

PAPER – 7 : DIRECT TAX LAWS

PART – I : STATUTORY UPDATES

Significant Notifications & Circulars Issued between 1.7.2011 and 31.10.2011

I. NOTIFICATIONS

1. Notification No. 49/2011 dated 6.9.2011

Notification of allowances and perquisites exempt under section 10(45)

The Finance Act, 2011 has inserted new clause (45) in section 10 to exempt specified allowances and perquisites received by Chairman or any other member, including retired Chairman or member of the Union Public Service Commission (UPSC). The exemption would be available in respect of such allowances and perquisites as may be notified by the Central Government in this behalf.

Accordingly, the Central Government has notified the following allowances and perquisites for serving Chairman and members of UPSC, for the purpose of exemption under section 10(45) -

- (i) the value of rent free official residence,
- (ii) the value of conveyance facilities including transport allowance,
- (iii) the sumptuary allowance and
- (iv) the value of leave travel concession.

In case of retired Chairman and retired members of UPSC, the following have been notified for exemption under section 10(45):

- (i) a sum of maximum ₹ 14,000 per month for defraying the service of an orderly and for meeting expenses incurred towards secretarial assistance on contract basis.
- (ii) the value of a residential telephone free of cost and the number of free calls to the extent of ₹1,500 pm (over and above free calls per month allowed by the telephone authorities)

This notification shall be effective retrospectively from 1st April, 2008.

2. Notification No. 50/2011 dated 9.9.2011

Notification of Long-term infrastructure bonds for section 80CCF

Section 80CCF exempts any amount paid or deposited by an individual or HUF as subscription to long-term infrastructure bonds notified by the Central Government, subject to a limit of ₹20,000.

Accordingly, the Central Government has specified the long term infrastructure bonds to be issued in the financial year 2011-12 by The Industrial Finance

Corporation of India (IFCI), The Life Insurance Corporation of India (LIC), The Infrastructure Development and Finance Company Ltd. (IDFCL), The India Infrastructure Finance Company Ltd. (IIFCL) and a Non-Banking Finance Company classified as an Infrastructure Finance Company by Reserve Bank of India, as long term infrastructure bonds for the purpose of the deduction under section 80CCF. The tenure of the bond shall be for a minimum period of ten years. The minimum lock-in period for investors shall be five years.

The notification further specifies certain conditions relating to limit on issuance, yield of the bond, end-use of the proceeds and reporting or monitoring mechanism. Further, it shall be mandatory for the subscribers to furnish their PAN to the issuer.

3. Notification No. 52/2011 dated 23-09-2011

Specification of bonds for interest exemption under section 10(15)(iv)(h)

Section 10(15)(iv)(h) exempts interest payable by any public sector company in respect of such bonds or debentures specified by the Central Government by notification in the Official Gazette. The notification would also specify the conditions subject to which the exemption would be available.

Accordingly, in exercise of the powers conferred in section 10(15)(iv)(h), the Central Government has specified the issue of tax free, secured, redeemable, non-convertible bonds of National Highways Authority of India (NHAI), Indian Railways Finance Corporation Ltd. (IRFCL), Housing and Urban Development Corporation Ltd.(HUDCL) and Power Finance Corporation (PFC) to be issued during the financial year 2011-12, the interest on which would be exempt under the said section.

The tenure of the bonds shall be ten to fifteen years. It shall be mandatory for the subscribers to furnish their PAN to the issuer. Further, it has been provided that such benefit shall be admissible only if the holder of such bonds registers his or her name and the holding with the said entity.

4. Notification No. 57/2011 dated 24.10.2011

Relaxation of time limit for submission of quarterly statements in case of a deductor being an office of Government

The CBDT has, through this notification, notified the Income-tax (Eighth Amendment) Rules, 2011 which shall come into force on 1st November, 2011. The said amendment Rules have given effect to following amendments:

(a) Rule 31A – Statement of deduction of tax under section 200(3)

- (i) Rule 31A(2) has been substituted to extend the time limit for submission of quarterly statements in case the deductor is an office of Government :

Date of ending of the quarter of the financial year	Due date in the case of a deductor, being an office of Government
30th June	31st July of the financial year
30th September	31st October of the financial year
31st December	31st January of the financial year
31st March	15th May of the financial year immediately following the financial year in which deduction is made

For other deductors, the due dates as prescribed earlier (i.e., 15th July, 15th October and 15th January of the financial year for quarters ending 30th June, 30th September and 31st December of the financial year, respectively) would continue to be applicable.

- (ii) In Rule 31A(4), clause (vii) has been inserted which requires the deductor to furnish, at the time of preparing statements of tax deducted, particulars of amount paid or credited on which tax was not deducted in view of the furnishing of declaration under section 197A(1) or 197A(1A) or section 197A(IC) by the payee.

(b) Rule 37BA – Credit for tax deducted at source for the purposes of section 199

Rule 37BA(1) provides that credit for tax deducted at source and paid to the Central Government shall be given to the person to whom the payment has been made or credit has been given (i.e., the deductee) on the basis of information relating to deduction of tax furnished by the deductor to the income-tax authority or the person authorized by such authority.

Clause (i) of Rule 37BA(2) has four sub-clauses (a) to (d) providing for the specific instances where income of the deductee is assessable in the hands of another person, consequent to which credit for tax deduction at source shall be given to the other person in those specific cases.

Clause (i) of Rule 37BA(2) has been substituted to provide that where under any provisions of the Act, the whole or any part of the income on which tax has been deducted at source is assessable in the hands of a person other than the deductee, credit for the whole or any part of the tax deducted at source, as the case may be, shall be given to the other person and not to the deductee. In effect, the specific situations have been substituted by a general provision.

However, the deductee should file a declaration with the deductor and the deductor should report the tax deduction in the name of the other person in the information relating to deduction of tax referred to in sub-rule (1) of Rule 37BA.

II. CIRCULARS**1. Circular No.4/2011 dated 19-7-2011****Guidelines for prior permission under section 281 to transfer or create charge on the assets of the business**

The CBDT has, through this circular, issued guidelines for granting of prior permission under section 281 of the Income-tax Act, 1961 to transfer or create a charge on the assets of the assessee to ensure uniformity on the issue -

- a) The taxpayer is required to apply in the prescribed form at least thirty days prior to the proposed date of transaction.
- b) Prior permission under section 281 to be granted by the Assessing Officer only under the following specified circumstances -
 - (i) If there is no demand outstanding and there is no likelihood of demand arising in the next six months, then the permission should be granted.
 - (ii) If undisputed demand is outstanding and there is no likelihood of demand arising in next six months, then, the taxpayer should pay the same along with interest due thereon and then permission should be granted.
 - (iii) If there is disputed demand outstanding, then the taxpayer should obtain stay for the same and indemnify the outstanding demand by way of bank guarantee or sufficient assets or by Department retaining the first charge on the assets proposed to be transferred or on which such charge is being created, to the extent of such demand. Thereafter, the permission under section 281 would be granted by the Assessing Officer.
 - (iv) If demand is likely to arise in the next six months, then the Assessing Officer should explore the possibility of action prescribed under section 281B.
- c) There would be only one level of intervention i.e., at the level of the range head for granting permission. The cases in which Assessing Officer would require such approval would be where -
 - (i) value of assets being transferred or on which charge is being created, or
 - (ii) the amount of charge being createdis rupees ten crores or more.
- d) The timelines for granting/refusing permission under section 281 by the Assessing Officer are as follows:
 - (i) If there is no demand outstanding and there is no likelihood of demand arising in the next six months, then the Assessing Officer should grant the permission within ten working days of the receipt of the application.
 - (ii) If undisputed demand is outstanding and there is no likelihood of demand arising in next 6 months, then the Assessing Officer should grant permission

within ten working days of payment of the outstanding demand along with interest due.

