited to residents. In respect of payments to non-residents, the provisions are contained under section 195.

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(3) The deduction of tax must be made at the time of crediting such interest to the payee or at the time of its payment in cash or by any other mode, whichever is earlier.

(4) Where any such interest is credited to any account in the books of account of the person liable to pay such income, such crediting is deemed to be credit of such income to the account of the payee and the tax has to be deducted at source.

(5) The account to which such interest is credited may be called "Interest Payable account" or "Suspense account" or by any other name.

(6) The deduction of tax at source is to be made in all cases where the amount of income by way of interest or, as the case may be, the aggregate of the amounts of interest credited or paid or likely to be credited or paid during the financial year to the account of or to the payee or any other person on his behalf is more than Rs.5,000.

(7) The rate at which the deduction is to be made are given in Part II of the First Schedule to the Annual Finance Act. *The rate at which tax is to be deducted is 10% both in the case of resident non-corporate assessees and domestic companies.*

(8) No deduction of tax shall be made in the following cases:

(a) If the aggregate amount of interest paid or credited during the financial year does not exceed Rs.5,000.

This limit is increased to Rs.10,000 in respect of interest paid on –

- (i) time deposits with a banking company;
- (ii) time deposits with a co-operative society engaged in banking business; and
- (iii) deposits with post office under notified schemes.

In all other cases, the limit would continue to be Rs.5,000.

The limit will be calculated with respect to income credited or paid by a branch of a bank or a co-operative society or a public company in case of:

- (i) time deposits with a bank
- (ii) time deposits with a co-operative society carrying on the business of banking; and
- (iii) deposits with housing finance companies, provided:
 - they are public companies formed and registered in India
 - their main object is to carry on the business of providing long-term finance for construction or purchase of houses in India for residential purposes.

The above ceiling will operate:

- (i) on a branch of a bank;
- (ii) with reference to only time deposits.

Hence, the interest on all other types of account such as savings account, recurring deposits etc., payable by a branch will have to be excluded to determine whether the interest exceeds Rs.5,000 or not. However, in respect of time deposits, interest on all such time deposits maintained with a branch has to be aggregated.

- (b) Interest paid or credited by a firm to any of its partners;
- (c) Interest paid or credited by a co-operative society to a member thereof or any other co-operative society;
- (d) Interest paid or credited in respect of deposits under any scheme framed by the Central Government and notified by it in this behalf;
- (e) Interest income credited or paid in respect of deposits (other than time deposits made on or after 1.7.1995) with
 - (i) a bank to which the Banking Regulation Act, 1949 applies; or
 - (ii) a co-operative society engaged in carrying on the business of banking.
- (f) Interest credited or paid in respect of deposits with primary agricultural credit society or a primary credit society or a co-operative land mortgage bank or a co-operative land development bank.
- (g) Interest income credited or paid by the Central Government under any provisions of the Income-tax Act, the Estate Duty Act, the Wealth-tax Act, the Gift-tax Act, the Companies (Profits) Surtax Act or the Interest Tax Act.
- (h) Interest paid or credited to the following entities:
 - (1) banking companies, or co-operative societies engaged in the business of banking, including co-operative land mortgage banks;
 - (2) financial corporations established under any Central, State or Provincial Act.
 - (3) the Life Insurance Corporation of India.
 - (4) companies and co-operative societies carrying on the business of insurance.
 - (5) the Unit Trust of India; and
 - (6) notified institution, association, body or class of institutions, associations or bodies.
- (i) income credited or paid by way of interest on the compensation amount awarded by the Motor Accidents Claims Tribunal where the amount of such income or, as the case may be, the aggregate of the amounts of such income credited or paid during the financial year does not exceed Rs.50,000.
- (j) income paid or payable by an infrastructure capital company or infrastructure capital fund or public sector company in relation to a zero coupon bond issued on or after 1.6.2005 (Refer chapter 1 for definitions of infrastructure capital company and infrastructure capital

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fund as per sections 2(26A) and 2(26B), respectively)

(9) The expression “time deposits” [for the purpose of (8)(a) above] means the deposits, excluding recurring deposits, repayable on the expiry of fixed periods.

(10) The time for making the payment of tax deducted at source would reckon from the date of credit of interest made constructively to the account of the payee.

(11) The following table shows the applicability of section 194A to various banks/co-operative societies:

Sl.No.	Entity	Nature of deposit	
		Term deposit	Other deposit
1.	Banking company to which Banking Regulation Act, 1949 applies	Applicable	N.A.
2.	Any bank or banking institution to which the Banking Regulation Act, 1949 applies	Applicable	N.A.
3.	Primary agriculture credit society	N.A.	N.A.
4.	Co-operative land mortgage bank	N.A.	N.A.
5.	Co-operative land development bank	N.A.	N.A.
6.	Any other co-operative society engaged in the business of banking.	Applicable	N.A.

28.3.5 Winnings from lotteries, crossword puzzles and horse races [Sections 194B and 194BB]

(1) Any income of a casual and non-recurring nature of the type of winnings from lotteries, crossword puzzles, card game and other game of any sort, races including horse races, etc. will be charged to income-tax at a flat rate of 30% [Section 115BB].

(2) According to the provisions of section 194B, every person responsible for paying to any person, whether resident or non-resident, any income by way of winnings from lottery or crossword puzzle or card game and other game of any sort, is required to deduct income-tax therefrom at the rate of 30% if the amount of payment exceeds Rs.5,000.

(3) Further, in a case where the winnings are wholly in kind or partly in cash and partly in kind but the part in cash is not sufficient to meet the liability of deduction of tax in respect of whole of the winnings, the person responsible for paying shall, before releasing the winnings, ensure that tax has been paid in respect of the winnings.

(4) Section 194BB casts responsibility on the following persons to deduct tax at source -

- (i) a bookmaker; or
 - (ii) a person to whom a licence has been granted by the Government under any law for the time being in force -
 - (a) for horse racing in any race course; or
 - (b) for arranging for wagering or betting in any race course.
- (5) The obligation to deduct tax at source under section 194BB arises when the abovementioned persons make payment of any income by way of winnings from any horse race in excess of Rs.2,500. The rate applicable for deduction of tax at source is 30%.
- (6) Tax will have to be deducted at source from winnings from horse races even though the winnings may be paid to the person concerned in installments of less than Rs.2,500. Similarly, in cases where the book-maker or other person responsible for paying the winnings, credits such winnings and debits the losses to the individual account of the punter, the set off of the loss against the income would be treated for this purpose as a constructive payment of the income.
- (7) In the context of the provisions of section 194BB, the expression 'any horse race' used therein must be taken to include, wherever the circumstances so necessitate, more than one horse race. Therefore, winnings by way of jack pot would also fall within the scope of section 194BB.

28.3.6 Payments to contractors and sub-contractors [Section 194C]

- (1) Section 194C provides for deduction of tax at source from the payment made to resident contractors and sub-contractors.
- (2) Any person responsible for paying any sum to a resident contractor for carrying out any work or supplying labour for carrying out any work (including supply of labour for carrying out any work) in pursuance of a contract between the contractor and the Central Government, a State Government, local authority, statutory corporation, a company, co-operative society, any statutory authority dealing with housing accommodation, any society registered under the Societies Registration Act, 1860, any trust or any university or any firm or any Government of a foreign State or foreign enterprise or any association or body established outside India or an individual, HUF, AOP or BOI subject to tax audit under section 44AB in the immediately preceding financial year must deduct income-tax at the prescribed rate from such sum at the time of credit or payment, whichever is earlier.

Payments made by Individuals, HUFs, AOPs and BOIs to a contractor would attract TDS if their total sales/turnover exceeds Rs.40 lakh (in case of business) and gross receipts exceed Rs.10 lakh (in case of profession) in the immediately preceding financial year. However, relief has been provided in respect of payments made by individuals/HUFs to a contractor exclusively for personal purposes.

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- (3) The prescribed rate is 1% in the case of advertising and 2% in any other case.
- (4) A contractor, not being an individual or a Hindu undivided family, will in the following cases, be required to deduct tax at the rate of 1% at the time of credit or payment, whichever is earlier, to a resident sub-contractor -
- (i) Where the contractor enters into an agreement with the sub-contractor for carrying out or for the supply of labour for carrying out the whole or any part of his work.
- (ii) Where the contractor enters into an agreement with the sub-contractor for supply of labour, either wholly or partly, which the contractor has undertaken to supply.
- (5) *The rate of TDS under section 194C on payments to contractors has been reduced with effect from 1.10.2009 to 1%, where the payee is an individual or HUF and would remain @2% in respect of other payees. The same rates of TDS would apply for both contractors and sub-contractors. These rates would apply for advertising contracts as well.*
- (6) *Further, in respect of payment to transport contractors and sub-contractors engaged in the business of plying, leasing and hiring goods carriages, TDS provisions would not apply if they furnish their PAN to the deductor. However, if they do not quote PAN, the rate will be 1% for an individual/ HUF transporter and 2% for other transporters upto 31.3.2010.*
- (7) *The following table shows a comparison of TDS rates prevalent upto 30.9.2009 vis a vis the rates applicable from 1.10.2009 –*

Payee	TDS rate applicable	
	Up to 30.9.2009	From 1.10.2009
Individual / HUF contractor	2%	1%
Other than individual / HUF contractor	2%	2%
Individual / HUF sub-contractor	1%	1%
Other than individual / HUF sub-contractor	1%	2%
Individual / HUF contractor/sub-contractor for advertising	1%	1%
Other than individual / HUF contractor/sub-contractor for advertising	1%	2%
Contractor in transport business	2%	Nil
Sub-contractor in transport business	1%	Nil

- (8) No deduction will be required to be made if the consideration for the contract does not exceed Rs.20,000. However, to prevent the practice of composite contracts being split up into contracts valued at less than Rs.20,000 to avoid tax deduction, it has been

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provided that tax will be required to be deducted at source where the amount credited or paid or likely to be credited or paid to a contractor or sub-contractor exceeds Rs.20,000 in a single payment or Rs.50,000 in the aggregate during a financial year.

(9) Work includes –

- (a) advertising;
- (b) broadcasting and telecasting including production of programmes for such broadcasting or telecasting;
- (c) carriage of goods or passengers by any mode of transport other than by railways;
- (d) catering;
- (e) *manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer.*

However, “work” shall not include manufacturing or supplying a product according to the requirement or specification of a customer by using raw material purchased from a person, other than such customer, as such a contract is a contract for ‘sale’. However, this will not be applicable to a contract which does not entail manufacture or supply of an article or thing (e.g. a construction contract).

It may be noted that the term “work” would include manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer. In such a case, tax shall be deducted on the invoice value excluding the value of material purchased from such customer if such value is mentioned separately in the invoice. Where the material component has not been separately mentioned in the invoice, tax shall be deducted on the whole of the invoice value.

(10) *No deduction is required to be made from the sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor, during the course of the business of plying, hiring or leasing goods carriages, if he furnishes his PAN to the deductor.*

(11) However, for this purpose, it is necessary to produce a declaration within the prescribed time to the concerned person paying or crediting such sum. Such declaration should be in the prescribed form and manner.

(12) Goods carriage means -

- (i) any motor vehicle constructed or adapted for use solely for the carriage of goods; or
- (ii) any motor vehicle not so constructed or adapted, when used for the carriage of goods.

The term “motor vehicle” does not include vehicles having less than four wheels and with engine capacity not exceeding 25cc as well as vehicles running on rails or vehicles adapted for use in a factory or in enclosed premises.

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(13) The substance of the provisions is explained hereunder:

- (i) The deduction of income-tax at source from payments made to non-resident contractors will be governed by the provisions of section 195.
- (ii) The deduction of income-tax will be made from sums paid for carrying out any work or for supplying labour for carrying out any work. In other words, the section will apply only in relation to 'works contracts' and 'labour contracts' and will not cover contracts for sale of goods.
- (iii) Contracts for rendering professional services by lawyers, physicians, surgeons, engineers, accountants, architects, consultants etc., can not be regarded as contracts for carrying out any "work" and, accordingly, no deduction of income-tax is to be made from payments relating to such contracts under this section. Separate provisions for fees for professional services have been made under section 194J.
- (iv) The deduction of income-tax must be made at the time of credit of the sum to the account of the contractor, or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier.
- (v) **Circular No.13/2006, dated 13.12.2006 - Applicability of TDS provisions of section 194C on contract for fabrication of article or thing as per specifications given by the assessee**

The CBDT has clarified the issue regarding the applicability of TDS provisions of section 194C on contract for fabrication of article or thing as per specifications given by the assessee. The CBDT observed that before taking a decision on the applicability of TDS under section 194C on a contract, it would have to be examined whether the contract in question is a contract for work or a contract for sale.

The CBDT clarified that the provisions of section 194C would apply in respect of a contract for supply of any article or thing as per prescribed specifications only if it is a contract for work and not a contract for sale as per the principles in this regard laid down in para 7(vi) of Circular No. 681, dated 8-3-1994. Para 7(vi) of Circular No.681 clarifies that where the property in the article or thing so fabricated passes from the fabricator-contractor to the assessee only after such article or thing is delivered to the assessee, such contract would be a contract of sale and would, therefore, fall outside the purview of section 194C.

28.3.7 Insurance commission [Section 194D]

- (1) Section 194D casts responsibility on any person responsible for paying to a resident any income by way of remuneration or reward.
- (2) Such income may be by way of insurance commission or other remuneration in consideration for soliciting or procuring insurance business (including the business relating to the continuance, renewal or revival of policies of insurance).

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(3) *Such person is required to deduct income-tax at the rate of 10%, both in the case of resident non-corporate assessees and domestic companies.*

(4) The deduction is to be made at the time of the credit of the income to the account of the payee or at the time of making the payment (by whatever mode) to the payee, whichever is earlier.

(5) The tax under this section has to be deducted at source only if the amount of such income or the aggregate of the amounts of such income credited or paid during the financial year to the account of the payee exceeds Rs.5000.

28.3.8 Payments to non-resident sportsmen or sports association [Section 194E]

(1) This section provides for deduction of tax at source in respect of any income referred to in section 115BBA payable to a non-resident sportsman (including an athlete) who is not a citizen of India or a non-resident sports association or institution.

(2) Deduction of tax at source @10% should be made by the person responsible for making the payment.

(3) Such tax deduction should be at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier.

(4) The following are the income referred to in section 115BBA -

- (i) income received or receivable by a non-resident sportsman (including an athlete) by way of -
 - (a) participation in any game or sport in India (However, games like crossword puzzles, horse races etc. taxable under section 115BB are not included herein); or
 - (b) advertisement; or
 - (c) contribution of articles relating to any game or sport in India in newspapers, magazines or journals.
- (ii) Guarantee amount paid or payable to a non-resident sports association or institution in relation to any game or sport played in India. However, games like crossword puzzles, horse races etc. taxable under section 115BB are not included herein.

28.3.9 Payments in respect of deposits under National Savings Scheme etc. [Section 194EE]

(1) The person responsible for paying any amount from National Savings Scheme Account under section 80CCA shall deduct income-tax thereon at the rate of 20% at the time of payment.

(2) However, no such deduction shall be made where the amount of payment or the aggregate amount of payments in a financial year is less than Rs.2,500.

(3) The provisions of this section shall not apply to the payments made to the heirs of the assessee.

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28.3.10 Repurchase of units by Mutual Fund or Unit Trust of India [Section 194F]

A person responsible for paying to any person any amount on account of repurchase of units covered under section 80CCB(2) shall deduct tax at source at the rate of 20% at the time of payment of such amount.

28.3.11 Commission etc. on the sale of lottery tickets [Section 194G]

(1) Under section 194G, the person responsible for paying any income by way of commission, remuneration or prize (by whatever name called) on lottery tickets in an amount exceeding Rs.1,000 shall deduct income-tax thereon at the rate of 10%.

(2) Such deduction should be made at the time of credit of such income to the account of the payee or at the time of payment of such income by cash, cheque, draft or any other mode, whichever is earlier.

(3) Where any such income is credited to any account, whether called "Suspense Account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section shall apply accordingly.

28.3.12 Commission or brokerage [Section 194H]

(1) Any person, not being an individual or a Hindu undivided family not subject to tax audit under section 44AB in the immediately preceding financial year, who is responsible for paying any income by way of commission (other than insurance commission) or brokerage to a resident shall deduct income tax at the rate of 10%.

(2) The deduction shall be made at the time such income is credited to the account of the payee or at the time of payment in cash or by issue of cheque or draft or by any other mode, whichever is earlier.

(3) Even where income is credited to some other account, whether called "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit to the account of the payee for the purposes of this section.

(4) No deduction is required if the amount of such income or the aggregate of such amount does not exceed Rs.2,500 during the financial year.

(5) "Commission or brokerage" includes any payment received or receivable, directly or indirectly, by a person acting on behalf of another person for services rendered, or for any services in the course of buying or selling of goods, or in relation to any transaction relating to any asset, valuable article or thing, other than securities.

(6) However, this section is not applicable to professional services. "Professional Services" means services rendered by a person in the course of carrying on legal, medical,

engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or such other profession as notified by the CBDT for the purpose of compulsory maintenance of books of account under section 44AA.

(7) Further, there would be no requirement to deduct tax at source on commission or brokerage payments by BSNL or MTNL to their public call office (PCO) franchisees.

28.3.13 Rent [Section 194-I]

(1) Any person, other than an individual or a HUF not subject to tax audit under section 44AB in the immediately preceding year, who is responsible for paying to a resident any income by way of rent shall deduct income tax at the rate of:

- (i) 15%, if the payee is an individual or HUF, and
- (ii) 20% in other cases.

(2) The rate of tax deduction would be 10% in respect of rental payments for use of plant, machinery and equipment, irrespective of whether the payee is an individual/HUF, firm, company or any other person.

(3) The rate of TDS under section 194-I has been reduced from 10% to 2% in respect of rent for plant, machinery or equipment and from 15%/20% to 10% in respect of other rental payments with effect from 1st October, 2009.

(4) This deduction is to be made at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of cheque or draft or by any other mode, whichever is earlier.

(5) No deduction need be made where the amount of such income or the aggregate of the amounts of such income credited or paid or likely to be credited or paid during the financial year to the account of the payee does not exceed Rs.1,20,000.

(6) "Rent" means any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of (either separately or together) any –

- (a) land; or
- (b) building (including factory building); or
- (c) land appurtenant to a building (including factory building); or
- (d) machinery; or
- (e) plant; or
- (f) equipment; or
- (g) furniture; or
- (h) fittings,

whether or not any or all of the above are owned by the payee.

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(7) Where any such income is credited to any account, whether called "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee and the provisions of this section will apply accordingly.

Applicability of TDS provisions under section 194-I to payments made by the customers on account of cooling charges to the cold storage owners.

CBDT Circular No.1/2008 dated 10.1.2008 provides clarification regarding applicability of provisions of section 194-I to payments made by the customers on account of cooling charges to the cold storage owners.

The main function of the cold storage is to preserve perishable goods by means of a mechanical process, and storage of such goods is only incidental in nature. The customer is also not given any right to use any demarcated space/place or the machinery of the cold store and thus does not become a tenant. Therefore, the provisions of 194-I are not applicable to the cooling charges paid by the customers of the cold storage.

However, since the arrangement between the customers and cold storage owners are basically contractual in nature, the provision of section 194-C will be applicable to the amounts paid as cooling charges by the customers of the cold storage.

Applicability of TDS provisions under section 194-I to service tax component of rental income

CBDT Circular No.4/2008 dated 28.4.2008 provides clarification on deduction of tax at source (TDS) on service tax component of rental income under section 194-I.

As per the provisions of 194-I, tax is deductible at source on income by way of rent paid to any resident. Further, rent has been defined in 194-I to mean any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of (either separately or together) any,-

- (a) land; or
- (b) building (including factory building); or
- (c) land appurtenant to a building (including factory building); or
- (d) machinery; or
- (e) plant; or
- (f) equipment; or
- (g) furniture; or
- (h) fittings,

whether or not any or all of the above are owned by the payee.

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Service tax paid by the tenant doesn't partake the nature of income of the landlord. The landlord only acts as a collecting agency for Government for collection of service tax. Therefore, tax deduction at source under section 194-I would be required to be made on the amount of rent paid/payable without including the service tax.

28.3.14 Fees for professional or technical services [Section 194J]

(1) Every person, other than an individual or Hindu undivided family not subject to tax audit under section 44AB in the immediately preceding financial year, who is responsible for paying to a resident any sum by way of fees for professional services or fees for technical services or royalty or non-compete fees referred to in section 28(va) shall deduct tax at source at the rate of 10%.

(2) The deduction is to be made at the time of credit of such sum to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier.

(3) No tax deduction is required if the amount of fees or the aggregate of the amounts of fees credited or paid or likely to be credited or paid during a financial year does not exceed Rs.20,000 in the case of fees for professional services, Rs.20,000 in the case of fees for technical services, Rs.20,000 in the case of royalty and Rs.20,000 in the case of non-compete fees. If A Ltd. pays Rs.17,000 towards fees for professional services, Rs.14,000 towards fees for technical services and Rs.19,000 towards royalty to a resident individual, say Mr.X, during the P.Y.2009-10, there would be no liability to deduct tax at source under section 194J since payment for each individual service does not exceed Rs.20,000 during the year.

(4) An individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB of the Income-tax Act during the financial year immediately preceding the financial year in which such sum by way of fees for professional or technical services is credited or paid shall be liable to deduct income-tax under this sub-section.

(5) However, such individual or Hindu Undivided family, shall not be liable deduct income-tax on the sum payable by way of fees for professional services, in case such sum is credited or paid exclusively for personal purposes.

(6) Where any fees for professional or technical services is credited to any account, whether called suspense account or by any other name, in the books of accounts of the person liable to pay such sum, such crediting shall be deemed to be credit of such sum to the account of the payee and tax has to be deducted accordingly.

(7) "Professional services" means services rendered by a person in the course of carrying on legal, medical, engineering or architectural profession or the profession of

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accountancy or technical consultancy or interior decoration or advertising or such other profession as is notified by the CBDT for the purposes of section 44AA or of this section.

(8) Other professions notified for the purposes of section 44AA are as follows:

- (a) Profession of “authorised representatives”;
- (b) Profession of “film artist”;
- (c) Profession of “company secretary”.

(9) *The CBDT has notified the services rendered by following persons in relation to the sports activities as Professional Services for the purpose of the section 194J:*

- (a) *Sports Persons,*
- (b) *Umpires and Referees,*
- (c) *Coaches and Trainers,*
- (d) *Team Physicians and Physiotherapists,*
- (e) *Event Managers,*
- (f) *Commentators,*
- (g) *Anchors and*
- (h) *Sports Columnists.*

(10) Accordingly, the requirement of TDS as per section 194J would apply to all the aforesaid professions. The term “profession”, as such, is of a very wide import. However, the term has been defined in this section exhaustively. For the purposes of TDS, therefore, all other professions would be outside the scope of section 194J. For example, this section will not apply to professions of teaching, sculpture, painting etc. unless they are notified.

(11) Explanation (b) to section 194J provides that the term ‘fees for technical services’ shall have the same meaning as in Explanation 2 to section 9(1) (vii). The term ‘fees for technical services’ as defined in Explanation 2 to section 9(i)(vii) means any consideration (including any lump sum consideration) for rendering of any of the following services:

- (i) Managerial services;
- (ii) Technical services;
- (iii) Consultancy services;
- (iv) Provision of services of technical or other personnel.

It is expressly provided that the term ‘fees for technical services’ will not include following types of consideration:

- (i) Consideration for any construction, assembly, mining or like project, or
- (ii) Consideration which is chargeable under the head ‘Salaries’.

28.3.15 Payment of compensation on acquisition of certain immovable property [Section 194LA]

(1) Section 194LA provides for deduction of tax at source by a person responsible for paying to a resident any sum in the nature of –

- (i) compensation or the enhanced compensation or
- (ii) the consideration or the enhanced consideration

on account of compulsory acquisition, under any law for the time being in force, of any immovable property (other than agricultural land).

(2) Immovable property means any land (other than agricultural land) or any building or part of a building.

(3) The amount of tax to be deducted is 10% of such sum mentioned in (1) above.

(4) The tax should be deducted at the time of payment of such sum in cash or by issue of a cheque or draft or by any other mode, whichever is earlier.

(5) No tax is required to be deducted where the amount of such payment or, as the case may be, the aggregate amount of such payments to a resident during the financial year does not exceed Rs.1 lakh.

28.3.16 Other sums (payable to non-residents) [Section 195]

(1) Any person responsible for paying interest or any other sum chargeable to tax (other than salaries) to a non-resident or to a foreign company is liable to deduct tax at source at the rates prescribed by the relevant Finance Act. Such persons are also required to furnish the information relating to payment of any sum in such form and manner as may be prescribed by the CBDT.

(2) In order to subject an item of income to deduction of tax under this section the payee must be a non-resident or a foreign company.

(3) The tax is to be deducted at source at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier.

(4) Where any interest or other sum as aforesaid is credited to any account, whether called "Interest payable account" or "Suspense account" or by any other name, in the books of account of the person liable to pay such income, such crediting shall be deemed to be credit of such income to the account of the payee.

(5) The statutory obligation imposed under this section would apply for the purpose of deduction of tax at source from any sum being income assessable to tax (other than salary income) in the hands of the non-resident/foreign company. However, no deduction shall be made in respect of any dividends declared/distributed/paid by a domestic company, which is exempt in the hands of the shareholders under section 10(34).

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(6) Payment to a non-resident by way of royalties and payments for technical services rendered in India are common examples of sums chargeable under the provisions of the Act to which the liability for deduction of tax at source would apply.

(7) In the case of interest payable by the Government or a public sector bank within the meaning of section 10(23D) or a public financial institution within the meaning of section 10(23D), deduction of tax shall be made only at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode.

28.3.17 TDS on income from Deep Discount Bonds

(1) The tax treatment of income from Deep Discount Bonds has been explained in the CBDT's Circular No.2/2002 dated 15.2.2002.

(2) Circular No.4/2004 dated 13.5.2004 issued by the CBDT clarifies that tax is required to be deducted at source under section 193 or 195, as the case may be, only at the time of redemption of such bonds, irrespective of whether the income from the bonds has been declared by the bond-holder on accrual basis from year to year or is declared only in the year of redemption.

(3) A person, who has declared the income from a Deep Discount Bond on annual accrual basis during the term of the bond, is entitled to make an application under section 197, requesting the Assessing Officer to issue a certificate for no deduction of tax or deduction at a lower rate. In such a case, the assessee should furnish, along with the prescribed Form No.13, details of the income offered for tax by him from year to year.

(4) In case the assessee is not the original subscriber, and has acquired the bonds from some other person, he shall furnish the relevant particulars including the name, address and PAN, of such other person.

(5) If the Assessing Officer is satisfied that the applicant assessee has declared his income from the bonds from year to year on accrual basis during the period the bond was held by him, he shall issue a certificate allowing the tax deduction at source at such reduced rate as is justified by the total income of the applicant in the year of redemption.

(6) An assessee, being a resident individual, who is the original subscriber of a Deep Discount Bond, may furnish a declaration in Form No.15H in the year of redemption in accordance with section 197A, if he has been declaring income on the bond from year to year on accrual basis, and no tax is payable on his total income, including the interest accruing during that year.

(7) However, such a declaration cannot be filed by an individual, other than a senior citizen being a resident individual of the age of 65 years or more during the relevant previous year, if the amount of accumulated interest, being paid on redemption, exceeds the maximum amount not chargeable to tax in his case.

28.3.18 Income payable net of tax [Section 195A]

(1) Where, under an agreement or other arrangement, the tax chargeable on any income referred to in the foregoing provisions of this Chapter is to be borne by the person by whom the income is payable, then, for the purposes of deduction of tax under those provisions such income shall be increased to such amount as would, after deduction of tax thereon, be equal to the net amount payable under such agreement or arrangement.

(2) However, no grossing up is required in the case of tax paid [under section 192(1A)] by an employer on the non-monetary perquisites provided to the employee

28.3.19 Interest or dividend or other sums payable to Government, Reserve Bank or certain corporations [Section 196]

(1) No deduction of tax shall be made by any person from any sums payable to -

- (i) the Government; or
- (ii) the Reserve Bank of India; or
- (iii) a corporation established by or under a Central Act, which is, under any law for the time being in force, exempt from income-tax on its income; or
- (iv) a Mutual Fund specified under section 10(23D).

(2) This provision for non-deduction is when such sum is payable to the above entities by way of -

- (i) interest or dividend in respect of securities or shares -
 - (a) owned by the above entities; or
 - (b) in which they have full beneficial interest or
- (ii) any income accruing or arising to them.

28.4 CERTIFICATE FOR DEDUCTION OF TAX AT A LOWER RATE [SECTION 197]

(1) This section applies where, in the case of any income of any person or sum payable to any person, income-tax is required to be deducted at the time of credit or payment, as the case may be at the rates in force as per the provisions of sections 192, 193, 194, 194A, 194C, 194D, 194G, 194H, 194-I, 194J, 194K, 194LA and 195.

(2) In such cases, the assessee can make an application to the Assessing Officer for deduction of tax at a lower rate or for non-deduction of tax.

(3) If the Assessing Officer is satisfied that the total income of the recipient justifies the deduction of income-tax at lower rates or no deduction of income-tax, as the case may be, he may give to the assessee such certificate, as may be appropriate.

(4) Where the Assessing Officer issues such a certificate, then the person responsible

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for paying the income shall deduct income-tax at such lower rates specified in the certificate or deduct no tax, as the case may be, until such certificate is cancelled by the Assessing Officer.

(5) Enabling powers have been conferred upon the CBDT to make rules for prescribing the procedure in this regard.

(6) *The CBDT has, in exercise of the powers conferred under section 119(1) of the Income-tax Act, 1961, directed that corporations which are established by a Central, State or Provincial Act for the welfare and economic upliftment of ex-servicemen and whose income qualifies for exemption from income-tax under section 10(26BBB) would also be exempt from tax deduction/collection at source on their receipts. This exemption shall be valid for 3 years from the date of issue of this order i.e., from 1.8.2008. However, this exemption shall not absolve such organisation from their statutory obligation of deducting TDS on all contractual payments made by them to other parties including sub-contractors etc.*

28.5 NO DEDUCTION IN CERTAIN CASES [SECTION 197A]

(1) This section enables an individual, who is resident in India and whose estimated total income of the previous year is less than the basic exemption limit, to receive dividends and any sum out of National Savings Scheme Account, without deduction of tax at source under sections 194 and 194EE, on furnishing a declaration in duplicate in the prescribed form and verified in the prescribed manner [Sub-section (1)].

(2) The declaration in the above form is to be furnished by the declarant to the person responsible for paying any income of the nature referred to in sections 194 or 194EE. The declaration will have to be to the effect that the tax on the estimated total income of the declarant of the previous year in which such income is to be included in computing his total income will be nil [Sub-section (1)].

(3) No deduction of tax shall be made under sections 193 or 194A or 194K, where a person, who is not a company or a firm, furnishes to the person responsible for paying any income of the nature referred to in section 193 or 194A or 194K, a declaration in writing in duplicate in the prescribed form to the effect that the tax on his estimated total income of the previous year in which such income is to be included in computing his total income will be nil [Sub-section (1A)].

(4) The provisions of this section will, however, not apply where -

- (i) the amount of any income from dividends,
- (ii) payments in respect of deposits under National Savings Schemes, etc. or
- (iii) income from interest on securities or interest other than "interest on securities" or units or
- (iv) the aggregate of the amounts of such incomes in (1), (2) and (3) above credited or paid or likely to be credited or paid during the previous year in which such income is to be

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included exceeds the maximum amount which is not chargeable to income-tax [Sub-section (1B)].

(5) For a senior citizen, who is of the age of 65 years or more at any time during the previous year, no deduction of tax shall be made under section 193 or section 194 or section 194A or section 194EE or section 194K, if they furnish a declaration in writing to the payer, of any amount or income mentioned in the above sections [Sub-section (1C)].

(6) Such declaration should be in duplicate in the prescribed form and verified in the prescribed manner to the effect that the tax on his estimated total income of the previous year in which such income is to be included in computing his total income will be nil. The restriction contained in sub-section (1B) will not apply to senior citizens [Sub-section (1C)].

(7) No deduction of tax shall be made by an Offshore Banking Unit from the interest paid on-

(i) deposit made by a non-resident/not-ordinarily resident on or after 1.4.2005; or

(ii) borrowing from a non-resident/not-ordinarily resident on or after 1.4.2005.

This provision is contained in sub-section (1D).

(8) On receipt of the declaration referred to in sub-section (1), (1A) or (1C), the person responsible for making the payment will be required to deliver or cause to be delivered to the Chief Commissioner or Commissioner, one copy of the declaration on or before the 7th day of the month following the month in which the declaration is furnished to him [Section 197A(2)].

