DIRECT TAXES CASE STUDY

FOR

CA FINAL May 2014

COMPILED BY

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MUMBAI (INDIA)

Source / Journals Referred:

- **Itatonline.org**, **Income tax Review: Monthly journal of The Chamber of Tax Consultants, BCAJ (Bombay Chartered Accountant Society) Monthly journal, AIFTP: All India federation of Tax Practioner Journal, Taxmann.com, Taxman : The tax law weekly, SOT : Selected Orders of ITAT, ITD : Income Tax tribunal decisions, DTR : Direct Tax Reporter, ITR : Income Tax Reporter, CTR Encyclopedia of Income Tax Law.**

All the case decisions compiled below are selected on the basis of their practical applications in the Income Tax proceedings. These cases are pronounced between the periods Jan 2013 to Dec 2013 specifically applicable for CA FINAL MAY 2014 term.

❖ Section 2(22)(e) : Not Applicable on inter corporate deposits (ICD) [IFB Agro Industries Ltd. vs. JCIT - ITAT Kolkata]

The assessee received an inter-corporate deposit of ₹ 11.20 crore from IFB Automotive Pvt. Ltd, a company in which it held 18% of the shares. Department had taken a view that ICD constituted "loans and advances" and was assessable as "deemed dividend" u/s 2(22)(e). ITAT held that S. 2(22)(e) refers to 'loans' and 'advances' and does not refer to a 'deposit'. The fact that the term 'deposit' does not mean a 'loan' and that the two terms are two different & distinct terms is evident from the Explanation to S. 269T and S. 269SS of the Act where both the terms are used. The distinction between a "loan" and a "deposit" is that in the case of a "loan", the needy person approaches the lender for obtaining the loan. The loan is lent at the terms stated by the lender. In the case of a "deposit", the depositor goes to the depositee for investing his money primarily with the intention of earning interest. Also, s. 2(22)(e) enacts a deeming fiction and cannot be given a wider meaning than what it purports to cover. It has to be interpreted strictly. Accordingly assessee appeal was allowed.

❖ Section 2(47): Amount received by the partner on his retirement is not chargeable to tax as capital gains. [CIT vs. Riyaz A Sheikh [Bombay HC]

The assessee, a partner in a firm, received ₹ 66 lakhs over and above his capital contribution on his retirement from the firm and claimed it as capital receipt. AO held that the retirement had resulted in a relinquishment of his pre-existing rights in the partnership firm and, therefore, the same was in the nature of capital gain on transfer of goodwill and liable to tax under s. 45 read with s. 2(47)(i) & (ii) of the Act. The CIT(A) and Tribunal reversed the AO on the ground that when a partner retires from the firm and receives his share of an amount calculated on the value of the net partnership assets including goodwill of the firm, there is no transfer of interest of the partner in the goodwill, and no part of the amount received is assessable as capital gain u/s 45 of the Act. In departmental appeal in HC, HC dismissed the same and affirmed the view taken by ITAT.

- ### Section 4 : Compensation on Loss of referral work is a capital receipt [Khanna & Annadhanam vs. CIT – Delhi HC]

The assessee, a firm of Chartered Accountants, was one of the associate members of Deloitte Haskins & Sells for 13 years pursuant to which it was entitled to practice in that name. Deloitte desired to merge all the associate members into one firm. As this was not acceptable to the assessee, it withdrew from the membership and received consideration of ₹ 1.15 crores from Deloitte. The said amount was credited to the partners' capital accounts & while filing the return of income, claimed it as a capital receipt. Department had treated this receipt as a revenue receipt. The matter ultimately travelled to HC. Hon'ble HC held that if the receipt represents compensation for the loss of a source of income, it would be capital and it matters little that the assessee continues to be in receipt of income from its other similar operations. When that source was unexpectedly terminated, it amounted to the impairment of the profit-making structure or apparatus of the assessee. It is for that loss of the source of income that the compensation was calculated and paid to the assessee. The compensation was thus a substitute for the source and hence is a capital receipt.

