

DIRECT TAXES / DIRECT TAX LAWS

AMENDMENTS BY THE FINANCE ACT, 2008

I INCOME-TAX ACT, 1961

1. RATES OF TAX

Section 2 of the Finance Act, 2008 read with Part I of the First Schedule to the Finance Act, 2008, seeks to specify the rates at which income-tax is to be levied on income chargeable to tax for the assessment year 2008-09. Part II lays down the rate at which tax is to be deducted at source during the financial year 2008-09 i.e. A.Y. 2009-10 from income subject to such deduction under the Income-tax Act; Part III lays down the rates for charging income-tax in certain cases, rates for deducting income-tax from income chargeable under the head "salaries" and the rates for computing advance tax for the financial year 2008-09 i.e. A.Y.2009-10. Part III of the First Schedule to the Finance Act, 2008 will become Part I of the First Schedule to the Finance Act, 2009 and so on.

Rates for deduction of tax at source for the A.Y.2009-10

Part II of the First Schedule to the Act specifies the rates at which income-tax is to be deducted at source during the financial year 2008-09 i.e. A.Y. 2009-10 from income other than "salaries". These rates of tax deduction at source are the same as were applicable for the A.Y.2008-09, except in the following cases -

- (i) Tax would be deductible@10% on income by way of interest payable on any security of the Central or State Government to a person, other than a company, resident in India.
- (ii) Tax would be deductible@15% instead of 10% on short-term capital gains referred to in section 111A in the case of non-residents and companies other than domestic companies.

Rates for deduction of tax at source from "salaries", computation of "advance tax" and charging of income-tax in certain cases during the financial year 2008-09

Part III of the First Schedule to the Act specifies the rate at which income-tax is to be deducted at source from "salaries" and also the rate at which "advance tax" is to be computed and income-tax is to be calculated or charged in certain cases for the financial year 2008-09 i.e. A.Y. 2009-10. The basic exemption limit has been increased and tax slabs have been rationalized in the case of individuals, HUFs, AOPs, BOIs and artificial juridical persons. The revised tax slabs are shown hereunder -

- (i) (a) Individual/ HUF/ AOP / BOI and every artificial juridical person

Level of total income	Rate of income-tax
Where the total income does not exceed Rs.1,50,000	Nil
Where the total income exceeds Rs.1,50,000 but does not exceed Rs.3,00,000	10% of the amount by which the total income exceeds Rs.1,50,000
Where the total income exceeds Rs.3,00,000 but does not exceed Rs.5,00,000	Rs.15,000 plus 20% of the amount by which the total income exceeds Rs.3,00,000
Where the total income exceeds Rs.5,00,000	Rs.55,000 plus 30% of the amount by which the total income exceeds Rs.5,00,000

The threshold exemption level has been raised from Rs.1,45,000 to Rs.1,80,000 for resident women and from Rs.1,95,000 to Rs.2,25,000 for resident individuals of the age of 65 years or more at any time during the previous year. The slab rates for these assesseees are as given in (b) and (c) below.

- (b) For resident women below the age of 65 years at any time during the previous year

Level of total income	Rate of income-tax
Where the total income does not exceed Rs.1,80,000	Nil
Where the total income exceeds Rs.1,80,000 but does not exceed Rs.3,00,000	10% of the amount by which the total income exceeds Rs.1,80,000
Where the total income exceeds Rs.3,00,000 but does not exceed Rs.5,00,000	Rs.12,000 plus 20% of the amount by which the total income exceeds Rs.3,00,000
Where the total income exceeds Rs.5,00,000	Rs.52,000 plus 30% of the amount by which the total income exceeds Rs.5,00,000

- (c) For resident individuals of the age of 65 years or more at any time during the previous year

Level of total income	Rate of income-tax
Where the total income does not exceed Rs.2,25,000	Nil

Where the total income exceeds Rs.2,25,000 but does not exceed Rs.3,00,000	10% of the amount by which the total income exceeds Rs.2,25,000
Where the total income exceeds Rs.3,00,000 but does not exceed Rs.5,00,000	Rs.7,500 plus 20% of the amount by which the total income exceeds Rs.3,00,000
Where the total income exceeds Rs.5,00,000	Rs.47,500 plus 30% of the amount by which the total income exceeds Rs.5,00,000

(ii) Co-operative society

There is no change in the rate structure as compared to A.Y.2008-09.

	Level of total income	Rate of income-tax
(1)	Where the total income does not exceed Rs.10,000	10% of the total income
(2)	Where the total income exceeds Rs.10,000 but does not exceed Rs.20,000	Rs.1,000 plus 20% of the amount by which the total income exceeds Rs.10,000
(3)	Where the total income exceeds Rs.20,000	Rs.3,000 plus 30% of the amount by which the total income exceeds Rs.20,000

(iii) Firm

The rate of tax for A.Y.2009-10 is the same as that for A.Y.2008-09 i.e. 30% on the whole of the total income of the firm.

(iv) Local authority

The rate of tax for A.Y.2009-10 is the same as that for A.Y.2008-09 i.e. 30% on the whole of the total income of the local authority.

(v) Company

The rates of tax for A.Y.2009-10 are the same as that for A.Y.2008-09.

(1)	In the case of a domestic company	30% of the total income
(2)	In the case of a company other than a domestic company	50% of specified royalties and fees for rendering technical services and 40% on the balance of the total income

Surcharge

The rates of surcharge applicable for A.Y.2009-10 are as follows -

(i) Individual/HUF/AOP/BOI

Where total income exceeds Rs.10,00,000, surcharge is payable at the rate of 10% on the income-tax computed in accordance with the provisions of Paragraph (i) [(a), (b) or (c)] above or section 111A or 112.

Marginal relief: In case of such individuals/HUFs/AOPs/BOIs having a total income exceeding Rs.10,00,000, the additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.10,00,000 should not be more than the amount of income exceeding Rs.10,00,000. This is called 'marginal relief'.

Income-tax on total income of Rs.10 lakh works out to Rs.2,05,000. Surcharge is not attracted on this tax since the total income does not exceed Rs.10 lakh. However, if the total income is, say, Rs.10,30,000, tax on the same would be Rs.2,35,400 (i.e. Rs.2,14,000 + 21,400, being surcharge of 10%). The additional tax works out to Rs.30,400 (i.e., 2,35,400-2,05,000). However, the additional tax cannot exceed the amount by which Rs.10,30,000 exceeds Rs.10,00,000. That is, the additional tax cannot exceed Rs.30,000. Therefore, the total tax payable would be only Rs.2,35,000 (i.e. 2,05,000 + 30,000). The marginal relief is Rs.400 (i.e. 30,400-30,000).

(ii) Artificial juridical person

Surcharge is payable at the rate of 10% of income-tax computed in accordance with the provisions of paragraph (i)(a) above or section 111A or section 112.

(iii) Firm/Domestic company

Where the total income exceeds Rs.1 crore, surcharge is payable at the rate of 10% of income-tax computed in accordance with the provisions of para (iii)/(v)(1) above or section 111A or section 112. Marginal relief is available in case of such firms/companies having a total income exceeding Rs.1 crore i.e. the additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.1 crore should not be more than the amount of income exceeding Rs.1 crore.

(iv) Foreign company

Where the total income exceeds Rs.1 crore, surcharge is payable at the rate of 2½% of income-tax computed in accordance with the provisions of paragraph (v)(2) above or section 111A or section 112. Marginal relief is available in case of such companies having a total income exceeding Rs.1 crore i.e. the additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.1 crore should not be more than the amount of income exceeding Rs.1 crore.

Education cess / Secondary and higher education cess on income-tax

The amount of income-tax as increased by the union surcharge should be further increased by an additional surcharge called the "Education cess on income-tax", calculated at the rate of 2% of such income-tax and surcharge. Education cess is leviable in the case of all assesseees i.e. individuals, HUFs, AOP/BOIs, co-operative societies, firms, local authorities and companies. Further, "Secondary and higher education cess on income-tax" @1% of income-tax and surcharge is leviable to fulfill the commitment of the Government to provide and finance secondary and higher education.

2. BASIC CONCEPTS

(a) Scope of definition of "agricultural income" expanded [Section 2(1A)]

Agricultural income is exempt from tax under section 10(1). The scope of "agricultural income" is defined in section 2(1A).

In the past, there have been court rulings that only if a nursery is maintained by carrying out the basic operations on land and subsequent operations in continuation thereof, income from such nursery would be treated as agricultural income and would qualify for exemption under section 10(1). The Supreme Court has, in CIT v. Raja Benoy Kumar Sahas Roy (1957) 32 ITR 466, held that the basic operations must be performed before any income can be called agricultural income. The basic operations involve cultivation of the ground, in the sense of tilling of the land, sowing of the seeds, planting and other similar operations on the land. Such basic operations demand the expenditure of human labour and skill upon the land itself and further, they are directed to make the crop sprout from the land. Therefore, income derived from sale of plants grown directly in pots would not be treated as agricultural income.

However, the Madras High Court, in CIT v. Soundarya Nursery (2000) 241 ITR 530, observed that nursing activity involves carrying out of several operations on land before the saplings were transplanted in suitable containers including pots and thereafter kept in shade or green house for further operation and growth. Therefore, income arising from nursery should be considered as agricultural income.

The Finance Act, 2008 has inserted Explanation 3 to section 2(1A) to provide that, with effect from A.Y.2009-10, the income derived from saplings or seedlings grown in a nursery would be deemed to be agricultural income, whether or not the basic operations were carried out on land. This amendment ratifies the view taken by the Madras High Court in favour of the taxpayer.

(Effective from A.Y. 2009-10)

(b) Scope of definition of charitable purpose restricted [Section 2(15)]

Section 2(15) defines "charitable purpose" to include relief of the poor, education, medical relief, and the advancement of any other object of general public utility.

In CIT v. Gujarat Maritime Board (2007) 295 ITR 561, the Supreme Court observed that the Gujarat Maritime Board was established for the predominant purpose of development of minor ports within the State of Gujarat, the management and control of the Board was essentially with the State Government and there was no profit motive. The assessee, Gujarat Maritime Board, was under a legal obligation to apply its income which was directly and substantially from the business held under trust for the development of minor ports in Gujarat. Therefore, the Supreme Court held that the assessee was entitled to be registered as “charitable trust” under section 12A.

A number of entities functioning on commercial basis claim exemption of their income either under section 10(23C) or section 11 on the foundation that they are charitable institutions. This is based on the contention that they are engaged in the “advancement of an object of general public utility” as is included in the fourth part of the present definition of “charitable purpose”. There were many decisions rendered in the past supporting the view that if unconnected business is held under a trust for promoting the object of general public utility and if profits are used for promoting such objects, income thereof shall be exempt, for example, the decision of the Supreme Court in CIT v. Madras Stock Exchange Ltd. (1981) 130 ITR 184. However, such a claim in respect of an activity carried out on commercial basis, goes against the basic intention of the provision.

Therefore, in order to limit the ambit of the phrase “advancement of any other object of general public utility”, section 2(15) has been amended to provide that “the advancement of any other object of general public utility” would not be a charitable purpose if it involves the carrying on of –

- (a) any activity in the nature of trade, commerce or business or,
- (b) any activity of rendering of any service in relation to any trade, commerce or business,

for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity, or the retention of such income, by the concerned entity. This is provided for in the newly inserted proviso to section 2(15). This amendment would affect the ratio laid down in the cases cited above.

However, it may be noted that sections 11(4) and 11(4A) have not been correspondingly amended. Section 11(4) clarifies that “property held under trust” includes a business undertaking so held. Section 11(4A) provides that exemption can be availed in respect of profits and gains of business if such business is incidental to the attainment of the objectives of the trust and separate books of account are maintained in respect of such business. It may be noted that while the intention of section 11(4A) is to provide exemption to such business income, subject to fulfillment of the conditions specified therein, the intention of the amendment in section 2(15) is to deny exemption in respect

of such income. The proviso to section 2(15) cannot override the provisions of section 11(4A), since it does not contain a non-obstante clause. Therefore, the proviso to section 2(15) has to be read subject to the exception contained in section 11(4A).

(Effective from A.Y. 2009-10)

3. INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME

(a) Exemption of income of a Sikkimese Individual [Section 10(26AAA)]

(i) New clause (26AAA) has been inserted in section 10 to provide that the following income, which accrues or arises to a Sikkimese individual, would be exempt from income-tax –

(a) income from any source in the State of Sikkim; or

(b) income by way of dividend or interest on securities.

(ii) However, this exemption will not be available to a Sikkimese woman who, on or after 1st April, 2008, marries a non-Sikkimese individual.

(Effective retrospectively from A.Y.1990-91)

(b) Exemption of income of an Agricultural Produce Market Committee or Board [Section 10(26AAB)]

New clause (26AAB) has been inserted in section 10 to provide exemption in respect of any income of an Agricultural Produce Market Committee or Board constituted under any law for the time being in force for the purpose of regulating the marketing of agricultural produce.

(Effective from A.Y.2009-10)

(c) Exemption of income of Coir Board [Section 10(29A)]

(i) Section 10(29A) provides for exemption of income of certain specified commodity boards and export development authorities.

(ii) This exemption been extended to any income accruing or arising to the Coir Board established under the Coir Industry Act, 1953 retrospectively with effect from A.Y.2002-03.

(Effective retrospectively from A.Y. 2002-03)

(d) Exemption of income received in a transaction of reverse mortgage [Section 10(43)]

Related amendment in section: 47

(i) The Finance Minister had, in his budget speech of Union Budget 2007-08, announced that the National Housing Bank would introduce the Reverse Mortgage scheme. This scheme is for the benefit of senior citizens, who own a residential house property. In order to supplement their existing income, they can mortgage their house property with a scheduled bank or housing finance

company, in return for a lump-sum amount or for a regular monthly/quarterly/annual income. The senior citizens can continue to live in the house and receive regular income, without the botheration of having to pay back the loan.