28.6 MISCELLANEOUS PROVISIONS

28.6.1 Tax deducted is income received [Section 198]

(1) All sums deducted in accordance with the foregoing provisions shall, for the purpose of computing the income of an assessee, be deemed to be income received.

(2) However, the tax paid by an employer under sub-section (1A) of section 192 on non-monetary perquisites provided to the employees, shall not be deemed to be income received by the assessee.

28.6.2 Credit for tax deducted at source [Section 199]

(1) Tax deducted at source in accordance with the above provisions and paid to the credit of the Central Government shall be treated as payment of tax on behalf of the-

(i) person from whose income the deduction was made; or

(ii) owner of the security; or

(iii) depositor; or

(iv) owner of property; or

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(v) unit-holder; or

(vi) shareholder.

(2) Any sum referred to in sub-section (1A) of section 192 and paid to the Central Government, shall be treated as the tax paid on behalf of the person in respect of whose income, such payment of tax has been made.

(3) The CBDT is empowered to frame rules for the purpose of giving credit in respect of tax deducted or tax paid under Chapter XVII. The CBDT also has the power to make rules for giving credit to a person other than the persons mentioned in (1) and (2) above. Further, the CBDT can specify the assessment year for which such credit may be given.

(4) *Accordingly, Rule 37BA providing for credit for tax deducted at source for the purposes of section 199 has been inserted with effect from 1.4.2009.*

Sub-rule (1) provides that credit for tax deducted at source and paid to the Central Government in accordance with the provisions of Chapter XVII, shall be given to the person to whom payment has been made or credit has been given (i.e., the deductee) on the basis of information relating to deduction of tax furnished by the deductor to the income-tax authority or the person authorised by such authority.

Sub-rule (2) provides that if the income on which tax has been deducted at source is assessable in the hands of a person other than the deductee, credit for tax deducted at source shall be given to the other person in cases where-

(a) the income of the deductee is included in the total income of another person under the provisions of section 60, section 61, section 64, section 93 or section 94;

(b) the income of a deductee being an association of persons or a trust is assessable in the hands of members of the association of persons, or in the hands of trustees, as the case may be;

(c) the income from an asset held in the name of a deductee, being a partner of a firm or a karta of a Hindu undivided family, is assessable as the income of the firm, or Hindu undivided family, as the case may be;

(d) the income from a property, deposit, security, unit or share held in the name of a deductee is owned jointly by the deductee and other persons and the income is assessable in their hands in the same proportion as their ownership of the asset:

However, in such cases, the deductee should file a declaration with the deductor. Such declaration filed by the deductee should contain the name, address, permanent account number of the person to whom credit is to be given, payment or credit in relation to which credit is to be given and reasons for giving credit to such person.

Also, the deductor should report the tax deduction in the name of the other person in the information relating to deduction of tax referred to in sub-rule (1). The deductor should

issue the certificate for deduction of tax at source in the name of the person in whose name credit is shown in the information relating to deduction of tax referred to in sub-rule (1) and should keep the declaration in his safe custody.

Sub-rule (3) provides that the credit for tax deducted at source and paid to the Central Government, shall be given for the assessment year for which such income is assessable. Where tax has been deducted at source and paid to the Central Government and the income is assessable over a number of years, credit for tax deducted at source shall be allowed across those years in the same proportion in which the income is assessable to tax.

Sub-rule (4) provides that credit for tax deducted at source and paid to the account of the Central Government shall be granted on the basis of –

- (i) the information relating to deduction of tax furnished by the deductor to the income-tax authority or the person authorized by such authority; and*
- (ii) the information in the return of income in respect of the claim for the credit,*
- (iii) subject to verification in accordance with the risk management strategy formulated by the Board from time to time.*

28.6.3 Duty of person deducting tax [Section 200]

(1) The persons responsible for deducting the tax at source should deposit the sum so deducted to the credit of the Central Government within the prescribed time [Sub-section (1)].

(2) Further, an employer paying tax on non-monetary perquisites provided to employees in accordance with section 192(1A), should deposit within the prescribed time, the tax to the credit of the Central Government or as the Board directs [Sub-section (2)].

(3) Sub-section (3) casts responsibility on the following persons –

- (i) any person deducting any sum on or after 1st April, 2005 in accordance with the foregoing provisions of this chapter; or,
- (ii) any person being an employer referred to in section 192(1A).

(4) These persons are responsible for preparing *such statements for such periods as may be prescribed*, after paying the tax deducted to the credit of the Central Government within the prescribed time.

(5) Such statements have to be delivered or caused to be delivered to the prescribed income-tax authority or the person authorised by such authority.

(6) Such statements should be in the prescribed form and verified in the prescribed manner.

(7) It should set forth such particulars and should be delivered within such time as may be prescribed.

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(8) Penalty of rupees one hundred per day of continuing default would be attracted under section 272A for failure to deliver or cause to be delivered within the prescribed time a copy of the statements as required above.

28.6.4 Correction of arithmetic mistakes and adjustment of incorrect claim during computerized processing of TDS statements [New Section 200A]

(i) *At present, all statements of tax deducted at source are filed in an electronic mode, thereby facilitating computerised processing of these statements.*

(ii) *Therefore, in order to process TDS statements on computer, electronic processing on the same lines as processing of income-tax returns has been provided by insertion of new section 200A with effect from 1st April, 2010.*

(iii) *The following adjustments can be made during the computerized processing of statements of tax deducted at source –*

(1) *any arithmetical error in the statement; or*

(2) *an incorrect claim, if such incorrect claim is apparent from any information in the statement.*

The term “an incorrect claim apparent from any information in the statement” shall mean such claim on the basis of an entry, in the statement, –

(a) *of an item, which is inconsistent with another entry of the same or some other item in such statement;*

(b) *in respect of rate of deduction of tax at source, where such rate is not in accordance with the provisions of the Act.*

(iv) *After making such adjustments, tax and interest [say, under section 201(1A)] would be calculated and sum payable by the deductor or refund due to the deductor will be determined.*

(v) *An intimation will be sent to the deductor, informing him of his tax liability or the refund due, within one year from the end of the financial year in which the statement is filed. The refund due shall be granted to the deductor.*

(vi) *For this purpose, the CBDT is empowered to make a scheme for centralized processing of statements of TDS to determine the tax payable by, or refund due to, the deductor.*

28.6.5 Consequences of failure to deduct or pay [Section 201]

(1) *The following persons shall be deemed to be an assessee in default if they do not deduct the whole or any part of the tax or after deducting fails to pay the tax -*

(i) *any person including the principal officer of a company, who is required to deduct any sum in accordance with the provisions of the Act; and*

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- (ii) an employer paying tax on non-monetary perquisites under section 192(1A).
- (2) However, no penalty shall be charged under section 221 from such person unless the Assessing Officer is satisfied that such person has failed to deduct and pay the tax without good and sufficient reasons.
- (3) Such person shall also be liable to pay simple interest @1% for every month or part of a month. Such interest is chargeable on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually paid.
- (4) Such interest should be paid before furnishing the statements in accordance with section 200(3).
- (5) Where the tax has not been paid after it is deducted, the amount of the tax together with the amount of simple interest thereon shall be a charge upon all the assets of the person or the company, as the case may be.
- (6) *An order under section 201(1) deeming a person to be an assessee-in-default for failure to deduct the whole or any part of the tax from a person resident in India has to be passed within two years from the end of the financial year in which the statement of TDS is filed by the deductor. Where no such statement is filed, such order can be passed up till four years from the end of the financial year in which the payment is made or credit is given.*
- (7) *However, the time limit for passing an order deeming a person to be an assessee-in-default in respect of F.Y.2007-08 and earlier years is 31st March, 2011.*
- (8) *Further, the exclusions from the time limit, as specified in Explanation 1 to section 153, would also apply to the above time limit for passing an order deeming a person to be an assessee-in-default. Also, the time limit would not apply to an order passed consequent to the direction contained in an order of the Commissioner under sections 263 and 264, Commissioner (Appeals) under section 250, Appellate Tribunal under section 254, Supreme Court/ National Tax Tribunal under section 260 and Supreme Court under section 262. Thus, the time limit would be extended where effect is to be given to various appellate proceedings or where proceedings are stayed.*
- (9) Section 201(1) deems a person to be an assessee-in-default if he –
 - (i) does not deduct tax; or
 - (ii) does not pay; or
 - (iii) after so deducting fails to pay

the whole or any part of the tax, as required by or under this Act.

Thus, section 201(1) contemplates three types of defaults. The default contemplated in (ii) is covered by the default contemplated in (iii). However, the time limit has been specified only for passing of orders relating to default contemplated in (i) above. There is no time limit

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specified in respect of the other defaults.

(10) Therefore, no time-limits have been prescribed for the order under section 201(1) where –

- (i) the deductor has deducted but not deposited the tax deducted at source, as this would be a case of defalcation of government dues,*
- (ii) the employer has failed to pay the tax wholly or partly, under sub-section (1A) of section 192, as the employee would not have paid tax on such perquisites,*
- (iii) the deductee is a non-resident as it may not be administratively possible to recover the tax from the non-resident.*

28.6.6 Deduction only one mode of recovery [Section 202]

- (1) Recovery of tax through deduction at source is only one method of recovery.
- (2) The Assessing Officer can use any other prescribed methods of recovery in addition to tax deducted at source.

28.6.7 Certificate for tax deducted [Section 203]

- (1) Every person deducting tax at source shall issue a certificate to the effect that tax has been deducted and specify the amount so deducted, the rate at which tax has been deducted and such other particulars as may be prescribed.
- (2) Every person, being an employer, referred to in sub-section (1A) of section 192 shall, within such period, as may be prescribed, furnish to the person in respect of whose income such payment of tax has been made, a certificate to the effect that tax has been paid to the Central Government, and specify the amount so paid, the rate at which the tax has been paid and such other particulars as may be prescribed.
- (3) However, where tax has been deducted or paid in accordance with the foregoing provisions of this Chapter on or after 1.4.2010, there is no requirement to furnish a certificate for tax deducted under section 203 in respect of such tax deducted or paid on or after 1.4.2010.

28.6.8 Common number for TDS and TCS [Section 203A]

- (1) Persons responsible for deducting tax or collecting tax at source should apply to the Assessing Officer for the allotment of a “tax-deduction and collection-account number”.
- (2) Section 203A(2) enlists the documents/certificates/returns/challans in which the “tax deduction account number” or “tax collection account number” or “tax deduction and collection account number” has to be compulsorily quoted. They are -
 - (i) challans for payment of any sum in accordance with the provisions of section 200 or section 206C(3);
 - (ii) certificates furnished under section 203 or section 206C(5);

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- (iii) statements prepared and delivered or caused to be delivered in accordance with the provisions of section 200(3) or section 206C(3).
- (iv) returns delivered in accordance with the provisions of section 206 or section 206C(5A)/(5B); and
- (v) in all other documents pertaining to such transactions as may be prescribed in the interests of revenue.

28.6.9 Furnishing of statement of tax deducted [Section 203AA]

- (1) This section provides for furnishing of a statement of the tax deducted on or after 1st April, 2008 by the prescribed income-tax authority or the person authorised by such authority referred to in section 200(3)
- (2) Such statement should be prepared and delivered to every person -
 - (a) from whose income, tax has been deducted or
 - (b) in respect of whose income, tax has been paid.
- (3) Such statement should be in the prescribed form specifying the amount of tax deducted or paid and other prescribed particulars.

28.6.10 Person responsible for paying taxes deducted at source [Section 204]

For purposes of deduction of tax at source the expression “person responsible for paying” means:

	Nature of income/payment	Person responsible for paying tax
(1)	Salary (other than payment of salaries by the Central or State Government)	(i) the employer himself; or (ii) if the employer is a company, the company itself, including the principal officer thereof.
(2)	Interest on securities (other than payments by or on behalf of the Central or State Government)	the local authority, corporation or company, including the principal officer thereof.
(3)	Any sum payable to a non-resident Indian, representing consideration for the transfer by him of any foreign exchange asset, which is not a short term capital asset	the authorised dealer responsible for remitting such sum to the non-resident Indian or for crediting such sum to his Non-resident (External) Account maintained in accordance with the Foreign Exchange Regulation Act, 1973 and any rules made thereunder.
(4)	Credit/payment of any other sum chargeable under the provisions of the Act	(i) the payer himself; or (ii) if the payer is a company, the company itself including the principal officer thereof.

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28.6.11 Bar against direct demand on assessee [Section 205]

Where tax is deductible at source under any of the aforesaid sections, the assessee shall not be called upon to pay the tax himself to the extent to which tax has been deducted from that income.

28.6.12 Furnishing of statements in respect of payment of interest to residents without deduction of tax [Section 206A]

(1) This section casts responsibility on every banking company or co-operative society or public company referred to in the proviso to section 194A(3)(i) to prepare *such statements for such period as may be prescribed* –

- if they are responsible for paying to a resident,
- the payment should be of any income not exceeding Rs.10,000, where the payer is a banking company or a co-operative society, and Rs.5,000 in any other case.
- such income should be by way of interest (other than interest on securities)

(2) The statements have to be delivered or caused to be delivered to the prescribed income-tax authority or the person authorised by such authority.

(3) The statements have to be in the prescribed form, verified in the prescribed manner and to be filed within the prescribed time, on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media.

(4) The Central Government may, by notification in the Official Gazette, cast responsibility on any person other than a person mentioned in (1) above.

(5) Such persons would be persons responsible for paying to a resident any income liable for deduction of tax at source.

(6) Such persons are vested with the responsibility to prepare and deliver or cause to be delivered statements within the prescribed time to the prescribed income-tax authority or the person authorized by such authority.

(7) Such statements should be in the prescribed form and verified in the prescribed manner.

(8) Such statements should be on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media.

28.6.13 Mandatory requirement of furnishing PAN in all TDS statements, bills, vouchers and correspondence between deductor and deductee [Section 206AA]

(i) *The non-quoting of PAN by deductees in many cases have led to delay in issue of refund on account of problems in the processing of returns of income and in granting credit for tax deducted at source.*

(ii) *With a view to strengthening the PAN mechanism, section 206AA has been inserted, with*

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effect from 1.4.2010, to provide that any person whose receipts are subject to deduction of tax at source i.e. the deductee, shall mandatorily furnish his PAN to the deductor failing which the deductor shall deduct tax at source at higher of the following rates –

- (1) the rate prescribed in the Act;
- (2) at the rate in force i.e., the rate mentioned in the Finance Act; or
- (3) at the rate of 20%.

For instance, in case of rental payment for plant and machinery, where the payee does not furnish his PAN to the payer, tax would be deductible @20% instead of @2% prescribed under section 194-I. However, non-furnishing of PAN by the deductee in case of income by way of winnings from lotteries, card games etc., would result in tax being deducted at the existing rate of 30% under section 194-B. Therefore, wherever tax is deductible at a rate higher than 20%, this provision would not have any impact.

(iii) Tax would be deductible at the rates mentioned above also in cases where the taxpayer files a declaration in Form 15G or 15H (under section 197A) but does not provide his PAN.

(iv) Further, no certificate under section 197 will be granted by the Assessing Officer unless the application contains the PAN of the applicant.

(v) If the PAN provided to the deductor is invalid or it does not belong to the deductee, it shall be deemed that the deductee has not furnished his PAN to the deductor. Accordingly, tax would be deductible at the rate specified in (ii) above.

(vi) These provisions will also apply to non-residents where tax is deductible on payments or credits made to them.

(vii) Both the deductor and the deductee have to compulsorily quote the PAN of the deductee in all correspondence, bills, vouchers and other documents exchanged between them.

28.7 TAX COLLECTION AT SOURCE [SECTION 206C]

Under section 206C, sellers of certain goods are required to collect tax from the buyers at the specified rates.

The specified percentage for collection of tax at source is as follows:

Nature of Goods	Percentage
(i) Alcoholic liquor for human consumption	1%
(ii) Tendu leaves	5%
(iii) Timber obtained under a forest lease	2.5%
(iv) Timber obtained by any mode other than (iii)	2.5%

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- | | |
|--|------|
| (v) Any other forest produce not being timber or
tendu leaves | 2.5% |
| (vi) Scrap | 1% |

However, no collection of tax shall be made in the case of a resident buyer, if such buyer furnishes to the person responsible for collecting tax, a declaration in writing in duplicate in the prescribed form and verified in the prescribed manner to the effect that goods referred to in column (2) of the above Table are to be utilised for the purpose of manufacturing, processing or producing articles or things and not for trading purposes. [Sub-section (1A)]

The person responsible for collecting tax under this section shall deliver or cause to be delivered to the Chief Commissioner or Commissioner one copy of the declaration referred to in sub-section (1A) on or before 7th of the month next following the month in which the declaration is furnished to him [Sub-section (1B)].

Sub-section (1C) provides for collection of tax by every person who grants a lease or a licence or enters into a contract or otherwise transfers any right or interest in any parking lot or toll plaza or a mine or a quarry to another person (other than a public sector company) for the use of such parking lot or toll plaza or mine or quarry for the purposes of business. The tax shall be collected as provided, from the licensee or lessee of any such licence, contract or lease of the specified nature, at the rate of 2% at the time of –

- (1) debiting of the amount payable by the licensee or lessee to his account or
- (2) at the time of receipt of such amount from the licensee or lessee –
 - (a) in cash or
 - (b) by the issue of a cheque or draft or
 - (c) by any other mode,whichever is earlier.

Two Explanations have been inserted w.e.f. 1.6.2007 to clarify the scope of the term 'mining and quarrying'.

Explanation 1 excludes mining and quarrying of mineral oil from the scope of 'mining and quarrying'.

Explanation 2 clarifies that 'mineral oil' includes petroleum and natural gas.

This amendment seeks to relieve the oil exploration and incidental services from the applicability of TCS provisions, since these services are in the organised sector.

The power to recover tax by collection under sub-section (1) or (1C) shall be without prejudice to any other mode of recovery [Sub-section (2)].

Any amount collected under sub-section (1) or (1C) shall be paid within the prescribed time to the credit of the Central Government or as the Board directs [Sub-section (3)].

The proviso to sub-section (3) casts responsibility on the person collecting tax on or after

1st April, 2005 in accordance with the provisions of the section. Such person is vested with the responsibility of preparing quarterly statements for the period ending on the 30th June, the 30th September, the 31st December and the 31st March in each financial year after paying the tax collected to the credit of the Central Government within the prescribed time. The statement should be delivered or caused to be delivered to the prescribed income-tax authority or the person authorised by such authority. The statement should be in the prescribed form and verified in the prescribed manner. The statement should set forth the prescribed particulars and should be filed within such time as may be prescribed. Penalty of Rs.100 per day of continuing default would be attracted under section 272A for failure to deliver or cause to be delivered in due time a copy of the statement as required above.

Any amount collected in accordance with the provisions of this section and paid to the credit of the Central Government shall be deemed to be payment of tax on behalf of the person from whom the amount has been collected. The CBDT may prescribe the rules based on which credit shall be given to such person for the amount so collected in a particular assessment year [Sub-section (4)].

Accordingly, Rule 37-I has been inserted providing for credit for tax collected at source for the purposes of section 206C(4).

Sub-rule (1) provides that the credit for tax collected at source and paid to the Central Government in accordance with provisions of section 260C, shall be given to the person from whom the tax has been collected, on the basis of the information relating to collection of tax at source furnished by the collector to the income-tax authority or the person authorized by such authority.

Sub-rule (2) provides that where tax has been collected at source and paid to the Central Government, credit for such tax shall be given for the assessment year for which the income is assessable to tax. Where tax has been collected at source and paid to the Central Government and the lease or license is relatable to more than one year, credit for tax collected at source shall be allowed across those years to which the lease or license relates in the same proportion.

Sub-rule (3) provides that the credit for tax collected at source and paid to the account of the Central Government shall be granted on the basis of -

- (i) the information relating to collection of tax furnished by the collector to the income-tax authority or the person authorized by such authority; and*
- (ii) the information in the return of income in respect of the claim for the credit,*

subject to verification in accordance with the risk management strategy formulated by the Board from time to time.

Every person collecting tax in accordance with the provisions of this section shall, within such period as may be prescribed from the date of debit or receipt of the amount, furnish

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to the buyer or licensee or lessee to whose account such amount is debited or from whom such payment is received, a certificate to the effect that tax has been collected specifying the sum so collected, the rate at which the tax has been collected and such other particulars as may be prescribed [Sub-section (5)].

The proviso to sub-section (5) provides that no certificate is required to be furnished in case where tax has been collected in accordance with the provisions of this section on or after 1st April, 2010. The second proviso casts responsibility on the prescribed income-tax authority or the person authorized by such authority. Such persons have now been vested with the responsibility to prepare and deliver a statement in the prescribed form specifying the amount of tax collected and such other particulars as may be prescribed, within the prescribed time after the end of each financial year beginning on or after 1.4.08.

The CBDT is empowered to frame a scheme for the purpose of filing of returns with such other authority or agency, if it considers necessary or expedient to do so.

Sub-section (5B) provides that the person responsible for collecting tax (other than a company/Central Government/State Governments) has the option to deliver or cause to be delivered such return on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media to the prescribed income-tax authority in accordance with such scheme as may be specified by the Board in this behalf.

The proviso to the said sub-section provides that where the person collecting tax is a company or the Central Government or a State Government, then such person is responsible to deliver or cause to be delivered, within the prescribed time after the end of each financial year, such returns on computer media under the said scheme.

Thus, filing of returns on computer media is compulsory where the seller is a company or the Central Government or a State Government. In every other case, the filing of returns on computer media is optional.

As per sub-section (5C), a return filed on computer media is deemed to be a return for the purposes of sub-section (5A) and the rules made thereunder. Such a return is also admissible as evidence in any proceedings made thereunder, without further proof of production of the original.

Rectification of defective TCS return [Section 206C(5D)]

Sub-section (5D) empowers the Assessing Officer, in case he considers that the return delivered or cause to be delivered under sub-section (5B) is defective, to -

- (i) intimate the defect to the person collecting tax and
- (ii) give him an opportunity of rectifying the defect within a period of -
 - (1) fifteen days from the date of such intimation or
 - (2) within such further period which the Assessing Officer may, in his discretion, allow on an application made in this behalf and

if the defect is not rectified within the said period of fifteen days or within such further

period so allowed, then, such return would be treated as an invalid return. The provisions of the Income-tax Act would apply as if such person had failed to deliver the return.

A person who is responsible for collecting the tax in accordance with the provisions of this section shall be liable to pay the tax to the credit of the Central Government, even if he has failed to collect the tax [Sub-section (6)].

Sub-section (6A) provides that any person responsible for collecting tax shall be deemed to be an assessee in default in respect of the tax if such person -

- (1) does not collect the whole or any part of the tax or
- (2) fails to pay such tax after having collected the tax.

However, no penalty shall be charged under section 221 from such person unless the Assessing Officer is satisfied that the person has without good and sufficient reasons failed to collect and pay the tax.

If the person responsible for collecting tax does not collect the tax or after collecting the tax fails to pay it as required under this section, he shall be liable to pay simple interest at the rate of 1% p.m. or part thereof on the amount of such tax from the date on which such tax was collectible to the date on which the tax was actually paid and such interest shall be paid before furnishing the quarterly statement for each quarter in accordance with the provisions of sub-section (3) [Sub-section (7)].

Where the tax has not been paid as aforesaid, after it is collected, the amount of tax together with the amount of simple interest thereon referred to in sub-section (7) shall be a charge upon all the assets of the person responsible for collecting tax [Sub-section (8)].

Further, sub-section (9) provides for issue of certificates by Assessing Officer for collection of tax at a lower rate than those specified in sub-section (1)/(1C). Such certificate shall be issued on an application made by the buyer or licensee or lessee in this behalf.

Sub-section (10) provides that the person responsible for collecting tax shall collect the same at the rate specified in such certificate until such certificate is cancelled by the Assessing Officer.

Sub-section (11) empowers the Board to make rules specifying the cases in which and the circumstances under which an application may be made for the grant of such certificate and the conditions subject to which certificate may be granted.

Definitions

- (a) "Buyer" means a person who obtains in any sale, by way of auction, tender, or any other mode, goods of the nature specified in the Table in sub-section (1) or the right to receive any such goods but does not include –
 - (i) a public sector company, the Central Government, a State Government, and an embassy, a high commission, legation, commission, consulate and the trade representation, of a foreign State and a club, or

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- (ii) a buyer in the retail sale of such goods purchased by him for personal consumption.
- (b) “Scrap” means waste and scrap from the manufacture or mechanical working of materials which is definitely not usable as such because of breakage, cutting up, wear and other reasons;
- (c) “Seller” means the Central Government, a State Government or any local authority or corporation or authority established by or under a Central, State or Provincial Act, or any company or firm or co-operative society and also includes an individual or a HUF whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which the goods of the nature specified in the Table in sub-section (1) are sold.

28.8 ADVANCE PAYMENT OF TAX [SECTION 207 TO 219]

1. Advance tax is payable in respect of all income including capital gains and casual income.
2. Under section 208, obligation to pay advance tax arises in every case where the advance tax payable is *Rs.10,000 or more*.

Enhancement of the limit for payment of advance tax : An assessee who is liable to pay advance tax of less than *Rs.10,000* will not be saddled with interest under sections 234B and 234C for defaults in payment of advance tax. However, the consequences under section 234A regarding interest for belated return shall continue.

No need for filing estimate: An assessee has to estimate his current income and pay advance tax thereon. He need not submit any estimate or statement of income to the Assessing Officer, except where he has been served with notice by the Assessing Officer.

Where obligation to advance tax has arisen, the assessee shall himself compute the advance tax payable on his current income at the rates in force in the financial year and deposit the same whether or not he has been earlier assessed to tax.

In the case of a person who has been already assessed by way of a regular assessment in respect of the total income of any previous year, the Assessing Officer, if he is of the opinion that such person is liable to pay advance tax, can serve a notice under section 210(3) requiring the assessee to pay advance tax. For this purpose, the total income of the latest previous year in respect of which the assessee has been assessed or the total income returned by the assessee for any subsequent previous year, whichever is higher, shall be taken as the basis for computation of advance tax payable.

The above notice can be served by the Assessing Officer at any time during the financial year but not later than the last date of February.

If, after sending the above order, but before 1st March of the financial year, the assessee furnishes a return relating to any later previous year or an assessment is completed in

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respect of a later return of income, the Assessing Officer can amend computation on the income to returned or assessed.

If assessee feels that his own estimate of advance tax payable would be less than the one sent by the Assessing Officer, he can file estimate of his current income and advance tax payable thereon. Where the advance tax payable or assessee's estimation would be higher than the tax computed by the Assessing Officer, then the advance tax shall be paid based upon such higher amount.

In all cases, the tax calculated shall be reduced by the amount deductible at source.

Advance tax shall be payable by companies and other assesseees as per the following schedule of installments:

Companies - Four installments

Due date of installment	Amount payable
On or before the 15th June	Not less than fifteen percent of such advance tax.
On or before the 15th September	Not less than forty five percent of such advance tax, as reduced by the amount, if any, paid in the earlier installment.
On or before the 15th December	Not less than seventy five percent of such advance tax, as reduced by the amount or amounts, if any, paid in the earlier installment or installments.
On or before the 15th March	The whole amount of such advance tax as reduced by the amount or amounts, if any, paid in the earlier installment or installments.

Non-corporate assesseees - Three installments

Due date of installment	Amount payable
On or before the 15th September	Not less than thirty percent of such advance tax
On or before the 15th December	Not less than sixty percent of such advance tax, as reduced by the amount, if any, paid in the earlier installment or installments.
On or before the 15th march	the whole amount of such advance tax as reduced by the amount or amounts, if any, paid in the earlier installment or installments.

Where advance tax is payable by virtue of the notice of demand issued by the Assessing Officer, the whole or the appropriate part of the advance tax shall be payable in the remaining installments.

Where the assessee does not pay any installment by the due date, he shall be deemed to be an assessee in default in respect of such installment.

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28.9 SCHEME OF MANDATORY INTEREST

28.9.1 Interest for defaults in furnishing return of income [Section 234A]

1. Where the return of income for any assessment year under sub-section 139(4) or in response to a notice under section 142(1), is furnished after the due date or is not furnished the assessee shall be liable to pay simple interest at the rate of 1% for every month or part of a month comprised in the period commencing on the day immediately following the due date and,
 - (a) where the return is furnished after the due date, ending on that date of furnishing the return; and
 - (b) where no return has been furnished, ending on the date of completion of assessment under section 144.
2. The amount on which interest will be payable will be the amount of the tax on the total income as determined under section 143(1) or on regular assessment, as reduced by the amount of -
 - (i) advance tax, if any, paid ;
 - (ii) any tax deducted or collected at source;
 - (iii) any relief of tax allowed under section 90 or 90A;
 - (iv) any deduction of tax allowed under section 91;
 - (v) any tax credit allowed to be set-off in accordance with the provisions of section 115JAA
3. 'Due date' means the date specified in section 139(1) as applicable in the case of the assessee.
4. The tax on total income as determined under section 143(1) shall not include additional income-tax payable under section 143.
5. Where in relation to an assessment year an assessment is made for the first time under section 147 the assessment so made shall be regarded as regular assessment for the purposes of this section.
6. The interest payable under this section shall be reduced by the interest paid under section 140A.
7. Where the return of income for any assessment year required by a notice under section 148 issued after the determination of income under section 143(1) or after completion of assessment under section 143(3) or section 144 or section 147 is furnished after the expiry of the time allowed under such notice, or is not furnished, the assessee shall be liable to pay simple interest at the rate of 1% for every month or part of a month comprised in the period commencing on the date immediately following the expiry of the time allowed as aforesaid and,
 - (a) where the return is furnished after the expiry of the time aforesaid ending on the date of furnishing the return;

- (b) where no return has been furnished ending on the date of completion of the reassessment or re-computation under section 147.
- 8. The amount on which the above interest is payable is the amount by which the tax on the total income determined on the basis of such reassessment or re-computation exceeds the tax on the total income determined under section 143(1) or on the basis of the earlier assessment aforesaid.
- 9. Where as a result of an appellate order or an order of the revision or an order from the Settlement Commission the interest payable is reduced or increased the Assessing Officer shall proceed as follows:
- 10. Where the interest is increased the Assessing Officer shall serve on the assessee a notice of demand in the prescribed form specifying the sum payable and such demand notice shall be a notice under section 156.
- 11. Where interest is reduced the excess paid shall be refunded.

28.9.2 Interest for defaults in payment of advance tax [Section 234B]: 1. The assessee will be liable to pay interest at the rate of 1% for every month or for part of month for the period starting from 1st April of the following financial year to the date of regular assessment on the amount of tax on the total income as determined under section 143(1) or on regular assessment after giving credit for any advance tax paid, tax deducted at source and collected at source, if the advance tax paid falls short of 90% of the 'assessed tax'.

2. The term 'assessed tax' means:

The tax on the total income determined under section 143(1) or on regular assessment as reduced by the amount of -

- (i) any tax deducted or collected at source on any income which is taken into account for calculating the total income.
 - (ii) any relief of tax allowed under section 90 or 90A;
 - (iii) any deduction of tax allowed under section 91;
 - (iv) any tax credit allowed to be set-off in accordance with the provisions of section 115JAA
3. An assessment made for the first time under section 147 shall be deemed to be regular assessment.
4. Tax on the total income determined under section 143(1) shall not include the additional income-tax if any, payable.
5. Where before the date of determination of total income under section 143(1) or completion of regular assessment, tax is paid by the assessee under section 140A:
- (i) interest shall be calculated up to the date on which the tax is so paid and reduced by the interest paid under section 140A.

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- (ii) Thereafter interest shall be calculated on the amount by which the tax paid under section 140A together with the advance tax paid falls short of the assessed tax.
- 6. Where as a result of an order of reassessment or re-computation under section 147 the amount on which interest is payable is increased the assessee shall be liable to pay simple interest at the rate of 1% for every month or part of a month, commencing on the day following the date of determination of total income under section 143(1), or regular assessment ending on the date of the reassessment or re-computation under section 147 on the amount by which the tax on the total income determined on the basis of reassessment or re-computation exceeds the tax on total income determined under section 143(1) on a regular assessment.
- 7. Where as a result of an appellate order, an order of revision or an order from Settlement Commission the interest payable is increased or reduced the Assessing Officer shall do as follows:
- 8. Where the interest is increased he shall serve a notice of demand on the assessee;
- 9. Where the interest is reduced the excess interest paid shall be refunded.

28.9.3 Interest for deferment of advance tax [Section 234C]:

In the case of companies: It has been provided that the shortfall for the purpose of charging interest for deferment of advance tax, in the case of companies, which are liable to pay advance tax shall be the difference between:

- (i) 15% of the tax due on the returned income and the advance tax paid by the company on or before 15th day of June;
- (ii) 45% of the tax due on the returned income and the advance tax paid by the company on or before 15th day of September;
- (iii) 75% of the tax due on the returned income and the advance tax paid by the company on or before 15th day of December.