- ### Section 9/ 40(a)(i) : Advertisement charges paid to Google & Yahoo is not taxable in India [ITO vs. Right Florist (p) Ltd. – ITAT Kolkata]

The assessee, a florist, paid a sum of ₹ 30.44 lakhs to Google Ireland Ltd and Yahoo USA for online advertising. The AO held that the assessee ought to have deducted TDS and that as there was a failure, the expenditure was not allowable u/s 40(a)(i). This was deleted by the CIT(A) on the ground that Google and Yahoo did not have a PE in India. On appeal by the department to the Tribunal, ITAT dismissed the departmental appeal by stating that :

A website does not constitute a 'permanent establishment' unless the servers on which websites are hosted are also located in the same jurisdiction. As the servers of Google and Yahoo are not located in India, there is no PE in India. Section 9(1)(i) does not apply as there is no "business connection" in India nor are the online advertising revenues generated in India serviced by any entity based in India. As regards s. 9(1)(vi), it is held that the advertising revenues are not assessable as "royalty". As regards s. 9(1)(vii), the services are not "managerial" or "consultancy" in nature as both these words involve a human element. On facts, the service rendered by Google & Yahoo is generation of certain text on the search engine result page. This is a wholly automated process. In the services rendered by the search engines, which provide these advertising opportunities, there is no human touch at all. The results are completely automated. Consequently, the whole process of actual advertising service provided by Google & Yahoo, even if it be a technical service, is not covered by the limited scope of s. 9(1)(vii). Consequently, the receipts in respect of online advertising on Google and Yahoo cannot be brought to tax in India under the provisions of the Act or the India US and India Ireland tax treaty.

❖ Section 14A: Applicable on tax free securities held as Stock in trade [D. H. Securities (p) Ltd. - ITAT Mumbai]

The assessee was engaged in the business of trading in shares and its main object is to earn profit on purchase and sale of shares. During the year the assessee had earned dividend income from such shares which was claimed as exempt. The assessee had not offered any disallowance u/s 14A as of the view that accrual of tax-free dividend on such shares was merely incidental to the holding of shares as stock-in-trade and that no disallowance could be made u/s 14A and Rule 8D. Assessee also stated that it had not incurred any direct or indirect expenditure to earn the said dividend. The AO had made the disallowance on a presumptive basis. The matter ultimately referred to the third member of ITAT as there was difference of opinion between the benches. The third member bench had ultimately decided that section 14A read with Rule 8D applies to shares held as stock-in-trade. Accordingly, disallowance u/s 14A can be made in conformity with law even where dividend income has been earned on shares held as stock-in-trade.

❖ Section 14A : Interest expenditure to be netted against the interest income for calculating disallowance. [ITO vs. Karnavati Petrochem (p) Ltd. - ITAT Ahmadabad]

In AY 2008-09, the assessee invested ₹ 95 lakhs in shares on which it earned ₹ 300 as dividend. The AO applied Rule 8D and made a disallowance of ₹ 15 lakhs. The assessee claimed that no expenditure had been incurred to earn the dividend income on the basis that while the interest expense was ₹ 1.83 crore, the interest income was ₹ 1.86 crore and there was a net surplus interest income of ₹ 3.79 lakh. The CIT(A) held that the AO had not established a nexus between the expenditure incurred and the tax free income and that as the assessee had net positive interest income, there could be no disallowance of the interest expenditure u/s 14A read with Rule 8D. He sustained the disallowance at 0.5% of the average investment. In departmental appeal, ITAT dismissed the same by stating that no nexus has been established by the AO between the expenditure incurred by the assessee and the tax free income earned by him. Further, as the interest income was more than interest expense and the assessee was having net positive interest income, the interest expenditure cannot be considered for disallowance u/s 14A and Rule 8D.

❖ Section 28 : Confiscation of goods by Customs Authorities [CIT vs. T.C. Reddy -AP HC]

The assessee, the proprietor of a pharmaceutical company, exported bulk drugs to Mexico through San Diego Port, California, USA. The goods were cleared by the Indian customs authorities and reached California, USA. During the transit from California to Mexico, the goods were seized by the Customs and Border Protection Force of the USA for some statutory violations. The assessee claimed business loss before the Assessing Officer as a bad debt and alternatively loss of stock-in-trade, which was denied. The matter travelled to HC. HC held that the amount was deductible as business loss.