- (iii) If there is disputed demand outstanding and the taxpayer has obtained stay and indemnified the demand, then the Assessing Officer should grant the permission within ten working days of the indemnification of the demand.
 - (iv) If demand is likely to arise in the next six months and the Assessing Officer is considering actions prescribed under section 281B for the assets excluding the asset under consideration, then the Assessing Officer should grant the permission within fifteen working days of the receipt of the application.
 - (v) If the taxpayer does not pay the undisputed outstanding demand or his application for stay of disputed demand is rejected or he is unable to indemnify the outstanding demand, the application shall be disposed of within a period of ten working days. In case the permission is not being granted, a speaking and reasoned order conveying refusal would be issued with the approval of the Range head within ten working days of expiry of time given to the taxpayer to pay the undisputed demand or rejection of his stay application, as the case may be.
- e) These time limits should be followed scrupulously by the Assessing Officers.
 - f) The validity of the letter granting permission under section 281 would be one hundred and eighty days from the:
 - (i) date of issue of approval, or
 - (ii) service of order of attachment under section 281B,
 whichever is earlier.
 - g) Once the asset is transferred or charge is created, the taxpayer should submit the documents, in this regard, to the Assessing Officer for his record.

2. Circular No. 7/2011 dated 27-09-2011

Procedure for refund of TDS under section 195 to the person deducting tax in cases where tax is deducted at a higher rate prescribed in the DTAA

The CBDT has, through this circular, modified Circular No.07/2007, dated 23.10.2007 which laid down the procedure for refund of tax deducted at source under section 195 of the Income-tax Act, 1961 to the person deducting tax at source from the payment to a non-resident. The said Circular allowed refund to the person making payment under section 195 in the circumstances indicated therein as the income does not accrue to the non-resident or if the income is accruing, no tax is due or tax is due at a lesser rate. The amount paid to the Government in such cases to that extent does not constitute tax.

The said Circular, however, did not cover a situation where the tax is deducted at a rate prescribed in the relevant DTAA which is higher than the rate prescribed in the Income-tax Act, 1961. Since the law requires deduction of tax at a rate prescribed in the relevant

DTAA or under the Income-tax Act, 1961 whichever is lower, there is a possibility that in such cases excess tax is deducted relying on the provisions of relevant DTAA.

Accordingly, in order to remove the genuine hardship faced by the resident deductor, the Board has modified Circular No. 07/2007, dated 23-10-2007 to the effect that the beneficial provisions under the said Circular allowing refund of tax deducted at source under section 195 to the person deducting tax at source shall also apply to those cases where deduction of tax at a higher rate under the relevant DTAA has been made while a lower rate is prescribed under the domestic law.

PART – II : JUDICIAL UPDATES

Significant Recent Legal Decisions

1. **Would refund of excise duty and grant of interest subsidy under the incentive scheme formulated by Central Government for public interest, namely, to accelerate industrial development, generate employment and create opportunities for self-employment in state of Jammu and Kashmir be treated as a revenue receipt or a capital receipt?**

Shree Balaji Alloys v. CIT (2011) 333 ITR 335 (J&K)

In the present case, the Tribunal contended that excise duty refund and grant of interest subsidy received by the assessee in pursuance of the New Industrial Policy introduced in Jammu and Kashmir were revenue receipt and not capital receipt on the grounds that:-

- (i) the aforesaid incentives were not given to establish industrial units because the industry was already established.
- (ii) the aforesaid incentives were not given to establish industrial units because the industry was already established.
- (iii) the aforesaid incentives were not given to establish industrial units because the industry was already established.
- (iv) the aforesaid incentives were not given to establish industrial units because the industry was already established.
- (v) the incentives were available only on commencement of commercial production.
- (vi) the incentives were recurring in nature.
- (vii) the incentives were not given for acquisition of capital assets.
- (viii) the incentives were given for easy market accessibility and to run the business more profitably.

The High Court observed that the fact that incentives would become available to industrial units entitled thereto from the date of commencement of commercial production and the fact that these were not granted for creation of new assets were not the sole criteria for determining the nature of subsidy. The fact that such incentives were provided to achieve a public purpose should also be considered to determine the nature of subsidy and hence, such

subsidy could not be construed as a production or operational incentive for the benefit of the assessee. Hence, the aforesaid incentives are capital receipts not liable to taxation.

2. **Can an assessee engaged in letting out of rooms in a lodging house also treat the income from renting of a building to bank on long term lease as business income?**

Joseph George and Co. v. ITO (2010) 328 ITR 161 (Kerala)

On the above issue, it was decided that while lodging is a business, however, letting out of building to the bank on long-term lease could not be treated as business. Therefore, the rental income from bank has to be assessed as income from house property.

3. **Would the phrase "used for purpose of business" in respect of discarded machine include use of such asset in the earlier years for claim of depreciation under section 32?**

CIT v. Yamaha Motor India Pvt. Ltd. (2010) 328 ITR 297 (Delhi)

The issue under consideration in this case is whether depreciation is allowable on the written down value of the entire block, even though the block includes some machinery which has already been discarded and hence, cannot be put to use during the relevant previous year.

On the above issue, it was observed that the expression "used for the purposes of the business" in section 32 when used with respect to discarded machinery would mean the use in the business, not in the relevant financial year/previous year, but in the earlier financial years. The discarded machinery may not be actually used in the relevant previous year but depreciation can be claimed as long as it was used for the purposes of business in the earlier years provided the block continues to exist in the relevant previous year. So, the condition for claiming depreciation in respect of the discarded machine would be satisfied if it is used in the earlier previous years for the business.

4. **Is the assessee entitled to depreciation on value of goodwill considering it as "other business or commercial rights of similar nature" within the meaning of an intangible asset?**

B. Raveendran Pillai v. CIT (2011) 332 ITR 531 (Kerala)

Under section 32(1)(ii), depreciation is allowable on intangible assets, being know-how, patents, copyrights, trade marks, license, franchise, or any other business or commercial rights of similar nature.

In this case, a hospital was run in the same building, in the same town, in the same name for several years prior to purchase by the assessee. By transferring the right to use the name of the hospital itself, the previous owner had transferred the goodwill to the assessee and the benefit derived by the assessee was retention of continued trust of the patients, who were patients of the previous owners. When goodwill paid was for ensuring retention and continued business in the hospital, it was for acquiring a business and commercial right and it was comparable with trade mark, franchise, copyright etc.,

referred to in the first part of clause (ii) of section 32(1) and so, goodwill was covered by the above provision of the Act entitling the assessee for depreciation.

5. **Can EPABX and mobile phones be treated as computers to be entitled to higher depreciation at 60%?**

Federal Bank Ltd. v. ACIT (2011) 332 ITR 319 (Kerala)

On this issue, the High Court held that the rate of depreciation of 60% is available to computers and there is no ground to treat the communication equipment as computers. Hence, EPABX and mobile phones are not computers and therefore, are not entitled to higher depreciation at 60%.

6. **Would expenditure incurred on feasibility study conducted for examining proposals for technological advancement relating to the existing business be classified as a revenue expenditure, where the project was abandoned without creating a new asset?**

CIT v. Priya Village Roadshows Ltd. (2011) 332 ITR 594 (Delhi)

In this case, the assessee, engaged in the business of running cinemas, incurred expenditure towards architect fee for examining the technical viability of the proposal for takeover of cinema theatre for conversion into a multiplex/ four-screen cinema complexes. The project was, however, dropped due to lack of financial and technical viability. The issue under consideration is whether such expenses can be treated as revenue in nature, since no new asset has been created.