It has also been provided that where the advance tax paid by the company on or before the 15th day of June is not less than 12% of the tax due on the returned income and the advance tax paid on or before the 15th day of September is not less than 36% of the tax due on the returned income, then the companies will not be liable to pay any interest on the amount of the shortfalls on the aforesaid dates.

In the case of any other assessee: The shortfall for the purpose of charging interest for deferment of advance tax shall be the difference between:

- (i) 30% of the tax due on the returned income and the advance tax paid on or before 15th day of September.
- (ii) 60% of the tax due on the returned income and the advance tax paid on or before 15th day of December.

Enlarging the scope of levy of interest for deferment of advance tax: The whole amount of the advance tax is required to be paid on or before 15th March during the financial year. The proviso to section 211(1), however, provides that any amount paid by way of advance tax on or before 31st March, is also to be treated as advance tax paid during the financial year. This proviso was inserted as certain High Courts had held that payment made after the 15th March during the financial year would not cease to be payment of advance tax. There is no penal provision in the law to enforce payment of the last installment of advance tax by 15th March. The aforesaid proviso and the absence of a penal provision have generated a tendency among the assesseees to make payment of advance tax only towards the last day of the financial year.

Section 234C(1) of the Income-tax Act therefore provides that where the whole amount of advance tax paid by an assessee on or before 15th March in the financial year is less than the tax due on the returned income, the assessee is liable to pay simple interest at the rate of 1% per month or part of the month on the amount of the shortfall from the tax due on the returned income.

An assessee is required to pay advance tax in specified installments on his estimated total income including capital gains and income from winnings from lotteries, horse races etc. covered by section 2(24)(ix). No interest will be levied under section 234C in respect of any shortfall in payment of advance tax due on returned income if the shortfall is on account of under estimation or failure to estimate the amount of capital gains or income under section 2(24) (ix) and the assessee has paid the whole amount of the tax payable in respect of the income as part of the installment of advance tax which is immediately due.

These provisions shall apply even in cases where no advance tax has been paid by the assessee who is liable to pay such tax during the financial year.

“Tax due on the returned income” means the tax chargeable on the total income declared in the return of income furnished by the assessee for the assessment year immediately following the financial year in which the advance tax is paid or payable, as reduced by the amount of –

- (i) any tax deductible or collectible at source on any income which is taken into account for calculating the total income.
- (ii) any relief of tax allowed under section 90 or 90A;
- (iii) any deduction of tax allowed under section 91;
- (iv) any tax credit allowed to be set-off in accordance with the provisions of section 115JAA

Payment of advance tax relatable to capital gain, etc. to be allowed in the remaining installments : Under section 234C penal interest is not charged on account of underestimate or failure to estimate either the amount of capital gain or of income from winnings from lottery, horse races, etc., referred to section 2(24)(ix) if the assessee pays the whole of the tax payable in respect of such income, as part of

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the installment of advance tax which is immediately due after such income is earned or by 31st March if no such installment is due.

This requirement of paying the whole of the tax was causing hardship as the entire tax laid to be paid on a short notice. In many cases, even the sale proceeds of the capital asset were not received before the advance tax payment became due. Section 234C allows the assessee to pay the tax in relation to capital gain or to income from winnings from lottery, horse races, etc., as part of the remaining installments of advance tax which are due in the financial year and if no installment is due then before 31st March of the previous year.

28.9.4 Interest on excess refund granted at the time of summary assessment – Section 234D

- (i) Under section 143(4), where a regular assessment under section 143(3) or section 144 is made, any tax or interest paid under section 143(1) shall be deemed to have been paid towards such regular assessment and if no refund is due on regular assessment or the amount refunded under section 143(1) exceeds the amount refundable on regular assessment, the whole or the excess amount so refunded is deemed to be tax payable by the assessee. However, no interest is charged for the period during which the refund amount has been utilised by the assessee.
- (ii) Therefore, section 234D was inserted to charge interest on excess refund granted at the time of summary assessment.
- (iii) Sub-section (1) provides that where any refund is granted to the assessee under section 143(1) and no refund is due on regular assessment or the amount refunded under section 143(1) exceeds the amount refundable on regular assessment, then the assessee shall be liable to pay simple interest at the rate of two-third per cent on the whole or the excess amount so refunded for every month or part of the month from the date of grant of the refund to the date of such regular assessment.
- (iv) Sub-section (2) further provides that the interest chargeable under sub-section (1) shall be reduced, where, as a consequence to the order passed due to rectification, appeal, revisions etc. under sections 154/155/250/254/260/262/263/264 or an order of the Settlement Commission under section 245D(4) of the Income-tax Act, the amount of refund granted under section 143(1) is held to be correctly allowed.
- (v) An assessment made for the first time under section 147 or section 153A shall be regarded as regular assessment for the purpose of this section.

28.10 COLLECTION AND RECOVERY OF TAX - OTHER METHODS

28.10.1 Payment of tax and defaults by the assessee [Section 220]: Any tax, interest, penalty, fine or any other sum specified in a notice of demand (other than those relating to advance payment of taxes) issued under section 156 must be paid within such time (not being less than seven days) as has been specified in the notice by the Assessing Officer with the prior approval of the inspecting Assistant Commissioner under the proviso to sub-section (1) of section 220. The Assessing Officer is authorised to extend the time for

payment or allow the payment of tax to be made in installments on receipt of an application from the assessee. Where an assessee, who has been granted permission to pay the tax in installments defaults in payment of any of the installments he will be deemed to be in default in respect of the whole of the amount then outstanding including the other installments which have not fallen due. An assessee, who fails to pay the tax within the time afore mentioned, is deemed to be in default. In the event interest at the rate of 1% for every month or part of the month after the expiry of 30 days from the date of service of notice to the date of payment of the tax calculated in the manner provided in Rules 118 and 119 of the Income-tax Rules, 1962, shall also be payable in addition to the amount of any penalty for non-payment which may be imposed by the Income-tax Officer.

If the default continues, the Assessing Officer may start recovery proceeding under sections 222 to 228 read with the Second Schedule and the Income-tax (Certificate Proceedings) Rules, 1962 except in cases (i) where the assessee cannot be treated as being in default or (ii) where the notice of demand was not duly served. However, where the assessee has filed an appeal under section 246 or 246A against the order of demand made by the Assessing Officer, he shall not be deemed to be in default in respect of the amount in dispute so long as the appeal is not disposed of. If an assessee has been taxed in respect of his foreign income arising in a country the laws of which restrict or prohibit the remittance of money into India, he should not be treated as being in default in respect of the tax which is due on the income which, by reason of such prohibition or restrictions, cannot be and has not been brought into India. For this purpose the income of the assessee must be deemed to have been brought into India if it has been utilised or could have been utilised for the purpose of any expenditure actually incurred by the assessee outside India or if the income, whether capitalised or not has been brought into India in any form.

Any Income-tax payable by a person on the amount of income voluntarily declared by him, which is outstanding for payment shall be deemed to be the tax due from the declarant on the date next following the expiry of the period allowed to him for payment and the same will be recoverable as arrears under the provisions of the Act.

Section 220(2A) empowers the Chief Commissioner or the Commissioner to reduce or waive any interest payable under section 220(2) if he is satisfied that:

- (i) payment of such amount would cause genuine hardship to the assessee.
- (ii) default in the payment of the amount on which interest was made payable under the said sub-section was due to circumstances beyond the control of the assessee.
- (iii) The assessee has co-operated in any enquiry relating to the assessment or any proceeding for the recovery of any amount due from him.

28.10.2 Penalty payable [Section 221]: Where an assessee is in default in payment of tax including advance tax and interest payable thereon, the Assessing Officer shall impose a penalty which in cases of continuing default, may be increased from time to time. The Assessing Officer should give the assessee a reasonable opportunity of being heard before levying such a penalty. A penalty may be levied on a legal representative for

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his own default in paying the tax due under an assessment on himself under section 159 or on the deceased. The penalty levied will be cancelled if the tax to which the penalty relates is wholly and finally reduced in appeal.

No penalty shall be levied on the assessee for default in payment of tax in cases where the Assessing Officer is satisfied that default was for good and sufficient reasons, the Taxation laws (Amendment and Miscellaneous Provisions) Act, 1986 has shifted the burden of proof upon the assessee. Accordingly penalty will not be levied under this section only when the assessee proves to the satisfaction of the Assessing Officer that the default was for good and sufficient reasons. However, no penalty can be imposed

- (i) for default in payment of a penalty already imposed;
- (ii) where the imposition of penalty does not take the form of an order and the order does not state specifically the sum which the assessee has to pay by way of tax, interest, penalty, etc.
- (iii) where the period specified in the notice has not expired;
- (iv) unless there is default in payment of the tax on the due date; even if a wrong date is specified in the notice of demand by mistake, no penalty can be levied until the date so specified has expired;
- (v) unless the notice of demand has been properly served;
- (vi) where the assessee has applied for granting stay of recovery proceedings;
- (vii) where the assessee is to be treated as not being in default under section 220(6) in respect of a case in appeal.
- (viii) where the assessee has preferred an appeal against the order of assessment or the notice of demand; and
- (ix) where an order of injunction has been issued by a Court restraining the Assessing Officer from taking any recovery proceeding. If the Assessing Officer is not aware of the order of injunction, the order of penalty passed by him would become void ab initio.

The Explanation to section 221(1) provides that an assessee would not cease to be liable to pay any penalty for his default or delay in payment of the tax merely by reason of the fact that before the date of levy of such penalty the tax which was in arrears had actually been paid by him. Thus wherever there is delay on the part of the assessee, he would be liable to penalty even though by the time the Assessing Officer initiates action for the levy of penalty the amount of tax in arrears is actually paid. An order imposing penalty is appealable and the assessee's right of appeal is subject to the condition that he must first pay the tax or penalty; the assessee should first pay the tax before filing the appeal.

28.10.3 Certificate to Tax Recovery Officer [Section 222]: 1. When an assessee is in default or is deemed to be in default in making a payment of tax the Tax Recovery Officer may draw up under his signature a statement in the prescribed form and specifying the amount of arrears due from the assessee (such statement being hereinafter and in the

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Second Schedule referred to as certificate) and shall proceed to recover from such assessee the amount specified in the certificate by one of more of the modes mentioned below in accordance with the Second Schedule.

- (a) Attachment and sale of the assessee's movable property.
- (b) Attachment and sale of assessee's immovable properties.
- (c) Arrest of the assessee and his detention in prison.
- (d) Appointing a receiver for the management of assessee's movable and immovable properties.

2. For the purpose of this section the assessee's movable or immovable property shall include any property which has been transferred directly or indirectly by the assessee to his spouse or minor child or son's wife or son's minor child otherwise than for adequate consideration and which is held by any of the persons aforesaid. So far as the movable or immovable property so transferred to his minor child or his son's minor child is concerned, they shall even after the date of attainment of majority by such minor child or son's minor child continue to be included in the assessee's movable or immovable property for recovering any arrears.

3. The Tax Recovery Officer may take action under sub-section (1) notwithstanding that proceedings or recovery of the arrears by any special mode have been taken.

28.10.4 Tax Recovery Officer by whom recovery is to be effected [Section 223]:

1. The Tax Recovery Officer competent to take action under section 222 shall be:

- (a) The Tax Recovery Officer within whose jurisdiction the assessee carries on business or profession is situated.
- (b) The Tax Recovery Officer within whose jurisdiction the assessee resides or any movable or immovable property of the assessee is situated.

2. The jurisdiction is assigned either by the Board or the Chief Commissioner or Commissioner who is authorised in this behalf by the Board under section 120.

3. Where an assessee has property within the jurisdiction of more than one Tax Recovery Officer and Recovery Officer by whom the certificate is drawn up

- (a) is not able to recover the entire amount by sale of the property within his jurisdiction.
- (b) he may send the certificate to a Tax Recovery Officer within whose jurisdiction the assessee has property. There upon the Tax Recovery Officer shall proceed to recover the amount as if the certificate was drawn up by him.

28.10.5 Stay of proceedings in pursuance of certificate and amendment or cancellation thereof [Section 225]: 1. It shall be lawful for the Tax Recovery Officer to grant time for the payment of any tax and when he does so he shall stay proceedings for the recovery of such tax until the expiry of the time so granted.

2. Where as a result of appeal the demand is reduced and the order is the subject

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matter of further proceedings the Tax Recovery Officer shall stay the recovery. Such part of the amount specified in the certificate as pertains to such deduction for the period in which an appeal or other proceedings remains pending.

3. Where a certificate has been drawn up and as a result of appellate order the amount is reduced, the Tax Recovery Officer shall modify the certificate or cancel it if it is necessary.

28.10.6 Other modes of recovery [Section 226]: 1. Where no certificate has been drawn up under section 222 the Assessing Officer may recover the tax by any one or more of the modes provided in the section.

2. Where a certificate has been drawn up under section 222, the Tax Recovery Officer may without prejudice to the modes of recovery specified in this section recover the tax by any one or more of the modes provide in this section.

3. This section enumerates the various modes of recovery by the Assessing or Tax Recovery Officer. Students may refer to the section for details.

28.10.7 Priority as regards recovery of taxes: Any claim in regard to any property in relation to which a notice under this section is issued, shall be void as against any demand contained therein. Where a person, on whom a notice (garnishee order) under this section has been served, objects on oath that the amount demanded from him is not due to the assessee or that he does not hold any money for or on behalf of the assessee, he cannot be compelled by the Assessing Officer to make the payment. But if it is later on found that such a statement made by him was false, he would personally become liable to pay the amount to the extent of his own liability to the assessee or to the extent of the assessee's liability, which ever is less. Such personal liability would arise even in cases where the person in receipt of a notice from the Assessing Officer makes a payment in disregard of the notice served on him.

Moneys belonging to the assessee in default which are in the custody of a Court or Receiver are also liable for attachment. Further, on being authorised by the Commissioner, the Assessing Officer is also empowered to recover the tax by distraint and sale of movable property as laid down in the Third Schedule. For details, students may refer to the Third Schedule in the Act. In addition, tax may be recovered, through the State Government if the recovery of tax in any area has been entrusted to it under the Constitution. In such a case the State Government may direct that the tax shall be recovered in respect of any particular area together with the municipal taxes or local rates by municipality or local authority (section 227).

28.10.8 Tax Clearance Certificate [Section 230]:

Sub-section (1) provides as follows -

- (i) No person, who is not domiciled in India and who has come to India in connection with business, profession or employment; and who has income derived from any source in India, shall leave the territory of India by land, sea or air unless he furnishes to the prescribed authority an undertaking in the prescribed form.

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- (ii) The said undertaking should be furnished from the employer of the said person or through whom such person is in receipt of the income.
- (iii) The undertaking should be to the effect that tax payable by such person who is not domiciled in India shall be paid by the employer or the person through whom any income is received.
- (iv) The prescribed authority shall, on receipt of the undertaking, immediately give to such person a no-objection certificate, for leaving India.
- (v) However, the provisions contained in sub-section (1) shall not apply to a person who is not domiciled in India but visits India as a foreign tourist or for any other purpose not connected with business, profession or employment.

Sub-section (1A) provides as follows -

- (i) Every person, who is domiciled in India at the time of his departure, shall furnish, to the income-tax authority or such other authority as may be prescribed his permanent account number allotted to him under section 139A, the purpose of his visit and the estimated period of his stay outside India.
- (ii) In case no such permanent account number has been allotted to him, or his total income is not chargeable to income-tax or he is not required to obtain a permanent account number under the Income-tax Act, a certificate in the prescribed form shall be furnished to the income-tax authority or such other authority, as may be prescribed.
- (iii) However, where an income-tax authority opines that there exist circumstances which render an Indian domiciled to obtain a certificate under this section, such person shall not leave the territory of India by land, sea or air unless -
 - (1) he obtains a certificate from the income-tax authority stating that he has no liabilities under the Income-tax Act 1961, the Wealth-tax Act, 1957, the Gift-tax Act, 1958 or the Expenditure-tax Act, 1987, or
 - (2) that satisfactory arrangements have been made for the payment of all or any of such taxes which are or may become payable by that person[First proviso to sub-section (1A)]
- (iv) No income-tax authority shall make it necessary for any person who is domiciled in India to obtain a certificate under this section unless he records the reasons therefor and obtains the prior approval of the Chief Commissioner of Income-tax. [Second proviso to sub-section (1A)].

If the owner or charterer of any ship or aircraft carrying persons from any place in India to any place outside India allows any of the above mentioned persons to travel by such ship or aircraft without first satisfying that such person is in possession of a certificate as required, he shall be personally liable to pay the whole or any part of the tax payable by such person. In such a case, the owner or charterer shall be deemed to be an assessee in default for such sum and recovery shall be as if it were an arrear of tax.

For the purpose of this section, the expressions "owner" and "charterer" include any

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representative, agent or employee empowered by the owner or charterer to allow persons to travel by the ship or aircraft.

28.10.9 Recovery by suit or under other law [Section 232]: Section 232 provides that the Assessing Officer or the Government can have recourse to the other modes of recovery under any other law for the time being in force, over the above various modes specified above to recover the tax dues under the Act, in the same way as other debts due to the Government. It shall also be lawful for the Assessing Officer or the Government to take recourse to any other law or file a suit in any manner for the recovery of the arrears due from the assessee.

28.11 REFUNDS

28.11.1 Eligibility and procedure: An assessee is entitled to claim a refund of tax if the tax actually paid (and not merely payable) by him or on his behalf for any assessment year exceeds the amount of tax with which he is properly chargeable under the Act for that year. This may arise usually as a result of excess deduction of tax at source from salaries, dividends, interest, to or as a result of excess payment of advance tax when the tax originally paid on assessment is reduced on appeal, revision, rectification or reference. Where such a claim or refund is made, the assessee cannot question the correctness or validity of the assessment or any other matter related thereto which has become final and conclusive. He is also debarred from asking for a review or revision of the assessment [Sections 237 and 242].

In case where the payer of income from salary, dividend, interest or other sum has wrongly deducted tax at source and paid the same to the credit of the Central Government, then it is the payer of the income who wrongly deducted tax (and not the recipient) who will be entitled to claim the refund provided that the recipient is neither taxable on the gross income nor entitled to credit in respect of the tax deducted. Where the tax payable by an unregistered firm is recovered from its partners the tax should be treated as having been paid by the firm and consequently, the application for refund must be made by the firm and not by the partner from whom the tax was recovered. In respect of tax free income (i.e. where salary, annuity, interest etc. is paid tax free) the amount of tax is included in the recipient's total income by adding it to the net income received; since the tax in such cases is deemed to have been deducted and paid on behalf of the recipient of the income, he would be entitled to claim a refund if the tax so paid is in excess of the amount with which he is properly chargeable.

Where the value of fringe benefits provided or deemed to have been provided by one employer is included under any provisions of Chapter XII-H in the value of fringe benefits provided or deemed to have been provided by any other employer, the latter alone is entitled to a refund under this Chapter in respect of such fringe benefits.

Generally, a claim for refund can be made only by the person on whose account the tax was already paid. But in cases where the income of one person is included in the total income of another person under sections 60 to 65, the latter person alone is entitled to

claim the refund. If any person is not able to claim or receive the refund due to him on account of his death, mental incapacity, insolvency, dissolution, liquidation, etc., his legal representative or trustee, guardian liquidator or receiver, the case may be, is entitled to claim or receive the refund on behalf of such person [Section 238].

All claims of refunds should be made in the prescribed form (Form No. 30) and verified in the prescribed manner in accordance with Rule 41 of the Income-tax Rule and shall be accompanied by the return of income except in cases where such a return had already been filed. The requirements of the Rule are mandatory in nature and if an application or refund is not in compliance with the requirement of the Rule, it would be invalid and consequently will not be entertained. The claim for refund should be supported by the certificate of tax deducted at source. The claim may be presented by the claimant in person or through a duly authorised agent or may be sent by post.

The time-limit for making application for refund is one year from the last day of the relevant assessment year. This applies for a claim in respect of fringe benefits also [Section 239].

The Court has no power to extend this period of limitation in any case. This period of limitation would not, however, apply to cases where a refund becomes due to the assessee as a result of an order in appeal, reference, revision or making any reassessment; but in cases where the refund is due to the assessee on the basis of the completed regular assessment, the assessee may file a suit for the refund due to him if it is not granted on his application or he may file a petition for a writ of mandamus to compel the Department to make the refund. Where the refund becomes due to the assessee as a result of an order passed in appeal, reference, revision or rectification, he need not make an application to claim the same. In such a case, the Assessing Officer is bound to pass an order of refund without waiting for the application from the assessee [Section 240].

Where, by the order aforesaid an assessment is cancelled and an order of fresh assessment is directed to be made the refund shall become due only on the making of such fresh assessment [Section 240].

Where the assessment is annulled the refund shall become due only of the amount of tax paid in excess of the tax chargeable on the total income returned by the assessee [Section 240].

28.11.2 Correctness of assessment not to be questioned [Section 242]

While making a claim for refund, an assessee cannot question the correctness of any assessment or other matter decided which has become final and conclusive or ask for a review of the same. The assessee shall not be entitled to any relief on such claim except refund of tax wrongly paid or paid in excess.

28.11.3 Interest on Refunds [Section 244A] : (a) Section 244A provides that interest at $\frac{1}{2}\%$ for every month or part of a month shall be payable on tax or penalty becoming refundable on account of excess payment of advance tax, advance tax on fringe benefits, tax deducted at source or collected at source and other tax or penalty becoming refundable.

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- (b) The period for which the interest is payable will be -
 - (i) Where the refund is of any advance tax or tax deducted or collected at source, the interest shall be payable for the period starting from 1st April to the date of the grant of refund.
 - (ii) Where the refund is of other taxes/penalties, the interest shall be paid for the period starting from the date of payment of such tax or penalty upto the date on which the refund is granted.
- (c) The assessee can claim interest on refund due also in pursuance of determination of total income under section 115WE(1) or section 143(1) or on regular assessment. However, no interest shall be payable if the amount of refund due is less than 10% of the tax determined u/s 143(1) or on regular assessment.
- (d) Where there is a delay in granting refund and the reasons for such delay are attributable to the assessee, either wholly or in part, the period of the delay so attributable to the assessee shall be excluded from the period for which interest is payable. In case any question arises as to the period of delay attributable to the assessee, it shall be decided by the Chief Commissioner or Commissioner.
- (e) Where as a result of an order passed under sections 115WE(3) or 115WF or 115WG or 143(3) or 144 or 147 or 154 or 155 or 250, 254, 260, 262, 263 or 264 or an order of Settlement Commission under section 245D, the amount on which interest is payable under section 244A is increased/reduced, the interest shall be increased or reduced accordingly.
- (f) Interest allowed u/s.244A is the income of the previous year in which it is allowed, and should be declared in the return of income furnished in the assessment year relevant to the previous year.

28.11.4 Set off of refunds against tax remaining payable [Section 245]

Where a refund is found due to any person, the Assessing Officer, Deputy Commissioner (Appeals), Commissioner (Appeals) or Chief Commissioner or Commissioner may, in lieu of payment of the refund, set off the amount to be refunded or any part of that amount, against any tax or interest remaining payable by the said person under the Act. However, the set off can be done only after giving intimation in writing to such person of the action proposed to be taken under this section.

28.11.5 Belated claim for refund – The Assessing Officers are authorised to admit belated refund claims u/s.237 as per CBDT Circular No.670 dated 26.10.93 as modified by Circular No.8 of 2001 dated 16.5.2001. However, the following conditions are to be satisfied –

- (i) The refund should be on account of advance tax or TDS or TCS and the amount of refund should not exceed Rs.1 lakh for any assessment year;
- (ii) The claim for refund should not be supplementary in nature; and
- (iii) The assessee's income is not assessable in the hands of any other person under any of the provisions of the Act.

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The Assessing Officer should obtain the approval of the Commissioner to dispose of refund claims up to Rs.10,000. For refund claims exceeding Rs.10,000 but not exceeding Rs.1,00,000, he should obtain the approval of Chief Commissioner or Director General. In respect of refund claims exceeding Rs.1,00,000 per assessee per year, the Board has to condone the delay.

28.11.6 Other Provisions: In all cases where an assessment or reassessment is completed and any tax, interest, penalty, fine or any other sum is payable by the assessee, the Assessing Officer shall serve upon the assessee a notice of demand specifying the sum so payable. Though the Act does not prescribe any time limit within which a notice of demand should be served on the assessee the notice of demand must be issued within a reasonable time [Section 156]. Likewise, where the assessment results in a loss and such loss is to be carried forward, the Assessing Officer shall notify to the assessee by an order in writing the amount of such loss computed by him [Section 157]. In cases where a registered firm is assessed or an unregistered firm is assessed under section 183(b) as registered, the Assessing Officer shall notify to the firm, by an order in writing the amount of total income assessed and its apportionment amongst the several partners [Section 158]. The assessee has a right of appeal against any order passed by the Assessing Officer under sections 157 and 158.

Self-examination questions

1. Discuss the provisions of section 194LA relating to TDS from compensation paid on acquisition of immovable property other than agricultural land.
2. Explain the terms “buyer”, “scrap” and “seller” as defined under *Explanation* to section 206C of the Income-tax Act, 1961.
3. What are the prescribed modes of recovery of tax by the Tax Recovery Officer under the provisions of the Income-tax Act?
4. ABC Ltd. failed to deduct tax at source under section 194J in respect of fees for professional services paid by it. The Assessing Officer levied penalty under section 271C for failure to deduct tax at source. In addition, the Assessing Officer also levied penalty under section 272A(2)(c) for failure to furnish return under section 206 and under section 272A(2)(g) for failure to furnish certificate of tax deducted at source as per the requirement of section 203. Is the action of the Assessing Officer correct in law?
5. Section 206C casts responsibility on the seller to collect tax at source, *inter alia*, on sale of alcoholic liquor for human consumption at the rate of 1% of “such amount” received from the buyer in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier. Whether collection of tax at source under section 206C would be on the price of liquor, including excise duty paid for purchase of liquor?

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You are required to answer this question with the aid of a recent case law.

6. Can stamp vendors be treated as agents of the Government for marketing stamp papers? If yes, can tax be deducted under section 194H in respect of discount given on sale of stamps by the Treasury to the stamp vendor?
7. ABC Shipping Corporation Ltd. was carrying on the business of transporting coal. It entered into a contract with the State Electricity Board for transporting coal from various ports. Since the ships owned by the company were not sufficient for executing the contracts, the company hired ships from other shipping companies and paid hire charges for use of ships. The company did not deduct tax at source under section 194C from payment of hire charges to the shipping companies. Therefore, the Assessing Officer treated the company as an "assessee-in-default". Discuss whether the action of the Assessing Officer is correct in law.
8. SFS Ltd. was engaged in the sale and export of sea food. It obtained a permit to fish in the Exclusive Economic Zone of India. In order to exploit the said fishing rights, it entered into an agreement chartering two fishing vessels, with a non-resident company. As per the terms of the agreement, SFS Ltd. had to pay 85% of fish catch towards the hire charges to the said non-resident company. This receipt in the form of 85% of the fish catch by the non-resident company was in India and all the formalities were completed in India. The assessing authority held that the assessee had made the payment to the non-resident company within the meaning of section 195 and was liable to deduct tax at source therefrom. Is the contention of the assessing authority correct? Discuss.

Answers

4. This issue came up before the High Court of Allahabad in *CIT-II, Lucknow vs. Sahara Airlines Ltd.* The High Court held that the provisions of sections 203 and 206 would be applicable only if tax has been deducted at source by the person concerned and he commits default in complying with any of the provisions of section 203 or 206. However, in a case where no tax has been deducted at source, the aforesaid provisions would not be attracted. For failure of the assessee in deducting tax at source, penalty can be imposed upon him under section 271C. Once a person concerned has been subjected to a penalty under section 271C for not deducting tax at source, there would not arise any occasion for levying penalty under section 272A(2)(c) and 272A(2)(g) for non-compliance of the provisions of sections 206 and 203. In other words, in case the tax has not been deducted at source, the question of issuing the certificate of tax deducted under section 203 and that of filing of return under section 206 would not arise at all. Therefore, the question of imposing penalty for violation of the provisions of section 203 and 206 would also not arise.

Therefore, the action of the Assessing Officer imposing penalty under sections 272A(2)(c) and 272A(2)(g) in a case where tax has not been deducted at source is not correct in law.

5. This issue was answered by the High Court of Madhya Pradesh in *Vinod Rathore vs. Union of India* (2005) 146 Taxman 32. The question for consideration before the Court was whether collection of tax at source under section 206C on the price of liquor shall include excise duty paid for purchase of liquor. The High Court held that the purchase price would include the excise duty paid by the buyer and collection of tax at source under section 206C on the price of liquor shall include excise duty paid for purchase of liquor.
6. In *Kerala State Stamp Vendors Association v. Office of the Accountant-General* (2006) 282 ITR 0007, the High Court held that stamp vendors cannot be treated as agents of the Government for marketing stamp papers. The discount given on sale of stamps by the Treasury to the stamp vendor is outside the scope of TDS provisions under section 194H.

The High Court observed that only commission and brokerage are subject to tax deduction under section 194H. Commission or brokerage is paid for services rendered in the course of sale. This implies services rendered by third parties like brokers or agents. It cannot mean services rendered by a buyer because a buyer is not rendering any service except buying. A price discount given by the seller to the buyer cannot be treated as commission or brokerage for services rendered in the course of buying and selling of goods. This is because the act of buying does not constitute rendering of any service. Therefore, stamp vendors cannot be treated as agents of the Government for marketing stamp papers and consequently, TDS provisions under section 194H are not attracted.

7. The Madras High Court, in *CIT v. Poompuhar Shipping Corporation Ltd.* (2006) 282 ITR 0003, held that the hiring of ships for the purpose of using the same in assessee's business would not amount to a contract for carrying out any work as contemplated in section 194C and therefore, payment of hire charges would not attract tax deduction under section 194C. Therefore, the action of the Assessing Officer is not correct in law.
8. The Andhra Pradesh High Court settled this issue in *Kanchanganga Sea Foods Ltd. v. CIT* (2004) 136 Taxman 8, where it was held that 85% of fish catch which was adjusted in discharge of liability of the assessee towards hire charges, would be receipt in the hands of non-resident company under section 5(2). Further, this receipt in the form of 85% of the fish catch by the non-resident company was in India since all the formalities were completed in India. It was further held that payment

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contemplated under section 195 not only includes cash payment or payment by cheque or draft, but also a payment given by any other mode. Therefore, the payment of hire charges made by the assessee by giving 85% of fish catch to the non-resident company amounted to payment as contemplated under section 195.

Therefore, the contention of the assessing authority is correct.

WEALTH TAX

LEVY OF WEALTH TAX

1.1 LEVY OF WEALTH TAX

The Wealth-tax Act came into force on 1st April, 1957. The Act seeks to impose an annual tax on the net-wealth of the specified classes of persons in respect of every assessment year commencing on and from 1st April, 1957. The tax is charged at the rate of 1% on the amount by which the net wealth of the assessee exceeds *Rs.30 lakh* as on a particular date which is known as the valuation date. The tax is levied in accordance with the rate specified in section 3(2).

1.2 APPLICABILITY

The Wealth-tax Act is applicable to the whole of India including Jammu & Kashmir. The Union Home Ministry has issued a notification extending the application of Wealth-tax Act 1957 to Sikkim. The Wealth-tax Act will, therefore, apply to the net wealth of the residents of Sikkim on the valuation date being 31st March, 1990 or thereafter. The constitutional validity of the Wealth-tax Act was upheld by the Supreme Court in *Sudhir Chandra Nawn vs. (1968-69) ITR 867*. However, the Jammu & Kashmir High Court held in *P.C. Oswal's case (1983) 14 Taxman 168*, that the Wealth-tax Act, in so far as it purports to be applicable to the State of Jammu and Kashmir is *ultra vires* the Constitution of India, as applied to the State.

In *CWT vs. Dr. Karan Singh (1993) 67 Taxman 3 (SC)* it was contended that the Wealth-tax Act was relatable only and exclusively to Entry 97 of List 1 and since the said Entry had no application to the State of Jammu and Kashmir, the Wealth tax Act could not be applied to the State of Jammu and Kashmir. The High Court held that in view of the special provision contained in Article 370, the Parliament did not have any legislative competence to extend the Act to the State of Jammu and Kashmir. However, on appeal, the Supreme Court held that in construing the language of constitutional enactments conferring legislative powers, the most liberal construction should be put upon the words so that the same have effect in their widest amplitude. The language of Entry 86 clearly indicates that the tax is upon the individuals and not directly upon the assets or upon their value. The Wealth Tax Act, as originally enacted was covered by Entry 86 of List 1 and its extension to the State of Jammu and Kashmir was perfectly constitutional. This decision impliedly overrules *P.C. Oswal's case* cited above.

1.2 Wealth Tax

1.3 DEFINITIONS

Section 2 of the Act defines the various terms used in the Act. A thorough knowledge of these definitions is a *sine qua non* for a proper understanding of the various other provisions of the Act. Some of the important definitions are discussed below while some others have been discussed at appropriate places.