❖ Section 32 : Depreciation on Website Expenditure [Make My trip (India) (p) Ltd vs. DCIT - Delhi ITAT]

The assessee was engaged in the business of tour and travel and for the purpose of its business, had developed a website on which information about its business was available. The assessee claimed depreciation on website development expenses under the block of intangible assets. During the assessment proceedings it was submitted by the assessee that website was an intangible asset similar in nature to know-how, patents, copyrights, trade mark, licence and franchise. The website was owned by the assessee and was used for the purpose of business or profession. Therefore, depreciation at the rate of software was applicable. AO had disallowed the depreciation claim of the assessee by treating it as capital in nature. CIT (A) held that depreciation @ 25% is permissible, which was also affirmed by ITAT.

❖ Section 36(1)(va) / 43B: Due date for the purpose of payment of EPF / ESIC [CIT vs. Kichha Sugar Company Ltd. Uttarakhand HC]

The assessee collected employees' Provident Fund contribution for payment to the provident fund authorities. However, the amount was not paid to the provident fund authorities within the "due date" specified in the Provident Fund Act though it was paid before the due date of filing the return of income. The AO assessed the amounts received as income u/s 2(24)(x) but refused to allow a deduction u/s 36(1)(va) on the ground that the amounts were not paid within the prescribed "due date". The matter travelled to HC. HC held that section 2(24)(x) provides that the amounts of employees' contribution to PF etc collected by the employer shall be assessed as his income. S. 36(1)(va) provides that the said employees' contribution shall be allowed as a deduction if paid within the "due date" specified in the relevant legislation. Section 43(B)(b) provides that any sum payable by the assessee as an employer by way of contribution to any provident fund etc shall be allowed if paid before the due date of filing the ROI. The "due date" referred to in s. 36(1)(va) must be read in conjunction with s. 43B(b) to mean the "due date" of filing the ROI.

❖ Section 36(1)(v) : Payment to LIC Group gratuity scheme is allowable expenditure. [CIT vs. Textool Co. Ltd. – SC]

The assessee set up a gratuity fund which was duly approved by the CIT. However, instead of making payment to the fund directly, the assessee paid an amount of ₹ 50 lakhs as initial contribution and an amount of ₹ 5 lakhs as annual premium to the LIC pursuant to the group Life Assurance Scheme framed by the LIC for the benefit of the employees of the assessee. The AO disallowed the claim for deduction on the ground that payment towards the gratuity fund was not made to an approved gratuity fund and was not allowable u/s 36(1)(v). The CIT(A), Tribunal and High Court upheld the assessee's claim on the basis that the payment to LIC under the Group Life Assurance Scheme was for the exclusive benefit of the employees of the assessee under the policy issued by it and that the conditions stipulated in s. 36(1)(v) had not been violated. On further appeal by the department, Hon'ble Supreme Court dismissed the appeal and held that from a bare reading of s. 36(1)(v), it is manifest that the real intention behind the provision is that the employer should not have any control over the funds of the irrevocable trust created exclusively for the benefit of the employees. On facts, it is evident that the assessee had absolutely no control over the fund created by the LIC for the benefit of the employees of the assessee and further all the contribution made by the assessee in the said fund ultimately came back to the Employees Gratuity Fund, approved by the CIT.

❖ Section 37 : Expenditure on acquiring master copy of software is deductible as revenue expenditure. [Oracle India (p) Ltd. vs. CIT [Delhi HC]

The assessee entered into a license agreement with Oracle Corp under which it acquired a non-exclusive & non-assignable right to duplicate software products which were owned by Oracle Corp and to sub-license the same to parties in India. The assessee paid recurring royalty of 30% for the said right. In addition to the royalty, the assessee periodically paid an amount towards "expenditure on import of software master copy". The said master copy was used to replicate the software. The assessee claimed that the said master copies were versions of Oracle's new product offerings which had very accelerated obsolescence and that at any point of time it was not possible to say whether the version will be current for one day or one month. The AO allowed a deduction for the recurring royalty but held that the expenditure for acquiring the software master copy was capital expenditure. Matter ultimately travelled to HC.

HC held that this was not a case where the master copies contained operating or system software, which normally did not require frequent up-gradation or changes. It is also not the case of an assessee which is the end user of software. It is a case where the assessee is required to repeatedly pay for the master copy media in view of frequent newer or updated versions of the application software from time to time. Once newer or better version of the application software is available, the earlier version is not saleable and does not have any market value for the seller i.e. the assessee. Also, as per the "matching concept" in accountancy, while determining whether expenditure is capital or revenue in nature, the question whether the expenditure would create an asset which is of value in further assessment periods and should be amortized (i.e. depreciated) as long as it has value (subject to the statutory provisions) requires to be considered. If the expenditure does lead to creation of an asset but of a limited or short life, it has to be treated as a liability and not as a fixed asset. The said expenditure cannot be valued for price for future financial years. Accordingly HC decided the issue in favour of the assessee.