- (ii) The loan will be given up to, say, 60% of the value of residential house property mortgaged. Also, the bank/housing finance company would undertake a revaluation of the property once every 5 years.
- (iii) The borrower can use the loan amount for renovation and extension of residential property, family's medical and emergency expenditure etc., amongst others. However, he cannot use the amount for speculative or trading purposes.
- (iv) The bank will recover the loan along with the accumulated interest by selling the house after the death of the borrower. The excess amount will be given to the legal heirs. However, before resorting to sale of the house, preference will be given to the legal heirs to repay the loan and interest and get the mortgaged property released.
- (v) This is no doubt a noteworthy social security measure for the aged. However, the tax consequences of such reverse mortgage needed clarification.
- (vi) Therefore, the Finance Act 2008 has inserted clause (xvi) in section 47 to clarify that any transfer of a capital asset in a transaction of reverse mortgage under a scheme made and notified by the Central Government would not amount to a transfer for the purpose of capital gains.
- (vii) Further, clause (43) has been inserted in section 10 to provide that the amount received by the senior citizen as a loan, either in lump sum or in installments, in a transaction of reverse mortgage would be exempt from income-tax.
- (viii) Capital gains tax liability would be attracted only at the stage of alienation of the mortgaged property by the bank/housing finance company for the purposes of recovering the loan.

(Effective from A.Y.2008-09)

- (e) Sunset clause for deductions under sections 10A and 10B to be deferred by one more year
 - (i) Under section 10A, deduction is available in respect of profits and gains derived from the export of articles or things or computer software by newly established undertakings located in any free trade zone or export processing zone or electronic hardware technology park or software technology park (notified by the Central Government).
 - (ii) Under section 10B, deduction is available in respect of profits and gains derived from the export of articles or things or computer software by newly established undertakings recognised as 100% export oriented undertaking

(EOU) under the Industries (Development and Regulation) Act, 1951.

- (iii) However, the deductions under these sections were to be allowed only up to A.Y.2009-10.
- (iv) The Finance Act, 2008 has extended the benefit of deductions under these sections for one more year. Hence, the benefit of deduction under these sections would be available for A.Y.2010-11 also. However, thereafter, with effect from A.Y.2011-12, no deduction would be allowed under these sections.

(Effective from A.Y.2008-09)

4. PROFITS AND GAINS OF BUSINESS OR PROFESSION

- (a) Deduction of contribution made to an Indian company for scientific research [Section 35(1)(iia)]

Related amendment in section: 35(2AB)

- (i) At present, a weighted deduction of 125% of the amount contributed to a scientific research association, university or other institution for scientific research is available under section 35(1)(i).
- (ii) This benefit of weighted deduction has now been extended to contribution made to companies for scientific research.
- (iii) However, such deduction would be available only if the company is registered in India and has as its main object the scientific research and development. Further, it should be approved by the prescribed authority and should fulfill the other prescribed conditions.
- (iv) This benefit is for encouraging outsourcing of scientific research, especially by small companies, who do not have sufficient resources for building in-house scientific facilities.
- (v) A company approved under section 35(1)(iia) will not be entitled to claim weighted deduction of 150% under section 35(2AB). However, it can continue to claim deduction under section 35(1)(i) in respect of the revenue expenditure incurred on scientific research.

(Effective from A.Y.2009-10)

- (b) Benefit of deduction of post-commencement preliminary expenses extended to the service sector [Section 35D]

Preliminary expenses are allowed as deduction under section 35D over a period of 5 successive years starting from the year of commencement of business i.e. one-fifth of the expenditure is allowed as deduction in each year. Such preliminary expenses incurred before commencement of business is allowed as deduction to companies in both the manufacturing and service sector.

However, so far, such expenses incurred after commencement of business for

extension of an industrial undertaking or for setting up a new industrial unit was allowed only for the companies in the manufacturing sector.

This benefit has now been extended to the companies in the service sector as well. This amendment has been effected by replacing the words “undertaking” and “unit” for the words “industrial undertaking” and “industrial unit”, respectively.

(Effective from A.Y.2009-10)

(c) Deduction of securities transaction tax paid [Section 36(1)(xv)]

Related amendment in sections: 40(a)(ib) and 88E

- (i) Up to A.Y.2008-09, rebate was allowed under section 88E on the amount of securities transaction tax paid. This rebate was allowed when the income from taxable securities transactions was included under the head ‘profits and gains of business or profession’. Section 40(a)(ib) provided that securities transaction tax paid would not be allowed as a deduction from business income.
- (ii) Rebate under section 88E would not be available to such assessees with effect from A.Y.2009-10.
- (iii) However, the amount of securities transaction tax paid by the assessee during the year in respect of taxable securities transactions entered into in the course of business shall be allowed as deduction under section 36 subject to the condition that such income from taxable securities transactions is included under the head ‘Profits and gains of business or profession’.
- (iv) Thus, securities transaction tax paid would be allowed as a deduction like any other business expenditure. Consequently, section 40(a)(ib) providing for disallowance of such expenditure has been omitted.
- (v) For example, if an individual who is a dealer in shares had paid Rs.10,000 as securities transaction tax and his tax on income from sale of such securities was Rs.1 lakh, he would have got a rebate of Rs.10,000 under section 88E and his tax liability would have been Rs.90,000. However, now, Rs.10,000 would be reduced while computing his business income and therefore, the benefit would be corresponding to the slab rate in which the individual’s case falls. Even if the individual falls in the tax bracket of 30%, he would get a tax benefit of only Rs.3,000 in respect of the securities transaction tax paid of Rs.10,000. The loss, in this case, would be Rs.7,000.

(Effective from A.Y.2009-10)

(d) Deduction of commodities transaction tax paid [Section 36(1)(xvi)]

- (i) A new tax called Commodities Transaction Tax (CTT) would be levied on taxable commodities transactions entered in a recognised association. This tax has to be levied from the date on which Chapter VII of the Finance Bill, 2008 comes into force by way of notification in the Official Gazette by the

Central Government.

'Taxable commodities transaction' means a transaction of purchase or sale in a recognised association of –

- (i) option in goods; or
 - (ii) option in commodity derivative; or
 - (iii) any other commodity derivative.
- (ii) This tax would be levied at the rates specified below, on taxable commodities transactions undertaken by the seller or the purchaser, as the case may be, as shown hereunder:-

S. No.	Taxable commodities transaction	Rate	Payable by
1.	Sale of an option in goods or an option in commodity derivative.	0.017% on option premium.	Seller
2.	Sale of an option in goods or an option in commodity derivative, where option is exercised.	0.125% on the settlement price of the option.	Purchaser
3.	Sale of any other commodity derivative	0.017% of the price at which the commodity derivative is sold.	Seller

- (iii) New clause (xvi) has been inserted in section 36 to provide that any amount of commodities transaction tax paid by the assessee during the year in respect of taxable commodities transactions entered into in the course of business shall be allowed as deduction subject to the condition that such income from taxable commodities transactions has been included under the head 'profits and gains of business or profession'. This is in line with the tax treatment of securities transaction tax paid.

(Effective from A.Y.2009-10)

- (e) Amendment of provisions relating to disallowance of interest, commission, rent etc. payable to a resident for non-deduction of tax at source or non-payment of tax deducted [Section 40(a)(ia)]
- (i) According to section 40(a)(ia), interest, commission, brokerage, rent, royalty, fees for technical/professional services payable to a resident or amounts payable (for carrying out any work contract) to a resident contractor/sub-contractor, on which tax is deductible at source shall be disallowed if –
 - (1) such tax has not been deducted; or
 - (2) such tax 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).

In case the tax is 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 deduction in computing the income of the previous year in which such tax was paid.

These provisions were incorporated by the Finance (No. 2) Act, 2004 with effect from the A.Y. 2005-06.

- (ii) The scheme of disallowance under section 40(a)(ia) has now been modified with retrospective effect from A.Y.2005-06.

This section now provides that interest, commission, brokerage, rent, royalty, fees for technical/professional services payable to a resident or amounts payable (for carrying out any work contract) to a resident contractor/sub-contractor, on which tax is deductible at source shall be disallowed if –

- (1) such tax has not been deducted; or
- (2) such tax, after deduction, has not been paid –
 - (a) on or before the due date specified in section 139(1), in a case where the tax was deductible and was so deducted during the last month (i.e., March) of the previous year;
 - (b) on or before the last day of the previous year, in any other case.

In case the tax is deducted in any subsequent year or has been deducted

- (a) during the last month (i.e., March) of the previous year but paid after the due date specified in section 139(1); or
- (b) during any other month (i.e., April to February) of the previous year but paid after the end of the previous year,

such sum shall be allowed as deduction in computing the income of the previous year in which such tax has been paid.

- (iii) If, for instance, tax on royalty paid to Mr.A, a resident, has been deducted during the period between April, 2008 to February, 2009, the same has to be paid by 31st March, 2009. If the deduction has been made in March 2009, the same has to be paid by 31st July/30th September 2009, as the case may be. Otherwise, the expenditure would be disallowed in computing the income for A.Y.2009-10.

If such tax deducted between April 2008 and February 2009 is paid after 31st March 2009, the same would be allowed as deduction in the year of payment. If the tax deducted in March 2009 has been paid after 31st July/30th September, 2009, the same would be allowed as deduction in the year of payment.

(Effective retrospectively from A.Y.2005-06)

- (f) Aggregate of payments made otherwise than by account payee cheque/ account payee bank draft during a day to a person to be considered for the purpose of disallowance under section 40A(3)
- (i) Section 40A(3)(a) provides for disallowance of expenditure incurred in respect of which payment is made in a sum exceeding Rs.20,000 otherwise than by account payee cheque or account payee bank draft. Section 40A(3)(b) also provides for deeming a payment as profits and gains of business or profession if the expenditure is incurred in a particular year but the payment is made in any subsequent year in a sum exceeding Rs.20,000 otherwise than by an account payee cheque or by an account payee bank draft. However, the provisions of this section are subject to exceptions as provided in Rule 6DD of the Income-tax Rules, 1962.
 - (ii) In order to escape disallowance under this section, there has been a practice of splitting up a high value payment into several cash payments, each below Rs.20,000, sometimes even during the course of a day. For example if, in respect of an expenditure of Rs.60,000 incurred by X Ltd., 4 cash payments of Rs.15,000 are made on a particular day to one Mr.Y – one in the morning at 10 a.m., one at 12 noon, one at 3 p.m. and one at 6 p.m., such expenditure did not attract disallowance under section 40A(3), since it was treated as four different payments.
 - (iii) This view was upheld by the Courts in CIT v. Aloo Supply Co. (1980) 121 ITR 680 (Ori) and CIT v. Kothari Sanitation & Tiles (P) Ltd. (2006) 282 ITR 117 (Mad.).
 - (iv) The Finance Act, 2008 has amended section 40A(3) to provide that such disallowance would now be attracted if the payment or aggregate of payments made to the same person during a day otherwise than by account payee cheque or account payee bank draft exceeds Rs.20,000. Therefore, in the above example, the entire expenditure of Rs.60,000 would now be disallowed under section 40A(3), since the aggregate of cash payments made during a day to Mr.Y exceeds Rs.20,000.
 - (v) A new sub-section (3A) has been inserted to further provide that if an expenditure is allowed on accrual basis and payment is made in a succeeding year in violation of the requirement of payment by account payee cheque/account payee bank draft, the payment so made shall be deemed to be the business income in the year of violation [if such payment/aggregate of payments made to a person in a day exceeds Rs.20,000].
- (Effective from A.Y.2009-10)
- (g) Depreciation provided in the books of account deemed to be depreciation actually allowed [Explanation 6 to section 43(6)]
- (i) Section 32(1)(ii) provides that depreciation shall be allowed at the prescribed percentage on the written down value (WDV) of any block of assets. Section

43(6)(b) provides that written down value in the case of assets acquired before the previous year means the actual cost to the assessee less all depreciation actually allowed to him under the Income-tax Act.

- (ii) Persons who were exempt from tax were not required to compute their income under the head "Profits and gains of business or profession". However, when the exemption is withdrawn subsequently, such persons became liable to income-tax and hence, were required to compute their income for income-tax purposes. In this regard, a question arises as to the basis on which depreciation is to be allowed under the Income-tax Act in respect of assets acquired during the years when the person was exempt from tax.
- (iii) There has been a judicial pronouncement on this issue holding that since there was no liability to tax, there was no need to compute the income of such person under the provisions of the Income-tax Act. Therefore, the depreciation provided in the books in the years when the income was exempt cannot be treated as the depreciation "actually allowed". Accordingly, the actual cost of the asset was the written down value for the purposes of claiming depreciation under the Income-tax Act in the previous year in which such person first ceases to enjoy the income-tax exemption.
- (iv) However, since this interpretation is not in conformity with the intent and purpose of the provisions of depreciation, Explanation 6 has been inserted in section 43(6) to provide that,-
 - (a) the actual cost of an asset has to be adjusted by the amount attributable to the revaluation of such asset, if any, in the books of account;
 - (b) the total amount of depreciation on such asset provided in the books of account of the assessee in respect of such previous year or years preceding the previous year relevant to the assessment year under consideration shall be deemed to be the depreciation actually allowed under the Income-tax Act for the purposes of section 43(6);
 - (c) the depreciation actually allowed as above has to be adjusted by the amount of depreciation attributable to such revaluation.

(Effective retrospectively from A.Y.2003-04)

5. CAPITAL GAINS

- (a) No capital gains on conversion of Foreign Currency Exchangeable Bonds into shares or debentures in a company [Section 47(xa)]

Related amendment in section: 49(2A)

- (i) In order to encourage the flow of foreign exchange to India, the Government, in 1992, had allowed established Indian companies to issue foreign currency convertible bonds (FCCB), with special tax scheme for non-resident investors. The Government has now allowed established Indian companies to issue

foreign currency exchangeable bond (FCEB). These are bonds expressed in foreign currency and the principal and interest in respect of such bonds is payable in foreign currency. The Central Government, has vide Notification No.G.S.R.89(E) dated 15.2.2008, introduced the "Issue of Foreign Currency Exchangeable Bonds Scheme, 2008" for facilitating the issue of FCEBs by Indian companies.

- (ii) The difference between FCCB and FCEB is that while FCCBs can only be converted into shares of the issuing company, FCEBs can also be converted into or exchanged for the shares of a group company. Therefore, in order to provide an equitable treatment to FCEBs, clause (xa) has been inserted in section 47 to provide that the conversion of FCEBs into shares or debentures of any company shall not be treated as a 'transfer'.
- (iii) Further, sub-section (2A) of section 49 has been substituted to provide that the cost of acquisition of the shares or debentures received upon conversion of the bond shall be the price at which the corresponding bond was acquired by the assessee.