On this issue, the High Court observed that, in such cases, whether or not a new business/asset comes into existence would become a relevant factor. If there is no creation of a new asset, then the expenditure incurred would be of revenue nature. In this case, since the feasibility studies were conducted by the assessee for the existing business with a common administration and common fund and the studies were abandoned without creating a new asset, the expenses were of revenue nature.

7. **Can expenditure incurred by a company on higher studies of the director's son abroad be claimed as business expenditure under section 37 on the contention that he was appointed as a trainee in the company under "apprentice training scheme", where there was no proof of existence of such scheme?**

Echjay Forgings Ltd. v. ACIT (2010) 328 ITR 286 (Bom.)

On this issue, it was observed that there was no evidence on record to show that any other person at any point of time was appointed as trainee or sent abroad for higher education. Further, the appointment letter to the director's son, neither had any reference number nor was it backed by any previous application by him. The appointment letter referred to "apprentice training scheme" with the company in respect of which no details were produced. There was no evidence that he was recruited as trainee by some open competitive exam or regular selection process. Hence, there was no nexus between the

education expenditure incurred abroad for the director's son and the business of the assessee company. Therefore, the aforesaid expenditure was not deductible.

8. **Can the waiver of principal amount of loan taken for purchase of capital asset by the bank be treated as “benefit arising out of business” or “a remission of trading liability” for taxability as business income of the company?**

Iskraemeco Regent Ltd. v. CIT (2011) 331 ITR 317 (Mad.)

The assessee company, engaged in the business of development, manufacturing and marketing of electro-mechanical and static energy meters, took a bank loan for purchase of capital assets. The grant of bank loan for purchase of a capital asset is a capital receipt and not a trading receipt. The provisions of section 41(1) are attracted only in case of remission of a trading liability. Since the loan was taken for purchase of capital assets, waiver of a portion of principal would not amount to remission of a trading liability to attract the provisions of section 41(1). Further, such waiver cannot be treated as a benefit arising out of business and consequently, section 28(iv) will not apply in respect of such loan transaction.

9. **Would the special provisions for computing profits under section 44BB be applicable to a non-resident carrying on business of seismic data acquisition and processing under contract with Indian concerns?**

Global Geophysical Services Ltd., In re (2011) 332 ITR 418 (AAR)

On an application made to the Authority of Advance Ruling by the non-resident on the above issue, the Authority observed that in an identical issue in *Geofizyka Torun SP. Z.O.O. (2010) 320 ITR 0268 (AAR)*, it was observed that without seismic data acquisition and interpretation, it is impractical to carry out the activity of prospecting of mineral oil and gas which is a step in aid to its exploration. The seismic data (in processed form) is used to create highly accurate images of the earth's sub-surface which in turn are used by the exploration and production companies for locating potential oil and gas reserves based upon the geology observed.

Accordingly, in this case, the AAR ruled that the said activities and services of the applicant clearly fell within the description of section 44BB and the income derived by the applicant under the contracts with Indian concerns, namely ONGC and Cairn Energy, for seismic data acquisition and processing were to be computed under the provisions of section 44BB.

10. **Can the Assessing Officer bring to tax the actual profits as per books of accounts, if the same is higher than 10% of receipts which are deemed to be the profits under section 44BBB in case of a foreign company engaged in turnkey projects?**

DIT v. DSD Noell GmbH (2011) 333 ITR 304 (Delhi)

In the present case, the assessee is a German company providing engineering and technical services for various projects eligible for presumptive taxation scheme under section 44BBB.

The assessee filed its return declaring a sum equal to 10% of the amount paid or payable to the assessee under the projects undertaken by it as deemed profits and gains chargeable to tax under the head "Profits and gains of business or profession" as per the provisions of section 44BBB. The Assessing Officer contended that on the basis of books of account maintained by the assessee, the profits could be more than 10% and therefore, the actual profits should be brought to tax by invoking sub-section (2) of section 44BBB.

On the above issue, the Delhi High Court held that if an assessee fulfills all the conditions mentioned in section 44BBB(1), the provisions of sections 28 to 44AA of the Act would not be applicable for computation of its business income, and a sum equal to 10% of the amount paid or payable to such foreign company would be deemed as its business income. Further, under section 44BBB(2), the assessee has the benefit of declaring before the Assessing Officer that the actual profits earned by it were less than 10% but the Revenue cannot take recourse of this sub-section to claim that the profits earned by the assessee were more than 10%.

11. **Can exemption under section 54 be claimed in respect of more than one residential flat acquired by the assessee under a joint development agreement with a builder, wherein the property owned by the assessee was developed by the builder who constructed eight residential flats in the said property, four of which were given to the assessee?**

CIT v. Smt. K. G. Rukminiamma (2011) 331 ITR 211 (Kar.)

The assessee, being the owner of a property, entered into a joint development agreement with a builder to develop the property. Under the agreement, the builder constructed eight residential flats and handed over four residential flats to the assessee. The entire cost of construction and other expenses were borne by the builder.

The issue under consideration is whether capital gains exemption under section 54 can be claimed in respect of the four residential flats treating them as "a residential house". In the present case, the Revenue contended that the benefit of deduction under section 54 could be availed only in respect of one residential flat and in respect of the remaining three residential flats, the assessee was not entitled to deduction under section 54.

The Karnataka High Court, applying the decision in *Anand Basappa (2009) 309 ITR 329 (Kar.)* to the present case, held that all the four flats are situated in the same residential building and hence, will constitute "a residential house" for the purpose of section 54. Therefore, the assessee would be entitled to deduction under section 54 in respect of all four flats.

12. **What can be the tests to determine "substantial part of business" of lending company for the purpose of application of exclusion provision under section 2(22)?**

CIT v. Parle Plastics Ltd. (2011) 332 ITR 63 (Bom.)

Under section 2(22), dividend does not include, *inter alia*, any advance or loan made to a shareholder by a company in the ordinary course of its business, where the lending of money

is a substantial part of the business of the company. The expression used in the exclusion provision of section 2(22) is "substantial part of the business". Sometimes a portion which contributes a substantial part of the turnover, though it contributes a relatively small portion of the profit, would be termed as a substantial part of the business. Similarly, a portion which is relatively small as compared to the total turnover, but generates a large portion, say more than 50% of the total profit of the company would also be a substantial part of its business. Percentage of turnover in relation to the whole as also the percentage of the profit in relation to the whole and sometimes even percentage of manpower used for a particular part of the business in relation to the total manpower or work force of the company would be required to be taken into consideration for determining the substantial part of business. The capital employed for a specific division of a company in comparison to total capital employed would also be relevant to determine whether the part of the business constitutes a substantial part.

In this case, 42% of the total assets of the lending company were deployed by it by way of loans and advances. Further, if the income earned by way of interest is excluded, the other business had resulted in a net loss. These factors were considered in concluding that lending of money was a substantial part of the business of the company. Since lending of money was a substantial part of the business of the lending company, the money given by it by way of advance or loan to the assessee could not be regarded as a dividend, as it had to be excluded from the definition of "dividend" by virtue of the specific exclusion in section 2(22).

- 13. Would the procurements of parts and assembling them to make windmill fall within the meaning of "manufacture" and "production" to be entitled for deduction under section 80-IB?**

CIT v. Chiranjeevi Wind Energy Ltd. (2011) 333 ITR 192 (Mad.)

The Supreme Court, in *India Cine Agencies v. CIT* (2009) 308 ITR 98, laid down that the test to determine whether a particular activity amounts to "manufacture" or not is whether new and different goods emerge having distinctive name, use and character. Further, the Supreme Court, in *CIT v. Sesa Goa Ltd. (2004) 271 ITR 331*, observed that the word "production" or "produce" when used in comparison with the word "manufacture" means bringing into existence new goods by a process, which may or may not amount to manufacture. It also takes in all the by-products, intermediate products and residual products, which emerge in the course of manufacture of goods.