❖ Section 37(1) : Illegal payments [CIT vs. Rajarani Exports – Calcutta HC]

The assessee exported tea to Iraq under the 'Oil for Food Program', as sanctioned by the United Nations. It paid commission of ₹ 1.28 crores to one Jordanian company. The Volcker Committee, which was set up to expose the 'Oil for Food scam' found that this company was a front company for the Iraqi regime, meant to receive illegal kickbacks, and did not render any services. The Department acting on the report, held that the commission paid by the assessee was "*illegal*" and not allowable under the Explanation to s. 37(1). The matter travelled to HC. Hon'ble HC had dismissed the departmental appeal by stating that the "purpose" of the expenditure has to be seen and if the payment is for bonafide business purposes, the fact that they end up being used as illegal kickbacks, will not attract Explanation to s. 37(1).

❖ Section 37(1) : No disallowance for penalty / violation of procedural law [CIT vs. The stock and bond trading company – Bombay HC]

The assessee paid penalty/fine to BSE/NSE for infringement of procedural rules such as failure to maintain margins, trading beyond exposure limits, late submission of margin certificates, delay in making payment & deliveries etc. The AO disallowed the claim for deduction on the ground that there was an infringement of statutory law laid down by SEBI and the Explanation to s. 37(1) was attracted. High Court held as the payments made by the assessee to the Stock Exchange for violation of their regulation was not on account of an offence which is prohibited by law and accordingly the invocation of the Explanation to s. 37 of the Act was not justified.

❖ Section 37(1) : Payment for club membership fees [KPMG India (p) Ltd vs. ACIT – Mumbai ITAT]

Assessee paid a sum of Rs. 13,750 to Oberoi Grand, Kolkata for the membership of its employee and claimed it as business expenditure. As per AO the said expenditure was the personal expenditure of the employee & it was not allowable as deduction. CIT (A) confirmed the addition. On appeal in Tribunal, the Tribunal allowed the deduction by stating that Club Membership fees for employees incurred by the assessee is a business expenditure and liable to deduction u/s 37 of the Act.

❖ Section 40(b): Ceiling on number of partners [M/s Deloitte Haskins & Sells vs. DCIT - ITAT Chennai]

The assessee, a firm of Chartered Accountants, filed a return offering income of ` 17.70 crores which was accepted by the AO u/s 143(3). The CIT then passed an order u/s 263 stating that the assessee had amended its partnership deed pursuant to which Mr. Mukund Dharmadhikari, who was already a partner of the firm, was added once again as a partner in a representative capacity, to represent Deloitte Haskins & Sells, Mumbai. As Mr. Dharmadhikari had the right to share profit, both in the representative capacity as well as in his individual capacity, the CIT held that the number of partners exceeded 20, the maximum allowed under the Partnership Act, 1932, and that the assessee had, therefore, to be treated as an Association of Persons. He held that the assessee was not entitled to claim a deduction u/s 40(b) for the salaries paid to its' partners.

In assessee's appeal, ITAT justified the action of the CIT u/s 263. A study of the partnership deed shows that Deloitte Haskins & Sells, Mumbai, which is the participating firm, is not a stranger to the assessee. The assessee can take policy decisions, which have a policy bearing on such firm, once there is an approval of the majority of the members of the "National Firm". Mukund Dharmadhikari was representing Deloitte Haskins & Sells, Mumbai, and the endeavour of the assessee was to bring on board the participating firm, on which it had powers to make policy decision, so that they became entitled for a share of profit. In other words, the effort of the assessee was to bring indirectly into the partnership M/s Deloitte Haskins & Sells, Mumbai, which was already a participating firm. The assessee was a renowned partnership firm and was well aware that number of partners cannot exceed 20. It is a well settled principle of law that what is permissible is tax planning, but not evasion. The AO did not apply his mind and go into these aspects and so the CIT was justified in directing him to look into the issue.