(Effective from A.Y.2008-09)

- (b) Increase in rate of tax in respect of short-term capital gains on transfer of equity shares or units of equity oriented fund on which securities transaction tax has been paid [Sections 111A & 115AD]
 - (i) As per section 111A, short-term capital gains on transfer of equity shares or units of equity oriented fund, on which securities transaction tax has been paid, would be taxed at a concessional rate of 10%. Section 115AD provides that the concessional rate of 10% would apply to such short-term capital gains arising to Foreign Institutional Investors also.
 - (ii) The Finance Act, 2008 has increased the rate of short-term capital gains tax under section 111A to 15% to align the same with the rate of dividend distribution tax under section 115-O.
 - (iii) However, if such shares/units are held for a period of more than one year, the long-term capital gains arising on their transfer would continue to be exempt under section 10(38).
 - (iv) Correspondingly, the rate of such short-term capital gains under section 115AD has also been increased to 15%.

(Effective from A.Y.2009-10)

6. DEDUCTIONS FROM GROSS TOTAL INCOME

- (a) Inclusion of new instruments under section 80C
 - (i) Under section 80C, a deduction of up to Rs.1 lakh is allowed to an individual or a Hindu undivided family (HUF) for making investments in eligible saving instruments or for incurring expenditure on tuition fee or repayment of housing loan.

- (ii) The scope of eligible saving instruments has been widened to give a fillip to small savings.
- (iii) The following investments would also be eligible for deduction under section 80C with effect from A.Y.2008-09 :-
 - (1) five year time deposit in an account under Post Office Time Deposit Rules, 1981; and
 - (2) deposit in an account under the Senior Citizens Savings Scheme Rules, 2004.
- (iv) However, they would be subject to the overall ceiling of Rs.1 lakh.
- (v) Further, it has been provided that where any amount is withdrawn by the assessee from such account before the expiry of a period of 5 years from the date of its deposit, the amount so withdrawn shall be deemed to be income of the assessee of the previous year in which the amount is withdrawn. Accordingly, the amount so withdrawn would be chargeable to tax in the assessment year relevant to such previous year.
- (vi) The amount chargeable to tax shall also include that part of the amount withdrawn which represents interest accrued on the deposit.
- (vii) However, if any part of the amount so received or withdrawn (including the amount relating to interest) has been subject to tax in any of the earlier years, such amount shall not be taxed again.

(Effective from A.Y.2008-09)

- (b) Deduction in respect of medical insurance premium [New section 80D]
 - (i) At present, deduction is allowed under section 80D up to a maximum of Rs.15,000 to an individual in respect of medical insurance premium paid for self, spouse, dependent parents and dependent children. In case the premium is paid in respect of a senior citizen, then, the maximum deduction would be Rs.20,000 instead of Rs.15,000.
 - (ii) In the case of a HUF, such deduction is allowed in respect of premium paid to insure the health of any member of the family.
 - (iii) The existing section 80D has been substituted.
 - (iv) An additional deduction of up to Rs.15,000 would be allowed in respect of medical insurance premium paid for insuring the health of a parent or parents. This would be in addition to the deduction of Rs.15,000 in respect of medical insurance premium paid for self, spouse and dependent children. Such additional deduction would be available even if the parents are not dependent on the individual.
 - (v) The maximum deduction would, therefore, be Rs.30,000 [i.e. Rs.15,000 + Rs.15,000] and in case any of the persons insured is a senior citizen,

Rs.35,000 [i.e. Rs.15,000 + Rs.20,000].

- (vi) For example, if Mr. Ganesh pays medical insurance premium of Rs.16,000 for insuring the health of himself, his spouse and his children and Rs.21,000 for insuring the health of his parents, then he would be eligible for a deduction of Rs.30,000 [Rs.15,000 + Rs.15,000] under section 80D, whether or not his parents are dependent on him. If either or both of his parents are senior citizens, then he would be entitled to a higher deduction of Rs.35,000 [Rs.15,000 + Rs.20,000].
- (vii) The maximum deduction available to a HUF would continue to be Rs.15,000 and in case any member is a senior citizen, Rs.20,000.
- (viii) The other conditions to be fulfilled are that such premium should be paid by any mode, other than cash, in the previous year out of his income chargeable to tax. Further, the medical insurance should be in accordance with a scheme made in this behalf by -
 - (a) the General Insurance Corporation of India and approved by the Central Government in this behalf; or
 - (b) any other insurer and approved by the Insurance Regulatory and Development Authority.

(Effective from A.Y.2009-10)

- (c) Restrictive clause for deduction in respect of refining of mineral oil [Section 80-IB(9)]
 - (i) Under section 80-IB(9), a 100% deduction is allowed in respect of profits and gains derived from commercial production or refining of mineral oil. The term 'mineral oil' does not include petroleum and natural gas for the purposes of claim of deduction under this sub-section.
 - (ii) The deduction under this sub-section is available to an undertaking for a period of seven consecutive assessment years including the initial assessment year –
 - (1) in which the commercial production under a production sharing contract has first started; or
 - (2) in which the refining of mineral oil has begun.
 - (iii) However, deduction under this sub-section would be allowed to an undertaking which begins refining of mineral oil on or after 1.4.2009 only if it fulfills the following conditions -
 - (1) it is wholly owned by a public sector company or any other company in which a public sector company or companies hold at least 49% of the voting rights;
 - (2) it is notified by the Central Government in this behalf on or before 31st May, 2008; and

(3) it begins refining not later than 31st March, 2012.

(Effective from A.Y.2008-09)

(d) Five year tax holiday to hospitals set up in areas other than excluded areas [Section 80-IB(11C)]

- (i) Hospitals set up in rural areas enjoy a five year tax holiday under section 80-IB(11B) if they are constructed during the period between 1.10.2004 and 31.3.2008 and fulfill the prescribed conditions.
- (ii) New sub-section (11C) has been inserted in section 80-IB to provide a five year tax holiday to hospitals set up in other than the excluded areas. Excluded area means the area comprising the urban agglomerations of Greater Mumbai, Delhi, Kolkata, Chennai, Hyderabad, Bangalore and Ahmedabad, the districts of Faridabad, Gurgaon, Ghaziabad, Gautam Budh Nagar and Gandhi Nagar and the city of Secunderabad.
- (iii) To be eligible for this benefit, the hospital should be constructed and should start functioning between 1.4.08 to 31.3.2013. Further, it should have at least 100 beds for patients. For claiming this benefit, it is necessary that the audit report signed and verified by a Chartered Accountant certifying that deduction has been correctly claimed should be filed along with the company's return of income.
- (iv) The construction of the hospital should be in accordance with the regulations or bye-laws of the local authority. The hospital shall be deemed to have been constructed on the date on which a completion certificate in respect of such construction is issued by the local authority concerned.

(Effective from A.Y.2009-10)

(e) Extension of five year tax holiday to hotels set up in the specified districts having a World Heritage Site [Section 80-ID]

- (i) Section 80-ID was inserted by the Finance Act, 2007 to provide a five-year tax holiday to new two, three and four star hotels and convention centres set up in the Northern Capital Region in view of the upcoming commonwealth games.
- (ii) The benefit of this five year tax holiday has now been extended to new two, three or four star hotels located in specified districts having a World Heritage Site. The specified districts are Agra, Jalgaon, Aurangabad, Kancheepuram, Puri, Bharatpur, Chhatarpur, Thanjavur, Bellary, South 24 Parganas, Chamoli, Raisen, Gaya, Bhopal, Panchmahal, Kamrup, Goalpara, Nagaon, North Goa, South Goa, Darjeeling and Nilgiri.
- (iii) For availing this benefit, the hotel should be constructed and should start functioning between 1.4.08 to 31.3.2013.
- (iv) Other conditions specified in section 80-ID would also be applicable to new hotels set up in these specified districts having a World Heritage Site.

(Effective from A.Y.2009-10)

7. ASSESSMENT OF VARIOUS ENTITIES

(a) Deferred tax and dividend distribution tax to be added back for computation of book profit [Section 115JB]

- (i) Section 115JB provides that if the tax computed under the Income-tax Act is less than 10% of book profits, then book profits is deemed to be the total income and tax is payable @10% thereon. For this purpose, book profit means the net profit as per the profit and loss account prepared in accordance with Parts II and III of Schedule VI to the Companies Act, as adjusted by certain additions/deductions as specified.
- (ii) One of the adjustments is to add back income-tax paid or payable, and the provision therefor. In order to clear the doubt as to whether income-tax includes only the tax or surcharge, cess etc. also, the Finance Act, 2008 has inserted Explanation 2 after sub-section (2) to clarify that income-tax includes
 - dividend distribution tax / tax on distributed income;
 - interest;
 - surcharge;
 - education cess; and
 - secondary and higher education cess.
- (iii) Further, Explanation 1 has been amended to provide that the net profit should be increased by the amount of deferred tax or provision therefor, if the same has been debited to profit and loss account and reduced by the amount of deferred tax, if any, credited to the profit and loss account.

(Effective retrospectively from A.Y.2001-02)

(b) No double taxation of dividend in certain cases [Sections 115-O]

- (i) Tax@15% is leviable on dividends declared, distributed or paid by a domestic company. However, there is a problem of double taxation/multiple taxation of dividend distributed under the current tax structure in India.
- (ii) The Finance Act, 2008 has sought to provide a partial relief from double taxation of dividends by inserting sub-section (1A) to section 115-O. A holding company receiving dividend from its subsidiary company can reduce the same from dividends declared, distributed or paid by it. For this purpose, a holding company is one which holds more than 50% of the nominal value of equity shares of the subsidiary.
- (iii) There are certain conditions to be fulfilled to avail this benefit. They are -
 - the subsidiary company should have actually paid the dividend distribution tax;
 - the holding company should be a domestic company; and

- it should not be a subsidiary of any other company.

- (iv) It may be noted that the matching principle does not apply i.e. dividend received from the subsidiary company during the year can be reduced from the dividend distributed by the holding company during the same year, irrespective of the period to which the dividends relate to. Even if the dividend received and dividend distributed relate to different periods, the same can be adjusted and tax can be paid by the holding company on the net figure. However, the dividend shall not be taken into account for reduction more than once.

(Effective from A.Y.2008-09)

8. INCOME-TAX ON FRINGE BENEFITS

(a) Relaxation of FBT provisions [Section 115WB & 115WC]

- (i) Under section 115WB(2), an employer would be deemed to have provided fringe benefits to its employee, if such employer incurs any expenditure, inter alia, for the purposes of entertainment, hospitality, conference, and sales promotion (including publicity). Section 115WC provides for valuation of such fringe benefits.
- (ii) The Finance Act, 2008 has given some relaxation in respect of Fringe Benefit Tax. Though no reduction of rate is proposed in respect of FBT, certain expenses have been excluded from the scope of FBT.
- (iii) Payment through pre-paid electronic meal card shall be excluded from hospitality expenditure and hence, would not be included for valuation of fringe benefit chargeable to tax, provided such card is not transferable and usable only at eating joints and fulfills such other prescribed conditions.
- (iv) Further, expenditure on or payment made for the maintenance of any accommodation in the nature of guest house would not be included for valuation of fringe benefits.
- (v) Also, the following expenditure would not be considered as employee welfare expenditure and hence, shall not be included for valuation of fringe benefits –
 - expenditure on providing creche facility for the children of employees;
 - expenditure on sponsoring a sportsman, being an employee; and
 - expenditure on organising sports events for employees.
- (vi) The value of fringe benefits on account of expenditure on festival celebration has been reduced from 50% to 20%.

(Effective from A.Y.2009-10)

(b) Definition of “securities” for levy of FBT amended [Section 115WB(1)]

- (i) The Finance Act, 2007 had inserted a new clause (d) in section 115WB(1) to provide for levy of FBT on the value of any specified security or sweat equity

shares allotted or transferred, directly or indirectly, by the employer free of cost or at concessional rate to his employees, including former employees.

- (ii) Clause (i) of the Explanation to clause (d) defines a specified security to mean “securities” as defined in section 2(h) of the Securities Contracts (Regulation) Act, 1956 and includes employees' stock option.
- (iii) This definition has been amended to clarify that it is the securities offered under an employees' stock option plan or scheme (where the employees' stock option has been granted under such plan or scheme) which is to be included within its scope and not the employees' stock option plan itself.

(Effective from A.Y.2008-09)

(c) FBT recovered by employer deemed as payment by employee [Section 115WKB]

- (i) Circular No.9, dated 20th December, 2007 issued by the CBDT clarifies, inter alia, that if FBT on account of share allotted or transferred under ESOPs has been paid by the employer, but recovered from an employee, it shall be deemed that the employee has paid the FBT. Consequently, the employee can claim credit for this deemed payment of FBT in a foreign country.
- (ii) This clarification has now been incorporated in the Income-tax Act itself in order to provide a firm basis to enable the employees to claim credit for tax so paid. A new section 115WKB has been inserted to provide that where fringe benefit tax (with respect to allotment or transfer of specified security or sweat equity shares) has been paid by the employer and subsequently recovered from the employee, the recovery of fringe benefit tax shall be deemed to be the tax paid by such employee in relation to value of fringe benefits provided to him. The deeming provision shall apply only to the extent to which the amount of recovery relates to the value of the fringe benefits provided to such employee.
- (iii) Further, in such a situation, the employee shall not be entitled for any refund out of such deemed payment of tax. Also, he shall also not be entitled to claim any credit of such deemed payment of tax against tax liability on other income or against any other tax liability.

(Effective from A.Y.2008-09)

9. ASSESSMENT PROCEDURE

- (a) Advancement of due date of filing return of income and return of fringe benefits [Section 115WD(1) & 139(1)]

Related amendment in section: 44AB

- (i) The due date for filing return of income is 31st October of the relevant assessment year in the case of the following assesseees –
 - Companies;

- Persons subject to tax audit; and
 - Working partners of firms subject to tax audit.
- (ii) The due date for filing return of fringe benefits is 31st October of the relevant assessment year in the case of the following assesseees –
- Companies; and
 - Persons subject to tax audit.
- (iii) The Finance Act, 2008 has advanced these due dates from 31st October to 30th September of the relevant assessment year.
- (iv) Section 44AB prescribes compulsory tax audit for assesseees carrying on business or profession, whose sales/turnover/gross receipts exceed the prescribed monetary limits. Such persons have to get their accounts audited by a Chartered Accountant before the specified date and furnish the audit report in the prescribed form. Specified date was defined to mean the 31st October of the relevant assessment year.
- (v) Consequent to advancement of the due date for filing return of income in respect of persons subject to tax audit, the specified date has also been advanced from 31st October to 30th September of the relevant assessment year.