1.3.1 Assessee: The term 'assessee' as defined in section 2(c), means a person by whom wealth-tax or any other sum of money is payable under this Act and includes (i) every person in respect of whom proceedings under the Act have been taken for the determination of wealth tax payable by him or by any other person or the amount of refund due to him or such other persons (ii) every person who is deemed to be an assessee under the Act and (iii) every person who is deemed to be an assessee in default under the Act.

1.3.2 Assessment Year and Valuation Date : The definition of these two related expressions are given in sections 2(d) and 2(q) respectively. As mentioned at the outset, wealth-tax is chargeable on the net wealth of an assessee as on the valuation date relevant to the assessment year in question. The expression 'assessment year' means the period of 12 months commencing on the 1st day of April every year falling immediately after the valuation date. The 'valuation date' means the last day of the previous year in respect of the assessment year for the purpose of income tax assessment.

It may be noted that as a result of the introduction of the financial year as the uniform accounting year under the Income- tax Act, the valuation date in all cases will be 31st March.

In the case of assesseees who are not liable to pay any income-tax the valuation date is always the 31st March immediately preceding such assessment year. Where an executor is to be assessed to wealth-tax under section 19A, in respect of assets left by a deceased person, the valuation date shall be the same valuation date as would have been adopted in respect of the deceased if he were alive.

It is to be noted that as the tax is charged on the net wealth of an assessee on the corresponding valuation date, the existence of assets on the valuation date is a necessary condition for the levy. Where there is change of ownership of assets on the valuation date, it is the net wealth at the last moment of that day and not the first moment or during the day which shall be the subject of the assessment of wealth-tax.

1.3.3 Assets [Section 2(ea)] : The following assets would be chargeable to wealth tax: Section 2(ea) of the Wealth-tax Act defines the term 'assets'. Accordingly "assets" mean:

- (i) Any building or land appurtenant thereto (hereinafter referred to as "house"), whether used for residential or commercial purposes or for the purpose of maintaining a guest house or otherwise including a farm house situated within twenty-five kilometres from local limits of any municipality (whether known as Municipality, Municipal Corporation or by any other name) or a cantonment Board, but does not include:

- (1) a house meant exclusively for residential purposes and which is allotted by a company to an employee or an officer or a director who is in whole time employment, having a gross annual salary of less than Rs.5,00,000.
 - (2) any house for residential or commercial purposes which forms part of stock-in-trade.
 - (3) any house which the assessee may occupy for the purpose of any business or profession carried on by him.
 - (4) any residential property that has been let out for a minimum period of 300 days in the previous year.
- (ii) **Motor cars:** All types of motor cars whether Indian or foreign will be treated as assets.
- ◆ **Exclusion:** Motor car used by the assessee in the business of running them on hire or as stock-in-trade will be excluded from the scope of the term “assets”.
- Example:** Maruti cars will not be treated as assets in the hands of Maruti Udyog Ltd. Similarly, in the hands of automobile dealers who purchase and sell cars, such cars will not be treated as assets.
- (iii) **Jewellery etc:** This head of assets includes jewellery, bullion and furniture, utensils or any other article made wholly or partly of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metal.
- ◆ **Definition:** The Act has given an inclusive definition of the term ‘jewellery’ to include ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stones and whether or not worked or sewn into any wearing apparel. It also includes precious or semi-precious stones, whether or not set in any furniture, utensils or other article or worked or sewn into any wearing apparel.
- ◆ **Exclusion:** Where any of the above assets is used by the assessee as stock-in-trade, it will not be considered as an asset.
- (iv) **Yachts, boats and aircraft:** It is to be noted that ships are not included in the definition.
- ◆ **Exclusion :** If the assessee uses the above assets for commercial purposes, then they will not be treated as assets. The term ‘commercial purposes’ has not been defined in the Act. It seems that even if the assessee uses these assets as stock-in-trade that will be treated as usage for commercial purposes. For example, aircraft will not be considered as assets in the hands of a company manufacturing aircraft or dealing with the purchase and sale of aircraft.
- (v) **Urban land :** Urban land means land situated in any area which is within the jurisdiction of a municipality or a cantonment board and which has a population of not less than 10,000. It also includes any land situated within 8 kilometers from the local limits of any municipality or cantonment board. Such area should be notified by the Central

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Government having regard to the extent of and scope for, urbanisation of that land and other relevant considerations.

◆ **Exclusions** : The following lands will not be considered as urban land and consequently outside the scope of the term “assets”:

- (a) Land on which construction of a building is not permissible under any law for the time being in force in the area in which such land is situated.
- (b) Land occupied by any building which has been constructed with the approval of the appropriate authority.
- (c) Unused land held by the assessee for industrial purposes for a period of two years from the date of its acquisition by him.
- (d) Any land held by the assessee as stock-in-trade for a period of ten years from the date of its acquisition by him.

Examples:

- 1. A acquires a plot of land measuring 500 square meters in New Delhi for constructing a house. He proposes lay out and gets the permission of Delhi Development Authority to build a house on the plot. However, he does not construct the house. The plot of land will be treated as urban land liable to wealth-tax.
- 2. In the above example, once A constructs house, the plot ceases to be an urban land. However, the house will be considered as an asset.
- 3. A was allotted an industrial plot in Ambattur industrial estate in Madras. This plot will not be considered as an urban land in A's hands for two years from the date of acquisition even if he does not start any industrial activity. But once the period of two years expires, the plot will be considered as an urban land in A's hands unless he makes use of it for industrial purposes.

(vi) Cash in hand:

- (a) **In the case of individual and HUF:** Cash in hand whether recorded or unrecorded in excess of Rs.50,000 will be considered as asset. Obviously, the limit of Rs.50,000 will be considered as on the valuation date. It is clear that cash in bank will not be treated as asset.
- (b) **In the case of other person:** Any amount not recorded in the books of account will be considered as an asset. The ceiling limit of Rs.50,000 is not applicable in the case. It follows that if cash is recorded, it will not be considered as an asset.

Example: On a raid conducted by the department in the premises of a company a sum of Rs.20 lakh was found and the same had not been recorded in the books of account. This sum of Rs.20 lakh will be considered as asset in the hands of the company.

1.3.4 Net Wealth : The expression 'net wealth' according to the section 2 (m) means the amount by which the aggregate value, computed in accordance with the provisions of this Act, of all the assets wherever located, belonging to the assessee on the valuation date, [including assets required to be included under section 4], in his net wealth as on that date under this Act, is in excess of the aggregate value of all the debts owed by the assessee, on the valuation date which have been incurred in relation to the said assets.

- ◆ **Company:** As noted earlier under section 3 of the Wealth-tax Act wealth-tax is leviable on three categories of tax-payers namely, individuals, Hindu undivided families and companies. The definition of the term 'Company' in section 2 (h) provides that it will have the same meaning assigned to it as in Clause (17) of section 2 of the Income-tax Act.

According to this definition the term 'company' means any Indian company or (ii) any body corporate incorporated by or under the laws of a country outside India or (iii) any institution association or body which is or was assessable or was assessed as a company for any assessment year under the 1922 Act or for any assessment year commencing after 1.4.1970, or (iv) any institution, association or body, whether incorporated or not, whether Indian or non-Indian, which is declared by the Board by general or special order to be a company provided that such institution, association or body shall be deemed to be a company only for such assessment year or assessment years as may be specified in the declaration. The definition has got much importance in view of the fact that no wealth-tax is chargeable on the entities falling outside the scope, of this definition.

1.3.5 India [Section 2(ka)]

'India' means –

- (i) the territory of India as per article 1 of the Constitution,
- (ii) its territorial waters, seabed and subsoil underlying such waters,
- (iii) continental shelf,
- (iv) exclusive economic zone or
- (v) any other specified maritime zone and the air space above its territory and territorial waters.

Specified maritime zone means the maritime zone as referred to in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976.

1.4 DEDUCTIBILITY OF TAX LIABILITIES

In the case of *Sethu Parvathi Bai vs. CWT* (1968) 69 ITR (SC), it was held that the wealth tax liability of an assessee on the valuation date for the assessment year beginning on the first day of April next following is 'debt owed' within the meaning of section 2(m) and would be deducted from the estimated value of the assets as on the valuation date.

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However, CBDT Circular No. 663 dt. 28-4-93 observes that consequent to the amendment of Section 2(m), w.e.f. the assessment the year 1993-94, the question has arisen regarding admissibility of deduction of the wealth tax liability for the purpose of computing the taxable net wealth. The Board has opined in the circular that the liability under the Wealth Tax Act is not a debt owed by the assessee incurred in relation to the assets taxable under Wealth Tax Act. The liability of wealth tax is the personal liability of the assessee. Moreover, this liability is not a debt incurred by the assessee but is created by the Statute. Therefore, no deduction is to be allowed for the wealth tax liability in the computation of the taxable net wealth of the assessee from the assessment year 1993-94 onwards.

It is debatable whether the amendment made by Finance Act, 1992 in section 2(m) overrules the decision of the Supreme Court cited above.

However, the circular has not mentioned anything about income-tax liability. It is a point to be considered whether income-tax liability at least to the extent attributable to chargeable assets could be treated as a debt incurred in relation to the assets taxable under the Wealth Tax Act. There appears to be a difference of opinion on this point and the matter is not free from doubt,

In *C.W.T. vs. Keshardeo S. Moraka* (1977) ITR. 576, the Bombay High Court held that when a deduction in respect of a decretal debt is claimed by an assessee in computing his net wealth under the Wealth-tax Act, 1957, the question to be considered is what is the quantum of the debt the particular assessee may be called upon to pay in law and if legally and validly he can be called upon to discharge the whole of the decretal debt, then it is a debt due by him for which deduction can be claimed in a wealth-tax return. In the case of joint and several liability a right of contribution will arise only if the debt was discharged and merely because there is a right of contribution in case the whole debt is discharged by the assessee, the entire amount due and payable does not cease to be debt. In this view of the matter, the Court held that in a case where a decree was passed against the assessee and two others jointly and severally, the entire amount of the decretal amount was admissible deduction in computing the wealth of the assessee. This Judgement has been followed in certain other cases also.

In *C.W.T. vs. H.H. Vijayamba Dowagar Maharani Saheb of Bhavnagar* (1979) 117 I.T.R. 784, the Supreme Court held that even a liability resulting from an enforceable, family arrangement is admissible as a 'debt' owed, under section 2(m). It may be noted that section 2(m) refers to debts actually and really owed by the assessee as distinguished from notional ones., thus estimated liability to capital gains on a notional sale would not be deductible as debt. [*Bharat Har Singhania Vs. C.W.T.* (1979) ITR.258 (All)].

However, it may be noted that the principles emerging from the above rulings would apply now in relation to debts which have been incurred in relation to the specified assets.

1.5 CHARGEABILITY

1.5.1 Persons chargeable to tax: Wealth tax is chargeable on the net wealth of every individual, Hindu undivided family and company at the rate of one percent of the amount by which the net wealth exceeds Rs.30 lakh.

The terms 'individual' and 'Hindu undivided family' have not been defined either in the Income-tax Act or in the Wealth-tax Act and, therefore, they have to be construed in their general

sense. For the purpose of wealth-tax, the word 'individual' has been interpreted in several cases to include a group or body of individuals like joint heirs, joint donees, joint purchasers, body of trustees, Mappilla, Marumakkathayam Tarward and a financial corporation established under the Central, Provincial or State Act.

As regards the Hindu undivided family, the expression is used with reference to all Schools of Hindu Law and it includes even a Jain undivided family [*C.W.T. vs. Shrimati Champa Kumari Singhi and others* (1972) 83 ITR. 720 (SC)].

It is to be noted that the expression Hindu undivided family is different from the Hindu coparcenary. The Hindu joint family consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters. A Hindu coparcenary, on the other hand, is a much narrower body than the joint or coparcenary property, those being sons, grandsons and great grandsons of the holder of the joint family property for the time being. Therefore, there may be Hindu undivided family, even when there is a single coparcener along with the widows of deceased members. If there is property belonging to the Hindu undivided family assessment can be made on the single coparcener in the status of Hindu undivided family. The Supreme Court held in *Narendranath vs. C.W.T.* (1969) 74 ITR 190, that there is nothing in the Wealth-tax Act to suggest that the Hindu undivided family as an assessable unit must consist of at least two male members. It was held that when a coparcener of a Hindu undivided family governed by Mitakshara School of Hindu Law having a wife and two minor daughters and no son receives his share in the joint family property on partition such property in the hands of the coparcener belong to the Hindu undivided family of himself, of his wife and minor daughter and cannot be assessed as his individual property. In view of this decision the joint family-property acquired by a single coparcener on partition or by survivorship along with his wife and minor daughter shall be assessed in the hands of the sole coparcener as the property of the Hindu undivided family and not that of an individual. Similarly any property in the hands of the sole surviving coparcener on the induction of a lineal descendent or in the presence of a person who is to be treated as member of the joint family, e.g., mother who is entitled to maintenance, has to be impressed with the character of the joint family property. However, a single member by himself, cannot constitute a Hindu undivided family and to constitute joint family, there must be more than one member. The word 'family' always signifies a group. Plurality of persons is an essential attribute of a family. A single person, male or female does not constitute a family. [*C.Krishna Prasad vs. C.I.T.* (1974) 97 ITR 493 (S.C.)].

In *C.W.T. vs. Gaitri Shanker Bhar* (1972) 841.T.R. 609, the Supreme Court affirming the view of the Calcutta High Court held that a joint family consisting of the legal heirs of deceased person did not come into existence spontaneously on the death of that person where he was governed by Dayabagha School of Hindu Law. After the death of a father, belonging to the Dayabagha School, his successors may live as Hindu undivided family or be separate. If they do not decide to live together as Hindu undivided family, they merely own the inherited

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property as joint property as tenants in common but do not form a joint family. A joint family amongst brothers under the Dayabagha law is not a creation of law but of desire to live jointly. On the facts of this case, the Court held that heir of the deceased had taken the property of the deceased in separate shares and that according to law each one of them become liable to pay wealth tax as an individual.

1.5.2 Nature of property inherited by a Hindu under section 8 of Hindu Succession Act: There was a judicial controversy regarding the issue as to whether the property which devolved on a Hindu, on the death of his father intestate, after the coming into force of the Hindu Succession Act, under section 8 of that Act, would constitute HUF property consisting of his own branch including his sons or his own individual property. The High Courts of Allahabad, Madras (Full Bench), M.P. and A.P. on the one side, held the view that such property would be individual property in the hands of the son while the Gujarat High Court on the other hand took the view that such property would be in the nature of joint family property in the hands of the son and not his separate property.

The Supreme Court has resolved this controversy in the case of *C.W.T. vs. Chander Sen* (1986) 161 ITR 370 (SC) by overruling the Gujarat High Court's decision and approving the view of the other courts. The Supreme Court pointed out that the Hindu Succession Act was enacted to amend and codify the law relating to intestate succession among Hindus. Section 8 of the Act lays down the scheme of devolution of the property of a Hindu dying intestate and the express words of this provision cannot be ignored and must prevail.

Certain heirs have been classified in the Schedule under section 8 on whom such property should devolve. Those specified in Class 1 take the property simultaneously to the exclusion of all other heirs. Class 1 heirs, include son, daughter, etc., including the son of a predeceased son but does not include specifically the grand son, being a son of son living. The Supreme Court emphasised that he (grand son) could not get any right in the property of his grandfather. In the view of the matter, the Supreme Court held that when son inherits the property in the situation contemplated by section 8 he does not take it as Karta of his own undivided family. The property which devolved on a Hindu on the death of his father intestate after the coming into force of the Hindu Succession Act, 1956 did not constitute HUF property consisting of his own branch including his sons.

In the case before the Supreme Court, R and his son C constituted a HUF. On 10-10-1961, there was a partial partition in the family by which the business was divided between the father and the son and thereafter it was carried on by a partnership consisting of the two. On 17-7-65 R died leaving behind his son C and his grandsons i.e. the sons of C. His wife and mother predeceased him and he had no other issue except C. On his death, there was a credit balance of Rs.1,83,043 in his account in the books of the firm. For the assessment year 1966-67 the sum of Rs.1,83,043 standing to the credit of R was not included in the net wealth of the family of C. (the assessee family) on the ground that this amount devolved on C to his individual capacity and was not the property of the assessee family. A sum of Rs.23,330 was

credited to the account of late R on account of interest accruing on his credit balance. In the proceedings under the IT Act for the assessment year 1967-68 the sum of Rs.23,330 was claimed as deduction.

The Assessing Officer disallowed the claim relating to interest on the ground that it was a payment made by C to himself. Likewise in the Wealth-tax assessment, the amount standing to the credit of R was included by Assessing Officer in the wealth of assessee family.

The Supreme Court based on the reasoning explained earlier, held on the facts of the case, that the sums standing to the credit of R belonged to C in his individual capacity and not the Hindu family and the interest of Rs.23,330 was an allowable deduction in respect of the income of the family from the business.

It is to be noted that the holder of an impartible estate is to be assessed to wealth-tax as an individual owner of the properties comprised in the estate. It may also be noted that firm or an association of persons is not chargeable to wealth tax as such. However, the value of the interest of the partner or the member in the assets of the firm or association determined in the manner laid down in Schedule III is to be included in the assessment of the net wealth of the individual concerned. These points will be considered later in the context of the discussion on section 4.

◆ **Exemption Limit :** Wealth tax shall be charged on the net wealth of every individual, Hindu undivided family and company at the rate of one percent of the amount by which the net wealth exceeds *Rs.30 lakh*.

1.5.3 Entities not liable to tax: According to section 45, no tax shall be levied under this Act in respect of the net wealth of:

- (a) any company registered under section 25 of the Companies Act, 1956;
- (b) any co-operative society;
- (c) any social club
- (d) any political party.
- (e) a Mutual Fund specified under section 10(23D) of the IT Act.

It may be noted that the expression 'political party' for the purposes of (i) above will have the meaning assigned to it in the Explanation to section 13A of the Income-tax Act. The expression would cover an association or body of individual citizens of India registered with the Election Commission of India as a political party and would also include a political party deemed to be registered with that Commission under the Election Symbols (Registration and Allotment) order, 1968.

1.5.4 Gamut of taxation: In computing the net wealth of an individual who is not a citizen of India or an individual or a HUF not resident in India or resident but not ordinarily resident in India or a non-resident company during the year on the valuation date, the following assets will not be taken into account:-

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- (i) The value of the assets and debts located outside India.
- (ii) The value of the assets in India represented by any loans or debts owing to the assessee.

However, in order to claim exemption, in respect of such assets, the interest payable on such loans or debts should not be includible in the total income of the assessee under section 10 of the Income-tax Act.

It is clear, therefore that the citizenship and the residential status affect both the chargeability and the liability under the Act. The residential status of the assessee is to be judged by the same principles as laid down in section 6 of the Income-tax Act.

◆ **Location:** The above discussion will also make it clear that for the purpose of computing the net wealth it is essential to ascertain location of assets and debts whether they are in India or outside India. The question as to where the asset is located is essentially one of fact and will have to be decided in the light of the available evidence. The following instructions have been issued by the Central Board of Direct Taxes for general guidance in this regard:

- (a) Tangible immovable property is situated in India if the property lies in India.
- (b) Rights or interest in or over immovable property (otherwise than by way of security) or benefits arising out of immovable property are located in India in the immovable property to which the rights are attached, or on of which the benefits arise, lies in India.
- (c) Rights or interest (otherwise than by way of security in/over tangible movable property are located in India, if such property is located in India or if it is in transit to India.
- (d) Debts: The general principle of law is that the debts are situate where the debtor resides and a stipulation that the payment should be made in a country where the debtor is not residing does not affect the general rule and therefore 'Debts' secured or unsecured (other than those dealt separately) are located in India if they are contracted to be repaid in India or if the debtor is residing in India.
- (e) Moneys kept in a bank account in the form of deposits or otherwise are located in India if the branch of the bank at which the account is kept is situated in India.
- (f) Security issued by the Central Government or a State Government or a Municipality or other local authority in India are located in India unless they are inscribed for payment outside India.
- (g) Shares, stocks, debentures or debenture stock in a company are located at the place where the company is incorporated.
- (h) Ships or aircraft are located in India if they are registered in India.
- (i) Copyright or licence to use any copyright material, a patent, a trade mark or design is located in India if the right arising, therefrom is exercisable in India.

- (j) Patents trade marks and designs are located in India if they are registered in India.
- (k) Rights or causes of action ex-delicto (i.e., arising out of wrongs) not included in any of the items mentioned above, are situated in India if they are enforceable in India.

It is not possible to give an exhaustive list of assets and the principle to be applied in determining the location of all assets. For assets which are not covered as the above items, the location has to be fixed having regard to the nature of the assets.

It is to be noted that although the Central Board had instructed that goods in transit to India are to be treated as located in India. Such instruction is no longer valid in view of the Supreme Court's decision in *C.W.T. Vs. Consolidated Pneumatic Tools Co. Ltd. (1971) 81, ITR 752*. In that case it was held that goods on the high seas even though on transit to India cannot be considered as assets located in India, and they are located outside India. In *C. W.T. Vs. Calcutta Tramways Co. Ltd. (1968) 66 ITR 471*, the Calcutta High Court held that the debentures by a company incorporated in England are located outside India even though they were secured by a floating charge on assets located in India.

1.6 DEEMED WEALTH

Assets belonging to others but includible in the net wealth of an individual [Section 4]

1.6.1 Assets transferred to certain persons: Section 4 extends the gamut of taxation of net wealth of an individual. It provides that net wealth of an individual will include, in certain circumstances, certain assets belonging to others. This section applies only to individuals and the term "individual" for this purpose includes both male and a female.

Section 4(1) (a) provides that in computing the net wealth of an individual, the value of assets which, on the valuation date, are held by the following persons should be included as if they belong to the individual:

- (1) Assets held by his/her spouse to whom such assets have been transferred directly or indirectly without adequate consideration or otherwise than in connection with an agreement to live apart.
- (2) Assets held by his/her minor child . It is significant to note that it is not necessary that such assets must have been transferred directly or indirectly by the individual to the minor. Consequently, all assets held by a minor child will be included in the net wealth of the individual. However, if such a minor child is (a) suffering from any disability of the nature specified in section 80U of the Income-tax Act or (b) a married daughter of such individual, there will be no such clubbing of wealth. The clubbing provisions will not apply in respect of such assets as have been acquired by the minor child out of his income earned from any manual work done by him or activity involving application of his skill, talent or specialised knowledge and experience. In all other cases of assets held by a minor child, the value of such assets will be clubbed with the value of assets held by the individual as per the procedure laid down in the provision.

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Where the clubbing provisions operate, the assets will be clubbed as follows:-

- (a) Where the marriage of his parents subsists, the assets will be clubbed in the net wealth of that parent whose net wealth (excluding assets of the minor child so includible) is greater.
- (b) Where the marriage of his parents does not subsist, they will be clubbed in the net wealth of that parent who maintained the minor child in the previous year as defined by the Income-tax Act.

Where any such assets are once included in the net wealth of either parent, such assets shall not be included in the net wealth of either parent in any succeeding year unless the Assessing Officer is satisfied after giving that parent an opportunity of being heard that it is necessary to do so.

- (3) Any other person or AOPs to whom such assets have been transferred by the individual directly or indirectly otherwise than for adequate consideration for the immediate or deferred benefit of the individual or his/her spouse.
- (4) Any person or AOPs to whom such assets have been transferred by the individual otherwise than under an irrevocable transfer.

It is significant to note that the term “transfer” has not been defined by the Wealth tax Act.

- (i) For the purposes of section 4, the expression “transfer” includes any disposition, settlement, trust, covenant, agreement or arrangement.
- (ii) The expression “irrevocable transfer” includes a transfer of assets which, by the term of the instrument effecting it, is not revocable for a period exceeding 6 years or during the life time of the transferee and under which the transferor derives no direct or indirect benefit, but does not include a transfer of assets if such instrument
 - (a) contains any provision for the retransfer directly or indirectly of the whole or any part of the assets or income therefrom to the transferor; or
 - (b) in any way gives the transferor a right to reassume power directly or indirectly over the whole or any part of the assets or income therefrom.

It will be interesting here to note the definition of transfer and revocable transfer under section 63 of the Income-tax Act.

Accordingly, for the purposes of section 60, 61, 62 and 63, a transfer shall be deemed to be revocable if-

- a) it contains any provision for the retransfer directly or indirectly of the whole or any part of the income or assets to the transferor or
- b) it in any way gives the transferor a right to reassume power directly or indirectly over the whole or any part of the income or assets.

Transfer includes any settlement, trust, covenant, agreement or arrangement.

As noted earlier, section 4 applies only to individuals and consequently transfer by HUF or transfer of HUF's property made by a Karta to coparcener's wife or minor child or even to his own wife as Karta will not fall under the purview of this section. The relationship of spouse must exist on the date of transfer and subsist on the valuation date. If the husband buys his property in the name of his wife or child out of his own funds, it would amount to transfer within the meaning of this section.

- (5) Assets held by son's wife of such individual to whom such assets have been transferred by the individual directly or indirectly on or after 1st June, 1973 otherwise than for adequate consideration.
- (6) Assets held by a person or association of persons to whom such assets have been transferred by the individual directly or indirectly on or after 1st June 1973 otherwise than for adequate consideration for the immediate or deferred benefit of the son's wife of such individual or both.

- ◆ **Transferred asset converted into another form — value of which asset is to be included:** Section 4(1)(a) specifically provides that the clubbing envisaged under the provision would operate whether the assets referred to above are held in the form in which they were transferred or otherwise.

There was a judicial controversy regarding the question as to where a transferred asset is converted into another form, whether the value of the originally transferred asset or the converted asset as on the valuation date is to be included in the net wealth. Recently, the Supreme Court resolved this controversy in *CWT vs. Kishanlal Bubna* (1993) 204 ITR 600 by holding that it is the value of the converted asset as on the valuation date that is to be included. The words, "such assets" in sub-clause (iii) of section 4(1)(a) do, no doubt refer to the assets described in clause (a) in the sense that they mean "those assets". But the use of the words "such assets" does not imply that it is only the value on the valuation date of the assets that were actually transferred which is to be taken into account and not of any assets to which those transferred assets may have been converted. The words "whether the assets referred to in any of the sub clauses aforesaid are held in the form in which they were transferred or otherwise" put the matter beyond doubt. Where, what is transferred by the assessee is money and the transferee utilises that money to acquire an asset, it is the value of that asset on the valuation date which is relevant for the purpose of inclusion in the net wealth of the assessee. Where, what is transferred by the assessee is an asset and the transferee disposes of that asset and acquires with the consideration received another asset it is the value of that acquired asset on the valuation date which is relevant for the purposes of computing the net wealth of the assessee.

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Illustration: Mr. A made a cash gift of Rs.1,00,000 to Mrs. A in 1987. Mrs. A purchased a let out flat in Delhi with that money. The value of the flat on 31st March 2009 i.e. valuation date of Mr. A's wealth-tax assessment was Rs.5,75,000. The value of the flat that is to be included in the net wealth of Mr. A as per section 4(1)(a) is Rs.5,75,000 and not Rs.1,00,000.

1.6.2 Share in Partnership firms or an Association of persons: Section 4(1) provides that where the assessee is a partner in a firm or is a member of an association of persons, the value of his interest in the assets of the firm or association determined in the manner laid down in Schedule III is to be included in his net wealth.

The manner in which such value is to be computed has been prescribed in Rule 16 of Schedule III of the Wealth-tax Act, 1957. Valuation of assets under Schedule III to the Act has been discussed in detail later in this chapter.

1.6.3 Conversion of separate property of an individual into HUF property or gift of individual property into HUF property: Section 4(1A) prevents the avoidance or reduction of tax liability through the device of converting separate property of an individual into joint property. The relevant provisions are explained below:

- (i) Where an individual converts his separate property into a joint family property of the Hindu undivided family of which he is a member, by impressing such property with the character of the joint family property or by throwing such property into common stock of the Hindu undivided family or by transferring such individual property to the family otherwise than for adequate consideration he will be deemed to have transferred the converted property through the family to the members of the family for being held by them jointly.
- (ii) In such a case the entire value of the property so converted or transferred would be included in the net wealth of the individual who made the conversion.
- (iii) In the event of a partial or total partition in the Hindu undivided family the shares allotted to the spouse of such individual in the converted or transferred property will be included in the net wealth of the individual on the footing that they represent assets transferred by the individual indirectly.

The term 'property' has been given an extended meaning for the purposes of this provision. It includes any interest in property movable or immovable the proceeds or sale thereof and money or investment for the time being representing the proceeds of sale thereof and where the property is converted into any other property by any method such other property.

Thus this provision covers not only conversion of individual property into H.U.F. property but also gift of individual property into H.U.F. property.

1.6.4 Gift by book entries: Sub-section (5A) provides that in cases where a gift of money from one person to another is made by means of entries in the books of account maintained

by the person making the gift or by an individual or H.U.F. or a partnership firm or an association of persons or body of individual with whom or with which the individual has any business or other relationship the value of such gift shall be included in the computation of the net wealth of the person who makes the gift, unless the person proves to the satisfaction of the Wealth-tax Officer that the money has actually been delivered to the other person at the time the entries were made.

1.6.5 Impartible estate: Section 4(6) provides that the holder of an impartible estate is deemed to be individual owner of all properties, comprised in the estate. Some properties, although partible by nature, can be impartible by custom or by the terms of a grant by Government in the sense that such properties always devolved on a single member of the family to the exclusion of other members. Impartible estate are estates which by special law or customs descend to one member and which are impartible, though they are joint property, in the eyes of law, belonging equally to other members. Ancient Zamindari estates descending to a single member by special family custom, jagirs, palayams in Tamil Nadu can be cited as examples of impartible estates.

As a result of the various legislations that have been and are being made by the various State Governments as well as Central Governments liquidating all Zamindari estates, big and small, whether partible or impartible and the abolition of the privileges of the former rulers of Indian States, the topic of ownership of impartible estates has got only academic importance now.

1.6.6 Tax treatment of members of co-operative housing societies, etc.: Sub-section (7) deals with tax treatment of members of co-operative society, company or other association of persons. Where the assessee is a member of a co-operative society, company or other association of persons and a building or part thereof is allotted or leased to him under a house building scheme of the society, company or association, as the case may be, the assessee shall, notwithstanding anything contained in this Act or any other law for the time being in force, be deemed to be the owner of such building or part and the value of such building or part, shall be included in computing the net wealth of the assessee; and, in determining the value of such building or part, the value of any outstanding installments of the amount payable under such scheme by the assessee to the society, company or association towards the cost of such building or part and the land appurtenant thereto shall, whether the amount so payable is described as such or in any other manner in such scheme, be deducted as a debt owed by him in relation to such building or part.

1.6.7 Tax treatment in the case of part performance etc. :

As per sub-section (8), a person

- (a) who is allowed to take or retain possession of any building or part thereof in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882;

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- (b) who acquires any rights (excluding any rights by way of a lease from month to month or for a period not exceeding one year) in or with respect to any building or part thereof by virtue of any such transaction as is referred to in clause (f) of section 269UA of the Income-tax Act, 1961 shall be deemed to be the owner of that building or part thereof and the value of such building or part shall be included in computing the net wealth of such person.

Section 269UA (f) defines “transfer” for the purposes of purchase of immovable properties by the Central Government.

Accordingly, “transfer”

- (i) in relation to any immovable property means transfer of such property by way of sale or exchange or lease for a term of not less than twelve years, and includes allowing the possession of such property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882).

Explanation : For the purposes of this sub-clause, a lease which provides for the extension of the term thereof by a further term or terms shall be deemed to be a lease for a term of not less than twelve years, if the aggregate of the term for which such lease is to be granted and the further term or terms for which it can be so extended is not less than twelve years.

- (ii) in relation to any immovable property of the nature referred to in sub-clause (ii) of clause (d) means the doing of anything (whether by way of admitting as a member of or by way of transfer of shares in a co-operative society or company or other association of persons or by way of any agreement or arrangement or in any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of, such property.

◆ Certain definitions for the purposes of section 4

- (i) the expression “transfer” includes any disposition, settlement, trust, covenant, agreement or arrangement;
- (ii) the expression “child” includes a step-child and an adopted child;
- (iii) the expression “irrevocable transfer” includes a transfer of assets which, by the terms of the instrument effecting it, is not revocable for a period exceeding six years or during the lifetime of the transferee, and under which the transferor derives no direct or indirect benefit, but does not include a transfer of assets if such instrument-
 - (a) contains any provision for the retransfer, directly or indirectly, of the whole or any part of the assets or income therefrom to the transferor; or
 - (b) in any way gives the transferor a right to reassume power, directly or indirectly, over the whole or any part of the assets or income therefrom;
- (iv) the expression “property” includes any interest in any property movable or immovable, the proceeds of sale thereof and any money or investment for the time being

representing the proceeds of sale thereof and where the property is converted into any other property by any method, such other property.