❖ Section 48: Taxability of ESOPs for Foreign Expatriate [ACIT vs. Robert Arthur Keltz - ITAT Delhi]

The assessee, an employee of M/s UTIO, USA, was granted "employee stock options" of 34000 shares on 9.01.2004 when he was outside India. The assessee was deputed to the India liaison office on 01.04.2006 and the stock options vested on 09.01.2007 when he was in India. The assessee exercised the stock options on 01.02.2007, when he was still in India. The AO held that as the assessee was in India on the date of vesting and exercise of the stock options, the entire benefit thereof was assessable as a perquisite in his hands. However, the CIT(A) held that as the employee had been in India for only for a part of the time of the vesting period, only a proportionate stock option benefit, which is attributable to the period spent in India accrued to the employee and was chargeable to tax in India.

In departmental appeal, ITAT held, if a part of the activity done by the assessee-employee has no relation to any India specific job or activity it is not chargeable to tax in India. On facts, the assessee was in India only for a short period i.e. 1.4.2006 onwards. Prior to that, he has not done any service connected with any activity in India. Accordingly, as the assessee has not rendered service in India for the whole grant period, only such proportion of the ESOP perquisite as is relatable to the service rendered by the assessee in India is taxable in India.

❖ Section 54 : Exchange of old flat with new one [Jatinder Kumar Mohan vs. ITO - Mum ITAT]

Assessee had exchanged old flat with new flat to be constructed by builder under development agreement. It claimed exemption u/s 54 in respect of capital gain on account of transfer of old flat. AO disallowed assessee's claim holding that assessee had neither purchased nor constructed house property within period prescribed u/s 54. The question rose before ITAT was (i) whether acquisition of new flat under a development agreement in exchange of old flat amounts to construction of new flat for purpose of claiming deduction u/s 54 (ii) Whether, therefore, assessee would be entitled to exemption if new flat had been constructed within a period of 3 years from date of transfer. ITAT had decided both issues in favour of the assessee.

❖ Section 54 / 54F : Exemption [CIT vs. Syed Ali – Andhra Pradesh HC]

The assessee offered long term capital gains on sale of property and claimed s. 54 deductions on the ground that he had purchase two adjacent residential flats. The AO held that the deduction could not be given for both flats on the ground that they were independent units, separated by a strong wall. The CIT(A) and Tribunal allowed the claim on the basis that s. 54 deduction was available for purchase of multiple flats, even if the flats were on different floors. On subsequent appeal HC had dismissed the departmental appeal by stating that the expression “a residential house” in s. 54 (1) has to be understood in the sense that the building should be of residential nature and “*a*” should not be understood to indicate a singular number. Where an assessee had purchased two residential flats, he is entitled to exemption u/s 54 in respect of capital gains on sale of its property on purchase of both the flats, despite the fact that the flats were purchased by separate sale deeds. Deduction is allowable even if the flats are on different floors.

❖ Section 143(3) : Assessment order without the signature of AO is void [M/s Vijay Corporation vs. ITO : ITAT Mumbai)

AO passed an assessment order u/s 143(3) and issued the Income-tax Computation Form (ITNS 150), Demand Notice u/s 156 and Penalty Notice u/s 271(1)(c). While all the other documents were signed by the AO, the assessment order was not signed. In reply to the assessee's contention that the assessment order was invalid, ITAT held that if the assessment order is not signed, then the fact that he has signed the tax computation form and the notice of demand is irrelevant. The omission to sign the assessment order cannot be explained by relying on s. 292B.

- Section 147: Fresh claim in reassessment proceedings. [Satyamanglam Co-operative society vs. ITO-Madras HC]

Assessee had raised fresh claim in the reassessment proceedings. Department had raised objection on the same. Matter ultimately travelled to HC. Hon'ble HC held that since the reassessment proceedings is for the benefit of the revenue and hence no fresh can be entertained in the reopening proceedings.

- Section 147 : Reopening on the basis of retrospective amendment is invalid [Ganesh Housing Corporation Ltd. vs. DCIT – Gujarat HC]

For AY 2006-07, the assessee claimed s. 80-IB (10) deduction of ₹ 11.38 crores which was accepted by the AO while passing order u/s 143(3). Subsequently, within 4 years from the end of the AY, the AO reopened the assessment u/s 148 on the ground that the assessee had not complied with s. 80-IB(10) including that after the insertion of the Explanation to s. 80-IB(10) by the FA (No. 2) Act 2009 w.r.e.f. 1.4.2000, a contractor was not eligible for deduction u/s 80-IB(10). The assessee challenged the s.148 notice by a Writ Petition. High Court by allowing the WP held that as regards the retrospective amendment, if an Explanation is added to a section for the removal of doubts, the implication is that the law was the same from the very beginning and the same is further explained by way of addition of the Explanation. <u>It is not a case of introduction of a new provision of law by retrospective operation</u>. As regards the formation of opinion, the assessee had disclosed all the material relevant for claiming s. 80-IB(10) deduction and there was no suppression of material.