(Effective from A.Y.2008-09)

- (b) Correction of arithmetic mistakes and adjustment of incorrect claim under sections 143(1) and 115WE
- (i) There is no provision for prima facie adjustment in the system of summary assessment prevalent since 1st June, 1999. The ambit of this system is restricted to only verifying whether taxes have been correctly paid on the income returned. Section 143(1) does not contain any provision for correcting arithmetical mistakes or internal inconsistencies.
- (ii) A significant amendment has been made by the Finance Act, 2008 with regard to the procedure to be followed under section 143(1). This section now seeks to allow the Assessing Officer to make such adjustments. It is stated that a simplified procedure which would enable such corrections as are listed in the amended section would prevent avoidable revenue loss.
- (iii) For this purpose, the Finance Act, 2008 has substituted section 143(1) to provide 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.
- (iv) Similar amendment has been made in section 115WE(1) to provide for

computation of value of fringe benefits of an assessee after making the following adjustments to the value of fringe benefits in the return -

- (a) any arithmetical error in the return; or
 - (b) an incorrect claim, if such incorrect claim is apparent from any information in the return.
- (v) 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.
- (vi) Tax and interest should be computed on the basis of the total income/ value of fringe benefits so computed after making the adjustments in (iii)/(iv) above.
- (vii) 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. In the case of fringe benefit tax, the tax and interest so computed would be adjusted by any advance tax paid, self-assessment tax and any amount paid otherwise by way of tax or interest.
- (viii) 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.
- (ix) If any amount of refund is due to the assessee, the same shall be granted to the assessee.
- (x) 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.
- (xi) On the other hand, where there is neither any adjustment nor any tax due from or refund payable to the assessee, the acknowledgement of the return shall be deemed to be the intimation under section 143(1) / 115WE(1).
- (xii) 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.

(xiii) 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, 2009.
- (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.

(Effective from A.Y.2008-09)

(c) Time limit for issue of notice for scrutiny under section 143(2) / 115WE(2)

- (i) Section 143(2)(ii) and 115WE(2) provides that notice has to be served within a period of 12 months from the end of the month in which the return of income/return of fringe benefits is furnished.
- (ii) Since this limitation period is with reference to the end of the month, the last day of every month becomes a time barring date, which leads to administrative inconvenience.
- (iii) Therefore, the Finance Act, 2008 now provides that notices under these sections have to be served on the assessee within a period of 6 months from the end of the financial year in which the return is furnished.

(Effective from A.Y.2008-09)

(d) Assessing Officer also empowered to extend suo motu the period of furnishing of audit report [Section 142(2C)]

- (i) Under section 142(2A), the Assessing Officer is empowered to direct a special audit, having regard to the nature and complexity of the accounts of the assessee and the interests of the revenue.
- (ii) Section 142(2C) requires the assessee to furnish the report of such audit to the Assessing Officer within such period as may be prescribed by the Assessing Officer.
- (iii) As per the proviso to section 142(2C), the Assessing Officer may extend the period for furnishing such report on an application made in this behalf by the assessee and when there are good and sufficient reasons for such extension.

However, the aggregate period of extension cannot exceed 180 days.

- (iv) This proviso has been amended to empower the Assessing Officer to extend the period of furnishing such report suo motu also.

(Effective from A.Y.2008-09)

- (e) Assessing Officer empowered to 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 [Insertion of second proviso to section 147]

- (i) The Assessing Officer can reopen a case under section 148 if he has reason to believe that any income has escaped assessment. In order to ensure that such power is used rationally and objectively by the Assessing Officers, sufficient measures have been provided in the Act. However, there have been contentions between the department and the assessee on the issue of valid reopening of assessment.

- (ii) In *Metro Auto Corporation v. ITO* (2006) 286 ITR 618, the Bombay High Court held that reassessment was not permissible when an assessment was pending in appeal before the Tribunal. In view of such interpretation, it may not be possible to issue notice under section 148 in any case which is pending before the Appellate Tribunals or Courts. Further, by the time the Tribunal or the Court judgment is received, reopening of the case may be barred by limitation. Such a situation is not in accordance with the legislative intent.

- (iii) The true legislative intent was correctly reflected in the Bombay High Court judgment in *CIT v. Sakseria Cotton Mills Ltd.* (1980) 124 ITR 570, where it was held that in a case where an assessment is made the subject of an appeal, only that part of the Assessing Officer's order merges with the appellate authority's order in respect of which the appellate authority has exercised the appellate jurisdiction. Hence, notice under section 148 can be issued for assessment/reassessment of income which has escaped assessment and which has not been made the subject matter of an appeal, reference or revision.

- (iv) Hence, in order to clarify the true legislative intent, a second proviso has been inserted in section 147 with effect from 1.4.2008 to provide that 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.

(Effective from A.Y.2008-09)

Note - Similar amendment has been made in section 17(1) of the Wealth-tax Act to provide that 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.

(Effective from A.Y.2008-09)

- (f) Notice under section 148 need not be issued by the Joint Commissioner/ Commissioner/Chief Commissioner himself [Section 151]
- (i) Under section 151, an Assessing Officer has to get the consent of the Joint Commissioner for issue of notice under section 148, in a case, where assessment under section 143(3) or section 147 has been made for the relevant assessment year. If notice is to be issued after expiry of four years from the end of the relevant assessment year, the consent of the Chief Commissioner/Commissioner is required.
 - (ii) In such situations, notice can be issued by the Assessing Officer only when the Joint Commissioner/Chief Commissioner/Commissioner, as the case may be, is satisfied, on the reasons recorded by the Assessing Officer, that there is a proper case for the issue of such notice.
 - (iii) In Dr. Shashi Kant Garg Vs. CIT 285 ITR 158, the Allahabad High Court has observed that in such a situation, notice under section 148 has to be issued by the Joint Commissioner himself, which is not in tune with the legislative intent of the section. The Joint Commissioner is only required to be satisfied with the reasons recorded by the Assessing Officer. He does not have to issue the notice himself.
 - (iv) Hence, in order to convey the true legislative intent, an Explanation has been inserted with retrospective effect from 1.10.98 to provide 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 148, need not issue the notice himself.
 - (v) Thus, where the approval of the Joint Commissioner/Chief 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.

(Effective retrospectively from 1.10.1998)

Note – Similar amendment has been made in section 17(1B) of the Wealth-tax Act to provide 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.

(Effective retrospectively from 1.10.1998)

- (g) Provision for assessment in the case of annulment of the proceeding under section 153A
- (i) Section 153A, which comes into operation whenever a search is conducted under section 132 or books of account or other documents or any assets are requisitioned under section 132A, provides for assessment or reassessment of total income in respect of each assessment year falling within a period of six assessment years immediately preceding the assessment year relevant to the previous year in which search is conducted or books of account, etc are requisitioned.
 - (ii) Section 153B provides the time limit for completing such assessment or reassessment.
 - (iii) In order to clarify the ambiguity in issues regarding revival of proceedings and time limits, the Finance Act, 2008 has made certain amendments in sections 153, 153A and 153B.
 - (iv) 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 [Sub-section (2) of section 153A].
 - (v) 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) of section 153]. 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.
 - (vi) 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, shall be excluded in computing the period of limitation for the purposes of section 153B [New clause (vii) of Explanation to section 153B].
- (Effective retrospectively from 1.6.2003)

- (h) Intimation under section 143(1) deemed to be notice of demand [Proviso to section 156]
 - (i) Section 156 provides that when any tax, interest, penalty, fine or other sum is payable in consequence of any order passed under the Act, the Assessing Officer should serve upon the assessee a notice of demand in the prescribed form specifying the sum so payable.
 - (ii) A proviso has been inserted to section 156 to provide that where any sum is determined to be payable by the assessee under section 143(1), the intimation under that section would be deemed to be a notice of demand for the purpose of section 156.
 - (iii) It may be noted that this deeming provision was earlier contained in section 143(1)(i) itself. Now, section 143(1) has been substituted and the deeming provision has been inserted in section 156.

(Effective from A.Y.2008-09)

10. COLLECTION AND RECOVERY OF TAX

- (a) Person not deducting tax also deemed to be an assessee in default [Sections 191 & 201]
 - (i) Section 201 provides that a person is deemed to be an assessee in default if he fails to deduct tax at source or fails to deposit the tax deducted at source after such tax has been deducted. The persons covered within the scope of section 201 are :-
 - (1) person referred to in section 200;
 - (2) the principal officer and the company of which he is the principal officer in the cases referred to in section 194 [relating to deduction of tax at source on dividends].
 - (ii) Under section 200(1), the following persons are required to pay the sum so deducted to the Central Government or as the CBDT directs within the prescribed time –
 - (1) any person deducting any tax at source in accordance with the provisions of Chapter XVII; and
 - (2) an employer referred to in section 192(1A).
 - (iii) Section 201(1) has been interpreted by Courts in a manner so as not to cover failure to deduct tax at source. Such a view is contrary to the true legal intention. Therefore, section 201(1) has been substituted with retrospective effect from 1.6.2002 to clarify that where a person, including the principal officer of a company,-
 - (i) who is required to deduct any sum in accordance with the provisions of Income-tax Act; or

- (ii) referred to in sub-section (1A) of section 192, being an employer, does not deduct, or after so deducting fails to pay, or does not pay, the whole or any part of the tax, as required by or under the Income-tax Act, he shall be deemed to an assessee in default.
- (iv) However, no penalty would be charged under section 221 from such person, unless the Assessing Officer is satisfied that such person has failed to deduct and pay such tax without good and sufficient reasons.
- (v) Similar amendment has been made in section 191 which 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.
- (vi) The Explanation to this section provided that if –
 - (1) the person referred to in section 200 [namely, the person deducting tax at source or an employer paying tax on non-monetary perquisites under section 192(1A) and who is required to pay within the prescribed time the sum so deducted to the credit of the Central Government]; and
 - (2) the Principal officer and the company in respect of which he is the Principal officer, in cases of TDS for dividends referred to in section 194, does not deduct the whole or part of the tax, and the assessee has not paid the tax direct, then, the person/principal officer/company responsible for deducting tax shall be deemed to be an assessee in default.
- (vii) This Explanation has been substituted with retrospective effect from 1.6.2003 to provide that a person (including the principal officer of a company) would be deemed to be an assessee in default if he -
 - (1) is required to deduct any sum in accordance with the provisions of the Act; or
 - (2) is an employer referred to in section 192(1A)
 and
 - (1) he does not deduct the whole or any part of such tax; or
 - (2) after deducting fails to pay the whole or any part of such tax.
 However, if the assessee himself has paid the tax directly, this provision will not apply.
- (b) Exemption of interest on corporate bonds from TDS requirements [Section 193]
 - (i) Section 193 provides for deduction of tax at source on any income by way of interest on securities payable to a resident.

- (ii) The proviso to this section exempts certain interest payments from the applicability of TDS provision under this section.
- (iii) The Finance Act, 2008 has inserted clause (ix) in the proviso to exempt any interest payable 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, from the requirement of deduction of tax at source.

(Effective from 1.6.2008)

(c) Widening the scope of coverage of TDS provisions under section 194C to include Association of Persons and Body of individuals subject to tax audit

- (i) Section 194C provides for deduction of tax at source from payments to contractors and sub-contractors.
- (ii) Sub-section (1) of this section lists the persons who are liable to deduct tax at source from payments to a resident contractor. So far, Association of Persons and Body of Individuals were not included in this list and were therefore, not liable to deduct tax at source under section 194C.
- (iii) The Finance Act, 2008 has now included within the scope of section 194C(1), Association of Persons and Body of Individuals whose total sales/gross receipts/turnover from the business or profession exceed the monetary limits specified in section 44AB during the financial year immediately preceding the financial year in which such sum is credited or paid to the account of the contractor.
- (iv) Thus, such AOPs and BOIs subject to tax audit in the immediately preceding financial year are liable to deduct tax at source from payments to resident contractors.

(Effective from 1.6.2008)

(d) Requirement of furnishing information relating to payment of any sum subject to deduction of tax at source under section 195 in the prescribed form and manner

Related amendment in section: 295

- (i) Sub-section (1) of section 195 requires any person responsible for paying any interest or any other sum chargeable to tax (except income under the head "salaries") to a non-resident or to a foreign company, to deduct tax at source at the rates in force.
- (ii) The Finance Act, 2008 has inserted sub-section (6) in section 195 to require the person referred to in section 195(1) to furnish the information relating to payment of any sum in such form and manner as may be prescribed by the CBDT.
- (iii) Consequential amendment has been made in section 295 which provides for the rule making powers of the CBDT. The CBDT has now been empowered to

make rules providing for the form and manner in which the information relating to payment of any sum may be furnished under section 195(6).

(Effective from A.Y.2008-09)

- (e) CBDT empowered to frame rules for giving credit in respect of TDS/TCS [Sections 199 and 206C(4)]

Related amendment in sections: 203(3), 206C(5) and 139(9).

- (i) The effective date of commencement of the scheme for dematerialisation of TDS and TCS certificates has been extended from 1.4.2008 to 1.4.2010. Accordingly, sections 203(3) and 206C(5) now provide for waiving the requirement of furnishing TDS/TCS certificate in respect of tax deducted or paid or collected on or after 1.4.2010.
- (ii) Section 139(9) has been amended to provide that a return of income shall be regarded as defective if it is not accompanied by, inter alia, proof of tax deducted at source or tax collected at source. Earlier, the proof of TDS/TCS was required only in respect of tax deducted or collected before 1.4.2008.
- (iii) In order to provide a certain degree of flexibility in the scheme for allowing credit to the assessee for TDS and TCS, sections 199 and 206C(4) have been substituted to provide that the manner in which the credit for TDS and TCS is to be given will be governed by the rules to be framed under section 199 and 206C(4).
- (iv) As per the provisions of section 199, as it stands at present, the credit for tax deducted at source has to be given -
 - (1) for the assessment year for which such income from which tax has been deducted is assessable; and
 - (2) to the person from whose income the deduction has been made.
- (v) This section has been substituted to provide relief on account of the genuine hardship caused on account of the tax being deductible at the time of credit or payment, whichever is earlier, irrespective of the method of accounting being followed by the person from whose income, tax is being deducted.
- (vi) New section 199(1) provides that any deduction of tax made and paid to the Central Government shall be treated as a payment of tax on behalf of the person in respect of whose income the deduction was made, or of the owner of the security, or of the depositor or of the owner of property or of the unit-holder, or of the shareholder, as the case may be.
- (vii) 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.
- (viii) 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 (vi) and (vii) above. Further, the CBDT can specify the assessment year for which such credit may be given.