In this case, Madras High Court, applying the above rulings of the Apex Court, observed that the different parts procured by the assessee could not be treated as a windmill individually. Those different parts had distinctive names and only when assembled together, they got transformed into an ultimate product which was commercially known as a "windmill". Thus, such an activity carried on by the assessee would amount to "manufacture" as well as "production" of a thing or article to qualify for deduction under section 80-IB.

Note: The definition of manufacture has been incorporated in section 2(29BA) by the Finance (No. 2) Act, 2009 w.e.f. from 01.04.2009, and it means, *inter alia*, a change in a

non-living physical object or article or thing resulting in transformation of the object or article or thing in to a new and distinct object or article or thing having a different name, character and use. Assembling of windmill at factory and putting them at site of customer apparently satisfies this definition of manufacture also.

- 14. Can an assessee not claiming deduction under section 80-IB in the initial years claim the said deduction for the remaining years during the period of eligibility, if the conditions are satisfied?**

Praveen Soni v. CIT (2011) 333 ITR 324 (Delhi)

On the above issue, the Delhi High Court held that the provisions of section 80-IB nowhere stipulated a condition that the claim for deduction under this section had to be made from the first year of qualification of deduction failing which the claim will not be allowed in the remaining years of eligibility. Therefore, the deduction under section 80-IB should be allowed to the assessee for the remaining years up to the period for which his entitlement would accrue, provided the conditions mentioned under section 80-IB are fulfilled.

- 15. Does income derived from sale of export incentive qualify for deduction under section 80-IB?**

CIT v. Jaswand Sons (2010) 328 ITR 442 (P&H)

On this issue, the High Court held that income derived from sale of export incentive cannot be said to be income “derived from” the industrial undertaking and therefore, such income is not eligible for deduction under section 80-IB.

- 16. Would grant of transport subsidy, interest subsidy and refund of excise duty qualify for deduction under section 80-IB?**

CIT v. Meghalaya Steels Ltd. (2011) 332 ITR 91 (Gauhati)

The Supreme Court, in *Liberty India v. CIT [2009] 317 ITR 218*, observed that section 80-IB provides for deduction in respect of profits and gains “derived from the business” of the assessee and accordingly, the Parliament intended to cover sources of profits and gains not beyond the first degree. There should be a direct nexus between the generation of profits and gains and the source of profits and gains, the latter being directly relatable to the business of the assessee. Any other source, not falling within the first degree, can only be considered as ancillary to the business of the assessee.

In this case, the High Court observed that the transport and interest subsidies were revenue receipts which were granted after setting up of the new industries and after commencement of production. The transport subsidy would have the effect of reducing the inward and outward transport costs for the purposes of determining the cost of production as well as for sales. However, the subsidy had no direct nexus with the profits or gains derived by the assessee from its industrial activity and the benefit to the assessee was only ancillary to its industrial activity. The subsidies were not directly

relatable to the industrial activity of the assessee, and hence they did not fall within the first degree contemplated by the Act. Therefore, the subsidies could not be taken into account for purposes of deduction under section 80-IB.

However, the payment of Central excise duty had a direct nexus with the manufacturing activity and similarly, the refund of the Central excise duty also had a direct nexus with the manufacturing activity, being a profit-linked incentive, since payment of the Central excise duty would not arise in the absence of any industrial activity. Therefore, the refund of excise duty had to be taken into account for purposes of section 80-IB.

Note: Similar ruling was pronounced by the Himachal Pradesh High Court in *CIT v. Gheria Oil Gramudyog Workers Welfare Association* (2011) 330 ITR 117, wherein it was held that interest subsidy received from the State Government cannot be treated as “profit derived from industrial undertaking” and hence was not eligible for deduction under section 80-IB.

17. Can interest under sections 234B and 234C be levied where a company is assessed on the basis of book profits under section 115JB?

Joint CIT v. Rolta India Ltd. (2011) 330 ITR 470 (SC)

On this issue, the Supreme Court observed that there is a specific provision in section 115JB(5) providing that all other provisions of the Income-tax Act, 1961 shall apply to every assessee, being a company, mentioned in that section. Section 115JB is a self-contained code pertaining to MAT, and by virtue of sub-section (5) thereof, the liability for payment of advance tax would be attracted. Therefore, if a company defaults in payment of advance tax in respect of tax payable under section 115JB, it would be liable to pay interest under sections 234B and 234C. Therefore, interest under sections 234B and 234C shall be payable on failure to pay advance tax in respect of tax payable under section 115JB.

Note – According to section 207, tax shall be payable in advance during any financial year, in accordance with the provisions of sections 208 to 219 (both inclusive), in respect of the total income of the assessee which would be chargeable to tax for the assessment year immediately following that financial year. Under section 115JB(1), where the tax payable on total income is less than 18.5% of “book profit” of a company, the “book profit” would be deemed to be the total income and tax would be payable at the rate of 18.5%. Since in such cases, the book profit is deemed to be the total income, therefore, as per the provisions of section 207, tax shall be payable in advance in respect of such book profit (which is deemed to be the total income) also.

18. Would the interest earned on surplus funds of a club deposited with institutional members satisfy the principle of mutuality to escape taxability?

Madras Gymkhana Club v. DCIT (2010) 328 ITR 348 (Mad.)

The assessee, club providing facilities like gym, library, etc, to its members earned interest from fixed deposits which it had made by investment of its surplus funds with its corporate members.

The High Court held that interest earned from investment of surplus funds in the form of fixed deposits with institutional members does not satisfy the principle of mutuality and hence cannot be claimed as exempt on this ground. The interest earned is, therefore, taxable.

- 19. Would the payments made by a company to BSNL/ MTNL for the services provided through interconnect / port / access / toll be treated as “fees for technical services” to attract the provisions of tax deduction at source under section 194J?**

CIT v. Bharti Cellular Ltd. & Hutchison Essar Telecom Ltd. (2011) 330 ITR 239 (SC)

On this issue, the Delhi High Court had held that the services rendered in relation to interconnection, port access did not involve any human interface and, therefore, the services could not be regarded as "technical services" as contemplated under section 194J. The expression "technical service" would have reference to only technical service rendered by a human. It would not include any service provided by machines or robots. The Delhi High Court, therefore, concluded that interconnect charges/port access charges could not be regarded as fees for technical services, and hence, TDS provisions under section 194J were not attracted.

The Supreme Court observed that the problem which arises in these cases is that there is no proper evidence from the side of the Department to show how human intervention takes place, particularly, during the process when calls take place. During the traffic of calls from one place to another, whether there is any manual intervention is one of the points which requires to be examined. Similarly, the basis for allotment of “capacity” to a service provider and consequences if such “capacity” is exhausted and “additional capacity” is required on an urgent basis, needs to be examined to study whether at that stage, any human intervention is involved. These types of matters cannot be decided without any technical assistance.

The Apex Court was of the view that the Department should not proceed solely on the basis of contracts placed before its officers, but should examine the matter with the support of technical experts so that such matters could be disposed of expeditiously on the basis of factual findings. Accordingly, the Apex Court remitted the matter to the Assessing Officer, directing him to examine the same with the assistance of a technical expert from the side of the Department and to decide the matter within a period of four months.

- 20. Can difference between published price and minimum fixed commercial price be treated as additional special commission in the hands of the agents of an airline company to attract TDS provisions under section 194H?**

CIT v. Qatar Airways (2011) 332 ITR 253 (Bom.)