- ◆ **Liability of transferee:** It may be noted that section 33 of the W.T Act fastens a liability on the transferees to pay the ratable part of tax on the assets held by them and which are included in the transferor's wealth under the provisions of section 4, under certain circumstances.

1.7 EXEMPTIONS

Section 5 enumerates assets that are not to be included in the net wealth of an assessee and on which the assessee is not required to pay any wealth tax. A thorough knowledge of this provision is important not only from the point of view of examination but also from the point of view of claiming one's rights under the Act. The properties which enjoy the exemption under various clauses of section 5 are listed below.

- (1) Any property held by the assessee under trust or other legal obligation for any public purpose of a charitable or religious nature in India [Clause (i)].

However, as under the Income-tax Act, the exemption under this provision will not be available in respect of business assets of public charitable or religious trusts and institutions except in the following cases:

- (a) Where the business is carried on by a trust wholly for public or religious purposes and the business consists of printing and publication of books or the business is of a kind notified by the Central Government in this behalf in the Official Gazette.
- (b) The business is carried on by an institution wholly for charitable purposes and the work in connection with the business is mainly carried on by the beneficiaries of the Institution.

The exemption which is available to the trustees of a public trust, is subject to the provisions of section 21A discussed later. It is to be noted that in the case of a trustee of a private trust, there is no exemption and the value of the trust property becomes includible in the net wealth of the trustee in his capacity as trustee.

The Bombay High Court held in *Trustees of Bhiwandiwalla Trust vs. C. W.T.* (1976) *I.T.R.* 709 that under section 5(i) all the objects need not fall within the expression "public purpose of a charitable or religious nature in India". It would be sufficient if the objects of the trust considered as a whole could be regarded to be within the expression. But the A.P. High Court held in *C.W.T. vs. Hyderabad Race Club* (1978) *I.T.R.* 453, that where assets are held for a public purpose which was both charitable and non-charitable in nature the assets held by assessee were liable to tax irrespective of whether they are applied solely for charitable purpose or for non-charitable purpose. The Andhra Pradesh High Court held in *C.W.T. vs. Trustees of H.E.H. The Nizam's Religious Endowment Trust*

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(1977) 1081. T.R. 229 that in order to be entitled to exemption under section 5(i) of the Wealth-tax Act, the property must be held under trust for religious and charitable purpose and such purpose must be confined in its scope to the taxable territories. The area or purpose of the trust is the decisive factor for claiming exemption.

However, exemption in respect of property forming part of business of the aforesaid institutions would now be available only if such institution satisfies the conditions of section 11(4A) of the Income-tax Act.

- (2) The interest of the assessee in the coparcenary property of the Hindu undivided family of which he is a member [Clause (ii)].
- (3) Any one building in the occupation of a Ruler, being a building which immediately before the commencement of the Constitution (26th Amendment) Act, 1971, was his official residence by virtue of a declaration by the Central Government [Clause (iii)].
- (4) Jewellery in the possession of a Ruler which is not his personal property and which is recognised by the Central Government as his heirloom [Clause (iv)].

This recognition of the jewellery in the possession of a Ruler as his heirloom is also subject to certain conditions and if any of the specified conditions is not fulfilled the Board has the power to withdraw the recognition. In such a case of withdrawal of the recognition, wealth-tax shall be payable by the Ruler for the assessment years for which the jewellery was exempted on account of the recognition. The fair market value of the jewellery on the date of the withdrawal of the recognition shall be deemed to be the fair market value of such jewellery on each successive valuation date relevant to the assessment years. However, in such a case, the aggregate amount of wealth tax payable in respect of the jewellery for all the assessment years (in respect of which tax becomes payable consequent on withdrawal of the recognition) shall not exceed 50% of its fair market value on the valuation date relevant for the assessment year in which recognition was withdrawn.

- (5) Clause (v) seeks to provide wealth tax exemption in respect of
 - (a) money
 - (b) value of assets brought into India and
 - (c) value of assets acquired by him out of such moneys to an assessee, who must be person of Indian origin or Indian citizen and who must have returned to India from a foreign country for settling down permanently.

This exemption will be available only for a period of seven assessment years commencing with the assessment year next following the date on which such persons returned to India.

In the case of a person covered by the provisions the moneys and the value of assets brought by him into India and the value of the assets acquired by him out of such

moneys within one year immediately preceding the date of his return and at any time thereafter will qualify for exemption.

The Explanation to this clause clarifies that the moneys standing to the credit of a person (to whom this clause is applicable in a non-resident external) account in any Bank in accordance with the Foreign Exchange Regulation Act, 1973 and rules made thereunder on the date of his return shall be deemed to be moneys brought by him into India on that date.

- (6) The following are exempt under clause (vi) in the case of an individual/HUF –
- a house or part of house, or
 - a plot of land not exceeding 500 sq. meters in area.

Self-examination questions

1. Define the following terms under the Wealth-tax Act -
 - (a) Assessment year and valuation date;
 - (b) Net wealth
2. A company incorporated outside India is not liable to wealth tax in India. Discuss.
3. A Cooperative Society formed for the purpose of construction of residential flats for its members acquired a large area of urban land for Rs.3 crores. The society had a membership of 10 members, all having equal share. The Assessing Officer proposes to tax urban land in the hands of the society.
 - (i) What is meant by urban land?
 - (ii) Is the action of the Assessing Officer correct?
 - (iii) Can the members of the society be assessed on their share in the value of the urban land?
4. Enumerate the entities to which the provisions of the Wealth-tax Act do not apply.
5. Discuss the provisions of the Wealth-tax Act regarding the inclusion of the wealth of minor child in the assessment of the parent. Enumerate the exceptions to this provision.
6. Under what circumstances can the net wealth of an individual include assets held by others?
7. Discuss the validity of the following proposition, setting forth the reasons for your answer – Wealth tax is not a debt owed on the valuation date and is therefore not deductible from net wealth.
8. Sterling Constructions Ltd. furnishes the following particulars of its wealth for the valuation date 31st March 2010. Compute its net wealth on valuation date. You are also required to compute the wealth-tax payable by the company for A.Y.2010-11.

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<i>Particulars</i>	<i>Rs. in lakh</i>
(i) Land in urban area (held as stock -in-trade since 1993)	52
(ii) Flats constructed remaining unsold (not held as stock)	47
(iii) Motor car (including one imported car worth Rs.8 lakh)	17
(iv) Jewellery	6
(v) Aircrafts	125
(vi) Ships	107
(vii) Cash in hand as per cash book	6.2
(viii) Bank balance	37.7
(ix) Guest house in rural area	13
(x) Residential flats of uniform area provided to 5 employees (salary of 2 employees exceed Rs.5 lakh p.a.)	25
(xi) Residential house provided to a whole-time director (whose salary is Rs.4 lakh p.a.)	9

The company has taken the following loans -

(a) For purchase of land in urban area	20
(b) For purchase of jewellery	4
(c) For purchase of guest house in rural area	10
(d) For purchase of ships	80

9. Ganesh furnishes the following particulars of his wealth for the valuation date 31st March 2010 -

Particulars	Rs. in lakhs
(i) Residential house at Chennai	45
(ii) Residential house at Coimbatore	20
(iii) Plot of land comprising an area of 300 square meters at Hyderabad	75
(iv) House at Chennai exclusively used for carrying on his business	25
(v) Commercial complex at Coimbatore	30
(vi) Residential house at Bangalore let out for 320 days during the relevant previous year	20
(vii) Motor cars used in business of running them on hire	15

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(viii) Shares in private limited companies	16
(ix) Cash in hand	2
(x) Jewellery	10

The company has taken the following loans -

(a) For purchase of land at Hyderabad	25
(b) For purchase of jewellery	7
(c) For purchase of shares in private limited companies	10

Amounts stated against assets, except cash in hand, are the values determined as per Section 7 of the Wealth tax Act, 1957 read with Schedule III thereto. Compute the net wealth of Ganesh on the valuation date 31.3.2010.

State the reasons for inclusion or exclusion of the various items

10. Mr. Suresh, a Not Ordinarily Resident in India, seeks your advice with regard to the furnishing of his Wealth-tax return. The value of assets held on 31.03.2010 is indicated below. You are requested to compute the taxable wealth of Mr. Suresh giving justification for the inclusion or exclusion of each item. The valuation date as indicated above is 31st March, 2010:

Particulars	Rs.
(i) Motor cars of foreign make held as Fixed Assets	10,00,000
(iii) Residential House Property at Nagpur let out w.e.f. 8 th April, 2009	10,00,000
(iv) Jewellery held	5,00,000
(v) Lands purchased for industrial purpose:	
On 21 st Feb, 2005	4,00,000
On 20 th June, 2009	8,00,000
(vi) Loan against the purchase of lands:	
On 21 st Feb, 2005	3,00,000
On 20 th June, 2009	5,00,000
(vii) Wealth-tax liability	15,000
(viii) Cash on hand	60,000

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(ix)	Cash at bank	2,00,000
(x)	Fixed Assets located in London	30,00,000
(xi)	Value of Assets held by Mrs. Suresh acquired out of the gifts received from her husband:	
	Shares and Securities	3,00,000
	Residential House Property at Pune	15,00,000

VALUATION UNDER WEALTH TAX ACT

2.1 VALUATION OF ASSETS [SECTION 7 READ WITH SCHEDULE III]

Under section 7, the value of any asset other than cash on the valuation date is to be determined in the manner laid down in the Schedule III to the Wealth-tax Act. Sub-section (2) of section 7 gives option to the assessee in the case of a house belonging to him and exclusively used by him for residential purposes to have the value determined under Schedule III as on the valuation date next following the date on which he became the owner of the house or the value determined for valuation date relevant to the assessment year ending on 1.4.71, whichever valuation date is later.

The *Explanation* to section 7(2) clarifies that where the house is constructed by the assessee, he shall be deemed to have become the owner of the house on the date on which the construction of such house was completed. For this purpose, the term “house” includes a part of a house being an independent residential unit.

Schedule III contains the rules for the valuation of various types of assets. It contains Parts A-H:

2.2 VALUATION OF ASSETS OTHER THAN CASH (PART-A)

- (a) Rule 1 in this part provides that the value of any asset other than cash for the purposes of the Wealth-tax Act shall be determined in the manner laid down in Rules 2 to 21.
- (b) Rule 2 contains the definition of various terms for the purposes of this Schedule. The following are some of the more important definitions:
 - (i) “accounting year” in relation to a company means, a period in respect of which any profit and loss account of the company laid before it in the annual general meeting is made up;
 - (ii) “gold” means, gold, including its alloy whether virgin, or melted or remelted, wrought or unwrought in any shape or form of a purity of not less than 9 carats

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and includes any gold coin [whether legal tender or not] in gold ornament and any other article of gold;

- (iii) “gold ornament” means, any article in a finished form made for personal adornment or for the adornment of any idol, deity or any other object of religious worship made of, or manufactured from gold, whether or not set with stones or gems, real or artificial or with pearls, cultured or imitation, or real or with all or any of them and includes parts, pendants or broken pieces of gold ornaments.
- (iv) “investment company” means, a company whose gross total income consists mainly of income which is chargeable to income- tax under the heads “income from house property”, “capital gains” and “income from other sources”.
- (v) “jewellery” includes -
 - (a) ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or semi-precious stones and whether or not worked out or sewn into any wearing apparel;
 - (b) precious or semi-precious stones, whether or not set in any furniture, utensils or any other article or worked out or sewn into any wearing apparel.

2.3 VALUATION OF IMMOVABLE PROPERTY (PART-B)

Rules 3-8 of Schedule III of the Wealth-tax Act, 1957, provide for the valuation of immovable property. The term immovable property includes commercial property also.

Step 1 : Gross maintainable rent (Rule 5) : The first step for finding out the valuation of immovable property is to find out the gross maintainable rent. Rule 5 defines gross maintainable rent. There are two situations here:

- (a) *Where the property is let:* Gross maintainable rent here means the annual rent received or receivable by the owner or the annual value assessed by the local authority in whose area the property is situated for the purpose of levy of property tax or any other tax on the basis of such assessment, whichever is higher;
- (b) *Where the property is not let out:* Gross maintainable rent means the annual rent assessed by the local authority or if there is no such assessment, the amount which the owner can reasonably be expected to receive as annual rent had such property been let.

Annual rent : For the purposes of the above rule “annual rent” means,

- (a) where the property is let out throughout the year ending on the valuation date, the actual rent received or receivable by the owner;

- (b) where the property is let for only a part of the previous year, the amount which bears the same proportion to the amount of actual rent received or receivable by the owner for the period for which the property is let as the period of taxable months bears to the number of months (including part of a month) during which the property is let during the previous year.

In the following cases, the actual rent is to be increased in the manner specified below :

- (i) Where the property is occupied by a tenant and he agrees to bear the municipal taxes, by the taxes so borne by him;
- (ii) Where the property is occupied by a tenant and he agrees to bear the cost of repairs, then, by 1/9th of the actual rent;
- (iii) Where the owner has accepted any amount as deposit (not being advance payment towards rent for a period of three months or less), by the amount calculated at the rate of 15% per annum on the amount of deposit outstanding from month to month, for the number of months (excluding part of a month) during which such deposit was held by the owner in the previous year and if the owner is liable to pay interest on such deposit, the increase to be made under this clause shall be limited to the sum by which the amount calculated as aforesaid exceeds the interest actually paid.
- (iv) Where the owner has received any amount by way of premium or otherwise as consideration for leasing of the property or any modifications of the terms of the lease, by the amount obtained by dividing the premium or other amount by the number of years of the period of the lease;
- (v) Where the owner derives any benefit or perquisite, whether convertible into money or not, as consideration for leasing of the property or any modification of the terms of the lease by the value of such benefit or perquisite.

Rent received or receivable: This term includes all payments for the use of the property by whatever name called, the value of all benefits or perquisites whether convertible into money or not obtained from a tenant and any sum paid by a tenant in respect of any obligation which but for such payment would have been payable by the owner.

Step 2: Net maintainable rent (Rule 4): For arriving at the net maintainable rent, the following amounts are to be deducted from the gross maintainable rent:

- (i) The amount of taxes levied by any local authority in respect of the property;
- (ii) 15% of the gross maintainable rent.

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Step 3: Valuation of immovable property (Rule 3)

- (i) The above net maintainable rent is to be multiplied by 12.5;
- (ii) Where the property is leasehold and the unexpired period of such lease is 50 years or more, the multiplying factor is 10.
- (iii) Where the property is leased out and the unexpired period of lease is less than 50 years, the multiplying factor is 8.
- (iv) Where such property is acquired or constructed after 31.3.74, if the value of cost of acquisition or construction plus improvement thereto is more than the value arrived at as above, the cost of acquisition or cost of construction as so increased will be the value of the property;
- (v) The restriction mentioned in point (iv) will not apply in the case of one house belonging to the assessee if the following conditions are satisfied:
 - (a) such house is acquired or constructed after 31.3.74;
 - (b) the house is exclusively used by the assessee for his own residential purposes throughout the period of 12 months immediately preceding the valuation date;
 - (c) cost of construction does not exceed Rs.50 lakhs if the house is situated at Bombay, Calcutta, Delhi or Madras or Rs.25 lakhs where the house is situated at any other place.
 - (d) where more than one house belonging to the assessee is exclusively used by him for residential purposes, the above relaxing provision will apply in respect of one house at the option of an assessee.

Adjustment to the above value: To the value as ascertained above, certain adjustments have to be made for unbuilt area of the plot of land. Rule 6 provides for the same:

Where the unbuilt area of the plot of land on which the property is constructed exceeds the specified area, such value will be increased by an amount calculated in the following manner:

- (a) where the difference between the unbuilt area and the specified area exceeds 5% but does not exceed 10% of the aggregate area by an amount equal to 20% of such value;
- (b) where the difference between the unbuilt area and the specified area exceeds 10% but does not exceed 15% of the aggregate area, by an amount equal to 30% of such value;

- (c) where the difference between the unbuilt area and the specified area exceeds 15% but does not exceed 20% of the aggregate area by an amount equal to 40% of such value.

Relevant definitions:

1. **Aggregate area:** This means, the aggregate of the area on which the property is constructed and the unbuilt area;
2. **Specified area:**
 - (a) Where the property is situated at Bombay, Calcutta, Delhi or Madras, 60% of the aggregate area;
 - (b) Where the property is situated at Agra, Ahmedabad, Allahabad, Amritsar, Bangalore, Bhopal, Cochin, Hyderabad, Indore, Jabalpur, Jamshedpur, Kanpur, Lucknow, Ludhiana, Madurai, Nagpur, Pune, Patna, Salem, Solahpur, Srinagar, Surat, Thiruchirappalli, Tirunelveli, Vadodara (Baroda) or Varanasi, 65% of the aggregate area;
 - (c) Where the property is situated at any other place, 70% of the aggregate area.

Proviso: Where under any law for the time being in force, the minimum area of the plot of land required to be kept as open space for the enjoyment of the property exceeds the specified area, such minimum area shall be deemed to be specified area.

Unbuilt area: This means, that part of such aggregate area on which no building has been erected.

Adjustment for unearned increase in the value of the land - Rule 7: It is possible that the assessee might have constructed the property on land obtained on lease from the Government, a local authority or any authority referred in section 10(20A) of the Income-tax Act. The Government or the authority concerned may be entitled to claim a specified part of the unearned increase in the value of the land at the time of the transfer of the property. In such a case, a reduction is to be made in the value of the property as determined under Rule 3. Accordingly, the amount to be claimed by the Government or 50% of the value of the property so determined whichever is less is to be deducted.

Definition - Unearned increase: This mean the difference between the value of such land on the valuation date as determined by the Government or such authority and the amount of premium paid or payable to the Government for the lease of such land.

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Rule 3 not to apply in certain cases (Rule 8) : The valuation procedure contains in Rule 3 will not apply in the following cases:

1. Where the Assessing Officer is of opinion that it is not practicable to apply the provisions of Rule 3 to such a case. Before forming such an opinion, the Assessing Officer must have regard to the facts and circumstances of the case. He must also get the previous approval of the Deputy Commissioner;
2. Where the difference between the unbuilt area and the specified area exceeds 20% of the aggregate area;
3. Where the property is constructed on leasehold land and the lease expires within a period not exceeding 15 years from the relevant valuation date and the deed on lease does not give an option to the lessee for the renewal of the lease.

In all the above circumstances, the value of the property shall be determined in the manner laid down in Rule 20.

2.4 GLOBAL METHOD OF VALUATION OF BUSINESS

Part D contains Rule 14 which provides the manner in which the net value of the assets of the business as a whole, having regard to the balance-sheet of such business, is to be determined.

Global method of valuation: In some cases the valuation of the various assets of business may involve considerable difficulty. In such case, if the accounts of the business are being regularly maintained instead of valuing each and every assets separately the Assessing Officer may determine the net value of the assets of the business as a whole having regard to the balance sheet of such business as on the valuation date after making the prescribed adjustment therein. Rule 14 of Schedule III specifies the adjustments to be made by the Assessing Officer wherever he applies this global method of. These rules provide a uniform and statutory basis for adjustments. The adjustment to be so made are discussed in the following paragraphs under three main heads as follows:

- (A) Adjustment in the value of assets:
- (B) Adjustment in the value of liabilities:
- (C) Exclusion of non-business assets and liabilities.

Adjustments in the value of assets

1. Adjustment in the value of an asset disclosed in the balance-sheet

The value of an asset disclosed in the balance sheet will be taken to be

- (i) where depreciation is admissible - its written down value;

- (ii) where depreciation is not admissible - its book value;
- (iii) in the case of closing stock its value adopted in the income-tax assessment for the relevant previous year.

Where the value of any of the asset referred to above, determined in accordance with the provisions of Schedule III as applicable to that particular asset or if there are no such provisions, determined as per Rule 20, exceeds the value arrived at as per (i), (ii) or (iii) above, by more than 20%, the higher value shall be taken to be the value of the asset.

The value of an asset not disclosed in the balance sheet shall be taken to the value determined in accordance with Schedule III as applicable to that asset.

2. Adjustments in the value of assets and liabilities

(i) Exclusion of certain assets from balance-sheet [Rule 14(2)(d)]:

- (a) Any amount paid as advance tax under the Income tax Act.
- (b) Bad debts appearing in the balance-sheet but allowed in the Income-tax assessment for the previous year relevant to the corresponding assessment year.
- (c) Assets exempted from wealth-tax.
- (d) Any amount in the balance sheet including debit balance in the Profit and Loss Account of the Profit and Loss Appropriation Account which does not represent the value of any asset.
- (e) Any asset shown in the balance sheet not really pertaining to the business.

(ii) Adjustment of liabilities [Rule 14(2)(e)]: The following amounts shown as liabilities in the balance-sheet are not to be taken into account -

- (a) Capital employed in business, other than those attributable to borrowed money.
- (b) Reserves by whatever name called. For this purpose, provision for any purpose other than taxation will be treated as reserve.
- (c) Provision made for meeting any future or contingent liability.

The *Explanation* to Rule 14 makes it clear that provision for any purpose other than taxation shall be treated as a reserve.

- (d) Any liability shown in the balance sheet not really pertaining to the business;
- (e) Any debt owed by the assessee to the extent to which it has been specifically utilised for acquiring an asset in respect of which wealth-tax is not payable under the Act; if however, it is not possible to calculate the amount of debt so

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utilised, it shall be taken as the amount which bears the same proportion to the total of the debts owed by the assessee as the value of that asset bears to the total value of the assets of the business.

After making all the above adjustments in the balance-sheet the Assessing Officer has to ascertain net value of the assets and liabilities. The excess of the assets over the value of liabilities will represent the net wealth of the business.

2.5 INTEREST IN FIRM OR ASSOCIATION OF PERSONS

Part E contains Rules 15 and 16 which provide the manner in which the value of the interest of a person in a firm of which he is a partner or an association of persons of which he is a member, is to be determined.

Rule 16 provides the computation of net wealth of the firm or an association of persons and its allocation amongst the partners or members. The provisions of this rule are on the same lines as those of the earlier Rule 2 of the Wealth-tax Rules, 1957.

The rule provides that the net wealth of the firm or the association has to be determined first. Then, that portion of the net wealth which is equal to the amount of its capital is to be allocated among the partners or members in the proportion in which capital has been contributed by them. The residue of the net wealth is to be allocated in accordance with the agreement of partnership or association for the distribution of assets in the event of the dissolution of the firm or association or in the absence of such agreement, in the proportion in which the partners or members are entitled to share profits. The sum total of the amount so allocated to a partner or members is to be treated as the value of the interest of the partner or members in the firm or association.

The net wealth of the firm or association may include the value of assets located outside India and in such a case the value of the interest of the partner or member in the assets located in India is to be determined having regard to the proportion which the value of such assets diminished by debts relating to those assets, bears to the net wealth of the firm or association [Clause (a) of Explanation to Rule 16].

The proviso to Rule 16, makes it clear that in determining the net wealth of the firm or association for the purposes of the rule, no account shall be taken of the exemptions in sub-sections (1) and (1A) of section 5.

Clauses (b) and (c) of the Explanation to Rule 16, provide that where the net wealth of the firm or association computed in accordance with this rule includes the value of any assets which are exempt from inclusion in the net wealth under sub-sections (1) and (1A) of section 5 or any assets referred to in section 5(2), the value of the interest of the partner or member shall be deemed to include the value of his proportionate share in the said assets and the provisions of sub-sections (1), (1A) and (2) would apply to him accordingly. These express provisions in the rules have resolved the earlier judicial controversy

regarding the question of application of the exemption provisions of section 5, while computing the value of the interest of a partner of a firm or member of an association.

It may be noted that clause (a) of section 4(1) applies to an individual and clause (b) dealing with share in partnership firms or association of persons not being a co-operative housing society applies to any assessee.

In the case of an assessee who is a partner in a firm or a member of an AOP the value of his interest in the assets of the firm or AOP determined in the manner laid down in Schedule III will be included in his net wealth as belonging to the assessee. The proviso to new Clause (b) also seeks to include the interest of a minor child in a firm or association of persons in the net wealth of the parent having a higher net wealth. It is to be noted that the new Rules 15 and 16 of the Schedule III seek to provide the manner in which the value of the interest of a person in a firm of which he is a partner or in an AOP of which he is a member is to be determined.

2.6 LIFE INTEREST

Part F contains Rule 17 which provides the manner in which the value of life interest of an assessee is to be determined.

The provisions of this rule are on the same lines as those of the earlier Rule 1B of the Wealth-tax Rules, 1957.

Rule 17 lays down that the market value of the life interest of an assessee is to be arrived at by multiplying the average annual income that accrued to the assessee from the life interest by $[1/(p+d)]-1$ where P represents the annual premium for a whole life insurance without profits on the life tenant for a unit sum assured as specified in an appendix to the Wealth-tax Rules and 'd' is equal to $i/(1+i)$, "i" being the rate of interest.

For this purpose the average, annual income is to be arrived at on the basis of the average of the annual gross income derived by the assessee from the life interest during the period of three years ending on the valuation date as reduced by the average of the expenses incurred on the collection of such income during the period. However the deduction on account of expenses on collection should in no case exceed five per cent of the average of the annual gross income. By reference to the Appendix to the Wealth-tax Rules one can impute the value of the life interest held by an assessee. That table on the Appendix gives the multipliers for the age up to 80 years. The multipliers are based on the above formula and the rate of interest adopted is 6.5% per annum. Where the life tenant cannot be insured at normal premium rates but only at higher rates, then the valuation has to be varied suitably. In any case, the value of the interest should not exceed the market value of the trust corpus as on the valuation date. If the age of tenant is 80 years or above, then *ipso facto*, the rule would not apply and the value would be nil.

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2.7 JEWELLERY

Part G contains rules 18 and 19 which provide the manner in which valuation of jewellery is to be determined.

1. The value of the jewellery shall be estimated to be the price which it would fetch if sold in the open market on the valuation date.
2. The return of net wealth furnished by the assessee shall be supported by -
 - (i) a statement in the prescribed form, where the value of the jewellery on the valuation date does not exceed Rs.5 lakh.
 - (ii) a report of a registered valuer in the prescribed form, where the value of the jewellery on the valuation date exceeds Rs.5 lakh.
3. In spite of the above provision, the Assessing Officer may, if he is of the opinion that the value of the jewellery declared in the return -
 - (a) is less than its fair market value by the percentage prescribed under section 16A(1)(b)(i).
 - (b) is less than its fair market value as referred to in section 16A(1)(a), refer the valuation of such jewellery to a Valuation Officer and the value of such jewellery shall be the fair market value as estimated by the Valuation Officer.

2.8 OTHER ASSETS

Part H contains rules 20 and 21 which provide that the value of any asset, other than cash, being an asset which is not covered by Rules 3 to 19 shall be estimated either by the Assessing Officer himself or by the valuation officer if reference is made to him under section 6A. This Rule further provides that in both these cases, the value shall be estimated to be the price which it would fetch in the case of assets not saleable in the open market, in the open market on the valuation date. Sub-rule (3) provides that where the value of an asset cannot be estimated because it is not saleable in the open market, the value shall be determined in accordance with guidelines or principles specified by the Board from time to time by general or special order.

Rule 21 provides that for the purposes of determining market value under any provision of this Schedule, the price or other consideration for which the property may be acquired by or transferred to any person under the terms of a deed of trust, or through or under any restrictive covenant in any instrument of transfer shall be ignored. This Rule enables the tax authorities to ignore restrictive covenants contained in an instrument of transfer of property which enables acquisition of such properties at stipulated prices, irrespective of the market value thereof.

Registered Valuers : Valuers are appointed by the Central Board of Direct Taxes. Section 34AB of the Wealth-tax Act, sets forth the procedure for registration of valuers. The Chief Commissioner or Director General maintain a register called the Register of Valuers in which the names and addresses of persons registered under section 34AB (2) of the Wealth-tax, as valuers, are entered. Persons who possesses the qualifications prescribed in this behalf may apply to Commissioner or Director General in the prescribed form along with the prescribed fees for registration as valuers. Rule 8 of the Wealth-tax Rules prescribes different qualifications for different classes of assets. The application for registration as valuer is to be made in Form "N" prescribed under Rule 8B of the Wealth-tax Rules. The application should contain a declaration to the effect that the applicant will:

- (i) make an impartial and true valuation of any asset which he may be required to value;
- (ii) furnish a report of such valuation in the prescribed form;
- (iii) charge fees at a rate not exceeding the rate or rates prescribed in this behalf;
- (iv) not undertake valuation of any asset in which he has a direct or indirect interest.

The valuers should act according to the above declaration. The fees charged by the registered valuer should not exceed the maximum limits laid down by Rule 8C. The report of valuation of different classes of assets is to be submitted by the registered valuer in the forms prescribed by Rule 8D.

Section 34AC places certain restrictions on practice as a registered valuer. It provides that no person either alone or in partnership with any other person, shall be entitled to practice, describe or hold himself out as a registered valuer permit him self to be so described or held out unless he is registered as a valuer or in the case of a partnership, unless all the partners are registered as valuers. It also imposes a ban on a company or other corporate body from practising describing itself or held out as registered valuers.

Section 34AD provides for the removal of the names of the valuers from the Register and also for their restoration under certain circumstances.

Section 34AE provides that any assessee who is entitled or required to attend before any Wealth-tax Authority or the Appellate Tribunal in connection with any proceeding relating to the valuation of any asset may be represented by a registered valuer. This right to appear through a registered valuer does not however extend to cases where the assessee is required under the Act to attend personally.

Section 34ACC and 35EE impose certain obligation on every registered valuer or a person who has made an application for registration as a valuer; if such valuers are convicted of any offence and sentenced to a term of imprisonment or found guilty of professional

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misconduct by the professional association or institution of which he is a member, they should intimate the particulars thereof to the CBDT, and the Board has been empowered to notify any punishment with rigorous imprisonment for a term which may extend to two years and liability to fine.

Self-examination questions

1. In certain circumstances, the procedure for valuation of house property as contained in rule 3 of schedule III of the Wealth-tax Act are not applicable. What are these circumstances? Explain.
2. Explain the procedure for adoption of the value of jewellery for the valuation date 31.3.2010 and subsequent three years, assuming the value of jewellery has been determined by the Valuation Officer as at 31.3.2009.
3. How is the value of interest of a person in a firm of which he is a partner determined under the Wealth-tax Act?
4. What are the provisions of the Wealth-tax Act relating to the valuation of assets of a business?
5. State the rule for determining value of life interest for wealth-tax purposes.

ASSESSMENT PROCEDURE

3.1 ADMINISTRATION

The machinery for the administration of wealth-tax is modeled on the lines of the Income-tax Act and in fact the wealth-tax is administered by the very same income-tax authorities who administer income-tax in relation to an assessee.

The Income-tax authorities specified in section 116 of the Income-tax Act shall be the Wealth tax authorities for the purposes of this Act and every such authority shall exercise the powers and perform the functions of a wealth tax authority under this Act. For this purpose his jurisdiction shall be the same as he has under the Income tax Act [Section 8]. Section 23A provides for a direct appeal before Commissioner (Appeals).

Section 9 provides that the provisions of section 118 of the Income-tax Act would apply in relation to control of wealth tax authorities also. Section 10 deals with instructions to subordinate authorities from time to time. Section 11 deals with jurisdiction of Assessing Officers and power to transfer cases.

Valuation Officers: Section 12A provides for the appointment of Valuation Officers by the Central Government. The expression 'Valuation Officers' for this purpose means and includes Regional Valuation Officers, District Valuation Officers and Assistant Valuation Officers. The Wealth-tax authorities are also empowered to appoint as many overseers, surveyors and assessors as may be necessary to assist the Valuation Officer in the execution of their functions. The powers of the Valuation Officer are specified in section 38A. Their jurisdiction is specified by Rule 3A of the Wealth-tax Rules.

3.2 ASSESSMENT PROCEDURE

3.2.1 Return of wealth: Every person having taxable wealth shall, on or before the due date, furnish a return of his net wealth as on the valuation date in the prescribed form. A person will also be liable to file the return if the net wealth of any other person in respect of which he is assessable under the Act exceeds the maximum amount not chargeable to tax.

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3.2.2 Revised return [Section 15]: If any person has not furnished a return within the time limit allowed under section 14(1) or in response to a notice issued under section 16(4)(i) or having furnished a return discovers any omission or wrong statement therein, he may furnish a return or a revised return. The time limit for filing such return is before the expiry of one year from the end of the relevant assessment year or before the completion of the assessment whichever is earlier.

3.2.3 Signing of return [Section 15A]: Section 15A provides that in the case of an individual the return should be signed by;

- (a) the individual himself;
- (b) where he is absent from India, by the individual himself or by any person authorised in this behalf;
- (c) where the person is mentally incapacitated from attending to his affairs, by his guardian, or any other person competent to act on his behalf; and
- (d) where for any other reason, it is not possible for the individual to sign the return, by any person authorised by him in this behalf.

In case (b) and (d) above, the person signing the return should hold a valid power of attorney from the concerned individual and it should be attached to the return.