- S. 147: Reopening in the absence of "fresh tangible material" is invalid [CIT vs. Amitabh Bachchan (Bombay HC)]

Assessee, a famous Bollywood Actor, filed ROI declaring income of ₹ 14.99 crores. A revised ROI was then filed claiming 30% ad-hoc expenses (₹ 6.31 crores) and offering income of ₹ 8.11 crores. When the AO asked the assessee to substantiate the expenses, he withdrew the claim. The AO passed order u/s 143(3). The AO then issued a s. 148 notice (within 4 years) to reopen the assessment on the ground that the claim for expenses (which was withdrawn) had to be assessed as "unexplained expenditure" u/s 69. The CIT (A) & Tribunal struck down the reassessment order on the ground that the material on the basis of which the assessment was sought to be reopened was always available at the time of the original proceeding and there was no new material.

Subsequently High Court had dismissed the departmental appeal by stating that the reopening on the basis that the said ad-hoc expenditure constituted "unexplained expenditure" u/s 69 was based on the same material. There was no fresh tangible material before the AO to reach a reasonable belief that the income liable to tax has escaped assessment. It is a settled position of law that review under the garb of reassessment is not permissible.

❖ Section 148 : Reopening based solely on departmental audit objection is void [Vijay Rameshbhai Gupta vs. ACIT – Gujarat HC]

The AO passed order u/s 143(3) in which he allowed the assessee's claim for business expenses. The Revenue Audit raised an objection that as the assessee's business had ceased, the income had to assessed as "other sources" and the expenditure disallowed. The AO replied to the Audit stating that the objection was not correct and that the assessment order was correct. The Revenue Audit thereafter wrote to the CIT that the AO's stand was not correct. Based on this, the AO issued notice u/s 148 (within 4 years from the end of the AY) to reopen the assessment and disallow the expenditure. The assessee challenged the reopening on the basis that the AO was compelled by the audit party to re-open the assessment though he was of the belief that no income had escaped assessment. Hon'ble HC had upheld the writ of the assessee by stating that if the AO acts under compulsion of the audit party and not independently, the action of re-opening would be vitiated. Consequently, the s. 148 notice had to be quashed.

❖ Section 194H : Commission for providing credit card facility [DCIT vs. Tata Teleservices Ltd. – ITAT Bangalore]

Assessee is a company engaged in the business of direct retail trading in consumer goods. Assessee claimed deduction of Rs. 16,34,000/- on account of commission paid to the credit card companies, which has been disallowed by the assessing officer in terms of S.40(a)(ia) on account of the failure of the assessee to deduct tax at source in terms of S.194H of the Act, while making the said commission payments. It was the contention of the assessee before the lower authorities that the assessee only receives the payment form the bank/credit card companies concerned, after deduction of commission thereon, and thus, this is only in the nature of a post facto accounting and does not involve any payment or crediting of the account of the banks or any other account before such payment by the assessee. The Tribunal held that the service fee charged by banks are bank charges and not commission, therefore the provisions of section 194H are not attracted.

❖ Section 195 : DTAA rate along with surcharge and education cess [ITO vs. M Far Hotels Ltd. – ITAT Cochin]

The assessee made a remittance of management fee and interest to a resident of France. The AO held that in deducting TDS thereon u/s 195, the assessee ought to have deducted surcharge and education cess. The assessee claimed that as the India-France DTAA was silent about inclusion of surcharge & education cess, it was under no obligation to do so. Matter travelled to ITAT. Hon'ble ITAT held India-France DTAA does not say anything about inclusion of surcharge and education cess for the purpose of deduction of tax at source. Therefore, there is an apparent conflict between the Income-tax Act and the DTAA between the two sovereign countries with regard to deduction of tax at source on surcharge and education cess. U/s 90(2) if the provisions of the DTAA are more beneficial to the taxpayer, the DTAA prevails over the Act. Since the DTAA is silent about the surcharge and education cess for the purpose of deduction of tax at source, the taxpayer may take advantage of that provision in the DTAA for deduction of tax.