In this case, the airline company sold tickets to the agents at a minimum fixed commercial price. The agents were permitted to sell the tickets at a higher price, however, up to the maximum of published price. Commission at the rate of 9% of

published price was payable to the agents of the airline company, on which tax was deducted under section 194H. The issue under consideration is whether the difference between the published price and the minimum fixed commercial price amounts to additional special commission in the hands of the agents to attract the provisions of section 194H.

On this issue, the Bombay High Court observed that the difference between the published price and minimum fixed commercial price cannot be taken as additional special commission in the hands of the agents, since the published price was the maximum price and airline company had granted permission to the agents to sell the tickets at a price lower than the published price. In order to deduct tax at source, the exact income in the hands of the agents must necessarily be ascertainable by the airline company. However, the airline company would have no information about the exact rate at which the tickets were ultimately sold by its agents, since the agents had been given discretion to sell the tickets at any rate between the minimum fixed commercial price and the published price. It would be impracticable and unreasonable to expect the airline company to get a feedback from its numerous agents in respect of each ticket sold.

Thus, tax at source was not deductible on the difference between the actual sale price and the minimum fixed commercial price, even though the amount earned by the agent over and above minimum fixed commercial price would be taxable as income in his hands.

- 21. Can discount given on supply of SIM cards and recharge coupons by a telecom company to its distributors under a prepaid scheme be treated as commission to attract the TDS provisions under section 194H?**

Vodafone Essar Cellular Ltd. v. ACIT (TDS) (2011) 332 ITR 255 (Kerala)

On this issue, the Kerala High Court observed that it was the SIM card which linked the mobile subscriber to the assessee's network. Therefore, supply of SIM card by the assessee-telecom company was only for the purpose of rendering continued services to the subscriber of the mobile phone. The position was the same so far as recharge coupons or e-topups were concerned which were only air time charges collected from the subscribers in advance under a prepaid scheme.

There was no sale of any goods involved as claimed by the assessee and the entire charges collected by the assessee from the distributors at the time of delivery of SIM cards or recharge coupons were only for rendering services to ultimate subscribers. The assessee was accountable to the subscribers for failure to render prompt services pursuant to connections given by the distributor. Therefore, the distributor only acted as a middleman on behalf of the assessee for procuring and retaining customers and therefore, the discount given to him was within the meaning of commission under section 194H on which tax was deductible.

22. Is disallowance under section 40(a)(i) for non deduction of tax at source attracted in respect of payment for purchase of software from a non-resident, by treating the same as royalty in case where the purchase is for subsequent resale in the Indian market?

CIT vs. Dynamic Vertical Software India P. Ltd. (2011) 332 ITR 0222 (Delhi)

In this case, the Delhi High Court held that since the assessee had purchased the software from Microsoft and subsequently sold the same in the Indian market, he had acted as a dealer and therefore the payment to the non-resident, Microsoft, can not be termed as royalty. Therefore, section 40(a)(i) would have no application in this case and the payment made to the non-resident cannot be disallowed under section 40(a)(i) on the ground that no tax was deducted at source.

23. Can penalty under section 271(1)(c) for concealment of income be imposed in a case where the assessee has raised a debatable issue?

CIT v. Indersons Leather P. Ltd. (2010) 328 ITR 167 (P&H)

The assessee company, after discontinuing its manufacturing business, leased out its shed along with fittings and disclosed the income as income from business, whereas the Revenue contended that the same be assessed as "Income from house property. The issue under consideration is whether penalty under section 271(1)(c) can be imposed in such a case.

On this issue, the High Court observed that, mere raising of a debatable issue would not amount to concealment of income or furnishing inaccurate particulars and therefore, penalty under section 271(1)(c) cannot be imposed.

24. Can the Tribunal exercise its power of rectification under section 254(2) to recall its order in entirety?

Lachman Dass Bhatia Hingwala (P) Ltd. v. ACIT (2011) 330 ITR 243 (Delhi)(FB)

On this issue, the Delhi High Court observed that the justification of an order passed by the Tribunal recalling its own order is required to be tested on the basis of the law laid down by the Apex Court in *Honda Siel Power Products Ltd. v. CIT (2007) 295 ITR 466*, dealing with the Tribunal's power under section 254(2) to recall its order where prejudice has resulted to a party due to an apparent omission, mistake or error committed by the Tribunal while passing the order. Such recalling of order for correcting an apparent mistake committed by the Tribunal has nothing to do with the doctrine or concept of inherent power of review. It is a well settled provision of law that the Tribunal has no inherent power to review its own judgment or order on merits or reappreciate the correctness of its earlier decision on merits. However, the power to recall has to be distinguished from the power to review. While the Tribunal does not have the inherent power to review its order on merits, it can recall its order for the purpose of correcting a mistake apparent from the record.

The Apex Court, while dealing with the power of the Tribunal under section 254(2) in *Honda Sael Power Products Ltd.*, observed that one of the important reasons for giving the power of rectification to the Tribunal is to see that no prejudice is caused to either of the parties appearing before it by its decision based on a mistake apparent from the record. When prejudice results from an order attributable to the Tribunal's mistake, error or omission, then it is the duty of the Tribunal to set it right. In that case, the Tribunal had not considered the material which was already on record while passing the judgment. The Apex Court took note of the fact that the Tribunal committed a mistake in not considering material which was already on record and the Tribunal acknowledged its mistake and accordingly, rectified its order.

The above decision of the Apex Court is an authority for the proposition that the Tribunal, in certain circumstances can recall its own order and section 254(2) does not totally prohibit so. In view of the law laid down by the Apex Court in that case, the decisions rendered by the High Courts in certain cases to the effect that the Tribunal under no circumstances can recall its order in entirety do not lay down the correct statement of law.

Applying the above-mentioned decision of the Apex Court to this case, the Delhi High Court observed that the Tribunal, while exercising the power of rectification under section 254(2), can recall its order in entirety if it is satisfied that prejudice has resulted to the party which is attributable to the Tribunal's mistake, error or omission and the error committed is apparent.

Note - *In deciding whether the power under section 254(2) can be exercised to recall an order in entirety, it is necessary to understand the true principle laid down in the Apex Court decision. A decision should not be mechanically applied treating the same as a precedent without appreciating the underlying principle contained therein. In this case, the Apex Court decision was applied since prejudice had resulted to the party on account of the mistake of the Tribunal apparent from record.*

- 25. In a case where there is a transfer of shares in a non-resident company from one non-resident to another non-resident, is it possible to infer that the transaction has significant nexus with India to attract the taxability provisions, if it ultimately resulted in transfer of controlling interest in Indian company?**

Vodafone International Holdings B.V. v. UOI (2010) 329 ITR 126 (Bom.)

Hutchison Essar Limited (HEL) is an Indian company carrying on the business of providing telecommunication services in India. Hutchison Telecommunication International Limited (HTIL) is a foreign company, registered in Hong Kong. Vodafone International Holdings B.V. (VIH BV), is a Netherlands company controlled by the Vodafone group.

A sale/ purchase agreement was entered in to between VIH BV and HTIL, under which HTIL agreed to procure and transfer to VIH BV, the entire issued share capital of CGP (a

foreign company registered in Cayman Islands, Mauritius) free from all encumbrances together with all rights attaching and accruing and together with assignment of loan interest.

VIB HV contended that the transaction represented a transfer of a capital asset, i.e., the share of CGP, and that any gain arising to the transferor or to any other person out of this transfer was not taxable in India because the asset was not situated in India as CGP is a foreign company and also the consideration was paid and received outside India, and hence, there was no sum chargeable to tax in India and the obligation to deduct tax at source by VIH BV under section 195 did not arise.