- (ix) Section 206C(4) has been substituted to provide that any amount collected in accordance with the provisions of section 206C and paid to the credit of the Central Government shall be deemed to be a payment of tax on behalf of the person from whom the amount has been collected. Accordingly, 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.

(Effective from A.Y.2008-09)

11. APPEALS AND REVISION

- (a) Aggregate period of stay not to exceed 365 days, even if delay is not attributable to the assessee [Section 254(2A)]
 - (i) Section 254(2A) provides that the Appellate Tribunal, where it is possible, may hear and decide an appeal within a period of four years from the end of the financial year in which such appeal is filed.
 - (ii) The Appellate Tribunal may, on merit, pass an order of stay in any proceedings relating to an appeal. However, such period of stay cannot exceed 180 days from the date of such order. The Appellate Tribunal has to dispose off the appeal within this period of stay.
 - (iii) Where the appeal has not been disposed off within this period and the delay in disposing the appeal is not attributable to the assessee, the Appellate Tribunal can further extend the period of stay originally allowed. However, the aggregate of period originally allowed and the period so extended should not exceed 365 days. The Appellate Tribunal is required to dispose off the appeal within this extended period.
 - (iv) The objective of these provisions is unambiguous that the Appellate Tribunal cannot grant stay either under the original order or under any subsequent order, beyond the period of 365 days in aggregate.
 - (v) However, the Bombay High Court in *Narang Overseas (P.) Ltd. v. ITAT* (2007) 295 ITR 22 observed that this limit would not apply where there is a delay beyond this period and the same is not attributable to the assessee. However, this decision does not reflect the true legal intention.
 - (vi) Therefore, section 254(2A) has been amended to clarify the correct intention. It has now been provided that 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.

- (vii) Accordingly, even if an appeal is not heard by the bench, say, due to the bench not functioning or due to the department seeking adjournment, the stay granted by the Appellate Tribunal shall stand vacated after the period of 365 days, inspite of the assessee having taken all steps to ensure speedy disposal of the appeal and having a good prima facie case.

(Effective from 1.10.2008)

- (b) Consequence of non-filing of appeal in respect of cases where the tax effect is less than the prescribed monetary limit [New section 268A]
 - (i) The Supreme Court has, in *M/s. Berger Paints India Ltd. v. CIT* (2004) 266 ITR 99, held that the revenue cannot challenge the correctness in the case of an assessee where the law laid down in another case by the High Court has been accepted by the revenue.
 - (ii) In order to reinstate the correct position of law, the Finance Act, 2008 has inserted section 268A, retrospectively with effect from 1.4.1999, to provide that where an appeal has not been filed by the revenue on any issue against any order passed by any appellate authority consequent to the tax effect being less than the prescribed monetary limit, the revenue shall not be precluded from filing an appeal on the same issue in any other case, either of the same assessee or other assessee. Further, it shall not be lawful for the assessee to contend that the revenue has accepted the decision on the disputed issue by not filing the appeal in any other case or in an earlier issue.
 - (iii) 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.
 - (iv) 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.
 - (v) 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.
 - (vi) 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.

- (vii) 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.

(Effective retrospectively from 1.4.1999)

12. PENALTY & PROSECUTION

- (a) Deemed satisfaction for initiation of penalty proceedings under section 271(1)(c) [Section 271(1B)]
 - (i) Under section 271(1), the Assessing Officer is empowered to levy penalty for certain offences detailed therein.
 - (ii) However, the Assessing Officer was required to be satisfied before levying such penalty, since it is not every addition which will merit penalty. Unless there is a prima facie case, penalty proceedings need not be initiated.
 - (iii) The Supreme Court, in CIT v. S.V. Angidi Chettiar (1962) 44 ITR 739, while dealing with penalty under section 28 of the Indian Income-tax Act, 1922, held that "satisfaction before conclusion of proceeding under the Act, and not issue of notice of initiation of any step for imposing penalty is a condition for the exercise of jurisdiction". The same matter came up once again before the Calcutta High Court in Backer Gray & Co. Ltd. (1978) 112 ITR 503. The Calcutta High Court relied on the Supreme Court decision in the above case and held that though the Income-tax Officer should be prima facie satisfied before the penalty notice is issued, it does not mean that he is required to record such satisfaction in writing in every case.
 - (iv) However, the Delhi High Court has, in CIT v. Ram Commercial Enterprises Ltd. (2000) 246 ITR 568, held that the Assessing Officer must record satisfaction in express terms.
 - (v) In view of conflicting legal opinion on this issue, sub-section (1B) has been inserted in section 271 with retrospective effect from 1.4.89, to clarify the true legislative intent.
 - (vi) It has now been unambiguously provided 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.

(Effective retrospectively from 1.4.1989)

Note – Similar amendment has been made in the Wealth-tax Act by insertion of sub-section (1A) in section 18 to provide that where any amount is added or disallowed in computing the net wealth of an assessee in any order of assessment or reassessment,

and such 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.

(Effective retrospectively from 1.4.1989)

- (b) Power of Commissioner to grant immunity from penalty and prosecution [Section 273AA & 278AB]

Related amendment in sections: 153 & 251

- (i) The Finance Act, 2008 has introduced certain provisions regarding immunity from penalty and prosecution. Also, the time limit for assessment relating to abatement of settlement proceedings has been provided.
- (ii) Wide-ranging amendments were made last year to the system of settlement of cases, which also provided for abatement of proceedings before the Settlement Commission under various circumstances. The Commissioner of Income-tax has now been empowered to grant immunity from penalty and prosecution in cases which abate.
- (iii) Section 273AA has been inserted to empower 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 245HA) to the Commissioner of Income-tax.
 - (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 Income-tax authority.
 - (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 income and the manner in which such income 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

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.

(iv) Section 278AB has been introduced to empower 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 245HA) to the Commissioner of Income-tax before institution of the prosecution proceedings after abatement.

(2) 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.

(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 income and the manner in which such income has been derived.

(4) 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.

(5) If the assessee fails to comply with any condition subject to which the immunity was granted, the same would be withdrawn.

(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 income-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.

(v) Section 251(1) lists the powers of the Commissioner (Appeals) in disposing of

an appeal. Clause (aa) has been inserted in section 251(1) to empower the Commissioner (Appeals), 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.

(Effective from A.Y.2008-09)

- (vi) Section 153 has been amended retrospectively with effect from 1.6.2007 to allow a minimum time period of one year to the income-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.

(Effective retrospectively from 1.6.2007)

13. MISCELLANEOUS PROVISIONS

(a) Authentication of notices and other documents [New section 282A]

- (i) The use of information technology by the Income-tax department in its major processes and procedures has been increasing in order to improve the level of service to the taxpayers.
- (ii) One step in this direction is the schemes for centralized processing of returns and centralised issuance of notices using information technology. For successful implementation of these schemes, it is necessary to dispense with the signature of the officer and to use a common seal. The introduction of such common seal in respect of issue of notices, intimations, etc., would be major step in minimizing taxpayers interface with the Department. This would also significantly reduce the discretion of the individual officer and ensure better accountability and compliance.
- (iii) Therefore, with this objective, section 282A has been inserted to provide 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.
- (iv) 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.

- (v) 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 (iv) above.

(Effective from 1.6.2008)

(b) Deemed service of valid notice in certain circumstances [New section 292BB]

- (i) It is an established law that statutory proceedings have to be initiated by valid service of notice. In CIT v. Hotline International (P.) Ltd. (2008) 296 ITR 333, it was held that if this requirement of valid service of notice is not observed, the proceeding itself would not be legal. In this case, the Delhi High Court rejected the contention of the Department that this proposition would not hold good where the assessee had participated in further proceedings, notwithstanding the fact that there was no proof of service of notice and the assessee denied such service. It was held that mere participation in the proceedings would not validate what was void ab initio.
- (ii) The Finance Act, 2008 has inserted a new section 292BB to provide 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.
- (iii) 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.

(Effective from A.Y.2008-09)

Note – Similarly, new section 42 has been inserted in the Wealth-tax Act to provide 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.

(Effective from A.Y.2008-09)

- (c) Presumption as to ownership of assets, books of accounts found during search under section 132 extended to survey cases also [Section 292C]
- (i) Section 292C provides for a rebuttable presumption with respect to books of account, other documents, 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.
 - (ii) In ITO v. Dr. Anand Chhabra (2007) 107 TTJ 831 (Jodh.), it was observed that the presumption in respect of statements taken during search under section 132(4) is not applicable for survey cases.
 - (iii) The Finance Act, 2008 has now amended section 292C with retrospective effect from 1.6.2002 to extend this presumption also to books of account, other documents, etc., found in the possession or control of any person in the course of a survey operation.
 - (iv) 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 with retrospective effect from 1st October, 1975.

Note – Similar amendment has been made in section 42D of the Wealth-tax Act, which provides for a rebuttable presumption with respect to books of account, other documents, articles or things including money found in the possession or control of any person in the course of a search under section 37A. 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 37B with retrospective effect from 1st October, 1975.

II. WEALTH-TAX ACT, 1957

Power of Commissioner to grant immunity from penalty and prosecution [Section 18BA & 35GA]

Related amendment in sections: 17A & 23A

- (i) The Finance Act, 2008 has introduced certain provisions regarding immunity from penalty and prosecution. Also, the time limit for assessment relating to abatement of settlement proceedings has been provided.
- (ii) Wide-ranging amendments were made last year to the system of settlement of cases, which also provided for abatement of proceedings before the Settlement Commission under various circumstances. The Commissioner has now been empowered to grant immunity from penalty and prosecution in cases which abate.
- (iii) Section 18BA has been inserted to empower 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.
- (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.
- (iv) Section 35GA has been introduced to empower 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.

- (v) Section 23A(9) provides that 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. Sub-section (9A) has been inserted in section 23A to empower 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, 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.
 (Effective from A.Y.2008-09)
- (vi) Further, section 17A has been amended retrospectively w.e.f. 1.6.2007 to allow 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.
 (Effective retrospectively from 1.6.2007)

NOTIFICATIONS / CIRCULARS ISSUED BETWEEN 1.5.2007 AND 30.4.2008

NOTIFICATIONS

1. NOTIFICATION NO. 208 / 2007, DATED 27-6-2007

Rule 6DD of the Income-tax Rules has been substituted. This Rule now provides for cases and circumstances in which payment in a sum exceeding twenty thousand rupees may be made otherwise than by an account payee cheque drawn on a bank or account payee bank draft.

As per this rule, no disallowance under clause (a) of sub-section (3) of section 40A shall be made and no payment shall be deemed to be the profits and gains of business or profession under clause (b) of sub-section (3) of section 40A where any payment in a sum exceeding twenty thousand rupees is made otherwise than by an account payee cheque drawn on a bank or account payee bank draft in the cases and circumstances specified hereunder, namely:

- (a) where the payment is made to
 - (i) the Reserve Bank of India or any banking company;
 - (ii) the State Bank of India or any subsidiary bank;
 - (iii) any co-operative bank or land mortgage bank;
 - (iv) any primary agricultural credit society or any primary credit society;
 - (v) the Life Insurance Corporation of India;
- (b) where the payment is made to the Government and, under the rules framed by it, such payment is required to be made in legal tender;
- (c) where the payment is made by
 - (i) any letter of credit arrangements through a bank;
 - (ii) a mail or telegraphic transfer through a bank;
 - (iii) a book adjustment from any account in a bank to any other account in that or any other bank;
 - (iv) a bill of exchange made payable only to a bank;
 - (v) the use of electronic clearing system through a bank account;
 - (vi) a credit card;
 - (vii) a debit card.
- (d) where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee;
- (e) where the payment is made for the purchase of -

- (i) agricultural or forest produce; or
 - (ii) the produce of animal husbandry (including livestock, meat, hides and skins) or dairy or poultry farming; or
 - (iii) fish or fish products; or
 - (iv) the products of horticulture or apiculture,
- to the cultivator, grower or producer of such articles, produce or products;
- (f) where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products;
 - (g) where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, profession or vocation, in any such village or town;
 - (h) where any payment is made to an employee of the assessee or the heir of any such employee, on or in connection with the retirement, retrenchment, resignation, discharge or death of such employee, on account of gratuity, retrenchment compensation or similar terminal benefit and the aggregate of such sums payable to the employee or his heir does not exceed fifty thousand rupees;
 - (i) where the payment is made by an assessee by way of salary to his employee after deducting the income-tax from salary in accordance with the provisions of section 192 of the Act, and when such employee -
 - (i) is temporarily posted for a continuous period of fifteen days or more in a place other than his normal place of duty or on a ship; and
 - (ii) does not maintain any account in any bank at such place or ship;
 - (j) where the payment was required to be made on a day on which the banks were closed either on account of holiday or strike;
 - (k) where the payment is made by any person to his agent who is required to make payment in cash for goods or services on behalf of such person;
 - (l) where the payment is made by an authorised dealer or a money changer against purchase of foreign currency or travellers cheques in the normal course of his business.

2. NOTIFICATION NO. 213/2007, DATED 3-8-2007

Section 2(48) defining zero coupon bonds requires that such bonds should be notified by the Central Government. Accordingly, the Central Government has, vide Notification No. 213/2007 dated 3.8.2007, specified the 15 year zero coupon bonds of Power Finance Corporation (PFC), to be issued on or before 31.3.2009, as zero coupon bonds for the purposes of section 2(48).

3. NOTIFICATION NO. 214/2007, DATED 3-8-2007

The Central Government has, vide notification no.214/2007 dated 3.8.2007 specified the cost inflation index for the financial year 2007-08. The CII for F.Y. 2007-08 is 551.