❖ Section 253 : Delay in filing the appeal due to fault of CA [Y P Trivedi vs. JCIT – ITAT Mumbai]

The assessee filed an appeal before the Tribunal which was delayed by 496 days. In the application for condonation of delay, the assessee claimed that he had handed over the papers to his Chartered Accountant and that the latter had mixed up the papers with other papers in his office which led to the delay. The department opposed the application on the ground that there was "gross negligence" on the part of the assessee and that sufficient cause for the delay was not explained. Hon'ble ITAT held that the facts do not suggest that the assessee has acted in a mala fide manner or that the reasons explained are only a device to cover an ulterior purpose. On facts, the reasons explained by the assessee show that due to bonafide mistake and inadvertence, the appeal could not be filed within the period of limitation. Accordingly, the delay of 496 days has to be condoned.

❖ Section 271(1)(c) : Voluntary disclosure does not absolve assessee from penalty. [MAK data (p) Ltd. vs. CIT – SC]

The assessee filed a return of income for AY 2004-05 declaring an income of ₹ 16 lakhs. During the course of the assessment proceedings, the AO noticed certain documents comprising of share application forms, bank statements, blank share transfer deeds etc had been impounded in the course of s. 133A survey proceedings conducted in the case of the assessee's. The AO sought specific information regarding the documents from the assessee. In reply to the show-cause notice, the assessee made an offer to surrender ₹ 40.74 lakhs with a view to avoid litigation and buy peace and to make an amicable settlement of the dispute. The AO assessed the said sum of ₹ 40.74 lakhs to tax and levied penalty u/s 271(1)(c) for concealment of income and not furnishing true particulars. The matter ultimately travelled to SC.

Hon'ble SC held that the AO shall not be carried away by the plea of the assessee like "voluntary disclosure", "buy peace", "avoid litigation", "amicable settlement", etc. to explain away its conduct. The question is whether the assessee has offered any explanation for concealment of particulars of income or furnishing inaccurate particulars of income. Explanation to s. 271(1) raises a presumption of concealment, when a difference is noticed by the AO, between reported and assessed income. The burden is then on the assessee to show otherwise, by cogent and reliable evidence. When the initial onus placed by the explanation, has been discharged by him, the onus shifts on the Revenue to show that the amount in question constituted the income and not otherwise. It is the statutory duty of the assessee to record all its transactions in the books of account, to explain the source of payments made by it and to declare its true income in the return of income filed by it from year to year. The AO has recorded a categorical finding that he was satisfied that the assessee had concealed true particulars of income and is liable for penalty. Accordingly Penalty confirmed by SC.

- Section u/s 271(1)(c): Penalty cannot be imposed for a "bona fide human error" [PWC vs. CIT (SC)] **Imp.**

The assessee filed a ROI together with the Tax Audit Report. In the Tax Audit Report, it was *disclosed* that an amount of ₹ 23 lakhs towards provision for gratuity was *not allowable* u/s 40A(7). However, in the computation of income, the said amount was not disallowed. The AO also overlooked the item and omitted to make a disallowance. Subsequently, he reopened the assessment u/s 147, disallowed the expenditure and levied penalty u/s 271(1)(c). The assessee explained that the omission to make a disallowance had occurred because it had a separate accounts department and there was "*some confusion*" and that the return was prepared by a *non-CA* and was signed a director who proceeded on the basis that the return was correctly drawn up. The CIT (A), Tribunal and High Court affirmed the levy of penalty on the ground that since the assessee was a well known and reputed Chartered Accountant firm and a tax consultant**,** it was not expected to make such a mistake and that there had been a failure to discharge the strict liability to furnish true and correct particulars of income.

On appeal, Supreme Court deleted the penalty by observing that though the assessee is undoubtedly a reputed firm and has great expertise available with it, it is possible that even the assessee could make a "silly" mistake**.** All that happened in the present case is that through a bona fide and inadvertent error failed to add the provision for gratuity to its total income. This can only be described as a human error which we are all prone to make. The calibre and expertise of the assessee has little or nothing to do with the inadvertent error. Consequently, given the peculiar facts of this case, the imposition of penalty on the assessee is not justified.