On the above issue, the Bombay High Court held that, that HTIL had an aggregate of 67% (approx.) of controlling interest in HEL by way of indirect equity shareholding, option agreements, finance agreements, shareholders agreements, etc., through CGP. The transaction between HTIL and VIH BV was structured so as to achieve the object of discontinuing the operations of HTIL in relation to the Indian mobile telecommunication operations by transferring the rights and entitlements of HTIL in HEL to VIH BV. The rights and entitlements included transfer of control premium, use and rights to the Hutch brand in India, a non-compete agreement with the Hutch group, the value of non-voting non-convertible preference shares, various loan obligations and the entitlement representing indirect interest in HEL.

The rights and entitlements of HTIL in HEL constituted capital assets within the meaning of section 2(14) to be covered in the phrase “property of any kind held by an assessee”. The consideration that was paid to HTIL by VIH BV included consideration for acquisition of diversified rights and entitlements. Therefore, the transaction had a significant nexus with India. The essence of the transaction was a change of controlling interest in HEL which represented a source of income in India.

26. Is wealth-tax leviable on the value of house under construction, where the construction was still incomplete on the relevant valuation date?

CIT v. Smt. Neena Jain (2011) 330 ITR 157 (P & H)

On this issue, the Revenue contended that the incomplete house of the assessee fell within the purview of assets in section 2(ea) of the Wealth-tax Act, 1957 and it was liable to wealth-tax. Consequently, the value of the plot and investment of assessee's share in construction of the residential house was added and tax was, accordingly assessed.

The High Court opined that the words “any building” could not be read in isolation and had to be harmoniously construed with the remaining portion of section 2(ea) i.e., whether the building was used for residential or commercial purposes or for the purpose of maintaining a guest house, because an incomplete building could not possibly either be used for residential or commercial purposes or for the purposes of maintaining a guest house. Therefore, the word “building” has to be interpreted to mean a completely

built structure having a roof, dwelling place, walls, doors, windows, electric and sanitary fittings etc.

In this case, the assessee was constructing the building after obtaining sanction from the appropriate authorities. Explanation 1(b) under section 2(ea) defining "urban land" for levy of wealth-tax, specifically excludes from its scope, the land occupied by any building which has been constructed with the approval of the appropriate authority. Therefore, the incomplete building of the assessee neither fell within the meaning of a building nor within the purview of "urban land" under section 2(ea). Consequently, the incomplete building is not an asset chargeable to wealth-tax.

- 27. Can "moneys payable" in respect of a building sold by the assessee (which has to be reduced from the opening written down value of the block of assets for calculating depreciation) be construed as the fair market value of the asset instead of the actual sale price?**

CIT v. Cable Corporation of India Ltd. (2011) 336 ITR 56 (Bom.)

On this issue, the Bombay High Court observed that the "moneys payable" to be reduced from the written down value of the block of assets as per section 43(6) is to be construed as per the meaning assigned to the same according to the *Explanation* below section 41(4) which states that the "moneys payable" in relation to the sale of a building, machinery, plant or furniture would be the price for which it is sold.

Therefore, the written down value of the asset falling within that block of assets at the beginning of the previous year has to be adjusted by the amount for which the asset is actually sold and not by its fair market value.

It may, however, be noted that, in case of scrap, the amount of scrap value (i.e. the fair market value) has to be reduced as per the provisions of section 43(6), to arrive at the written down value at the end of the year.

- 28. Can the Assessing Officer issue notice under section 154 to rectify a mistake apparent from record in the intimation under section 143(1), after issue of a valid notice under section 143(2)?**

CIT v. Haryana State Handloom and Handicrafts Corporation Ltd. (2011) 336 ITR 699 (P&H)

On this issue, the Punjab and Haryana High Court referred to the Delhi High Court ruling in *CIT v. Punjab National Bank (2001) 249 ITR 763*, where it was held that rectification of an intimation cannot be made after issuance of notice under section 143(2) and during the pendency of proceedings under section 143(3). It was held that if any change was permissible to be effected, the same can be done in the assessment under section 143(3) and not by exercising the power under section 154 to rectify the intimation issued under section 143(1).

In the present case, the Punjab and Haryana High Court relying, *inter alia*, on the said decision held that the scope of proceedings under section 143(2) is wider than the power of rectification of mistake apparent from record under section 154. The notice under section 143(2) is issued to ensure that the assessee has not understated the income or has not computed excessive loss or underpaid the tax. It is only on consideration of the matter and on being satisfied that it is necessary or expedient to do so that the Assessing Officer issues the notice under section 143(2). Therefore, the the Assessing Officer has to proceed under section 143(3) and issue an assessment order. If issue of notice under section 154 is permitted to rectify the intimation issued under section 143(1), then it would lead to duplication of work and wastage of time.

Therefore, it was concluded that proceedings under section 154 for rectification of intimation under section 143(1) cannot be initiated after issuance of notice under section 143(2) by the Assessing Officer to the assessee.

- 29. Can the Assessing Officer reassess issues other than the issues in respect of which proceedings were initiated under section 147 when the original “reason to believe” on basis of which the notice was issued ceased to exist?**

Ranbaxy Laboratories Ltd. v. CIT (2011) 336 ITR 136 (Delhi)

In the present case, the assessee company was engaged in the business of manufacture and trading of pharmaceutical products. The Assessing Officer accepted the returned income filed by the assessee but initiated reassessment proceedings under section 147 in respect of the addition to be made on account of club fees, gifts and presents and provision for leave encashment. It was observed that the Assessing Officer had reason to believe that income has escaped assessment due to claim and allowance of such expenses and accordingly, he issued notice under section 148. However, after sufficient enquiries were made during reassessment proceedings, the Assessing Officer came to the conclusion that no additions are required to be made on account of these expenses. Therefore, while completing the reassessment he did not make additions on account of these items but instead made additions on the basis of other issues which were not the original “reason to believe” for the issue of notice under section 148. The Assessing Officer made such additions on the basis of *Explanation 3* to section 147 as per which the Assessing Officer may assess the income which has escaped assessment and which comes to his notice subsequently in the course of proceedings under section 147 even though the said issue did not find mention in the reasons recorded in the notice issued under section 148.

The issue under consideration is whether the Assessing Officer can make an assessment on the basis of an issue which came to his notice during the course of assessment, where the issues, which originally formed the basis of issue of notice under section 148, were dropped in its entirety.

As per section 147, the Assessing Officer may assess or reassess such income **and also** any other income chargeable to tax which has escaped assessment and which comes to

his notice in the course of proceedings under this section. The Delhi High Court observed that the words “and also” used in section 147 are of wide amplitude.

The correct interpretation of the Parliament would be to regard the words '**and also**' as being “conjunctive and cumulative with” and not “in alternative to” the first part of the sentence, namely, “the Assessing Officer may assess and reassess *such income*”. It is significant to note that Parliament has not used the word 'or' but has used the word 'and' together and in conjunction with the word 'also'. The words '*such income*' in the first part of the sentence refer to the income chargeable to tax which has escaped assessment and in respect of which the Assessing Officer has formed a reason to believe for issue of the notice under section 148. Hence, the language used by the Parliament is indicative of the position that the assessment or reassessment must be in respect of the income, in respect of which the Assessing Officer has formed a reason to believe that the same has escaped assessment and also in respect of any other income which comes to his notice subsequently during the course of the proceedings as having escaped assessment. If the income, the escapement of which was the basis of the formation of the “reason to believe” is not assessed or reassessed, it would not be open to the Assessing Officer to independently assess only that income which comes to his notice subsequently in the course of the proceedings under the section as having escaped assessment. If he intends to do so, a fresh notice under section 148 would be necessary.

- 30. Would the words “shall be issued” used in section 149 mean ‘mere signing of notice by the Assessing Officer’ or ‘handing over of the said notice in the hands of the proper officer for serving it to the assessee’ to constitute a valid notice issued within the prescribed time limit?**

Kanubhai M. Patel (HUF) v. Hiren Bhatt or his successors to Office (2011) 334 ITR 0025 (Guj.)