S. No.	Financial Year	Cost Inflation Index
1.	1981-82	100
2.	1982-83	109
3.	1983-84	116
4.	1984-85	125
5.	1985-86	133
6.	1986-87	140
7.	1987-88	150
8.	1988-89	161
9.	1989-90	172
10.	1990-91	182
11.	1991-92	199
12.	1992-93	223
13.	1993-94	244
14.	1994-95	259
15.	1995-96	281
16.	1996-97	305
17.	1997-98	331
18.	1998-99	351
19.	1999-2000	389
20.	2000-01	406
21.	2001-02	426
22.	2002-03	447
23.	2003-04	463
24.	2004-05	480
25.	2005-06	497
26.	2006-07	519
27.	2007-08	551

4. NOTIFICATION NO. 262/2007, DATED 16-10-2007

Rule 117C has been inserted in the Income-tax Rules, 1962 to empower the Tax Recovery Officer to exercise or perform certain powers and functions of an Assessing Officer.

The Chief Commissioner or the Commissioner, by general or special order in writing, may authorise a Tax Recovery Officer to exercise or perform the powers and functions conferred on or assigned to an Assessing Officer under section 154 for rectifying any mistake apparent from record in respect of an order passed by the Assessing Officer consequent to which a sum is payable and the Tax Recovery Officer has drawn a Certificate under section 222 in respect of such sum. The Tax Recovery Officer shall exercise or perform such powers and functions concurrently with the Assessing Officer.

5. NOTIFICATION NO. 264/2007, DATED 23-10-2007

Valuation of specified security or sweat equity share being a share in the company for the purpose of levy of fringe benefit tax (FBT).

The Finance Act, 2007 has amended the provisions of the Income-tax Act to provide that employers will be liable to pay fringe benefit tax on the value of ESOPs granted to employees as and when the ESOPs were allotted or transferred to the employees. The value of ESOPs for the purposes of levy of FBT shall be the fair market value of the ESOPs on the date of vesting of the options as reduced by the amount actually paid, or recovered from, the employee.

Explanation (i) to clause (ba) of sub-section (1) of section 115WC of the Income-tax Act defines fair market value to mean the value determined in accordance with the method as may be prescribed by the Board. Accordingly, a new Rule 40C has been inserted in the Income-tax Rules for this purpose.

The new Rule 40C, which will take effect from the 1st April, 2008 and will, accordingly, apply in relation to the assessment year 2008-09 and subsequent years, provides as follows -

- (1) For the purposes of clause (ba) of sub-section (1) of section 115WC, the fair market value of any specified security or sweat equity share, being an equity share in a company, on the date on which the option vests with the employee, shall be determined in the manner laid down in (2) and (3) below.
- (2) In a case where, on the date of the vesting of the option, the share in the company is listed on a recognized stock exchange, the fair market value shall be the average of the opening price and closing price of the share on that date on the said stock exchange. However, where, on the date of vesting of the option, the share is listed on more than one recognized stock exchanges, the fair market value shall be the average of opening price and closing price of the share on the recognised stock exchange which records the highest volume of trading in the share.

Further, if, on the date of vesting of the option, there is no trading in the share on any recognized stock exchange, the fair market value shall be -

- (a) the closing price of the share on any recognised stock exchange on a date closest to the date of vesting of the option and immediately preceding such date; or
 - (b) the closing price of the share on a recognised stock exchange, which records the highest volume of trading in such share, if the closing price, as on the date closest to the date of vesting of the option and immediately preceding such date, is recorded on more than one recognized stock exchange.
- (3) In a case where, on the date of vesting of the option, the share in the company is not listed on a recognized stock exchange, the fair market value shall be such value of the share in the company as determined by a merchant banker [Category I merchant banker registered with SEBI] on the specified date [i.e. the date of vesting of the option or any date earlier than the date of the vesting of the option, not being a date which is more than 180 days earlier than the date of the vesting].
- (4) Closing price of a share on a recognised stock exchange on a date shall be the price of the last settlement on such date on such stock exchange. However, where the stock exchange quotes both buy and sell prices, the closing price shall be the sell price of the last settlement.
- (5) Opening price of a share on a recognised stock exchange on a date shall be the price of the first settlement on such date on such stock exchange. However, where the stock exchange quotes both buy and sell prices, the opening price shall be the sell price of the first settlement.
- (6) "Specified date" means –
- (i) the date of vesting of the option;
 - (ii) any date earlier than the date of vesting of the option, not being a date which is more than 180 days earlier than the date of vesting.
6. NOTIFICATION NO. 271/2007 DATED 7-11-2007

The Finance Act, 2007 has introduced a deeming provision to define concession in the matter of rent by inserting Explanations to section 17(2)(ii) with retrospective effect from 1.4.2006, that is, with effect from assessment year 2006-07. This has necessitated reduction of rates in case of both rent free and concessional rent accommodations and leased accommodation in Table I of rule 3 with retrospective effect from 1st April, 2006, that is, in relation to assessment year 2006-07 and subsequent years. The amendment has taken place in valuation of perquisite of unfurnished accommodation (rent free and concessional) provided to other than Government employees.

Employee	Value of perquisite
Where the accommodation is owned by the employer.	Where accommodation is provided in a city where population as per 2001 census is: (a) 10 lakh or less – 7.5% of salary; (b) More than 10 lakh upto 25 lakh -10% of salary. (c) More than 25 lakh – 15% of salary in respect of the period during which the said accommodation was occupied by the employee during the previous year as reduced by the rent, if any, actually paid by the employee.
Where the accommodation is taken on lease or rent by the employer and provided to the employee	The value of perquisite would be the lower of the following: (a) Actual amount of lease rental paid or payable by the employer ; or (b) 15% of salary. This value would be reduced by the rent, if any, actually paid by the employee.

Further, the Finance Act, 2005 had inserted a new Chapter XII-H in the Act, relating to levy of fringe benefit tax on the employer with effect from 1st April, 2006, i.e., applicable for assessment year 2006-07 and subsequent years. Accordingly, rule 3 was amended vide notification number S.O. 265(E) dated the 28th February, 2005, to avoid double taxation on certain items.

Since, Chapter XII-H relating to Fringe Benefit Tax, as provided in the Finance Act, 2005, is not applicable to the employer, being an individual or a Hindu undivided family or any fund or trust or institution eligible for exemption under clause (23C) of section 10 or registered under section 12AA, rule 3 is required to be amended so as to include valuation of perquisite in case of benefits provided by such employers to its employees. Accordingly, sub-rules 2, 6, 7 (ii), (iii), (iv), (v) and (vi) have been inserted to provide for such valuation. Sub-rule 7(ix) has been inserted to provide for valuation of any other benefit or amenity, etc. in residual cases relating to any employer. These sub-rules will take effect from 1st April, 2008 and will, accordingly, apply in relation to A.Y.2008-09 and subsequent years.

The following perquisites provided by an employer, who is not liable to pay fringe benefit tax under Chapter-XIIH, shall be chargeable to tax in the hands of the employee under the head "Salaries".

Motor Car - Rule 3(2)

Sl. No.	Circumstances	Where cubic capacity of engine does not exceed 1.6 litres	Where cubic capacity of engine exceeds 1.6 litres
(1)	(2)	(3)	(4)
(1)	Where the motor car is owned or hired by the employer and (a) is used wholly and exclusively in the performance of his official duties; (b) is used exclusively for the private or personal purposes of the employee or any member of his household and the running and maintenance expenses are met or reimbursed by the employer; (c) is used partly in the performance of duties and partly for private or personal purposes of his own or any member of his household and	No value, provided the documents specified in Note 2 below this table are maintained by the employer. Actual amount of expenditure incurred by the employer on the running and maintenance of motor car during the relevant previous year including remuneration, if any, paid by the employer to the chauffeur as increased by the amount representing normal wear and tear of the motor car and as reduced by any amount charged from the employee for such use.	No value, provided the documents specified in Note 2 below this table are maintained by the employer. Actual amount of expenditure incurred by the employer on the running and maintenance of motor car during the relevant previous year including remuneration, if any, paid by the employer to the chauffeur as increased by the amount representing normal wear and tear of the motor car and as reduced by any amount charged from the employee for such use.

	(i) the expenses on maintenance and running are met or reimbursed by the employer, (ii) the expenses on running and maintenance for such private or personal use are fully met by the assessee.	Rs.1,200 (plus Rs.600, if chauffeur is also provided to run the motor car) Rs.400 (plus Rs.600, if chauffeur is provided by the employer to run the motor car)	Rs.1,600 (plus Rs.600, if chauffeur is also provided to run the motor car) Rs.600 (plus Rs.600, if chauffeur is also provided to run the motor car)
(2)	Where the employee owns a motor car but the actual running and maintenance charges (including remuneration of the chauffeur, if any) are met or reimbursed to him by the employer and (i) such reimbursement is for the use of the vehicle wholly and exclusively for official purposes, (ii) such reimbursement is for the use of the vehicle partly for official purposes and partly for personal or private purposes of the employee or any member of his household.	No value, provided that the documents specified in Note 2 below this table are maintained by the employer. The actual amount of expenditure incurred by the employer as reduced by Rs.1,200 (plus Rs.600, if chauffeur is also provided to run the motor car). However, the documents specified in Note 2 below this table should be maintained by the employer.	No value, provided that the documents specified in Note 2 below this table are maintained by the employer. The actual amount of expenditure incurred by the employer as reduced by Rs.1,600 (plus Rs.600, if chauffeur is also provided to run the motor car). However, the documents specified in Note 2 below this table should be maintained by the employer.

(3)	Where the employee owns any other automotive conveyance but the actual running and maintenance charges are met or reimbursed to him by the employer and (i) such reimbursement is for the use of the vehicle wholly and exclusively for official purposes, (ii) such reimbursement is for the use of the vehicle partly for official purposes and partly for personal or private purposes of the employee.	No value, provided that the documents specified in Note 2 below this table are maintained by the employer. The actual amount of expenditure incurred by the employer as reduced by an amount of Rs.600, provided the documents specified in Note 2 below this table are maintained by the employer.	Not applicable
-----	---	---	----------------

Note -

- (1) Where one or more motor-cars are owned or hired by the employer and the employee or any member of his household are allowed the use of such motor-car or all or any of such motor-cars (otherwise than wholly and exclusively in the performance of his duties), the value of perquisite shall be the amount calculated in respect of one car in accordance with Sl. No. (1)(c)(i) of the above Table as if the employee had been provided one motor-car for use partly in the performance of his duties and partly for his private or personal purposes and the amount calculated in respect of the other car or cars in accordance with Sl. No. (1)(b) of the above Table as if he had been provided with such car or cars exclusively for his private or personal purposes.
- (2) Where the employer or the employee claims that the motor-car is used wholly and exclusively in the performance of official duty or that the actual expenses on the running and maintenance of the motor-car owned by the employee for official purposes is more than the amounts deductible in Sl. No. 2(ii) or 3(ii) of the above Table, he may claim a higher amount attributable to such official use and the value of perquisite in such a case

shall be the actual amount of charges met or reimbursed by the employer as reduced by such higher amount attributable to official use of the vehicle provided that the following conditions are fulfilled:

- (a) the employer has maintained complete details of journey undertaken for official purpose which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon;
 - (b) the employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.
- (3) The normal wear and tear of a motor-car shall be taken at 10 per cent per annum of the actual cost of the motor-car or cars.

Free or concessional tickets [Sub-rule (6) of Rule 3]

The value of any benefit or amenity resulting from the provision by an employer (who is not liable to pay FBT) engaged in the carriage of passengers or goods to any employee or to any member of his household for personal or private journey free of cost or concessional fare in any conveyance owned, leased or made available by any other arrangement shall be the value at which such benefit or amenity is offered by such employer to the public. Any amount recovered from the employee for such benefit or amenity shall be reduced in determining the value of the perquisite.

However, this sub-rule shall not apply to the employees of an airline or the railways.

Travelling, touring and accommodation [Sub-rule 7(ii) of Rule 3]

The value of travelling, touring, stay and other expenses borne by the employer for any holiday availed by the employee or any member of his household shall be the amount of the expenditure incurred by the employer. This provision applies in respect of trips other than those which are exempt under section 10(5) read with Rule 2B. If the facility is maintained by the employer and it is not available uniformly to all employees, the value of benefit shall be taken to be the value at which such facilities are offered by other agencies to the public.

Where the employee is on official tour and the expenses are incurred in respect of any member of his household accompanying him, the amount of expenditure so incurred shall also be a fringe benefit or amenity. However, if the official tour is extended as a vacation, the value of such fringe benefit will be limited to the expenses incurred in relation to such extended period of stay or vacation. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity.

Free or concessional food and non-alcoholic beverages [Sub-rule 7(iii) of Rule 3]

The value of free food and non-alcoholic beverages provided by the employer shall be the amount of expenditure incurred by the employer as reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity. However, the following shall not be chargeable as perquisites:

- (a) Free food and non-alcoholic beverages provided by the employer during the working hours at office or business premises up to Rs.50 per meal;
- (b) Free food and non-alcoholic beverages provided through paid vouchers which are not transferable and usable only at eating joints if the value thereof is up to Rs.50 per meal;
- (c) Tea or snacks provided during working hours; and
- (d) Free food and non-alcoholic beverages during working hours provided in a remote area or an offshore installation.

Value of gift, voucher or token in lieu of such gift [Sub-rule 7(iv) of Rule 3]

The value of any gift, or voucher or token in lieu of which such gift may be received by the employee or by member of his household on ceremonial occasions or otherwise from the employer shall be the sum equal to the amount of such gift. If the value of such gift, voucher or token is below Rs. 5,000 in the aggregate during the previous year, the value of perquisite shall be taken as nil.

Credit card expenses [Sub-rule 7(v) of Rule 3]

The amount of expenses including membership fees and annual fees incurred by the employee or any member of his household which is charged to a credit card (including add-on-card) provided by the employer or otherwise, paid for or reimbursed by the employer shall be taken to be the value of perquisite chargeable to tax. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity. However, such expenses incurred wholly and exclusively for official purposes would not be treated as a perquisite if the following conditions are satisfied:

- (a) complete details in respect of such expenditure are maintained by the employer which may, inter alia, include the date of expenditure and the nature of expenditure;
- (b) the employer gives the certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties;

Club expenditure [Sub-rule 7(vi) of Rule 3]

If employer reimburses or makes payment of any expenditure incurred in a club including the amount of annual or periodical fee for the employee or any member of household, the actual amount of such expenditure shall be the value of perquisite. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity. Where the employer has obtained corporate membership of the club and the facility is enjoyed by the employee or any member of his household, the value of perquisite shall not include the initial fee paid for acquiring such corporate membership.