The two provisos seek to provide that where a company is not resident in India, the return may be signed and verified by a person holding valid power of attorney from the company and it should be attached to the return. Further where a company is being wound up, whether under the orders of the court or otherwise, or where any person has been appointed as receiver, the return should be signed and verified by the liquidators referred to in section 178(1) of the Income-tax Act. Where the management of the company has been taken over by the Central Government or any State Government under any law the return should be signed and verified by the principal officer thereof.

3.2.4 Self-assessment [Section 15B]: (i) Where any tax is payable on the basis of any return furnished under section 14 or section 15 or in response to a notice under section 16(4)(i) or under section 17 after taking into account the amount of tax already paid, the assessee shall be liable to pay such tax together with interest payable for any delay in furnishing the return. Such payment must be made before furnishing the return and the return shall be accompanied by proof of payment of such tax and interest.

(ii) Where the amount paid by the assessee falls short of the aggregate of the tax and interest as mentioned above, the amount so paid shall first be adjusted towards the interest payable and the balance, if any, shall be adjusted towards the tax payable.

(iii) Once regular assessment is made, any amount payable as above, shall be deemed to have been paid towards such regular assessment.

- (iv) Failure to pay self-assessment tax will make the assessee an 'assessee in default' in respect of the tax or interest or both remaining unpaid.

Section 16: Section 16 is similar to section 143 of the Income-tax Act.

- (1) Accordingly, where a return has been made under section 14 or section 15 or in response to a notice under section 16(4)(i)(a) if any tax or interest is found due on the basis of such return after adjustment of any amount paid, an intimation shall be sent to the assessee specifying the amount payable. Such an intimation shall be deemed to be a notice issued under section 30 and the provisions of the Act will apply accordingly. Such an intimation shall not however be sent after the expiry of two years from the end of the assessment year in which the net wealth was first assessable.

If any refund is due on the basis of such return it will be granted to the assessee and an intimation to this effect shall be sent to the assessee.

Except as otherwise provided in section 16(1), the acknowledgement of the return shall be deemed to be intimation under section 16(1) where either no sum is payable by the assessee or no refund is due to him.

- (2) Where a return has been made under section 14 or section 15, or in response to a notice under clause (i) of sub-section (4) of this section, the Assessing Officer shall, if he considers it necessary or expedient to ensure that the assessee has not understated the net wealth or has not underpaid the tax in any manner, serve on the assessee a notice requiring him, on a date to be specified therein, either to attend the office of the Assessing Officer or to produce, or cause to be produced there, any evidence on which the assessee may rely in support of the return:

However, no notice under this sub-section shall be served on the assessee after the expiry of twelve months from the end of the month in which the return is furnished.

- (3) On the day specified in the notice issued under sub-section (2) or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by order in writing, assess the net wealth of the assessee and determine the sum payable by him on the basis of such assessment.
- (4) For the purposes of making an assessment under this Act, the Assessing Officer may serve on any person who has made a return under section 14 or section 15 or in whose case the time allowed under sub-section (1) of section 14 for furnishing the return has expired, a notice requiring him, on a date to be specified therein,
- (i) where such person has not made a return [within the time allowed under sub section (1) of section 14] to furnish a return of his net wealth or the net wealth of

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any other person in respect of which he is assessable under this Act on the valuation date, in the prescribed form and verified in the prescribed manner, setting forth the particulars of such net wealth and such other particulars as may be prescribed, or

- (ii) to produce or cause to be produced such accounts, records or other documents as the Assessing Officer may require.

(5) If any person -

- (a) fails to make the return required under sub-section (1) of section 14 and has not made a return or a revised return under section 15, or
- (b) fails to comply with all the terms of a notice issued under sub-section (2) or sub-section (4),

the Assessing Officer, after taking into account, all relevant material which he has gathered, shall after giving such person an opportunity of being heard, estimate the net wealth to the best of his judgement and determine the sum payable by the person on the basis of such assessment:

Provided that such opportunity shall be given by the Assessing Officer by serving a notice calling upon the person to show cause, on a date and time to be specified in the notice, why the assessment should not be completed to the best of his judgement:

Provided further that it shall not be necessary to give such opportunity in a case where a notice under sub-section (4) has been issued prior to the making of the assessment under this sub-section.

(6) Where a regular assessment under sub-section (3) or sub-section (5) is made,-

- (a) any tax or interest paid by the assessee under sub-section (1) shall be deemed to have been paid towards such regular assessment;
- (b) if no refund is due on regular assessment or the amount refunded under sub-section (1) exceeds the amount refundable on regular assessment, the whole or the excess amount so refunded shall be deemed to be tax payable by the assessee and the provisions of this Act shall apply accordingly.

3.2.5 Reference to Valuation Officer: Section 16A provides that for the purpose of making an assessment Assessing Officer may refer the valuation of any asset to a Valuation Officer. In case where the value of an asset has been estimated by a registered valuer, a reference may be made to the Valuation Officer, if the Assessing Officer considers that the estimate made by the registered valuer is less than its fair market value and consequently requires an upward revision. In any other case, such a reference may be made if the Assessing Officer considers it necessary to do so on account of the nature

of the asset and other relevant considerations or he is of the opinion that the fair market value of the asset exceeds the value of the asset as returned by more than 33-1/3% of the assets as returned by more than Rs.50,000.

On a reference having been made to the Valuation Officer, he will proceed to value the asset after giving notice to the assessee to produce or cause to be produced before him, such accounts, records or other documents as he may require. For this purpose, he shall have all the powers vested in a Court under the Code of Civil Procedure 1980. Where the Valuation Officer is of the opinion that the value of the assets has been correctly declared in the return made by the assessee, he will pass an order to that effect. Where, however, the Valuation Officer is of the opinion that the value of the asset is higher than the value declared in the return made by the assessee or where the asset is not disclosed or the value of the asset is not declared in such return or where no such return has been made the Valuation Officer is required to serve on the assessee a notice intimating the value which he proposes to estimate and give the assessee an opportunity to state his objections, if any, to the proposed valuation on a date fixed by the Valuation Officer. On the date so specified the assessee shall have the option either to state his objections personally or through a registered valuer or in writing before the Valuation Officer and to produce or cause to be produced such evidence as the assessee wants to rely in support of his objections.

After hearing all the evidence which the assessee produced and that which the Valuation Officer may require on any specified point and considering all the material which the Valuation Officer has gathered, he shall estimate the value of the assets and send a copy of his order to the Assessing Officer and to the assessee. The order of the Valuation Officer, so far as the Valuation of the asset in question is concerned, shall be binding on the Assessing Officer, who after receiving the order shall proceed to complete the assessment in conformity with the estimate of the Valuation Officer.

The Assessing Officer is statutorily bound by the valuation report submitted by the Valuation Officer and he has no option but to complete the assessment in conformity with the assessment of the Valuation Officer insofar as the valuation of the assets in question are concerned - *CWT vs. Rahman (1991) 189 ITR 307 (All)* and *M.C. Khunnah vs. Union of India (1979) 189 ITR 414 (All)*.

3.2.6 Assessment of escaped wealth: Sub-sections (1), (1A) and (1B) of section 17 deal with assessment of escaped wealth.

- (a) Reassessment proceedings can be taken if the Assessing Officer has reason to believe that the net wealth chargeable to tax has escaped assessment, whether by reason of under-assessment or assessment at too low a rate or otherwise.
- (b) Notice has to be served subject to the conditions of sections 17 and 17A, requiring the person to furnish a return in the prescribed form and in the prescribed manner within such period along with such other particulars as may be required by the notice.
- (c) On the basis of the same, the Assessing Officer may proceed to assess or reassess such net wealth and also any other wealth that has escaped assessment and comes

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which to the notice of the Assessing Officer in the course of the proceedings under this provision. The Assessing Officer may assess or reassess the net wealth which is chargeable to tax and has escaped assessment other than the net wealth which is the subject matter of any appeal, reference or revision.

- (d) As assessment completed under section 16(3), scrutiny assessment or reassessment under section 17 (wealth escaping assessment) can be reopened after 4 years from the end of the relevant assessment year only if the wealth has escaped assessment due to the failure on the part of the assessee to file a return of wealth (under section 14/15/16(4) or to disclose fully and truly all material facts necessary for his assessment.
- (e) For this purpose, production before the Assessing Officer of account books or other evidence from which material evidence could with due diligence have been discovered by the Assessing Officer would not necessarily amount to disclosure.
- (f) Before issuing any notice under section 17(1), the Assessing Officer should record his reasons for doing so.
- (g) The time limits for issue of notice are now dependent upon the amount of wealth which has escaped assessment. The new provisions are indicated below:

Notice can be issued	
upto 4 years from the end of the relevant assessment year	even beyond 4 years but before 6 years from the end of the relevant assessment year
In respect of any amount of wealth escaping assessment	Only if the escaped wealth is Rs.10 lakhs or or more.

- (h) Notice under section 17 can be issued at any time to give effect to any directions contained in any order passed under sections 23, 24, 25, 27 or 29 or by a court in any proceeding which need not necessarily be under the Wealth-tax Act.

For the above purposes, the following will also be deemed to be cases where net wealth chargeable to tax has escaped assessment.

- (i) cases of failure to file return of net wealth by persons having wealth exceeding basic exemption limit.
- (ii) where return of wealth has been furnished but no assessment has been made and it is noticed by the Assessing Officer that the assessee has understated his wealth or claimed excessive exemptions or deductions.

3.2.7 Sanctioning Authorities: The sanctioning authorities for issue of notice under section 17 are as follows:

- (i) Where a scrutiny assessment is to be reopened:
 - (a) Notice under section 17 can be issued only by an Assessing Officer. Where the Assessing Officer is below the rank of Assistant Commissioner, or the Deputy Commissioner notice can not be issued unless the Joint Commissioner is satisfied on the reasons recorded by such Assessing Officer that it is a fit case for the issue of the notice.
 - (b) If notice under section 17 is to be issued after the expiry of 4 years from the end of the relevant assessment year, sanction of the Chief Commissioner or Commissioner is necessary.
- (ii) In any other case:
 - (a) Notice under section 17 can be issued by any Assessing Officer as in (a) above.
 - (b) If notice under section 17 is to be issued after the expiry of 4 years from the end of the relevant assessment year, sanction of the Joint Commissioner will be necessary.

It may be noted that the Joint Commissioner, the Commissioner or the Chief Commissioner, as the case may be, on being satisfied with the reasons recorded by the Assessing Officer about the fitness of a case for the issue of notice under section 17, need not issue the notice himself. Thus, where the approval of the Joint Commissioner/Chief Commissioner/Commissioner is required for issue of notice under section 17, it is not necessary that such notice should be issued by the Joint Commissioner/Chief Commissioner/Commissioner himself. It would be sufficient if the Assessing Officer issues the notice.

3.2.8 Time limit for completion of assessment/reassessment [Section 17A]

- (1) Sub-section (1) of section 17A provides that no order of assessment shall be made under Section 16 at any time after the expiry of 21 months from the end of the assessment year in which the net wealth was first assessable.
- (2) Sub-section (2) provides that no order of assessment/reassessment shall be made under section 17 after the expiry of 9 months from the end of the financial year in which the notice under sub-section (1) of section 17 was served.
- (3) Sub-section (3) provides that where a fresh assessment is to be made in pursuance of order passed by the Deputy Commissioner (Appeals) in an appeal under section 23A, or by the Appellate Tribunal in an appeal under section 24, or by the Commissioner in an order of revision under section 25 such fresh assessment may be made at any time before the expiry of 9 months from the end of the financial year in which the order under section

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23A or section 24 is received by the Chief Commissioner or the order under section 25 is passed by the Commissioner.

(4) Sub-section (4) provides that where assessment or reassessment on the assessee or any person is made to give effect to any finding or direction contained in an order under section 23 (A.A.C) or section 24 (Tribunal) or section 25 (Revision by Commissioner) or section 27 (order a High Court in reference) or section 29 (order of the Supreme Court in an appeal (or in an order of any court in a proceeding otherwise than by way of appeal of reference, such proceeding shall be subject to the time limit mentioned in the item (6) above [Section 17(4)]).

(5) *Explanation 1* to section 17A(4) provides that the following will be excluded in computing the period of limitation.

- (a) Time taken in reopening the whole or any part of the proceeding or in giving an opportunity to the assessee to be re- heard under the proviso to section 39.
- (b) The period not exceeding sixty days commencing from the date on which the wealth-tax officer received the declarations from the assessee under section 18C and ending with the date on which an order under sub-section (5) of that section is passed by him.
- (c) The period of pendency of proceeding before the Wealth-tax settlement commission.
- (d) The period during which assessment proceedings are stayed by an order or injunction of any court.

Where immediately after the exclusion of the aforesaid period, the period of limitation available to the Assessing Officer for making an assessment is less than 60 days, such remaining period shall be extended to 60 days and the aforesaid period of limitation shall be deemed to be extended accordingly

Further, section 17A allows a minimum time period of one year to the Wealth-tax authority before whom the case was pending when the application was filed with the Settlement Commission. This revised time limit is deemed to apply to all cases where settlement proceedings have abated from 1.6.2007 and thereafter

(6) Where in a direction under section 23,24,25,27 or 29 or an order of a court any asset is excluded from the net wealth of one person and held to be the asset of another person then an assessment in respect of such asset on such other person shall for the purposes of section 17(2) and section 17A, be deemed to be one made in consequence of, or to give effect to any finding or direction contained in the said order. However, before the order is passed, such other person should be given an opportunity of being heard.

3.2.9 Interest for defaults [Section 17B]: Section 17B provides for mandatory interest for defaults in furnishing return of net wealth. The assessee will be liable to pay simple interest at the rate of 1% for every month or part of a month comprised in the period

commencing on the date immediately following the due date as specified in section 14(1) as applicable in the case of the assessee and ending on the date of furnishing of the return in a case where the return under section 14/15 or in response to a notice under 16(4)(i) is furnished after the due date.

Where the return is not furnished, the interest is to be paid for the period commencing from the date immediately following the due date and ending on the date of completion of assessment under section 16(5). Such interest is to be paid on the amount of tax payable on the net wealth as determined under section 16(1) or on regular assessment. For this purpose, where an assessment is made for the first time under section 17 the assessment so made shall be regarded as regular assessment.

For the purpose of computing this interest, the tax payable on the net wealth as declared in the return will be taken as the basis.

The interest payable under section 17B(1) will be reduced by the interest if any paid under section 15B (self-assessment) towards the interest chargeable under section 17B.

Sub-section (3) provides for a similar levy of interest where the return of net wealth for any assessment year is required by a notice under section 17(1). Such a notice could have been issued either after the determination of net wealth under section 16(1) or after the completion of an assessment under section 16(3) or 16(5) or 17. In such cases, where the return is furnished after the expiry of the time allowed under such notice, a simple interest @1% for every month or part of a month is to be paid for the period commencing on the date immediately following the expiry of the time allowed and ending with the date of furnishing the return. Where no return has been furnished in response to such a notice, the interest should be paid up to the date of completion of assessment under section 17.

The interest should be paid on the amount by which the tax on the net wealth determined on the basis of such reassessment exceeds the tax on the net wealth as determined on the basis of the earlier assessment.

Where as a result of an order passed in an appeal, revision, rectification or by settlement commission the amount of tax on which interest is payable under this provision has been increased or reduced, the interest shall be increased or reduced, accordingly. Where the interest is so increased, a notice of demand will be served by the Assessing Officer and where the interest is reduced the excess interest paid will be refunded.

3.2.10 Avoidance of repetitive appeals [Section 18C]: This provision lays down the procedure to be followed when an identical question of law is pending before the High Court or Supreme Court. Where an assessee claims that any question of law arising in his case (any proceedings for assessment of net wealth or imposition of penalty) for an assessment year, which is pending before the Assessing Officer or the Appellate Commissioner or the Appellate Tribunal is identical with a question of law arising in his case for another assessment year which is pending in appeal before the High Court u/s

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27A or in appeal before the Supreme Court u/s 29, he may, furnish to the Assessing Officer or the appellate authority concerned, as the case may be a declaration in the prescribed form, that if the authority concerned agree to follow the final decision on the question of law in the pending appeal, he shall not raise such a question of law in the later case in an appeal before any appellate authority or in appeal before the High Court u/s 27A or in appeal before the Supreme Court u/s 29.

On receipt of such declaration the Assessing Officer or the concerned appellate authority (after giving opportunity to the Assessing Officer) may by order in writing admit the claim of the assessee, on being satisfied that the question of law arising in the pending reference is identical with the question of law in the later case, which is now under assessment or appeal. If he is not so satisfied, he may reject the claim. When the claim is admitted, the Assessing Officer or the appellate authority, as the case may be, may dispose of the relevant case, without awaiting the final decision on the question of law in the other case. The assessee will not be entitled to raise in relation to the relevant case such question of law in appeal before any appellate authority. When the decision of the Court in the other case become final, it shall be applied to the later case. The Assessing Officer or the appellate authority, as the case may be, shall, if necessary, amend the order passed in the later case conformably to such final decision of the Court in the earlier case of the assessee.

An order passed under this provision admitting or rejecting the claim shall be final and not appealable and cannot be called into question in any proceeding by way of appeal or revision.

3.3 ASSESSMENT IN SPECIAL CASES

3.3.1 Assessment of executors: Where a person dies, his executors, administrator or other legal representative becomes liable in respect of the liability to wealth-tax for the valuation dates falling before the person's death which has remained unassessed or undischarged on the date of death. The liability cannot in any case, exceed the value of the estate of the deceased person which comes into possession of such executor, administrator or legal representative [Section 19].

Section 19A would apply only to a case where an assessee dies after executing a will and appointing an executor. It does not apply to cases of inheritance. The inheritor is liable himself under section 3 [*CWT vs. Keshub Mahindra* (1983) 130 ITR 22 Bom.]

In *Smt. Yawarunnisa Begum vs. W.T.O.* (1975 100 ITR. 645 A.P.) it was held that the legal representatives of the deceased- assessee are not liable for penalty for the default committed by the deceased- assessee under section 18. The liability of the legal representative is only to pay the tax assessed to be payable or any other sums which would have been payable by the deceased. Section 19(8) does not authorise the

department to levy penalty on the legal representative for the default committed by the deceased under section 14, inasmuch as section 19(3) has not included any liability of the legal representative in this respect. The Madras High Court also expressed similar view in *[C.W.T. vs. Varadarajan (122) I.T.R. 1014]*.

Section 19A provides for the assessment of executors in respect of the estate of a deceased person for a period from the date of the death of the deceased till the completion of the distribution of the beneficiaries.

The net wealth in respect of the estate of a deceased person is assessed in the hands of executors (including administrator or any other person administering the estate of a deceased person). For all purposes of assessment, the executor becomes the representative assessee of the deceased and the status is that of an individual. His residential status and citizenship would also be the same as those of the deceased on the valuation date immediately preceding his death. However, if there are more executors than one having an indivisible title and interest the co-executors receiving the income and acting jointly would be assessed in the status of a 'body of individuals'.

Separate assessments are to be made in respect of the net wealth as on each valuation date as is included in the period from the date of the death to the date of complete distribution among the beneficiaries of the estate according to their several interests. Some of the assets may be distributed to specific legatees during the period of administration. In computing the net wealth on any valuation date assessable in the hands of the executors, any assets distributed to or applied to the benefit of any specific legatees prior to the particular valuation date shall be excluded. But the assets so excluded shall to the extent such assets are held by the legatee on the valuation date, be included in the net wealth of such specific legatee on the valuation date.

The assessment of an executor under section 19A shall be made separately from any assessment that may be made on him in respect of his own net wealth or on the net wealth of the deceased under section 10.

3.3.2 Assessment after partition of Hindu Undivided Family: Section 20 lays down that if the Assessing Officer finds at the time of making an assessment that a H.U.F. has been partitioned, then if he is satisfied that the joint family property has been partitioned as a whole in definite portions, he shall have to record a finding and pass orders to that effect. In such a case, he will have to make an assessment on the net wealth of the undivided family as such in respect of all previous years completed before the date of partition (not the date of the order recognising partition) for which the assessments are yet to be made. The liability in respect of such assessment is joint and several for such members or group of members.

If partition by metes and bounds has taken place on the last day of the previous year relevant to the year of assessment, the undivided family has to be assessed under the

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Wealth-tax as such in spite of the partition having taken place so far as that assessment year is concerned. The last day of the previous year is the 'valuation date'— Refer to section 2(q). If the partition had taken place on any date in the previous year prior to the 'valuation date' the assessment of that previous year would not be governed by section 20 but by section 3. In other words, in such cases, the divided members would have to be separately assessed in respect of their divided portion or shares in the usual manner as for any other individuals.

If the Assessing Officer is not satisfied that a partition as claimed by the assessee has taken place, he may pass an order declaring that the family shall be deemed, for purposes of the Wealth-tax Act, to continue to be a joint family and is liable to be assessed as such. When an order recognising partition on a particular date has been passed each member of group or members, as the case may be, will be required to include in his net wealth on a particular valuation date, the value of the family property falling to his share and remaining with him on such valuation date.

De-recognition of partial partition: With a view to curbing the practice of creating multiple Hindu undivided families by making partial partitions, section 20A has been introduced. Under this provision, partial partitions of Hindu undivided family effected after 31st December, 1978 will not be recognised for tax purposes.

(1) It provides that in the case where a partial of a HUF has taken place after 31st December, 1978, such family shall continue to be liable to be assessed as a HUF as if no such partition had taken place i.e. the property shall be deemed to continue to belong to the HUF and no member shall be deemed to have separated from the family.

(2) Each member or group of members of such family immediately before such partial partition and the family shall be jointly and severally liable for any tax, penalty, interest, fine or any other sum payable under the Wealth-tax Act by the family in respect of any period whether before or after such partial partition.

(3) The several liability of any member or group of members of such family shall be computed according to the partition of the joint family property allotted to him at the time of such partial partition. The term 'partial partition' for the purpose will have the same meaning assigned to it in clause (b) of the Explanation to section 171 of the Income-tax Act.

The Supreme Court has upheld the constitution validity of the provisions of section 20A de-recognising partial partition.

3.3.3 Assessment when assets are held by a Court of Wards, Administrator General etc: If court of wards, administrator general or legatees etc fall within the scope of taxable entity contained in the charging section wealth tax will be chargeable at the rate of one per cent on their net wealth.

3.3.4 Assessment of charitable trust in certain special circumstances: Section 21A contemplates forfeiture of exemption available to charitable trusts under section

5(l)(i) in cases of diversion of property or of income from property held under trust. The section is analogous to section 13 of the Income-tax Act. Under this new provision, where any property is held under trust or any legal obligation for any public purpose of a charitable or religious nature in India and-

- (i) any part of such property or income of such trust, including voluntary contribution except for forming a part of the corpus is used or applied directly or indirectly for the benefit of any person referred to in section 13(3) of Income-tax Act; or
- (ii) any part of the income of the trust including such voluntary contributions, being a trust created after 1st April, 1952 enures directly or indirectly for benefit of any of the prohibited category of persons wealth-tax is to levied on the whole of the trust property as if it were held by a resident India citizen; or
- (iii) funds of the trust are invested in shares of a company or deposited or held by the trust in contravention of the provisions of section 13(1)(d) of the Income-tax Act,

then wealth tax at the maximum marginal rate, i.e. the rate of wealth tax applicable in relation to the highest slab of wealth in the case of an individual, will be levied. It has also specifically provided that no exclusion will be made under the provisions of section 5.

In the case of trusts created prior to 1st April, 1962 the use of application referred to in (i) above is by way of compliance with a mandatory term of the trust, there will be no forfeiture of the exemption available under section 5(i).

The third proviso to section 21A provides that (i) scientific research association enjoying exemption of income under section 10(21) will not be subject to the restriction mentioned in (i) and (ii) above. So far as investing or depositing of funds or holding of shares by these institutions, restrictions placed by the proviso to section 10(21) will be applicable.

Therefore we can see that scientific research association are subject only to the restrictions mentioned in the proviso section 10(21) of the Income-tax Act so far as the application or investment of their income or property is concerned. Contravention of the above restrictions will make them liable to wealth tax at the rates specified in section 3(2). None of the above three restrictions will be applicable to the following:

- (a) University or other educational institution [Section 10(22)]
- (b) Hospitals [Section 10(22A)]
- (c) Approved charitable trust [Section 10(23B)]
- (d) Public charitable institutions [Section 10(23C)]

The prohibited category of persons referred to in section 13(3) are as follows:

- (i) the author of the trust or the founder of the institution, (ii) any person who has made substantial contribution to the trust or institution (iii) where such author, founder or person

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is a Hindu undivided family, a member of the family (iv) any trustee, or manager of the institution, (v) any relative of such author, founder, person, member, trustee or manager as aforesaid and (vi) concern in which any of the person referred to in items (i) to (iv) above as a substantial interest.

In this context, the term 'relative' in relation to an individual means (i) spouse of the individual; (ii) brother or sister of the individual; (in) brother or sister of the spouse of the individual, (iv) any lineal ascendant or descendant of the individual; (v) any lineal ascendant or descendant of the spouse of the individual; (vi) spouse of a person referred to in (ii), (iii), (iv) or (v) and (vi) any lineal descendant of a brother or sister of either the individual or of the spouse of the individual.

For the purposes of section 21A, any part of the property or income of a trust shall be deemed to have been used or applied for the benefit of any of the specified categories of person if it can be deemed to have been so used or applied within the meaning of section 13(l)(c) of the Income-tax Act at any time during the period of the twelve months ending within the relevant valuation date.

3.3.5 Association of persons without specified shares of members [Section 21AA] : Sub-section (1) of section 21AA provides that where assets chargeable to wealth-tax are held by an association of persons other than the company or a cooperative society or a society registered under the Societies Registration Act, 1986 or under any law corresponding to that Act in force in any part of India and individual shares of the member of association in the income or assets or both, of the association on the date of its formation or at any time thereafter are indeterminate or unknown, wealth-tax will be levied and recovered from such association in the same manner and to the same extent as an individual citizen of India and resident in India.

Where any business or profession carried on by an association of persons, referred to in the above paragraph, has been discontinued or the association has been dissolved the Assessing Officer will be empowered to make an assessment on the net wealth of the association, as if no such discontinuance or dissolution had taken place and all other provisions of the Act including the provisions relating to the levy of penalty or any other sum will apply to such assessments. The Assessing Officer, Deputy Commissioner (Appeals), and the Commissioner (Appeals) are being empowered to impose or direct the imposition of penalty referred to in sections 18 and 18A, if such association has been found to be guilty of any of the acts specified in those sections. Every person who was a member of the association at the time of such discontinuance or dissolution and legal representative of any deceased person will be jointly and severally liable for the tax and penalty or other sums payable. Where any such discontinuance or dissolution takes place after any proceeding in respect of an assessment year have commenced, the proceedings may be continued against the persons referred to earlier from the stage at which it stood at the time of such discontinuance or dissolution."

3.3.6 Assessment of persons residing outside India: If the person liable to tax under this Act resides outside India, the tax may be assessed on the agent of such person [Section 22(1)]. The agent is a person appointed *ad hoc* by the Assessing Officer. The Assessing Officer chooses the agent from the following three categories:

- (a) persons employed by or on behalf of the outsider;
- (b) persons acting as media of transmission to the outsider of income, profit or again; and
- (c) persons having the possession or custody of any assets of outsider.

The first category of persons would include all regular and authorised agents and also factors, commission agents, etc, whether appointed in writing or not. It would also include all such persons who would be regarded in law as agents by virtue of the conduct of parties. The second category of persons are those who form the channel for the flow of money from India to the outsider. It is transference of the income, profits or gains belonging to the outsider that attracts the liability to be appointed as agents. Transference of any other funds of a capital nature would not require appointment of agent. The third category comprises persons who are in a possession of the assets of the outsider under some lawful title or persons who happen to be in physical or has custody of any assets of the outsider [Section 22(2)]. Before deeming a person to be an agent as aforesaid, he must be given an opportunity of being heard by the Assessing Officer [Section 22(3)].

Such an agent is entitled to be reimbursed by his principal on whose account he pays the amount of wealth-tax. For this purpose he can retain the amount from the money that may be in his possession or may come to him as an agent. The power of retention out of any money payable by the agent to his principal residing outside India may also be exercised by him when he apprehends that he may be assessed as an agent. In such case, if any disagreement as to the amount to be so retained arises between him and his principal, then the agent may obtain from the Assessing Officer a certificate showing the amount to be so retained pending settlement of the liability. The certificate shall be warrant of the agent for retaining that amount [Section 22(6)].

Despite the aforementioned provisions of this section any arrears of tax due from a person residing outside India may be recovered also in accordance with the provisions of this Act from any assets of such person, which are or may at any time come within India [Section 22(7)].

3.4 PENALTIES [SECTION 18]

If any of the authorities is satisfied in the course of any proceedings under the Wealth-tax Act that any person has committed the prescribed defaults, he may, by order in writing direct that such person shall pay a penalty as specified in the order.

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3.4.1 Defaults : The following are the specified defaults:

1. Failure to comply with a notice under section 16(2) or (4);
2. Concealment of particulars of any assets;
3. Furnishing inaccurate particulars of any assets or debts.

The first default would attract a penalty of a sum which shall not be less than Rs.1,000/- and which may extend to Rs.25,000/- for each such failure. Further, in the case of such defaults, no penalty shall be levied if the person proves that there was a reasonable cause for such failure.

In the case of concealment of particulars of wealth or furnishing inaccurate particulars, the minimum penalty will be the amount of tax sought to be evaded and the maximum penalty will be five times the amount of tax sought to be evaded.

There are 6 Explanations expanding the scope of the section levying penalty.

Explanation 1 defines the expression 'the amount of tax sought to be avoided for the purposes of section 18(1)(iii). The expression denotes the amount that is arrived at by taking the difference between the tax on the net wealth assessed and that would be chargeable had such net wealth been reduced by the amount of concealed wealth and debts in respect of which inaccurate particulars have been furnished.

Explanation 2 provides that where, in respect of facts material to the computation of the net wealth of an assessee, he furnishes no explanation or he cannot substantiate the explanation offered by him or the explanation offered by him is found to be fake, the relevant assets shall be deemed to be his concealed assets. However, if the explanation offered is *bona fide* and the assessee has disclosed all facts material to the computation of his net wealth such deeming provision will not operate. The deemed concealment will apply where the assessee offers an explanation which he is not able to substantiate and fails to prove that such explanation is *bona fide* and that all the facts relating to the same and material to the computation of his net wealth have been disclosed by him. Students may note that the burden to prove that his explanation is *bona fide* etc. has been specifically placed upon the assessee.

Explanation 3 brings within the scope of deemed concealment cases of failure without reasonable cause, to furnish return of net wealth by any person within the period specified in section 17A(1). Such a penalty can be imposed where no notice has been issued to the person under section 16(4) (i) or 17(1) and the Assessing Officer or the Deputy Commissioner (Appeals) or the Commissioner (Appeals) or the Commissioner is satisfied that in respect of such assessment year such person has assessable net wealth. Such a levy can take place notwithstanding that such person furnishes the return of his net wealth at any time after the expiry of either of the periods aforesaid applicable to him in pursuance of a notice under section 17.

Explanation 4 provides that the assessee will be presumed to have concealed his wealth if the value of any asset returned by him is less than 70% of the value determined in assessment.

Explanation 5 In a case where an assessee is found in the course of a search under section 37A to be the owner of any money, bullion, jewellery or other valuable article or thing and the assessee claims that such assets represent wholly or partly, his wealth for (a) any valuation date falling before the date of the search but return in respect of the net wealth on such valuation date has not been furnished before the date of the search or such assets have not been declared in any return furnished before that date or (b) that such assets represent his wealth for any valuation date falling on or after the date of the search, then the assessee shall be deemed to have concealed the particulars of such assets or to have furnished inaccurate particulars of such assets, notwithstanding the fact that such assets are declared by the assessee in any return of net wealth furnished on or after the date of search. Consequently, in such cases penalty will be levied for concealment of wealth.

These provisions will not apply in a case where the relevant assets are recorded, on or before the date of search in the books of account maintained by the assessee or they are otherwise disclosed to the Commissioner before the date of search.

Explanation 6 seeks to exclude the application of the penalty provisions in relation to adjustments made under the proviso to clause (a) of section 16(1) in respect of which additional wealth-tax is charged.

Where any amount is added or disallowed in computing the net wealth of an assessee in any order of assessment or reassessment and the said order contains a direction for initiation of penalty proceedings under section 18(1)(c), such an order of assessment or reassessment shall be deemed to constitute satisfaction of the Assessing Officer for initiation of the penalty proceedings [Sub-section (1A)].

Sub-section (3) of section 18 provides that where a penalty order under section 18(1) is passed by the Income-tax Officer, and the amount of penalty exceeds Rs.10,000, the prior approval of the Joint Commissioner is required. Where the order is passed by the Assistant Commissioner or Deputy Commissioner such a prior approval is necessary only where the penalty exceeds Rs.20,000.