❖ Section 271(1)(c) : CA's opinion will not make the claim genuine [Chadha Sugars (p) Ltd vs. ACIT – ITAT Delhi)

Assessee obtained the opinion of a Chartered Accountant on whether expenditure on fees to the Registrar of Companies for increasing authorized capital can be claimed as revenue expenditure. The CA relied on judicial precedents and opined that the issue was debatable and a claim could be made on the basis that if two views were possible, the view in favour of the assessee should be taken. The assessee claimed deduction and even the tax auditor did not qualify the same. The claim of the assessee was rejected by AO and levied penalty u/s 271(1)(c), which was confirmed by CIT (A). ITAT had confirmed the penalty u/s 271(1)(c) by stating that opinion of CA's does not make claim bonafide one.

❖ Section 271(1)(c): No immunity from penalty even if amount disclosed as per CA certificate [CIT vs. HCIL Kalindee ARSSPL [Delhi HC]

The assessee claimed deduction u/s 80IA on the ground that it has executed an eligible infrastructure project. A copy of Form No.3CB, 3CD and Form No.10CCB was filed with the return in support of the claim. In the assessment order, the AO denied 80-IA deduction on the ground that the assessee had not executed the work but had given a sub-contract to another party and that it was not eligible u/s 80-IA(13). The assessee accepted the denial of the claim. The AO levied penalty u/s 271(1)(c) for filing inaccurate particulars of income which was upheld by the CIT(A). The Tribunal deleted the penalty on the ground that the claim for deduction u/s 801A was on the basis of a certificate of the CA, was bona fide and all the material facts relevant thereto had been furnished.

On departmental appeal in HC, HC had confirmed the penalty. The fact that the claim for deduction u/s 80IA was duly supported by the Chartered Accountant's Certificate and prescribed forms signed by the CA cannot absolve and protect an assessee who furnishes in-accurate particulars because then in all cases where a form/certificate is furnished by the CA but a wrong claim of deduction is made, no penalty u/s 271(1)(c) can be imposed. Merely because the assessee complies with the statutory procedural requirement of filing the prescribed form and certificate of the CA cannot absolve the assessee of its liability if the act or attempt in claiming the deduction was not bona fide.

❖ Section 271(1)(c) : Mistake of CA does not attract penalty [CIT vs. Somany Evergreen – Bombay HC]

The assessee filed a return of income in which it committed two mistakes (i) Depreciation was claimed at ₹ 1.70 crores instead of at ₹ 1.05 crores due to a mistake in calculation, (ii) the assessee sold its garment manufacturing machine and suffered a loss of ₹ 21.68 lakhs thereon. Though the loss was on capital account, it was claimed as a revenue deduction. In the course of the assessment proceedings, the assessee realized its mistake and withdrew the claim for excess depreciation and the claim for the loss. The AO levied penalty u/s 271(1)(c) on both issues which was confirmed by the CIT(A). However, the Tribunal held that both mistakes had occurred due to a mistake/ wrong advice given by the Chartered Accountant and that there was a bona fide mistake. It was also held by ITAT that the bonafide of the assessee is established from the fact that the assessee accepted the mistake and did not prefer any appeal against the order of the AO. Departmental Appeal in HC was dismissed as the bonafide mistake on the part of the assessee was not disputed by the department.

- Section 271(1)(c): No penalty for non-debatable claim if there is disclosure in the return. [CIT vs. Nalin P Shah [Bombay HC]

Though the income from the transfer of units of a mutual fund is exempt u/s 10(33), the assessee claimed a deduction for the loss of ₹ 3.08 crores suffered by him on transfer of US 64 units. The AO disallowed the loss on the ground that the exemption in s. 10(33) applied to a loss as well and imposed penalty u/s 271(1)(c). Matter was finally settled in HC. Hon'ble HC had upheld the penalty as the assessee had disclosed all details in the return of income, at the highest it can be said that the claim of the assessee was not sustainable in law. But as there was no furnishing of inaccurate particulars or concealment of income on the part of the assessee. Penalty u/s 271(1)(c) could not be levied.

Note: For Full texts of the decisions / citations as well as any queries, Feel free to contact us at "bikashbogi@yahoo.co.in" / or www.sbrca.in / or https://www.facebook.com/sbrca

BEST OF LUCK

Success is not the matter of being the BEST & WINNING the race: Success is a matter of HANDLING the WORST & FINISHING the Race.