In the present case, the assessee filed a return of income for the assessment year 2003-04. The assessee did not receive any notice under section 143(2). On 8th April, 2010, the assessee received a notice under section 148 dated 31st March, 2010 for the assessment of income relating to assessment year 2003-04 under section 147. The assessee, on inquiry from the post office, found out that the department had sent the covers for issuing notice to the speed post centre (for booking) only on 7th April, 2010 and not on 31st March, 2010 and the Revenue also did not challenge this finding of the assessee.

The assessee, therefore, challenged the legality and validity of the notices dated 31st March, 2010 issued by the department under section 148 as being time barred contending that the impugned notices have been issued beyond the time limit prescribed under the provisions of section 149 i.e. after a period of six years from the end of the relevant assessment year. The assessee contended that the date of issue of the notices under section 148 would be the date on which the same have been dispatched by

registered post i.e. 7th April, 2010 and not the date of signing of the notice by the Assessing Officer i.e. 31st March, 2010.

The Gujarat High Court observed that the core issue which arises for consideration is the date when the notice under section 148 can be said to have been issued. For this purpose, it is necessary to examine the true meaning of the phrase '**shall be issued**' as employed in section 149(1) according to which no notice under section 148 'shall be issued' for the relevant assessment year, if the specified time period (i.e. 4 years/6 years, as the case may be) has elapsed from the end of the relevant assessment year.

The Gujarat High Court observed that according to Black's Law Dictionary, the term 'issue' when used with reference to writs, process, and the like, would mean as importing delivery to the proper person, or to the proper officer for service etc. Therefore, any notice may be considered to be issued if made out and placed in the hands of a person authorised to serve it, and with a bona fide intent to have it served. The expression '**shall be issued**' in section 149 would, therefore, have to be read in the above mentioned context.

In the present case, the notice has been signed on 31st March, 2010, whereas the same were sent to the speed post centre for booking only on 7th April, 2010. From the above definition of the word "issue", it is apparent that mere signing of notices on 31st March, 2010 cannot tantamount to issuance of notice as contemplated under section 149. The date of issue would be the date on which the same were handed over for service to the proper officer, which, in the facts of the present case, would be the date on which the said notices were actually handed over to the post office for the purpose of effecting service on the assessee.

Hence, the date of issue of the said notice would be 7th April, 2010 and not 31st March, 2010. Therefore, the aforesaid notice under section 148 in relation to the assessment year 2003-04, having been issued on 7th April, 2010, is beyond the period of six years from the end of the relevant assessment year and clearly barred by limitation.

- 31. Can the Commissioner initiate revision proceedings under section 263 on the ground that the Assessing Officer's order not initiating penal proceedings was erroneous and prejudicial to the interest of the Revenue, in a case where non-initiation of penal proceedings was a pre-condition for surrender of income by the assessee?**

CIT v. Subhash Kumar Jain (2011) 335 ITR 364 (P&H)

In the present case, an addition of ₹ 9,91,090 was made in the assessment of the assessee under section 143(3) on account of agricultural income, since the assessee failed to explain the source of agricultural income as declared by him in the return of income. The said addition was made on the basis of the report submitted by the Inspector pointing out the defects in the documents furnished by the assessee. As a result, the assessee made an offer to surrender ₹ 9,91,090 subject to a condition that no

penal action under section 271(1)(c) would be initiated. The Assessing Officer accepted the same as the department did not have any documentary evidence against the assessee and the assessment was made only on the basis of the report by the Inspector. Accordingly, the assessment was framed by the Assessing Officer without initiating the penalty proceedings under section 271(1)(c). The Commissioner of Income-tax, exercising his power under section 263, directed the Assessing Officer to frame a fresh assessment order after taking into account the facts attracting the penal action under section 271(1)(c), considering the original order erroneous and prejudicial to the interest of the Revenue.

The issue under consideration in this case is whether, when the Assessing Officer, while passing the assessment order under section 143(3), had given effect to the office note that the surrender of the agricultural income which was made by the assessee would not be subject to penal action under section 271(1)(c) and accordingly not levied penalty, can the Commissioner of Income-tax, in exercise of his power under section 263, hold the order of the Assessing Officer to be erroneous and prejudicial to the interest of the Revenue.

On this issue, the Punjab and Haryana High Court observed that, on perusal of the office note issued by the Assessing Officer, it was clear that the assessee had made surrender of income with a clear condition that no penal action under section 271(1)(c) would be initiated. The office note further depicts that the offer of the assessee was accepted by the Department. Once that was so, the Commissioner cannot take a different view and levy penalty. The High Court relied on the decision of the Bombay High Court in *Jivatlal Purtapshi v. CIT (1967) 65 ITR 261*, where it was observed that an order based on an agreement cannot give rise to grievances and the same cannot be agitated.

32. Can winnings of prize money on unsold lottery tickets held by the distributor of lottery tickets be assessed as business income and be subject to normal rates of tax instead of the rates prescribed under section 115BB?

CIT v. Manjoo and Co. (2011) 335 ITR 527 (Kerala)

On the above issue, the Kerala High Court observed that winnings from lottery is included in the definition of income by virtue of section 2(24)(ix). Further, in practice, all prizes from unsold tickets of the lotteries shall be the property of the organising agent. Similarly, all unclaimed prizes shall also be the property of the organising agent and shall be refunded to the organising agent.

The High Court contended that the receipt of winnings from lottery by the distributor was not on account of any physical or intellectual effort made by him and therefore cannot be said to be "income earned" by him in business. The said view was taken on the basis that the unsold lottery tickets cease to be stock-in-trade of the distributor because, after the draw, those tickets are unsaleable and have no value except waste paper value and the distributor will get nothing on sale of the same except any prize winning ticket if held by him, which, if produced will entitle him for the prize money. Hence, the receipt of the

prize money is not in his capacity as a lottery distributor but as a holder of the lottery ticket which won the prize. The Lottery Department also does not treat it as business income received by the distributor but instead treats it as prize money paid on which tax is deducted at source.

Further, winnings from lotteries are assessable under the special provisions of section 115BB, irrespective of the head under which such income falls. Therefore, even if the argument of the assessee is accepted and the winnings from lottery is taken to be received by him in the course of his business and as such assessable as business income, the specific provision contained in section 115BB, namely, the special rate of tax i.e. 30% would apply.

Therefore, the High Court held that the rate of 30% prescribed under section 115BB is applicable in respect of winnings from lottery received by the distributor.

- 33. Would non-resident match referees and umpires in the games played in India fall within the meaning of sportsmen to attract taxability under the provisions of section 115BBA, and consequently attract the TDS provisions under section 194E in the hands of the payer?**

Indcom v. Commissioner of Income-tax (TDS) (2011) 335 ITR 485 (Calcutta)

On this issue, the Calcutta High Court observed that, in order to attract the provisions of the section 194E, the person should be a non-resident sportsperson or non-resident sports association or institution whose income is taxable as per the provisions of section 115BBA.

The umpires and the match referees can be described as professionals or technical persons who render professional or technical services, but they cannot be said to be either non-resident sportsmen (including an athlete) or non-resident sports association or institution so as to attract the provisions of section 115BBA and consequently, the provisions of tax deduction at source under section 194E are also not attracted in this case. Though for the purpose of section 194J, match referees and umpires are considered as professionals, the tax deduction provisions thereunder are attracted only in case where the deductee is a resident individual, which is not so in the present case.

Therefore, although the payments made to non-resident umpires and the match referees are “income” which has accrued and arisen in India, the same are not taxable under the provisions of section 115BBA and thus, the assessee is not liable to deduct tax under section 194E.