Where a penalty is levied by a Deputy Commissioner (Appeals), the Chief Commissioner or the Commissioner or Appellate Tribunal, a copy of the order should be sent to the concerned Assessing Officer.

No order imposing a penalty shall be passed in a case where the assessment to which proceedings for imposition of penalty relate is the subject matter of appeal to the Deputy Commissioner (Appeals) or the Commissioner (Appeals) under section 23 or an appeal to the

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Tribunal under section 24(2), after the expiry of the financial year in which the proceedings in the course of which action for the imposition of penalty has been initiated are completed or 6 months from the end of the month in which the order of the Deputy Commissioner (Appeals) or the Commissioner (Appeals) or as the case may be, the Appellate Tribunal is received by the Chief Commissioner or the Commissioner, whichever is later.

Where the relevant assessment order is the subject matter of revision under section 25(2) the order of penalty has to be passed before the expiry of 6 months from the end of the month in which such order of revision is passed.

In any other case, the penalty order has to be passed before the expiry of the financial year in which the proceedings in the course of which action for the imposition of penalty has been initiated are completed or six months from the end of the month in which the action for imposition of penalty is initiated, whichever is later.

3.4.2 Penalty for failure to answer questions, sign statements, furnish information etc. [Section 18A]: This section provides for levy of a minimum penalty of Rs.500 and which may go up to a maximum of Rs.10,000 for each of the following default or failure :

1. (a) Failure to answer any question put by a Wealth-tax authority in exercise of his power.
- (b) Refusal to sign any statement made in the course of any proceedings which a Wealth-tax authority may legally require a person to sign.
- (c) Failure to attend to give evidence or produce books of accounts or other documents in response to summons issued under section 37(1).

In the case of (c) above, no penalty will be levied if the person concerned proves that there was reasonable cause for the failure.

2. Failure to furnish in due time any statement or information which a person is bound to furnish to the Assessing Officer under section 38 would also lead to levy of penalty or a sum which shall not be less than Rs.100 and may extend to Rs.200 for everyday during which the default continues. Here also, if the person concerned proves reasonable cause for the failure, no penalty will be levied.
3. The penalty in respect of (1) or (2) above can be levied by any wealth tax authority. not lower in rank than a Joint Director/Joint Commissioner, if the default occurs in the course of proceedings before such authority. In any other case, the penalty under section 18A can be levied by the Joint Director or the Joint Commissioner.
4. Before levying penalty under this provision the assessee must be given an opportunity of being heard

3.4.3 Power to reduce or waive penalty [Section 18B]: This section gives very wide powers to the Chief Commissioner or the Commissioner for waiving or reducing the

penalty. An order of reduction or waiver of penalty may be made either on an application by the assessee or on the Commissioner's own motion.

Under this section, the power to reduce or waive penalty is confined to penalty for concealment under section 18(1)(iii). The Chief Commissioner or the Commissioner can reduce or waive the minimum penalty only if the assessee makes a full and true disclosure of all particulars regarding his wealth before Assessing Officer. In the case of both these defaults, there are two more conditions to be satisfied so that the Chief Commissioner or the Commissioner can reduce or waive the minimum penalty. The conditions are (1) that the assessee should have co-operated in any enquiry relating to the assessment of his net wealth and (2) that he should have either paid or made satisfactory arrangement for payment of any tax or interest payable in respect of the relevant assessment year. An assessee will be deemed to have made full and true disclosure of the particulars of his assets, or debts in any case where the excess of net wealth assessed over the net wealth returned is of such a nature as not to attract the provisions of section 18(1)(c). In cases of concealment or inaccurate particulars, if the amount in respects of which the penalty is imposable for furnishing the relevant assessment year or where such disclosure relates to more than one assessment year, such amount for any one of the relevant assessment years exceeds Rs.5,00,000/- the Commissioner cannot reduce or waive the penalty without obtaining the previous approval of the Chief Commissioner or Director General, as the case may be.

If in the case of person, reduction or waiver has been allowed once, he shall not be entitled to any relief or any subsequent occasion under this section. The Commissioner may, on any application made by the assessee and after recording his reasons, reduce or waive any penalty payable by the assessee or may stay or compound any proceedings for its recovery, if he is satisfied that it is a case of genuine hardship and the assessee has been co-operative. It is to be noted that the order of the Commissioner reducing or waiving penalty under this section will be final and cannot be challenged in any court.

3.4.4. Power of Commissioner to grant immunity from penalty [Section 18BA]

Section 18BA empowers the Commissioner to grant immunity from penalty.

- (1) The application for the immunity has to be made by the assessee (person whose case has been abated under section 22HA) to the Commissioner.
- (2) Where penalty was levied before or during the pendency of settlement proceedings, then the assessee can approach the Commissioner for immunity at any time.
- (3) However, if no penalty was levied till the time of abatement of proceedings before Settlement Commission, then the assessee must make an application for immunity before the imposition of penalty by the Wealth-tax authority.

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- (4) The Commissioner can grant immunity, subject to such conditions as he may think fit to impose, on being satisfied that the assessee has –
 - (i) co-operated in the proceedings after abatement; and
 - (ii) made a full and true disclosure of his net wealth and the manner in which such net wealth has been derived.
- (5) The immunity granted shall stand withdrawn, if such assessee fails to comply with any condition subject to which the immunity was granted.
- (6) The immunity granted to a person may, at any time, be withdrawn by the Commissioner, if he is satisfied that such person had, in the course of any proceedings, after abatement, -
 - (i) concealed any particulars material to the assessment from the wealth-tax authority; or
 - (ii) given false evidence.

Consequently, such person would become liable to the imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

3.5 SETTLEMENT OF CASES

Chapter VA (sections 22A to 29M) gives a statutory basis for settlement of cases which are necessitated at times in the interest of the revenue. The Constitution of the Settlement Commission and their powers and functions are explained briefly in the following paragraphs.

As per section 22A(b), 'Case' means any proceeding under this Act for the assessment under this Act, of any person in respect of any assessment year or assessment years which may be pending before an Assessing Officer on the date on which an application under sub-section (1) of section 22C is made.

However, application cannot be made to the Settlement Commission, where

- notice for assessment/reassessment has been issued under section 17.
- search has been initiated under section 37A or requisition has been made under section 37B followed by assessment or reassessment.
- fresh assessment has been directed on account of the original assessment being set aside by the Commissioner(Appeals)/Appellate Tribunal/Commissioner under sections 23A/24/25.

Therefore, no such proceedings, except original assessment proceedings, should be pending at the time of making an application to the Settlement Commission.

Further, the additional amount of wealth-tax offered and interest thereon should be paid before filing the application and proof of payment should be attached with the application.

3.5.1 Constitution: Settlements are to be made by a Commission called the Wealth-tax Settlement Commission. The Commission shall consist of a Chairman and as many vice-chairmen and other members as the Central Government thinks fit. The chairman and members shall be appointed by the Central Government from amongst persons of integrity and outstanding ability and shall possess special knowledge of and experience in problems relating to direct taxes and business account. Until such whole time members are appointed, the Central Government are empowered to require from time to time any members of the Board to function as part time members of the Settlement Commissions [Section 22B].

22BA deals with the jurisdiction and powers of Settlement Commission. Accordingly the jurisdiction, powers and authority of the Settlement Commission may be exercised by Benches. A Bench shall be presided over by the Chairman or a Vice-Chairman and shall consist of two other members. The Bench for which the Chairman is the Presiding Officer shall be the principal Bench and the other Benches shall be known as additional Benches. The Chairman may authorise the Vice-Chairman or other member appointed to one Bench to discharge also the functions of the Vice- Chairman or other member of another Bench.

When one of the members is unable to discharge his functions owing to absence, illness or any other cause or in the case of vacancy in the office of the Presiding Officer or any other member, the remaining two persons may function as the Bench and if the Presiding Officer of the Bench is not one of the remaining two persons, the senior among the remaining two persons, the senior among the remaining persons shall act as the Presiding Officer. Provision has also been made for the transfer of a case from a two member Bench to a three-member Bench.

The Chairman may, for the disposal of any particular case, constitute a Special Bench consisting of more than three members. The places at which the principal and additional Benches shall sit will be notified by the Central Government.

The Commission shall, subject to the provisions of this Chapter have power to regulate its own procedure and the procedures of Benches thereof in all matters arising out of the exercise of its power or of the discharge of its functions including the places at which the Bench shall hold their meetings.

Section 22BB provides for the circumstances under which the Vice-Chairman will discharge the functions of the Chairman. Section 22BC gives power to the Chairman to transfer any case pending before one Bench to another Bench.

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The decision of a Bench is to be by majority but if the members are equally divided they shall state the point of different persons to the Chairman who will either hear it himself or refer it to one or more of the other members of the Commission and such point shall be decided according to the opinion of the majority of all members who heard the case.

3.5.2 Application for settlement [Section 22C]: 1. An assessee, may at any stage of a case relating to him, make an application to the Settlement Commission to have the case settled. The application for settlement should *inter alia* contain a full and true disclosure of the applicant's wealth which has not been disclosed before the Assessing Officer the manner in which such wealth has been derived and the additional amount of wealth tax payable on such wealth [Sub-section (1)]

2. The additional amount of wealth-tax has to be calculated in the following manner as provided in the new sub-section (1B) of section 22C read with the amended sub-section (1C), in a case where the income disclosed in the application relates to only one previous year–

(i)	If the applicant has not furnished a return in respect of the net wealth of that year.	Wealth-tax should be calculated on the wealth disclosed in the application as if such wealth is the net wealth. Such tax represents the additional amount of wealth-tax
(ii)	If the applicant has furnished a return in respect of the net wealth of that year.	The wealth-tax should be calculated on the aggregate of net wealth returned and the wealth disclosed in the application i.e. as if the aggregate represents the net wealth. The additional amount of wealth-tax is the amount calculated on such aggregate as reduced by the amount of wealth-tax calculated on the net wealth returned for that year.

3. Where the wealth disclosed in the application relates to more than one previous year, then the above procedure is to be adopted in respect of each previous year and the aggregate of tax payable is to be calculated [Sub-section (1D)].

4. Where any books of account or other documents belonging to an assessee are seized under section 37A, the assessee would not be entitled to make a settlement application before the expiry of 120 days from the date of seizure [Sub-section (1E)].

5. Every settlement application made under sub-section (1) should be accompanied by the prescribed fees of Rs.500 [Sub-section (2)].

6. The settlement application made under sub-section (1) cannot be withdrawn by the applicant [Sub-section (3)].

7. The assessee should also intimate to the Assessing Officer in the prescribed manner that he has made an application to the Settlement Commission. Such intimation should be made on the same date when he makes an application to the Settlement Commission [Sub-section (4)].

3.5.3 Procedure before the Settlement Commission [Section 22D]**(1) Admission of Petition [Sub-section (1) of section 22D]**

- (i) On receipt of the settlement application, the Settlement Commission shall issue a notice to the applicant within 7 days from the date of receipt of application.
 - (ii) After hearing the applicant, the Settlement Commission shall pass an order either rejecting or allowing the application to be proceeded with within 14 days from the date of application.
 - (iii) Application not disposed off within 14 days shall be treated as admitted.
- (2) A copy of every order shall be sent to the applicant and to the Commissioner [Sub-section (1A) of section 22D].

(3) Deemed date of admission/disposal of Settlement applications made before 1.6.2007 [Sub-section (2A) of section 22D]

- (i) Settlement applications made prior to 1.6.2007, if not disposed off by 31st May, 2007, shall be deemed to be admitted, if the additional wealth-tax on the wealth disclosed in such application and the interest thereon is paid on or before 31.7.2007.
- (ii) 31.7.07 shall also be deemed to be the date of the order of rejection or admission for such applications.

(4) Time limit for furnishing report by Commissioner and passing order by the Settlement Commission [Sub-sections (2B) & (2C) of section 22D]

- (i) The Settlement Commission shall call for a report from the Commissioner within the time limit specified below –

(i)	In respect of an application admitted under section 22D(1)	Within 30 days from the date of application
(ii)	In respect of an application deemed to have been admitted under section 22D(2A)	On or before 7.8.2007

- (ii) The Commissioner is required to furnish the report within 30 days from the receipt of communication from the Settlement Commission.

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- (iii) The Settlement Commission can also pass an order declaring the application as invalid on the basis of the report of the Commissioner.
- (iv) Such order should be passed in writing within 15 days of the receipt of report after giving the applicant an opportunity of being heard.
- (v) A copy of the order should be sent to the applicant and the Commissioner.
- (vi) However, in a case where the Commissioner has not furnished the report within the prescribed time, the Settlement Commission shall proceed further in the matter without the report of the Commissioner.

(5) Status of pending settlement applications as on 1st June 2007, which are already admitted under the old provisions[Sub-section (2D) of section 22D]

All settlement applications which are admitted under the existing provisions of section 22D(1), but for which an order under section 22D(4) is not passed before 1.6.2007, will not be allowed to be proceeded with further unless the applicant pays the additional wealth-tax and interest thereon on or before 31.7.2007.

(6) Proceedings after admission [Sub-section (3) of section 22D]

- (i) The Settlement Commission may call for records from the Commissioner in respect of an application which has not been declared invalid under sub-section (2C) or an application which has been allowed to be further proceeded with under sub-section (2D).
- (ii) After examination of such records, the Settlement Commission may require the Commissioner to make further enquiry or investigation and furnish a report on the matters covered by the application and any other matter relating to the case.
- (iii) The Commissioner shall furnish the report within a period of 90 days of the receipt of communication from the Settlement Commission.
- (iv) If the Commissioner fails to furnish the report within the said period of 90 days, the Settlement Commission may proceed to pass an order under sub-section (4) without such report.

(7) Final order of settlement [Sub-sections (4) and (4A) of section 22D]

- (i) The Settlement Commission may pass such order as it thinks fit on the matters covered by the application and any other matter relating to the case not covered by the application but referred to in the report of the Commissioner.
- (ii) Such order should be passed by the Settlement Commission after –
 - (1) examining the records and report of the Commissioner, if any, received at the time of admission or on investigation or enquiry conducted as per the instructions of the Settlement Commission;

- (2) giving an opportunity of being heard to the applicant and the Commissioner;
 - (3) examining such further evidence as may be placed before it or obtained by it.
- (iii) The time limit for passing such order is –

(1)	In respect of an application made on or after 1.6.2007	Within 12 months from the end of the month in which the application was made.
(2)	In respect of an application filed before 1.6.2007 [under sub-section (2A) or (2D)]	On or before 31.3.2008

(8) The materials brought on record before the Settlement Commission shall be considered by the members of the bench before passing any order [Sub-section (5)].

(9) Such order shall provide for the terms of settlement, including any demand by way of tax, penalty or interest, the manner of payment of the sum due under settlement etc. It shall also provide that the settlement shall not be valid if it is subsequently found to have been obtained by fraud or misrepresentation of facts [Sub-section (6)].

(10) Where the tax payable in pursuance of an order passed by the Settlement Commission is not paid by the assessee within 35 days of receipt of a copy of final order, the assessee shall be liable to pay simple interest @ 1¼% for every month or part of a month on the outstanding amount from the date of expiry of 35 days. Such liability will arise even in cases where the commission extended the time allowed for such payment or permitted payment by installment [Sub-section (6A)].

(11) If a settlement becomes void, the proceeding with respect to matters covered by the settlement shall be deemed to have been received and the Wealth-tax authority shall complete such proceedings within a period of two years from the end of the financial year in which the settlement become void [Sub-section (7)].

3.5.4 Power of Settlement Commission to order provisional attachment to protect revenue [Section 22DD]

(i) Under section 22DD, the Settlement Commission is empowered to provisionally attach the property belonging to the applicant for protecting the interest of the revenue. The manner in which such provisional attachment is to be effected is provided in the Second Schedule to the Income-tax Act, 1961. Such provisional attachment is valid for a period of 6 months, after which it ceases to have effect.

(ii) The Settlement Commission may, for reasons to be recorded in writing, extend the aforesaid period by such further period or period as it thinks fit. The power to provisionally attach property is available to the Settlement Commission for an unlimited period.

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3.5.5 Powers of the Settlement Commission : The Settlement Commission has been conferred with all powers which are invested in a Wealth-tax authority under the Act [Section 22F(2)]. In respect of an application made under section 22C on or after 1.6.2007, such exclusive jurisdiction would begin with the date of filing of application with the Settlement Commission. The exclusive jurisdiction of the Settlement Commission would end on –

- (a) the date of passing an order under section 22D(4); or
- (b) the date of passing the order rejecting the application (made on or after 1.6.2007) under section 22D(1); or
- (c) the date on which the application is not allowed to be proceeded with under section 22D(2A); or
- (d) the date on which the application is declared invalid under section 22D(2C); or
- (e) the date on which the application is not allowed to be further proceeded with under section 22D(2D).

The following additional powers have also been conferred on the Commission:

(i) **To reopen completed proceedings [Section 22E]**

If the Settlement Commission is of the opinion that for the proper disposal of the case pending before it, it is necessary or expedient to reopen any proceeding connected with the case, but which has been completed under Income-tax Act, 1961 by any Income-tax authority before the application of the assessee under section 22C was made, it may, with the concurrence of the applicant, reopen such proceedings and pass such orders thereon as it deems fit as if the case in relation to which the application for the settlement had been made by the applicant covered by the proceedings for reopening of assessments as well. Before initiating the proceedings for reopening of assessment in any case, the reasons for arriving at the opinion for such reopening of the assessment must be recorded by the Settlement Commission. However, no proceeding shall be reopened by the Settlement Commission under this section if the period between the end of the assessment year to which such a proceeding relates and the date of application for settlement exceeds nine years.

Further, the Settlement Commission shall not have any power to reopen the proceedings in respect of an application made on or after 1.6.2007.

- (ii) **To grant and withdraw immunity from prosecution and penalty [Section 22H]:** The Settlement Commission may, if it is satisfied that the applicant has co-operated with it in the proceeding before it and made full and true disclosure of his wealth and

the manner in which it has been acquired, grant the applicant immunity from prosecution and penalty.

Under section 22H, the Settlement Commission may grant immunity from prosecution for any offence under the Indian Penal Code, Income-tax Act and any other Central Act. This power has now been restricted in respect of application made under section 22C on or after 1.6.2007. In respect of such cases, the Settlement Commission shall not grant immunity from prosecution for any offence under the Indian Penal Code or under any Central Act other than the Income-tax Act and Wealth-tax Act.

However, in respect of applications pending as on 1.6.2007, the Settlement Commission has the power to grant immunity from prosecution for any offence under the Indian Penal Code and other Central Acts also.

The Settlement Commission can grant partial immunity also from imposition of penalty. Such immunity can be withdrawn by it at any time under the following circumstances:

- (a) If the applicant has not complied with the conditions subject to which the immunity was granted.
- (b) If it is found that the applicant has during the proceeding before the Settlement Commission, concealed material particular relating the settlement.
- (c) If the applicant has given false evidence during the proceedings before the Settlement Commission.

When the immunity is withdrawn by the Settlement Commission, the authorities concerned can start proceeding for prosecution under the law applicable at the relevant time and can also impose penalties. In coming the time limit for starting prosecution on for levy of penalty, the period during which the immunity subsisted will be excluded.

The proviso to section 22H(1) precludes the Commission from granting immunity from prosecution in cases where the prosecution has been launched prior to the date of receipt of application for settlement. Sub-section (1A) provides that an immunity granted by the commission to any person shall stand withdrawn i.e. the discretionary power available to the Settlement Commission under (a) above has been withdrawn on failure of such person to pay tax with the time allowed or to comply with any other condition subject to which immunity was granted.

3.5.6 Abatement of proceeding before the Settlement Commission [Sections 22HA & 22HAA]

- (i) In the following cases, the proceedings before the Settlement Commission shall abate on the specified date as given below –

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	Case	Specified date
(1)	where an application made to the Settlement Commission on or after 1.6.2007 has been rejected under section 22D(1).	The date on which the application was rejected.
(2)	where any application is not allowed to be proceeded with under section 22D(2A) or further proceeded with under section 22D(2D).	31.7.2007
(3)	where an application has been declared invalid under section 22D(2C).	The last day of the month in which the application was declared invalid.
(4)	Where an order under section 22D(4) has not been passed within the time allowed under section 22D(4A).	The date on which the time or period specified in section 22D(4A) expires.

- (ii) On abatement of proceedings, the case would revert back to the Assessing Officer having jurisdiction or any other wealth-tax authority before whom the proceedings were pending at the time of making the application. Such wealth-tax authority shall dispose of the case in accordance with the provisions of the Act.
- (iii) For completing the proceedings, the Assessing Officer or other wealth-tax authority shall be entitled to use the material and information produced by the assessee before the Settlement Commission as if such material and information had been produced before the Assessing Officer or other wealth-tax authority. Similarly, the Assessing Officer or other wealth-tax authority shall be entitled to use the results of the inquiry held or evidence recorded by the Settlement Commission in the course of the proceedings before it, as if such inquiry or evidence had been held or recorded by him in the course of the proceedings before him.
- (iv) The period from the date on which the application was made before the Commission up to the date on which proceedings get abated shall be excluded from the time limit for completion of proceedings by the Assessing Officer and for payment of interest under section 34A.
- (v) In case of abatement of settlement proceedings, the Assessing Officer is required to give credit for the tax and interest paid on or before the date of making the application or during the pendency of the case before the Settlement Commission [Section 22HAA] .

3.5.7 Order of Settlement Commission to be conclusive [Section 22-I]

Section 22-I provides that every order of the Settlement Commission passed under section 22D(4) shall be conclusive in respect of the matters contained therein and consequently no matter covered by the settlement order shall be liable to be reopened in any proceeding under the Wealth-tax Act or under any other law for the time being in force except, however, in those cases wherein the reopening of the case is specifically provided in Chapter VA of the Wealth-tax Act.

3.5.8 Recovery of settled amount [Section 22J]

According to section 245J, any amount specified in an order of settlement passed by the Settlement Commission under section 22D(4), may be recovered and any penalty for default in making the payment may be imposed and recovered from the person concerned in accordance with the provisions of section 32. The power for making the recovery if any, as may be specified by the Settlement Commission in the order passed by it. The right of recovery may be exercised by the Assessing Officer having jurisdiction over the person who has made the application for settlement under section 22C.

3.5.9 Bar on subsequent application for settlement [Section 22K]

- (i) In the event of occurrence of any of the following, the person concerned shall not be entitled to apply for settlement in relation to any other matter –
 - (1) the order of settlement passed under section 22D(4) provides for imposition of penalty for concealment of income; or
 - (2) after the passing of order under section 22D(4) in relation to a case, the person is convicted of an offence under Chapter XXII in relation to that case; or
 - (3) the case of such person was sent back to the Assessing Officer by the Settlement Commission on or before 1.6.2002.
- (ii) Further, with effect from 1.6.2007, the option of going to the Settlement Commission would be available only once in the lifetime of a person. Therefore, where an application for settlement is made on or after 1.6.2007 and such application has been allowed to be proceeded with, then such person will not be subsequently entitled to make any application under section 22C.

3.5.10 Proceedings to be judicial proceedings [Section 22-L]

Any proceeding under Chapter VA before the Settlement Commission shall be deemed to be judicial proceedings within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code, 1860.

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3.6 APPEALS AND REVISION

3.6.1 Appeal against orders of Assessing Officers: An appeal against the order of the Assessing Officer lies to the Commissioner (Appeals), who is the first appellate authority.

3.6.2 Appealable orders before Commissioner (Appeals) [Section 23A]: Any person may appeal to the Commissioner (Appeals) against an assessment or order in respect of the following :

- (a) Objecting to net wealth computed
- (b) Objecting to amount of wealth tax determined
- (c) Denying liability to be assessed under this Act
- (d) Objecting to penalty imposed under section 18/18A
- (e) Objecting to order passed under section 20
- (f) Objecting to penalty imposed under section 221 of the Income tax Act as applied under section 32 for the purposes of wealth tax
- (g) Objecting to order made under section 22 treating him as agent of a person residing outside India.
- (h) Objecting to an order by the Assessing Officer under section 35 having the effect of enhancing the assessment or reducing a refund or refusing to allow the claim made by the assessee under that section.
- (i) Objecting to any order of the Valuation Officer under section 35 having the effect of enhancing the assessment or reducing a refund or refusing to allow the claim made by the assessee under that section.
- (j) Objecting to penalty imposed by the Joint Director or Joint Commissioner under section 18A.

The appeal should be in the prescribed form and should be made on payment of Rs.250.

3.6.3 Procedure in appeal to Commissioner(Appeals): 1. An appeal must be presented within 30 days of the receipt of the demand of notice relating to the assessment or penalty objected to, or the date on which the order objected to is communicated to the assessee. However, the Commissioner (Appeals) may admit an appeal after expiration of the aforesaid period if he is satisfied that the appellant had sufficient cause for not presenting the appeal within the specify period.

2. No appeal by an assessee shall be admitted unless at the time of filing the appeal he has paid the tax due on the net wealth returned by him.

3. The Commissioner (Appeals) shall fix a day and place for the hearing and may, from time to time, adjourn the hearing.

4. In case of appeal against the valuation of an asset, where such valuation has been done by a Valuation Officer, the Commissioner (Appeals) shall give such Valuation Officer an opportunity of being heard. In any other case, on a request being made by the Assessing Officer, the Commissioner (Appeals) shall give an opportunity of being heard to any Valuation Officer nominated for the purpose by the Assessing Officer.
5. During the course of the hearing, the Commissioner (Appeals) may allow the appellant to go into any ground of appeal not specified earlier.
6. Before disposing of an appeal, the Commissioner (Appeals) may make such further enquiry as he thinks of fit.
7. The Commissioner (Appeals) may also considered and decide any matter arising out of the proceedings notwithstanding that such matter was not raised earlier by the appellant.

3.6.4 Order of Commissioner (Appeals) under section 23A: 1. The Commissioner (Appeals) may pass such order as he thinks fit which may include an order enhancing the assessment or penalty.

2. The order shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision.
3. A copy of the order shall be forwarded the Appellant and the Chief Commissioner or Commissioner.
4. In every appeal, where it is possible, the Commissioner (Appeals) may hear and decide such appeal within one year from the end of financial year in which such appeal is filed under this section.
5. In disposing of an appeal, the Commissioner (Appeals) may consider and decide any matter arising out of the proceedings in which the order appealed against was passed, notwithstanding that such matter was not placed before the Commissioner (Appeals) by the appellant.
6. *The Commissioner (Appeals), in disposing of an appeal against the assessment order in respect of which the proceeding before the Settlement Commission abates under section 22HA, is empowered to confirm, reduce, enhance or annul the assessment after taking into consideration the following -*
 - (1) *all the material and other information produced by the assessee before the Settlement Commission;*
 - (2) *the results of the inquiry held by the Settlement Commission;*
 - (3) *the evidence recorded by the Settlement Commission in the course of the proceedings before it; and*
 - (4) *such other material as may be brought on his record.*

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3.6.5 Commissioner's power to revise orders passed by his subordinates [Section 25]

(1) Revision of orders prejudicial to assessee [Sub-section (1)]: 1. The Commissioner has the power to revise any order passed by any authority subordinate to him. For this purpose even a Deputy Commissioner (Appeals) shall be deemed to the subordinate to him.

2. The Commissioner may, either on his own motion on an application made by the assessee, revise an order passed by his subordinate. For this purpose, he may call for the record of any proceeding under the Act, and make such enquiry as he thinks fit.

3. Order passed under sub-section (1) of this section cannot be prejudicial to the assessee.

4. The Commissioner does not have the power to revise an order in the following circumstances:

(i) Where the assessee right to obtain relief by way of appeal to Deputy Commissioner (Appeals) or Commissioner (Appeals) or the Appellate Tribunal has not expired or where the assessee has not waived his right of appeal;

(ii) Where the order is the subject matter of appeal before Deputy Commissioner (Appeals), Commissioner (Appeals) or the Tribunal.

5. Where the application for revision is made by the assessee, it must be accompanied by a fee of Rs.25.

6. The application for revision must be made within one year from the date of the order which is sought to be revised.

However, the Commissioner may extend the period if he thinks fit.

7. Where the order is sought to be revised by the commissioner on his own motion, the time limit is 1 year from the date of subordinate authority's order.

8. The Commissioner shall pass the order of revision within 1 year from the end of the financial year in which the application was made. In computing this period of limitation, the time taken in giving an opportunity to the assessee to be reheard under the proviso to section 39 and any period during which any proceeding under section 25 is stayed by an order or injunction of any court shall be excluded.

(2) Revision of orders prejudicial to revenue [Sub-section (2)]: 1. Under this sub-section the Commissioner has the power to revise any order of an assessing officer which is prejudicial to the interest of revenue.

2. For this purpose, he may call for and examine the record of any proceeding under the Act. After giving the assessee an opportunity to be heard, and after making such enquiry as he thinks fit, the Commissioner may pass the revision order.
3. He may enhance, modify or cancel the Assessing Officer's order and may direct a fresh assessment to be made.
4. No order shall be made under this sub-section after the expiry of 2 years from the end of the financial year in which the order sought to be revised was passed.
5. For the purpose of this sub-section, the Commissioner shall be competent to revise an order of assessment passed by an Assessing Officer on all matters except those that have been considered and decided in appeal.

3.6.6 No time limit for revising an order to give effect to any finding or direction contained in an order of the Appellate Tribunal, National Tax Tribunal (NTT), the High Court or the Supreme Court [Section 25(4)]:

Section 25(4) provides that an order in revision may be passed at any time in the case of an order which has been passed in consequence of, or to give effect to, any finding or direction contained in an order of the Appellate Tribunal, **National Tax Tribunal (NTT)**, the High Court or the Supreme Court.

3.6.7 Appeal to Appellate Tribunal from orders of Commissioner [Section 24]:

1. An assessee can file an appeal to the Appellate Tribunal against the following orders:
 - (a) Order passed by the Deputy Commissioner (Appeals) or Commissioner (Appeals) under section 18 or 18A or 23 or 23A or 37(2)
 - (b) Order passed by the Chief Commissioner or Commissioner under section 18 or 18A or 25(2)
 - (c) Order passed by the Director General or Director under section 18A.
2. The Commissioner may file an appeal to the Tribunal against section 23A.
3. The appeal is to be made within 60 days of the date on which the order is communicated to the assessee or the Commissioner, as the case may be.
4. The appeal shall be in the prescribed form and verified in the prescribed manner and shall be accompanied by a fee of Rs.1000/-

However, where the appeal does not relate to net wealth as computed by the Assessing Officer, the fee will be Rs.500.

5. Section 24(2A) enables the Assessing Officer or the assessee as the case may be, to file a memorandum of cross-objections within 30 days of receipt of notice of the appeal by the other party.

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6. In appropriate cases, the Tribunal may admit an appeal, or permit the filing of a memorandum of cross-objections after the expiry of the relevant period.
7. When the valuation of any asset is in dispute before the Tribunal and the valuation of the asset was made by the Valuation Officer, the Appellate Tribunal shall give an opportunity for hearing such Valuation Officer. In any other case, where no such valuation has been made at the stage of assessment or where such Valuation Officer is not available, the Tribunal if so, requested by the Assessing Officer shall be given an opportunity for hearing to Valuation Officer nominated by the Assessing Officer,
8. No order enhancing an assessment or penalty shall be made under the person affected thereby has been given a reasonable opportunity of showing cause against such enhancement.
9. The Appellate Tribunal, where it is possible, may hear and decide such appeal within a period of 4 years from the end of the financial year in which such appeal was filed.
10. The cost of any appeal to the Appellate Tribunal shall be at the direction of that Tribunal.
11. A copy of every order passed by the Appellate Tribunal shall be forwarded to the assessee and the Commissioner.

3.6.8 Appeal to the Appellate Tribunal from orders of enhancement by the Chief Commissioner or Commissioner [Section 26]:

1. Any assessee may appeal to the Tribunal objecting to the following orders:
 - (i) an order passed by the Chief Commissioner or Commissioner under section 18 or 18A or 25(2);
 - (ii) an order passed by the Director General or Director under section 18A.
2. The appeal must be made within 60 days of the date on which the order is communicated to the assessee.
3. The appeal shall be in the prescribed form and shall be accompanied with a fee of Rs.250.

3.6.9 Direct appeal to High Court [Section 27A]: 1. The assessee or the Chief Commissioner or Commissioner may file an appeal to a High Court against any order passed under section 24 or 26 or section 35(1)(e). This is applicable only in respect of filing of appeals on or after 1.10.98 but **before the date of establishment of NTT.**

2. The appeal must be made within 120 days of the day on which he is served with notice of the order.
3. In case of an order passed by the Appellate Tribunal under section 24(1), an appeal shall lie to the High Court **before the date of establishment of the NTT**, only if the High Court is satisfied that the case involves a substantial question of law. **Thereafter, the appeal shall lie to the NTT.**

4. The Memorandum of Appeal shall state precisely the substantial question of law involved in the appeal under this section.
5. Where the High Court is satisfied that a substantial question of law is involved, it shall formulate the question.
6. The appeal shall be heard only on the question so formulated, and the respondent shall be allowed to argue during the hearing that the case does not involve such question.
7. The High Court shall decide the question of law so formulated and deliver such judgement as it deems fit. The judgment shall contain the ground on which the decision is founded. The Court may also award such cost as it deems fit.
8. The provisions of the Court of Civil procedure, 1908 relating to appeals to High Court shall apply in a case of Appeals under this section.