If the employer provides uniformly to all employees the use of health club, sports and similar facilities, there will be no taxable perquisite in respect of such facilities. Besides, there will be no taxable perquisite if the club expenditure is incurred wholly and exclusively for business

purposes and the following conditions are fulfilled:

- (a) complete details in respect of such expenditure are maintained by the employer which may, inter alia, include the date of expenditure and the nature of expenditure and its business expediency;
- (b) the employer gives a certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties.

Other benefit or amenity [Sub-rule 7(ix) of Rule 3]

The value of any other benefit or amenity, service, right or privilege provided by the employer shall be determined on the basis of cost to the employer under an arms' length transaction as reduced by the employee's contribution, if any. However, there will be no taxable perquisite in respect of expenses on telephones including mobile phone actually incurred on behalf of the employee by the employer i.e., if an employer pays or reimburses telephone bills or mobile phone charges of employee, there will be no taxable perquisite.

7. NOTIFICATION NO. 281/2007, DATED 27-11-2007

The Finance Act, 2007 inserted a new section 80-ID in the Income-tax Act, 1961 to provide for a 100% deduction of the profits and gains derived by an undertaking from the business of operating a hotel or from the business of building, owning and operating a convention centre in a specified area subject to the conditions prescribed therein.

Clause (a) of sub-section (6) of section 80-ID of the said Act defines a 'convention centre' as a building of prescribed area and having such other facilities as may be prescribed. Accordingly, a new rule 18DE and a new form 10CCBBA have been inserted in the Income-tax Rules for this purpose.

Rule 18DE prescribes the following conditions to be fulfilled in order to avail deduction under section 80-ID:

- (a) the convention centre shall have a minimum covered plinth area of 25,000 sq. mts;
- (b) it shall have minimum of 3,000 seating capacity;
- (c) there shall be minimum of 10 convention halls;
- (d) the convention centre shall have convention halls, whether called conference halls or seminar halls or auditorium for holding seminars and conferences;
- (e) each convention hall of the convention centre shall be equipped with modern public address system, slide and power-point projection system and LCD projector or video screening facility;
- (f) the convention centre shall have a documentation centre with computers and printers, telephone with STD or ISD facilities, e-mail, photocopy and scanning facility along with trained operators to provide these facilities;

- (g) the convention centre shall be completely centrally air-conditioned;
- (h) the convention centre shall have adequate parking facility and other public convenience as per local building regulations and should also fulfill all local building regulations in respect of fire and safety.

In addition to the above facilities, the convention centers may have the following:

- (a) an amphitheatre and landscaped open spaces for outdoor conference or seminar related activities;
- (b) a kitchen, dining facility, cafeteria or restaurant only to support events in the convention centre.

The new rule 18DE and the new form 10CCBBA will take effect from 1st April, 2008 and will, accordingly, apply in relation to A.Y.2008-09 and subsequent years.

8. NOTIFICATION NO. 2/2008, DATED 8-1-2008

The CBDT has substituted the existing Rule 18C with new Rule 18C, which lays down the following eligibility criteria for Industrial Parks to claim benefit under section 80-IA (4)(iii) -

- (1) The undertaking should begin to develop, develop and operate or maintain and operate an industrial park any time during the period from 1.4.2006 to 31.3.2009.
- (2) The undertaking and the Industrial Park should be notified by the Central Government under the Industrial Park Scheme, 2008.
- (3) The undertaking should continue to fulfill the conditions envisaged in the Industrial Park Scheme, 2008.

9. NOTIFICATION NO. 6/2008, DATED 14-1-2008

Section 10(15)(vii) exempts interest on bonds issued by a local authority or by a State Pooled Finance Entity and notified by the Central Government in the Official Gazette. Accordingly, the Central Government has specified the "Tax-free Pooled Finance Development Bonds" under Pooled Finance Development Fund Scheme of Government of India, interest from which would be exempt under section 10(15)(vii).

10. NOTIFICATION NO. 7/2008, DATED 15-1-2008

As per section 10(39), any specified income arising from any notified international sporting event held in India, to the person or persons notified by the Central Government in the Official Gazette, is exempt from tax. Accordingly, in exercise of the powers conferred by section 10(39), the Central Government has notified the following:

- (a) the Commonwealth Games Federation, London, United Kingdom as the person,
- (b) the Commonwealth Games 2010 to be held in India, as the international sporting event,
- (c) the income arising to Commonwealth Games Federation from Commonwealth Games 2010 on account of Host Fee, received or receivable from the Organising Committee

Commonwealth Games 2010 Delhi, India amounting to 7.3 million GBP, as the specified income,

for the purposes of exemption under section 10(39).

11. NOTIFICATION NO. 11/2008, DATED 18-1-2008

The Finance Act, 2007 has amended the provisions of the Income-tax Act to provide that employers will be liable to pay fringe benefit tax on the value of ESOPs granted to employees as and when the specified security or sweat equity share were allotted or transferred to the employees. The value of ESOPs for the purposes of levy of FBT would be the fair market value of the specified security or sweat equity share on the date of vesting of the options as reduced by the amount actually paid, or recovered from, the employee.

Explanation (i) to clause (ba) of sub-section (1) of section 115WC of the Income-tax Act defines fair market value to mean the value determined in accordance with the method as may be prescribed by the Board. A new rule 40D has been inserted in the Income-tax Rules w.e.f. A.Y.2008-09 for the purposes of valuation of specified security not being an equity share in the company.

As per new Rule 40D, for the purposes of section 115WC(1)(ba), the fair market value of any specified security, not being an equity share in a company, on the date on which the option vests with the employee, shall be such value as determined by a merchant banker on the specified date.

12. NOTIFICATION NO. 20/2008, DATED 5-2-2008

The CBDT has inserted new Rule 14B, which lays down the guidelines for the purposes of determining expenses for audit under section 142(2A).

The said notification 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.

13. NOTIFICATION NO. 21/2008, DATED 5-2-2008

Section 36(1)(xii) provides that deduction shall be allowed in respect of any expenditure (not being a capital expenditure) incurred by a corporation or a body corporate, by whatever name called, if such corporation or a body corporate is, inter alia, notified by the Central Government in the Official Gazette. Accordingly, the Central Government has notified the Oil Industry Development Board for the purpose of deduction under section 36(1)(xii), w.e.f. A.Y.2008-09.

14. NOTIFICATION NO. 23/2008, DATED 6-2-2008

Section 2(48) defining zero coupon bonds requires that such bonds should be notified by the Central Government. Accordingly, the Central Government has, vide this Notification, specified the 10 year zero coupon bonds of National Housing Bank (NHB), to be issued on or before 31.3.2009, as zero coupon bonds for the purposes of section 2(48).

15. NOTIFICATION NO. 34/2008, DATED 13-3-2008

The CBDT has inserted a new Rule 125 which has made electronic payment of taxes (including interest and penalty) by corporate assessees and assessees subject to tax audit mandatory on or after 1st April 2008. Electronic payment of taxes means payment of taxes by way of internet banking facility or credit or debit cards.

16. NOTIFICATION NO. 45/2008, DATED 24-3-2008

The CBDT has inserted a new Rule 8D which lays down the method for determining amount of expenditure in relation to income not includible in total income.

If the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with –

- (a) the correctness of the claim of expenditure by the assessee; or
- (b) the claim made by the assessee that no expenditure has been incurred in relation to exempt income for such previous year,

he shall determine the amount of expenditure in relation to such income in the manner provided hereunder -

The expenditure in relation to income not forming part of total income shall be the aggregate of the following:

- (i) the amount of expenditure directly relating to income which does not form part of total income;
- (ii) in a case where the assessee has incurred expenditure by way of interest during the previous year which is not directly attributable to any particular income or receipt, an amount computed in accordance with the following formula, namely :

$$A \times \frac{B}{C}$$

Where,

A = amount of expenditure by way of interest other than the amount of interest included in clause (i) incurred during the previous year;

B = the average of value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

C = the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year;

- (iii) an amount equal to one-half per cent of the average of the value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.

'Total assets' means total assets as appearing in the balance sheet excluding the increase on account of revaluation of assets but including the decrease on account of revaluation of assets.

CIRCULARS

1. CIRCULAR NO.4/2007 DATED 15.6.2007

This Circular provides the tests for distinction between shares held as stock-in-trade and shares held as investment.

The Income Tax Act, 1961 makes a distinction between a capital asset and a trading asset. Capital asset is defined in section 2(14). Long-term capital assets and gains are dealt with under section 2(29A) and section 2(29B). Short-term capital assets and gains are dealt with under section 2(42A) and section 2(42B). Trading asset is dealt with under section 28.

The Central Board of Direct Taxes (CBDT) had, through Instruction No.1827 dated August 31, 1989, brought to the notice of the Assessing Officers that there is a distinction between shares held as investment (capital asset) and shares held as stock-in-trade (trading asset). In the light of a number of judicial decisions pronounced after the issue of the above instructions, the same have been further updated for the information of assesseees as well as for guidance of the Assessing Officers.

- (1) The Supreme Court, in, CIT (Central), Calcutta vs Associated Industrial Development Company (P) Ltd 82 ITR 586, observed that:

"Whether a particular holding of shares is by way of investment or forms part of the stock-in-trade is a matter which is within the knowledge of the assessee who holds the shares and it should, in normal circumstances, be in a position to produce evidence from its records as to whether it has maintained any distinction between those shares which are its stock-in-trade and those which are held by way of investment."

- (2) In the case of CIT, Bombay vs H. Holck Larsen 160 ITR 67, the Supreme Court observed that:

"The High Court, in our opinion, made a mistake in observing whether transactions of sale and purchase of shares were trading transactions or whether these were in the nature of investment was a question of law. This was a mixed question of law and fact."

- (3) The Authority for Advance Rulings (AAR) 288 ITR 641, referring to the decisions of the Supreme Court in several cases, has culled out the following principles :-
- (i) where a company purchases and sells shares, it must be shown that they were held as stock-in-trade and that existence of the power to purchase and sell shares in the memorandum of association is not decisive of the nature of transaction;
 - (ii) the substantial nature of transactions, the manner of maintaining books of accounts, the magnitude of purchases and sales and the ratio between purchases and sales and the holding would furnish a good guide to determine the nature of transactions;
 - (iii) ordinarily the purchase and sale of shares with the motive of earning a profit, would result in the transaction being in the nature of trade/adventure in the nature of trade; but where the object of the investment in shares of a company is to derive income by way of dividend etc. then the profits accruing by change in such investment (by sale of shares) will yield capital gain and not revenue receipt.

It is possible for a tax payer to have two portfolios, i.e., an investment portfolio comprising of securities which are to be treated as capital assets and a trading portfolio comprising of stock-in-trade which are to be treated as trading assets. Where an assessee has two portfolios, the assessee may have income under both heads i.e., capital gains as well as business income.

The above principles would help in determining whether, in a given case, the shares are held by the assessee as investment (and therefore giving rise to capital gains) or as stock-in-trade (and therefore giving rise to business profits). It is to be noted that no single principle would be decisive and the total effect of all the principles should be considered to determine whether, in a given case, the shares are held by the assessee as investment or stock-in-trade.

2. CIRCULAR NO. 6/2007, DATED 11-10-2007

This Circular is to clarify the issue of allowability of the claim of harvesting and transportation expenses incurred by the Co-operative sugar mills for procuring sugarcane from farmers, who are members of such Co-operative Sugar Mills and who are bound under an agreement to supply the sugarcane exclusively to the concerned sugar Mill.

The issue of allowability of such expenses in the case of Co-operative Sugar Mills has been examined by the CBDT. These expenses are incurred by the Sugar Mills for ensuring an adequate and sustained supply of freshly cut sugarcane that is an essential input for the continuous running of such Mills. These expenses are, therefore, incurred for commercial expediency and are prima facie wholly and exclusively for the purpose of business. Such expenses are, therefore, allowable in the computation of the income of the Co-operative Sugar Mills.

3. CIRCULAR NO. 1/2008, DATED 10-1-2008

This Circular 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 provisions of section 194-C would be applicable to the amounts paid as cooling charges by the customers of the cold storage.

4. CIRCULAR NO. 2/2008, DATED 22-2-2008

Securities and Exchange Board of India (SEBI) vide Circular No. MRD/DoP/SE/DEP/Cir. 14/2007, dated 20-12-2007, has decided to permit all classes of investors (individuals, institutional, etc.) to short sell. Further, with a view to provide a mechanism for borrowing of securities to enable settlement of securities sold short, SEBI has also decided to put in place a full-fledged Securities Lending and Borrowing (SLB) Scheme for all market participants in the Indian securities market under the overall framework of Securities Lending Scheme, 1997 of SEBI.

In this context, the following taxation issues have arisen in respect of transactions under the scheme of securities lending -

- (i) Would the lending/borrowing of securities under the Securities Lending Scheme amount to a transfer under section 2(47) in the hands of the lender?
- (ii) Would lending/borrowing of the securities be subject to Securities Transaction Tax (STT)?

The Lending and Borrowing of Securities under the new scheme notified by SEBI vide Circular No. MRD/DoP/SE/DEP/Cir.14/2007, dated 20-12-2007 is in accordance with the overall framework of the Securities Lending Scheme of 1997. Accordingly, the provisions of section 47(xv) will be equally applicable in respect of the transactions under the new scheme.

Securities Transaction Tax (STT) is levied on purchase or sale of an equity share, unit and derivative, under such circumstances as specified in section 98 of the Finance (No. 2) Act, 2004. The transactions in the nature of lending and borrowing under the new scheme do not fall within the scope of section 98 to the Finance (No.2) Act, 2004. Therefore, the transactions of lending and borrowing are not liable to Securities Transaction Tax (STT).

5. CIRCULAR NO. 4/2008, DATED 28-4-2008

This Circular 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.

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.

6. CIRCULAR NO. 9/2007, DATED 20-12-2007

Explanatory circular on Fringe Benefit Tax arising on allotment or transfer of specified securities or sweat equity shares

1. In terms of the provisions of Chapter XII-H of the Income-tax Act, an employer, being a company, is liable to pay Fringe Benefit Tax (FBT) in respect of the fringe benefits provided or deemed to have been provided by it to its employees, directly or indirectly, during the previous year.

With a view to bring grant of stock options by employers to employees within the purview of FBT, Finance Act, 2007 has inserted a new clause (d) in section 115WB(1). The salient features of this provision are:-

- (i) FBT shall apply in all cases where any specified security or sweat equity shares has been allotted or transferred by the employer to his employees;
- (ii) FBT shall be payable in the previous year in which such allotment or transfer has taken place;
- (iii) the provisions of this new clause shall apply even if the allotment or transfer is made directly or indirectly;
- (iv) the provisions of this new clause shall apply even if the allotment or transfer is free of cost or at concessional rate;

- (v) the provisions of this new clause shall apply even if the allotment or transfer is to current or former employee or employees;
- (vi) the provisions of this new clause shall apply in cases where the allotment or transfer is on or after 1st April, 2007.

The expressions specified security and sweat equity shares have also been defined. The value of fringe benefit is subjected to FBT at the prevailing rate, which is currently 30% plus surcharge plus education cess.

2. Method of computation of the value of the fringe benefit

Under the existing provisions contained in section 115WC, the method of computation of the value of fringe benefits referred to in section 115WB has been provided. A new clause (ba) has been inserted in sub-section (1) of the said section 115WC to provide for computation of fringe benefit related to allotment or transfer of specified security or sweat equity shares by employers to employees.

It has been provided that the value of fringe benefit in such cases shall be determined in accordance with the formula -

$A - B$

Where,

A = the Fair Market Value (FMV) of the specified security or sweat equity shares on the date of vesting of the option. Such value has to be determined in accordance with the method as may be prescribed by the CBDT; and

B = the amount, if any, actually paid by, or recovered from the employee;

Option means a right but not an obligation granted to an employee to apply for the specified security or sweat equity shares at a predetermined price.

The CBDT has, vide notification S.O. number 1805(E) dated 23rd October, 2007, inserted Rule 40C in the Income-tax Rules, which has prescribed the method for determination of fair market value of specified security or sweat equity share, being a share in the company [See Notification No.264/2007 dated 23.10.2007 given under Notifications].

3. Determination of the cost of acquisition for capital gains purposes

Consequent to insertion of clause (ba) in sub-section (1) of section 115WC providing for the valuation of fringe benefits referred to in clause (d) of sub-section (1) of section 115WB, a new sub-section (2AB) has been inserted in section 49.

This new sub-section provides that the cost of acquisition of specified security or sweat equity shares shall be the fair market value which has been taken into account while computing the value of fringe benefit under the new clause (ba) of sub-section (1) of section 115WC.

4. Determination of the period of holding

A new sub-clause (hb) has also been inserted in clause (i) of Explanation 1 to clause (42A) of section 2. This new sub-clause provides that the period of holding in case of such specified security or sweat equity shares, in the hand of the employee, shall be reckoned from the date of allotment or transfer of such security or shares.

5. Recovery of FBT by the employer from its employee

A new section 115WK has also been inserted enabling the employer to recover the fringe benefit tax from the employee in respect of specified security or sweat equity shares, if such security or shares are transferred or allotted to the employee on or after 1st April, 2007.

It has been prescribed that the employer can vary the agreement or scheme under which such specified security or sweat equity shares has been allotted or transferred. The agreement or scheme can be varied with a purpose to recover from the employee the fringe benefit tax to the extent to which such employer is liable to pay the fringe benefit tax in relation to the allotment or transfer of such specified security or sweat equity shares to such employee.

6. Illustration

The above amendments are explained with the help of an illustration.

A company X grants option to its employee R on 1st April, 2004 to apply for 100 shares of the company at a pre-determined price of Rs.50 per share with date of vesting of the option being 1st April, 2006 and exercise period being 1st April, 2006 to 31st March, 2010.

Employee R exercises his option on 31st March, 2007 and shares are allotted/transferred to him on 3rd April, 2007. On 25th October, 2007, these shares are sold for Rs.200/- each. On the date of vesting of the option, fair market value of the share was Rs.80/- per share. The tax implication of above situation will be as under:-

Since shares are allotted or transferred on or after 1st April, 2007, provisions of fringe benefit tax are attracted. Fringe benefit with respect to employee R is $(Rs.80 - Rs.50) \times 100 = Rs. 3,000$.

Company X will pay fringe benefit tax on Rs.3,000.

Cost of acquisition in the hands of employee R = Rs.80 per share

Capital gain = $(Rs.200 - Rs.80) \times 100 = Rs.12,000$

Period of holding = 3rd April, 2007 to 25th October, 2007 i.e., less than 12 months. Hence, the amount of Rs.12,000 will be charged to tax as short term capital gain.

7. Frequently Asked Questions

1. Whether a foreign company is liable to pay FBT on shares allotted or transferred to the employees of its Indian subsidiary?

In terms of the provisions of Chapter XII-H of the Act, an employer, being a company, is liable to pay FBT in respect of the fringe benefits provided or deemed to have been provided by it to its employees, directly or indirectly, during the previous year. Since the shares are allotted or transferred to employees of the Indian subsidiary, by virtue of their employment with the subsidiary company, the liability to pay fringe benefit tax on such shares vests upon the Indian subsidiary and not on the foreign company.

2. Whether charge back of costs by the foreign company to the Indian subsidiary is relevant to determine the obligation of the Indian company to pay FBT?

As stated in answer No.1, the Indian subsidiary is liable to fringe benefit tax irrespective of whether or not there is a charge back of cost by the foreign holding company.

3. Will FBT apply in case of employees of the Indian subsidiary for shares awarded by the foreign holding company if the employees of the Indian subsidiary are allotted or transferred shares while outside India?

In the answer to Question No.20 of CBDT Circular No.8/2005 dated 29.8.2005, it has been clarified that an employer is liable to fringe benefit tax on the value of fringe benefits provided or deemed to have been provided to employees based in India. Therefore, an Indian subsidiary would be liable to pay FBT in respect of the value of the shares allotted or transferred by the foreign holding company if the employee was based in India at any time during the period beginning with the grant of the option and ending with the date of vesting of such option (hereafter such period is referred to as grant period), irrespective of the place of location of the employee at the time of allotment or transfer of such shares.

4. How will the value of fringe benefit be determined in case where the employee was based in India only for a part of the grant period?

In a case where the employee was based in India only for a part of grant period, a proportionate amount of the value of the fringe benefit will be liable to FBT. The proportionate amount shall be determined by applying to the value of the fringe benefit, the proportion which the length of the period of stay in India by the employee during the grant period bears to the length of the grant period.

The value of fringe benefit means the fair market value of the specified security or sweat equity shares, on the date on which the option vests with the employee, as reduced by the amount actually paid by, or recovered from, the employee in respect of such shares.

5. Whether a foreign company is liable to fringe benefit tax in respect of shares allotted or transferred to an employee who is deputed to work in India in the year of such allotment or transfer?

A foreign company is liable to FBT in respect of shares allotted or transferred to its employee who is based in India. However, in such cases only a proportionate amount of the value of the fringe benefit will be liable to FBT. The proportionate value shall be determined by applying to the value of the fringe benefit, the proportion which the length of the period of stay in India by the employee during the grant period bears to the length of the grant period.

The value of fringe benefit means the fair market value of the specified security or sweat equity shares, on the date on which the option vests with the employee, as reduced by the amount actually paid by, or recovered from, the employee in respect of such shares.

6. What will be the cost of acquisition of shares, referred to in question nos 4 and 5, where only a proportionate value of fringe benefit has been subjected to FBT?

In accordance with section 49(2AB), the cost of acquisition of such shares shall be the fair market value on the date on which the option vests with the employee. The calculation of fringe benefit for the purpose of determining FBT does not change this value. Hence, the subsequent calculation of reducing such fair market value by the amount actually paid by or recovered from the employee as well as the calculation of proportionate value in certain cases, referred to in Question No.4 & 5 above, will not change the cost of acquisition.

7. Where the benefit on account of shares allotted or transferred under Employee Stock Option Plans (ESOPs) is taxed in the hands of the employees in different countries, would the employer still be liable to FBT? If yes, can the employer claim credit for payment of tax by the employee in other countries?

Employer will be liable to FBT in India irrespective of whether employees have been charged to tax in different countries or not. An employer cannot claim any credit in India against its FBT liability for taxes paid by employees in other countries.

8. Where FBT, on account of shares allotted or transferred under ESOPs, has been paid by the employer in respect of an employee based in India and subsequently recovered from him, can such employee claim credit in a foreign country for this FBT paid by the employer in India?

Ordinarily, the employee is liable to tax in respect of fringe benefits received by him from his employer. However, the taxation of fringe benefits in the hands of the employee raises several problems. Accordingly, it was decided to introduce FBT as a surrogate tax on employer in respect of the fringe benefits provided or deemed to have been provided by it to its employees during the

previous year. This being so, in a case where FBT, on account of share allotted or transferred ESOPs, has been paid by the employer in respect of an employee based in India and subsequently recovered from him; the FBT is effectively paid by the employee in respect of fringe benefits enjoyed by him. Therefore, such employee can claim credit, in a foreign country, for the FBT, on account of shares allotted or transferred under ESOPs, paid by the employer in India.

9. Whether the benefits arising on account of shares allotted or transferred under ESOPs can be taxed as a perquisite under section 17 of the Act instead of being taxed as fringe benefit under Chapter XII-H of the said Act, at the option of the employer?

Any fringe benefit liable to be taxed in the hands of the employer under Chapter XII-H cannot be taxed in the hands of the employee as a perquisite under section 17 of the said Act. Therefore, an employer does not have an option to tax the benefit arising on account of shares allotted or transferred under ESOPs as perquisite which otherwise is to be taxed as fringe benefit.

10. Whether there will be any FBT liability in a case where the FMV on the date of vesting is less than the price paid by the employee to the employer for allotment or transfer of shares?

No. FBT would not be payable in such cases.

11. What will be the valuation methodology for foreign companies if the shares are not listed in a recognized stock exchange in India but are listed on any globally recognised stock exchange?

If the shares are not listed in a recognized stock exchange in India, the shares will be treated as unlisted. Accordingly, such shares will have to be valued by category 1 Merchant Banker registered with Securities and Exchange Board of India. However, if the shares are listed in any globally recognised stock exchange, the merchant banker shall use the listed price as one of the basis for valuation and recommend the best value.

12. Whether an independent valuation carried by any foreign merchant banker/other experts as recognized for the purposes of valuation in the foreign country be treated as sufficient compliance for the purposes of valuation of fringe benefit arising on account of allotment or transfer of shares under ESOPs of an unlisted foreign company or is it mandatory that the merchant banker should be registered with the Securities and Exchange Board of India?

For the purposes of valuation of fringe benefit arising on account of allotment or transfer of shares under ESOPs of an unlisted foreign company, it is mandatory for the valuer to be a Category I Merchant Banker registered with the Securities and Exchange Board of India.

13. When there exists different methods for valuing FMV for unlisted companies, which method should be used by the merchant bankers to determine the FMV?

The Merchant Banker should determine the FMV on the basis of alternative methods and recommend the most appropriate value.

14. What is the significance of specified date? Whether the valuation is to be made on a specified date or specified security or sweat equity share is to be valued as on the specified date?

The process of valuation may be carried out by the merchant banker at any time before or after the date of vesting of the option, but the specified security or the sweat equity share is required to be valued as on the specified date.

15. What is the FMV that a company should adopt if the shares have been valued by more than one merchant banker or by one merchant banker on more than one occasion?

The valuation which value the specified security or sweat equity share on the specified date, which is closest to the date of the vesting of the option, should be adopted, if the shares have been valued by more than one Merchant Banker or by one Merchant Banker on more than one occasion.

16. Whether the fringe benefit arising on account of shares allotted or transferred under an ESOP is allowed as deduction in calculating the taxable income of the employer company?

In case where the employer purchases the shares and then subsequently transfers such shares to its employees, the expenditure so incurred is allowable as deduction in computing the taxable income of the employer company. However, if the shares are allotted to the employees from the share capital of the company, no deduction is allowable in computing the taxable income of the company since no expenditure has been incurred by it.

17. Whether ESOPs issued to non-executive directors or non-employees liable to FBT?

Benefit arising out of ESOPs issued to non-employees will not be liable to FBT. However, in such cases, the taxability of such benefits in the hands of the non-employees will be determined in accordance with the existing law.

18. Which method, first-in-first-out (FIFO) or last-in-first-out (LIFO) shall be followed in case there are multiple date of vesting for different number of shares. For example, if the dates of vesting are:

31 Mar 06 - 300 options FMV Rs.8 per share (one share per option)

31 Mar 07 - 300 options FMV Rs.9 per share (one share per option) and the employee is allotted 500 shares as on 30th September 2007, how will FBT be calculated?

In such cases, the First-in-First-Out (FIFO) method shall be followed. Hence, the FBT shall be calculated with respect to 300 shares at FMV of Rs.8 per share and 200 shares at FMV of Rs.9 per share.

19. Whether it is binding upon the Assessing Officer to accept the valuation made by the merchant banker?

It is binding upon the Assessing Officer to accept the valuation made by the Merchant Banker unless the valuation by such banker is perverse.

20. How would the recovery of FBT be treated in the hands of the employer?

Since FBT is not an allowable deduction in computation of the income of the employer, any recovery of FBT will not be treated as income in his hands.

21. What should be the mechanism and timing of recovery of FBT?

The law does not provide for any specific mechanism or timing of recovery of FBT.

22. Is it lawful for the employer to recover FBT with respect to ESOPs granted prior to April 1, 2007?

It would be lawful for the employer to recover FBT with respect to ESOPs granted prior to April 1, 2007, but allotted or transferred to the employee after such date.

23. What will be the date of allotment of an Employee Stock Option?

The date of allotment of an Employee Stock Option shall be the date on which the underlying asset is allotted or transferred to the employee

24. Whether the FBT recovered from the employee would form the cost basis for employee for calculating Capital Gain on subsequent sale of shares?

No. The recovery of FBT from the employee by the employer will not change the cost of acquisition of the shares in the hand of the employee.

25. Will Rule 40C of Income-tax Rules also apply in a case where shares are allotted or transferred to an employee under Employee Stock Purchase Plan, or Employee Stock Option Scheme, or Employee Stock Ownership Plan, or Employee Stock Purchase Scheme, or Employee Stock Option Scheme or Employee Appreciation Rights or Plans?

Rule 40C shall apply in all cases where specified security or sweat equity shares, being shares in a company, are allotted or transferred to an employee under any scheme or plan or otherwise. For the purpose of this circular an Employees Stock Option Plan shall include all such schemes or plans, etc.