3.6.10 Hearing by High Court [Section 28]: 1. An appeal under section 27A shall be heard by the bench of not less than 2 Judges of the High Court and it shall be decided in accordance with the opinion of such judges or of the majority of such judges, if any.

2. Where the judges shall state the point upon which they differ and the case shall then be heard only upon that point by one or more judges of the High Court. Such point shall then be decided according to the majority opinion of the judges including the judges who first heard it.

3.6.11 Appeal to Supreme Court [Section 29]: 1. An appeal shall lie to the Supreme Court from any judgment of the High Court delivered **before the date of establishment of the NTT**, on a reference made under section 27 or appeal made under section 27A only if the High Court certifies it to be a fit case for appeal to the Supreme Court. **Thereafter, an appeal shall lie to the Supreme Court from any judgment of the NTT as per the provisions of the National Tax Tribunal Act, 2005.**

2. Where the judgement of the High Court is varied or reversed by the Supreme Court under this section, effect shall be given to the order on the basis of a certified copy of the judgement delivered.

3. The High Court may, on application made to it for the execution of any order of the Supreme Court in respect of any cost awarded by it, transit the order for execution to any court subordinate to it.

3.6.12 Wealth-tax to be paid in all cases [Section 29A]: Notwithstanding that a reference has been made to the High Court or the Supreme Court, or an appeal has been preferred to the Supreme Court under this Act **before the commencement of the National Tax Tribunal Act, 2005**, wealth-tax shall be payable in accordance with the assessment made in the case.

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3.7 COLLECTION AND REFUND

3.7.1 Collection and recovery of tax: The Assessing Officer is under an obligation to serve upon the assessee a notice of demand in the prescribed form specifying the sum payable, if any as tax, interest, penalty, fine or any order passed under this Act [Section 31]. The amount specified in the aforesaid notice of demand is to be paid within 30 days of the notice. However, the Assessing Officer may specify in the notice a lesser period than that of 30 days, if the full respite of 30 days is reasonably believed to be likely to be detrimental to revenue. But he may do so only with the previous approval of the Deputy Commissioner [Section 31(1) and the proviso].

Any failure on the part of the assessee to pay the amount within such period as specified in the preceding paragraph will render him liable to payment of interest @ 1% for every month or part of a month comprised in the period commencing from the day immediately following the end of the period mentioned in 31(1) and ending with the day on which the amount is paid. But if in consequence of an order under sections 23, 23A, 24, 25, 26, 27, 29 or 35 the amount on which interest was payable as aforesaid had been reduced, the interest will accordingly suffer reduction, and the interest paid in excess, shall be refunded [Section 31(2) and the proviso]. Sub-section (2A) empowers the Chief Commissioner or the Commissioner to reduce or waive the interest payable under section 31(2) for reasons of hardship, circumstances beyond control and the co-operation extended by the assessee.

Without prejudice to the provisions of sub-section (2), if the assessee makes an application before the due date under sub-section (1) expires, the Assessing Officer may either extend the time for payment or allow payment by installments. But while doing so the Assessing Officer may lay down such conditions as the circumstances of the case might warrant [Section 31(3)].

The modes of recovery of tax, interest, penalty, etc. are similar to those prescribed under sections 221 to 227, 228A, 229, 231 and 232 of the Income-tax Act and the Second and Third Schedules thereto and any rules made thereunder [Section 32].

Any reference to section 173 and section 220(2) or (6) or (7) of the Income-tax Act will be treated as references to section 22(7) and section 31(2) or (6) or (7) of the Wealth-tax Act respectively. The Chief Commissioner or the Commissioner and the Tax Recovery Officer referred to in the Income-tax Act shall be deemed to be the corresponding wealth-tax authorities for the purpose of recovery of wealth-tax and sums imposed by way of penalty, fine and interest.

3.7.2 Liability of transferees: Section 33 provides that in cases (falling under the purview of section 4) out of the tax assessee in the hands of the transferor individual that portion which is attributable to the transferred assets (on a pro rata basis) may be recovered from the transferee. Where the assets are transferred more than one person

jointly, all such persons are jointly and severally liable for the apportioned tax. If the transferee or joint transferees fail to pay the tax as specified in the notice of demand he or they would be deemed to be assesses in default and all the provisions in regard to recovery would apply to them.

3.7.3 Refunds [Section 34A] : (a) If as result of any order passed in an appeal or other proceeding (including a rectification proceeding), the refund of any amount becomes due to the assessee the Assessing Officer should refund to the assessee the amount due to him without his being required to make any claim in that behalf [Section 34A(1)]. In other words, it not necessary for the assessee to make a claim in that behalf.

Sub-section (3) of the section further provides that where a refund is so due and the Assessing Officer does not grant the refund within 6 months from the date of the order, the Central Government shall pay to the assessee simple interest at 6% per annum on the amount of refund due from the date immediately following the expiry of the 6 month period to the date on which the refund is due.

(b) The proviso to section 34A(1) provides that (i) where an assessment is set aside with the direction to make it afresh, any refund will become due only after the fresh assessment is made and (ii) where an assessment is annulled, the tax on the net wealth returned will not be refunded. Only the tax paid in excess of the tax chargeable on the net wealth returned will be refunded.

(c) According to sub-section (2), where refund of any amount becomes due to the assessee as a result of an order under this Act or under the provisions of sub-section (1) of section 16 after a return has been made under section 14 or section 15 or in response to a notice under clause (i) of sub-section (4) of section 16 and the Assessing Officer is of the opinion having regard to the fact that (i) a notice has been issued or is likely to be issued under section 16(2) in respect of the said return or (ii) the order is the subject matter of an appeal or further proceeding or (iii) any other proceeding under this Act is pending, that the grant of the refund is likely to adversely affect the revenue the Assessing Officer may, with the previous approval of the Chief Commissioner or the Commissioner, withhold the refund till such time as the Chief Commissioner or the Commissioner may determine.

(d) Sub-section (4B) provides that where refund becomes due to the assessee, he shall be entitled to receive in addition to the said amount simple interest thereon calculated at the rate of $\frac{1}{2}\%$ for every month or part thereof comprised the period or periods from the date or dates of payment of the tax or penalty to the date on which the refund is granted. The expression 'date of payment of the tax or penalty' for this purpose means the date on and from which the amount of tax or penalty specified in the notice of demand is paid in excess of such demand.

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(e) For the purpose of computing the period of delay any delay in proceedings (including assessment proceedings) attributable to the assessee shall be excluded.

(f) There is also a provision for automatic revision of interest on refund where the refund has been increased or reduced on reassessment, appeal, revision, rectification or by an order of the Settlement Commission.

(g) The Assessing Officer, or the Deputy Commissioner (Appeals) or the Commissioner (Appeals) or the Chief Commissioner, as the case may be, has the power under section 34A(5) to set off the amount of refund or any portion of the amount against the sum, if any remaining payable under this Act by the person to whom the refund is due. Such a person must, however be informed in writing of the action proposed to be taken.

3.8 PROSECUTION

3.8.1 Summary of offences and prosecution: Section 35A to 35N, deal with prosecutions for offences under the Wealth-tax-Act. These provisions envisage a variety of offences and harsh punishment for the same.

The nature of the offences and the quantum of penalty or other punishment prescribed are briefly indicated below in a tabular form:

No.	Nature of the offence	Relevant Section	Quantum of penalty or punishment
1A.	Wilful attempt to evade tax, penalty.	Section 35A(1)	(i) In a case, where the amount sought to be evaded exceeds 1 lakh, rigorous imprisonment for a minimum term of 6 months up to a maximum term of 7 years and fine. (ii) In any other case, rigorous imprisonment for a minimum term of 3 months up to a maximum term of 3 years and fine.
1B.	Wilful attempt to evade payment of tax, penalty or interest	Section 35A(2)	Rigorous imprisonment for a minimum term of 3 months up to a maximum term of 3 year and in the discretion of the Court also with fine.

For the purpose of both the above offences, willful attempt to evade tax etc. shall also include a case, where any person -

- (i) has in his possession or control, any books of account or other documents relevant to any proceeding under the Act containing a false entry or statement; or
- (ii) makes or cause to be made any false entry or statement in such books of account or other documents; or
- (iii) willfully omits or causes to be omitted, any relevant entry or statement in such books account or other documents; or
- (iv) causes any other circumstance to exist which will have the effect of enabling a person to evade and tax, penalty or interest.

2.	Willful failure to furnish return of net wealth under section 14(1) or 14(2) or 17(1).	Section 35B	Same as in 1A above. Penalty or prosecution under this section will not be attracted if the return is furnished by the assessee before the expiry of assessment year and the tax payable on the wealth determined on regular assessment does not exceed Rs.3,000.
3.	Willful failure to produce accounts records, etc. on or before the date specified in section 16(4)	Section 35C	Rigorous imprisonment up to 1 year or with fine equal to a sum calculated at a rate which shall not be less than Rs.4 or more than Rs.10 for every day during which the default continues, or with both.
4.	False statement in a verification under the Act (other than under section 34AB) or under any rule.	Section 35D	Same as in 1A above
5.	False statement in a verification mentioned in section 34AB (registration of valuers).	Section 35E	Imprisonment for a term which may extended to 6 months or with fine or with both.

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6.	Failure by a registered valuer, without reasonable cause or excuse, to intimate to the Board particulars of conviction or finding referred to in section 34ACC.	Section 35EE	Imprisonment up to two years and fine.
7.	Contravention of order issued to effect constructive seizure	Section 35EEE	If a person makes any contravention of the above-mentioned orders he shall be punishable with rigorous imprisonment for a term which may extend to five years and with fine
8.	Abetting or inducing another person to deliver a false account, statement or declaration in relation to any return of wealth or to commit an offence under section 35A(1). (Willful attempt to evade tax, etc.)	Section 35F	Same as in 1A above.
9.	Punishment of second and subsequent offences under : section 35A(1) above “ 35B above “ 35D above “ 35F above	Section 35G	If a person convicted of an offence under section 35A(1) or 35B or 35D or 35F is again convicted under any of these sections he shall be punishable for the second and subsequent offences with rigorous imprisonment for a minimum term of 6 months and upto a maximum of 7 years and with fine.

3.8.2 Power of Commissioner to grant immunity from prosecution [Section 35GA]

Section 35GA empowers the Commissioner to grant immunity from prosecution.

- (1) The application for the immunity must be made by the assessee (person whose case has been abated under section 22HA) to the Commissioner before institution of the prosecution proceedings after abatement.

- (2) If prosecution proceedings were instituted before or during the pendency of settlement proceedings, then the assessee can approach the Commissioner for immunity any time. However, if the assessee has received any notice etc. from the Wealth-tax authority for institution of prosecution, then he must apply to the Commissioner for immunity, before actual institution of prosecution.
- (3) The Commissioner can grant immunity, subject to such conditions as he may think fit to impose, on being satisfied that the assessee has –
 - (i) co-operated in the proceedings after abatement; and
 - (ii) made a full and true disclosure of his net wealth and the manner in which such net wealth has been derived.
- (4) Where application for settlement under section 22C had been made before the 1st June, 2007, the Commissioner can also grant immunity from prosecution for any offence under this Act or under the Indian Penal Code or under any other Central Act.
- (5) The immunity granted shall stand withdrawn, if such assessee fails to comply with any condition subject to which the immunity was granted.
- (6) The immunity granted to a person may, at any time, be withdrawn by the Commissioner, if he is satisfied that such person had, in the course of any proceedings, after abatement, -
 - (i) concealed any particulars material to the assessment from the Wealth-tax authority; or
 - (ii) given false evidence.

Consequently, the person may be tried for the offence with respect to which the immunity was granted or for any other offence of which he appears to have been guilty in connection with the proceedings.

3.8.3 Offences by Hindu Undivided Families

Section 35H provides that where the offence has been committed by a HUF, the Karta shall be deemed to be the guilty of the offence and shall be liable to be proceeded against and punished accordingly unless he can prove that the offence was committed without his knowledge or that he had exercised due diligence to prevent the commission of such offences. The section also makes a member of the family equally guilty in case where the offence was committed with his consent or convenience or due to his neglect.

3.8.4 Offences by Companies

- (a) Under section 35HA, where an offence has been committed by a company, the company as well as the person who was in charge of, and was responsible for the conduct

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of the business at the time when the offence was committed will be deemed to be guilty of the offence.

(b) It is also provided that, where the offence had been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the offence.

(c) In respect of the some of the offences, it is provided that the person found guilty shall be punishable with rigorous imprisonment and with fine. A company being a juristic person cannot be punished with imprisonment. It can be punished with fine only.

(d) Sub-section (3) provides that if an offence under the Act has been committed by a person being a company, it shall be punished with fine.

(e) Every other person who was in charge of and was responsible for the conduct of business of the company, or any director, manager, secretary or other officer of the company (with whose consent or connivance of or due to whose failure, the offence was committed) is liable for punishment of imprisonment and fine wherever so provided.

3.8.5 Other provisions governing prosecutions

Section 35-I lays down that a person can be proceeded against for an offence under the Act only at the instance of the Chief Commissioner or the Commissioner (Appeals) either before or after the institution of proceedings, the Chief Commissioner or the Commissioner can also compound any offence under the Act.

Section 35J makes offences punishable under section 35A (willful attempt to evade tax penalty, etc.), section 35B (failure to furnish returns, etc.), section 35D (false statement in verification, etc.) and section 35F (abetment of false return, etc.) non-cognizable under the Code of Criminal Procedure, 1973. Section 35M bars the application of section 360 of the Code of Criminal Procedure, 1973 and the Probation of Offenders Act, 1958, unless the person convicted of an offence under the Act is under 18 years of age. Section 35K bars prosecution under Section 35A or 35D in relation to the assessment for an assessment year in respect of which the penalty imposed or imposable on him under Section 18(1)(iii) has been reduced or waived by an order under section 18B. Section 35K also lays down that where any proceeding for prosecution has been taken against any person, any statement made or account or other document produced by such person before any of the Wealth-tax authorities shall not be in admissible as evidence for the purpose of such proceedings merely on the ground that such statement was made or such account or other document was produced in the belief that the penalty imposable would be reduced or waived under section 18B or that the offence in respect of which such proceedings was taken would be compounded.

Section 35K provides for bar on prosecution and inadmissibility of evidence in certain circumstances on the lines of section 279(1A) of the Income-tax Act.

3.8.6 Presumption as to books of account etc.

Section 35N provides that where -

- (i) books of account or other documents, articles or things including money found in the possession of any person during search made under section 37A or
- (ii) books of account, documents, or inventory of any articles or thing taken in custody by an officer or authority under sub-section (1) or section 37B and delivered to a requesting officer under sub-section (2) of section 37B

are tendered as evidence by the prosecution against such person and the person who is accused of abetment of false return under section 35F, the provision of section 37A(5)-presumption as to books of account, documents, etc. will apply.

Section 36: Section 36 provides for production of evidence in prosecution for offences under the Act on the same lines as those of section 279B of the Income-tax Act.

3.8.7 Power to tender immunity from prosecution: The Central Government has been empowered by section 36A with a view to obtain evidence of any person, appearing directly or indirectly to be concerned in or privy to the concealment of particulars in respect of net wealth or to the evasion of payment of tax on net wealth to tender such person immunity from prosecution for offence as well as from the imposition of any penalty under this Act. However, this tender of immunity is not irrevocable in character. The Central Government may withdraw it, if it thinks that the person who was granted the immunity and subsequently either fails to comply with the condition on which such immunity was granted or was willfully concealing anything or giving false evidence.

3.8.8 Power to take evidence on oath: The Wealth-tax authorities including Valuation Officers shall have the same powers as the Court has under the Civil Procedure Code when trying suit as in respect of the following matters:

- (i) discovery and inspection;
- (ii) enforcing the attendance of any person and examining him on oath;
- (iii) compelling the production of books of account and other document;
- (iv) issuing commissions [section 37(1)].

The provisions of section 37 are on the same lines as those of section 131 of the Income-tax Act. Accordingly, the Valuation Officer also is an authority and the power to summon, etc. has been conferred on Valuation Officer also.

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3.9 SEARCH AND SEIZURE

3.9.1 Power of search and seizure: Sections 37A and 37B deal with this power.

The warrant of authorisation to make search and to seize could be issued by the Director General or the Director or the Chief Commissioner or the Commissioner or any such Joint Director or the Joint Commissioner may be empowered by the Board in this behalf.

The warrant of authorisation can be issued in the case of the following persons:

- (a) Any person who has received a notice under section 16(4) or a summon under section 37 to produce books of account or other documents but has failed or omitted so to produce.
- (b) Any person to whom the aforesaid notice or summon has actually been or might be served and who will not or would not produce any books of account or other documents which will be useful or relevant for the purpose of any proceeding under the Act.
- (c) Any person who is in possession of any articles or things including those disproportionate to his known assets, particulars of which will be useful or relevant to any proceeding under this Act.

In the above cases, the authorised officer will have the power to enter and search any building, place, vessel, vehicle or aircraft where he has reason to suspect that such books of account or other documents, articles of things including money are kept. The officer can also search any person who got out of or is about to get into or is in the building, place, vessel, vehicle or air craft when the officer has reason to suspect that such person has secreted about his person any books of account, documents, money, bullion, jewellery or other valuable article etc. The authorised officer can break open the lock of any door, box, locker, safe, almirah or other receptacle where the keys are not available and seize any such books of account or other documents, place marks of identification on them and make a note or inventory of them.

If any building, place, vessel, vehicle or aircraft which is to be searched is situated in an area over which a particular Commissioner has jurisdiction, whereas the assessee in whose case the search is to be made, is under the jurisdiction of another Commissioner, the warrant of authorisation can be issued by any of the two Commissioners. In case where search has been authorised by one Commissioner etc. but some of the premises to be searched fall outside his jurisdiction, the Commissioner available locally is empowered to authorise extension of search of premises not mentioned in the search authorisation issued by the first Commissioner, etc. where he is satisfied that such extension of the search is necessary.

Where any books of account, document, bullion, jewellery, etc. are found in possession of a person or in control of any person or in the course of any search the Wealth-tax Authority can draw the following presumptions:

- (a) That such books of accounts, documents, money, bullion; jewellery etc. belong to that person.
- (b) That the contents of such books of accounts and documents are true.
- (c) That the signature, the books of account, documents, etc. purported to be in the handwriting of a particular person are in his handwriting and documents stamped and executed or attested were duly stamped and executed or attested. The assessee can rebut the presumption by proving the real fact by conclusive evidence. The books of account or other documents seized can be retained by the authorised officer for a period not exceeding 180 days from the date of seizure. It can be retained for period exceeding 180 days only with the approval of the Commissioner and only after recording the reasons for such retention. However, even the Commissioner cannot authorise such retention for a period exceeding 30 days after all proceeding under the Act in respect of the year for which the books of account or other documents are relevant the completed.

Whenever necessary, the authorised officer will have to transfer the books of accounts, documents and other seized assets to the Assessing Officer who exercises jurisdiction over the assessee within a period of 15 days of the seizure. After such transfer is made, the power of retention of book, documents and assets shall be exercised by Assessing Officer who has jurisdiction over the case.

If the legal owner of the books of account, etc. from whom these are seized objects to the aforementioned approval of the Commissioner, he may make an application to the Board stating the reasons for objections and requesting for their return. There upon, the Board after giving the applicant an opportunity for being heard may pass order as it thinks fit. The provisions of the Code of Criminal Procedure Code, 1973 relating to searches and seizure will be applicable to searches under the Wealth-tax Act also.

3.9.2 Power to requisition books of account, etc. : Section 37B deals with power to requisition books of account, documents and other valuable assets which have been seized by other authority such as Customs, Police, etc. According to this provision, the Director General or the Director or the Chief Commissioner or the Commissioner can authorise a Deputy Director or the Deputy Commissioner or the Assistant Director or the Assistant Commissioner or the Assessing Officer or receive from any authority which has seized books of account, documents or other-assets. The Director of Inspection or C.I.T. can issue requisition to such authority to return the seized books of account and other assets to the authorised officer on receipt of such requisition, the authority concerned shall be bound to return the seized books of account assets, etc., to the authorised

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officer. He may do so immediately on receipt of such requisition or at a time when the said books and other assets are no longer required by such authority. Such books of accounts, documents, and other assets shall be treated as if they were seized in the course of search made under section 37A(1) and the provisions of sub-section (12) would be applicable to them.

Section 37C deals with the method of application of assets seized and retained in the course of search.

Section 38 deals with the power of the Assessing Officer to obtain information not merely from the assessee but also from other persons. Section 8A as pointed out earlier deals with the powers of Valuation Officer. Section 39 deals with the effect of transfer of authorities on pending proceeding. Section 41 deals with service of notice.

3.10 MISCELLANEOUS PROVISIONS

3.10.1 Transfers to defraud revenue [Section 34B]: The provisions of section 34B are as follows:

- (1) There would be automatic lien for taxes due not only during the course of pendency of proceeding but even after the finalisation thereof up to the stage a notice under rule 2 of the Second Schedule to the Income-tax Act, 1971 as made applicable to the Wealth tax Act is issued.
- (2) The department would no longer be under an obligation to prove that the transfer was effected with the intention to defraud revenue.
- (3) The charge or transfer shall not be void if made for adequate consideration and without any notice of the pendency of proceedings or without notice of tax etc, payable by the assessee or if made with previous permission of the Assessing Officer.
- (4) The lien would be on assets of the nature of land, buildings, machinery plant, share, securities and fixed deposits in banks; not being stock-in-trade of the business and the same would be operative only if the amount of tax payable or is likely to be payable exceed Rs.5,000 and the asset charged or transferred exceed in value Rs.10,000.

3.10.2 Provisional attachment of property [Section 34C]: Section 34C empowers the Assessing Officer to make a provisional attachment on the assets of tax payer whose case is under investigation even before a tax demand is actually raised against him if he is of the opinion that it is necessary to do so for the purpose of protecting the interests of the revenue. However, for this purpose he should take the previous approval of the Chief

Commissioner or the Commissioner. The provisional attachment will be initially for a period of six months, but may be extended by the Chief Commissioner or the Commissioner for reasons to be recorded in writing by a further period or periods not exceeding in all two years.

3.10.3 Rectification of Mistakes [Section 35]: With a view to rectifying any mistake apparent from record:

- (i) The Assessing Officer may amend any order of assessment or refund or any other order passed by him;
- (ii) A Wealth-tax authority may amend any intimation sent by it under section 16(1) or enhance or reduce the amount of refund granted by it under that sub-section;
- (iii) The Valuation Officer may amend any order passed by him under section 16A;
- (iv) The Joint Director or the Joint Commissioner or the Director or the Commissioner or the Deputy Commissioner (Appeals) or Commissioner (Appeals) may amend any order passed under section 18A;
- (v) The Deputy Commissioner (Appeals) or the Commissioner (Appeals) to amend any order passed by him under section 23;
- (vi) The Commissioner may amend any order passed by him under section 25;
- (vii) The Appellate Tribunal may amend any order passed by it under section 18 or 24 [Section 35(1)].

If the amount of tax, penalty or interest determined as a result of the first appeal or revision against the order referred to in the erstwhile section 2(m)(iii) is paid within six months of the date of the order passed in such appeal or revision, the Assessing Officer may, in spite of anything to the contrary in this Act, rectify the assessment as if such rectification were that of a mistake apparent on record. The rectification may be done by allowing a deduction to the extent of the aforesaid tax, penalty or interest paid [Section 35(2)].

The authority concerned may, on its own motion, rectify the mistake in the aforementioned circumstances. But it must do so, when the mistake is brought to its notice by the assessee. If, however, the authority concerned is the Valuation Officer or the Deputy Commissioner (Appeals) or the Commissioner (Appeals) or the Appellate Tribunal it must rectify the mistake brought to its notice by the Assessing Officer as well [Section 35(3)].

The aforesaid amendment may have the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee. In any one of these circumstances, an amendment shall be made only if the authority concerned has given

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notice to the assessee of its intention so to do and has allowed him a reasonable opportunity of being heard [Section 35(4)].

Where the amendment has the effect of enhancing the value of any asset, the Valuation Officer will be required to notify the assessee of his intention to make the amendment and provide him a reasonable opportunity for being heard. Any order of amendment passed by the Valuation Officer will have to be in writing and copies thereof will have to be sent to the assessee and to the Assessing Officer. The Assessing Officer will thereafter be required to make necessary amendment to the assessment order so as to give affect to the changes made in the valuation of the asset. An amendment under this section cannot to be made after the expiry of a period of 4 years from the end of the financial year in which the order in first appeal or revision or as the case may be, the order sought to be rectified was passed and not from the date of the order.

However, where the Valuation Officer has made any amendment in the order passed by him under section 16A, the consequential amendment to the order of assessment made by the Assessing Officer at any time before the expiry of one from the date of Valuation Officer's under section 35 [Section 35(7A)].

The Central Board of Direct Taxes has clarified that a mistake arising as a result of subsequent interpretation of law by the Supreme Court would constitute a mistake apparent from the record; and the rectification action under section 35 of the Wealth-tax Act would be in order [*Circular No. 1036, dated January 24, 1977*].

3.10.4 Deemed service of valid notice in certain circumstances [Section 42]

Section 42 provides that the assessee would be precluded from raising any objection in any proceeding or inquiry that the notice was not served upon him or was not served in time or was served in an improper manner, if he had appeared in any proceedings or co-operated in any inquiry relating to assessment or re-assessment.

In short, if the assessee had appeared in any proceedings or co-operated in any enquiry, it shall be deemed that any notice required to be served on him has been duly served upon him in time in accordance with the provisions of the Act. However, such deeming provision would not apply where the assessee has raised an objection (regarding non-service of notice or non-service of notice in time or improper service of notice) before the completion of such assessment or reassessment.

3.10.5 Publication of information regarding assessee [Section 42A]: The Central Government may if it thinks necessary and expedient in the public interest to do so, cause to be published the names of the assesseees as well as any other particulars relating to

any proceedings or prosecutions in respect of such assessee in any manner it thinks fit. But either until the time for judgement on appeal with the Deputy Commissioner (Appeals) or, as the case may be, the Commissioner (Appeals) or with the first Appellate Court as the case may be, has expired or until the time the appeal if already preferred, has been disposed of, no publication shall be made in relation to any penalty imposed. However, the government can publicise prosecutions for offences under the Act even before the matter has been disposed of by the first Appellate Court where an appeal has been filed:

3.10.6 Return of wealth not to be invalid due to technical defects [Section 42C]:

This section provides that on return of wealth, assessment notice, summons or other proceedings under the Act shall be invalid merely by reason of any mistake, defect or omission, if the return of wealth, etc. is in substance and effect in conformity with or according to the intent and purpose of Act.

3.10.7 Disclosure of information regarding assessee [Section 42B]: Wherein a person makes an application to the Commissioner in the prescribed form any information in respect of any assessment under the Wealth-tax Act, the Commissioner may furnish or cause to be furnished the information asked for in respect of the assessment only. But before doing so, he must be satisfied that it is in the public interest to do so. If this condition is fulfilled, his decision to furnish the information is final and cannot be called into question in any court of law.

3.10.8 Presumption as to assets, books of account, etc. [Section 42D]

This section provides that where any books of account or other documents, articles or things including money are found in the possession or control of any person in the course of a search under section 37A or where any books of account, other documents or assets have been delivered to the requisitioning officer in accordance with the provisions of section 37B, it may, in any proceeding under this Act, be presumed that -

- (1) such books of account or other documents, articles or things including money belong to such person;
- (2) the contents of such books of account and other documents are true; and
- (3) the signature and every other part of such books of account or other documents which purport to be in the handwriting of any particular person or which may reasonably be assumed to have been signed by, or to be in the handwriting of, any particular person, are in that person's handwriting;
- (4) In the case of a document stamped, executed or attested, that it was duly stamped, executed or attested by the person by whom it purports to have been so executed or attested.

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Section 43 provides that no suit shall lie in any Civil Court to set aside or modify any order under the Act. It also provides for the immunity of the Government and its officers not merely in respect of acts authorised by the Act but also for acts done without jurisdiction but in bona fide belief and in good faith that they were authorised.

Section 44 relates to appearance before tax authorities by authorised representatives. Section 44A empowers the Central Government to enter into agreement with any foreign country or specified territory outside India for the avoidance or relief of double taxation or for exchange of information for the prevention of avoidance of wealth-tax or for investigation of cases of such evasion or avoidance or for recovery of tax. Section 44B provides for unilateral relief in the case of countries with which no agreement exists.

All three provisions are exactly on the same lines as those of corresponding provision in the Income-tax Act. Students are advised to read these provisions from the bare Act.

3.10.9 Rounding off net wealth and tax, etc. : Section 44C provides for rounding off net wealth to the nearest multiple of one hundred rupees; similarly, section 44D provides for rounding off of wealth-tax, interest, penalty, fine or any other sum payable and the amount of refund due under the provisions of the Act to the nearest rupee.

3.10.10 Rule making powers : Section 46 deals with the power of the Central Board of Direct Taxes to make rules for carrying out the purposes of this Act.

Note –

National Tax Tribunal (NTT) means the National Tax Tribunal established under section 3 of the National Tax Tribunal Act, 2005. The National Tax Tribunal Act, 2005 has been enacted by the Parliament in pursuance of Article 323B of the Constitution. It came into force with effect from December 28th, 2005. The notified date of establishment of the National Tax Tribunal by the Central Government is 6th January, 2006.

The objective behind the enactment of the National Tax Tribunal Act, 2005 is to modify the present system of appeals under the Income-tax Act by substituting the National Tax Tribunal for the High Court, for facilitating quick adjudication of disputes under direct and indirect tax laws and achieve uniformity in the interpretation of central legislation.

This Act provides that, on establishment of the National Tax Tribunal, High Courts will not have appellate jurisdiction in matters of direct and indirect taxes. This Act vests jurisdiction in NTT to decide direct and indirect tax disputes on appeal from the decision of the respective Appellate Tribunals. Appeal to NTT can be filed both by the assessee and the revenue, from an order passed by the ITAT or CESTAT, on a substantial question of law. Appeal to NTT will lie only if the NTT is satisfied that the case involves a

substantial question of law. The NTT shall formulate the substantial question of law for the purpose of hearing of appeal by it.

A party to an appeal, other than the Government, may either appear in person or authorize one or more chartered accountants or legal practitioners or any person duly authorized by him or it to present the case before the NTT. The Government may authorize one or more legal practitioners or any of its officers to present its case before the NTT. It may be noted that the Act does not permit chartered accountants to present the case of the Government before the NTT.

The Act provides that any person, including any department of the Government, aggrieved by any decision or order of NTT may file an appeal to the Supreme Court within 60 days from the date of communication of the decision or order of the NTT to him. The Supreme Court can allow filing of the appeal beyond 60 days, if the appellant was prevented by sufficient cause from filing the appeal within the said period of 60 days.

However, the Bombay High Court, in P.C.Joshi vs. Union of India (2006) 152 Taxman 285, has passed an ad-interim order restraining the Government from constituting the NTT and transferring the matters pending in the High Court to the NTT. Therefore, the constitution of the NTT will take effect only after the stay is vacated.

Self-examination questions

1. What is the procedure under the Wealth-tax Act, for assessment of persons residing outside India? What are the provisions for recovery of tax from him?
2. The concept of partial partition is alien to the Wealth-tax Act. Discuss.
3. State the circumstances in which the Assessing Officer can refer valuation of an asset to the Valuation Officer.
4. When is a person deemed to have concealed the particulars of his net wealth, within the meaning of section 18 of the Wealth-tax Act?
5. Can the Assessing Officer refer valuation of assets to the Departmental Valuation Officer for the purpose of making an assessment in a case where no return of wealth has been filed by the assessee?

Answer

5. This question was answered by the Punjab & Haryana High Court in *CWT v. Anil Tayal (HUF) (2006) 285 ITR 243*. The High Court observed that the object of section 16A of the Wealth-tax Act, 1957 is to enable the Assessing Officer to refer the issue relating to the value of any asset to a Valuation Officer for the purpose of making

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assessment. The expression “in any other case” in clause (b) of section 16A(1) is wide enough to include a case where no return has been filed by the assessee. If a narrow view is taken that a reference under section 16A(1) can be made only where the return has been filed, then the expression “in any other case” in clause (b) of section 16A(1) and the expression “where no such return has been made” in sub-section (4) of section 16A would become redundant. Therefore, a reference under section 16A(1) could be made even where no return has been filed by the assessee under section 14 or section 15.