Note - It may be noted that since income has accrued and arisen in India to the non-resident umpires and match referees, the TDS provisions under section 195 would be attracted and tax would be deductible at the rates in force.

PART – III : QUESTIONS AND ANSWERS**QUESTIONS****Incomes which do not form part of total income**

1. (a) "The Finance Act, 2011 has inserted clause (45) in section 10 to exempt all allowances and perquisites paid to Chairman or a retired Chairman or any member or retired member of the Union Public Service Commission" – Examine the correctness or otherwise of this statement.

[Hints: Section 10(45) of the Income-tax Act, 1961]

- (b) Explain the tax treatment of income of notified infrastructure debt funds to be set up in accordance with the prescribed guidelines. Also, explain the tax treatment of interest income from such funds in the hands of the recipient, who is a non-resident, and the applicability of TDS provisions in this regard.

[Hints: Section 10(47), section 139(1), section 115A, section 194LB of the Income-tax Act, 1961]

Charitable trusts and institutions

2. An institution having its main object as "advancement of general public utility" received ₹ 50 lakhs in aggregate during the P.Y.2011-12 from an activity in the nature of trade. It applied its entire receipt from such activity during the same year for its main object i.e. advancement of general public utility.
- (i) What would be the tax consequence of such receipt and application thereof by the institution?
- (ii) Would your answer be different if the institution had received ₹ 25 lakhs (instead of ₹ 50 lakhs) in aggregate during the P.Y.2011-12 from an activity in the nature of trade?
- (iii) What would be your answer if the main object of the institution is "preservation of environment" and the institution receives ₹ 50 lakhs from a trading activity and applies 85% of the said receipts for its main object?

[Hints: Section 2(15) of the Income-tax Act, 1961]

Profits and gains of business or profession

3. Hotelia Ltd. commenced operations of the business of a new four-star hotel in Pune on 1.4.2011. The company incurred capital expenditure of ₹ 25 lakhs during the period January, 2011 to March, 2011 exclusively for the above business, and capitalized the same in its books of account as on 1st April, 2011. Further, during the P.Y.2011-12, it incurred capital expenditure of ₹ 75 lakhs (out of which ₹ 35 lakhs was for acquisition of land) exclusively for the above business. Compute the income under the head "Profits and gains of business or profession" for the A.Y.2012-13, assuming that Hotelia Ltd. has fulfilled all the conditions specified for claim of deduction under section 35AD and has not claimed any

deduction under Chapter VI-A under the heading “C. – Deductions in respect of certain incomes”. The profits from the business of running this hotel (before claiming deduction under section 35AD) for the A.Y.2012-13 is ₹ 15 lakhs. Assume that the company also has another existing business of running a three-star hotel in Nagpur, which commenced operations six years back, the profits from which are ₹ 80 lakhs for the A.Y.2012-13.

[Hints: Section 35AD, section 73A of the Income-tax Act, 1961]

4. (a) Alpha Marine Ltd. made a cash payment of ₹ 40,000 on 15.12.2011 to local fishermen, who regularly supply to them lobsters and crabs. Would the provisions of section 40A(3) be attracted in respect of such payment? What would be your answer if such cash payments are made to a trader who supplies lobsters and crabs?

[Hints: Section 40A(3) of the Income-tax Act, 1961, Rule 6DD of the Income-tax Rules, 1962 and Circular 10/2008 dated 5.12.2008]

- (b) Mr. Vallish, a non-resident, operates an aircraft between Hong Kong and Mumbai. He received the following amounts in the course of the business of operation of aircraft during the year ending 31.3.2012:

- (i) ₹ 4 crores in India on account of carriage of passengers from Mumbai.
- (ii) ₹ 2 crore in India on account of carriage of goods from Mumbai.
- (iii) ₹ 3 crores in India on account of carriage of passengers from Hong Kong.
- (iv) ₹ 1 crore in Hong Kong on account of carriage of passengers from Mumbai.

The total expenditure incurred by Mr. Vallish for the purposes of the business during the year ending 31.3.2012 was ₹ 4 crores.

Compute the income of Mr. Vallish chargeable to tax in India under the head “Profits and gains of business or profession” for the assessment year 2012-13.

[Hints: Section 44BBA of the Income-tax Act, 1961]

Capital Gains

5. (i) Sridhar inherits a house property from his father, who had mortgaged it. Sridhar discharges the mortgage debt and later, sells the property. Can he claim the amount paid to the mortgagee as cost of improvement in computing the capital gain?

[Hints: RM Arunachalam v. CIT (1997) 227 ITR 222 (SC)]

- (ii) Ganesh mortgaged his house property and utilized the mortgage amount to perform the marriage of his son. He paid the amount to the mortgagee later. Upon sale of the said property thereafter, he claims the mortgage debt discharged as forming part of the cost of acquisition. Can capital gain be computed accepting his claim?

[Hints: V.S.M.R. Jagadish Chandran v. CIT (1997) 227 ITR 240 (SC) or CIT v. Roshanbabu Mohammed Hussein Merchant (2005) 144 Taxman 720 / 275 ITR 0231(Bom.)]

Income from other sources

6. Under section 2(22), dividend does not include, *inter alia*, any advance or loan made to a shareholder by a company in the ordinary course of its business, where the lending of money is a "substantial part of the business" of the company. Discuss, with the aid of a recent case law, as to what can be the tests to determine "substantial part of the business" of lending company for the purpose of application of exclusion provision under section 2(22)?

[Hints: Section 2(22) of the Income-tax Act, 1961 and CIT v. Parle Plastics Ltd. (2011) 332 ITR 63 (Bom.)]

Deductions from Gross Total Income

7. (a) Examine, with the aid of recent case laws, whether the following would qualify for deduction under section 80-IB –
- Income derived from sale of export incentive;
 - Transport subsidy and interest subsidy; and
 - Refund of excise duty.

[Hints: Section 80-IB of the Income-tax Act, 1961, Liberty India v. CIT [2009] 317 ITR 218 (SC), CIT v. Jaswand Sons (2010) 328 ITR 442 (P&H) and CIT v. Meghalaya Steels Ltd. (2011) 332 ITR 91 (Gauhati)]

- (b) Can an assessee, who has not claimed deduction under section 80-IB in the initial years, claim deduction under the said section for the remaining years during the period of eligibility, if the stipulated conditions are satisfied? Examine, with the aid of a recent case law.

[Hints: Praveen Soni v. CIT (2011) 333 ITR 324 (Delhi)]

Assessment of Firms/LLPs

8. "Certain Limited Liability Partnerships (LLPs) to be subject to Alternate Minimum Tax" – Elucidate, explaining the provisions introduced for levy of such tax. Also, point out the difference, if any, between the concept of "Alternate Minimum Tax" on LLPs and "Minimum Alternate Tax" on companies.

[Hints: Section 115JB, section 115JC, section 115JD, section 115JE of the Income-tax Act, 1961]

9. M/s. LMN, a partnership firm, submits the following profit and loss account for computation of its business income for the assessment year 2012-13.

Profit and loss account for the year ending 31.03.2012

Expenses	₹	Income	₹
To Salaries	3,18,000	By Gross profit	6,47,000

" Rent	46,000	Dividend from Indian company	8,000
" Interest	80,000		
" Depreciation	32,000		
" Other Administrative expenses	55,000		
" Contribution to provident fund	24,000		
" Net profit	<u>1,00,000</u>		
Total	<u>6,55,000</u>	Total	<u>6,55,000</u>

Additional information:

- (i) Salaries include ₹ 1,50,000 paid to working partner L and ₹ 1,00,000 to working partner M.
- (ii) Interest paid includes ₹ 54,000, being interest paid on loan given by partner M at the rate of 18% simple interest.
The salary and interest payments are authorized by the partnership deed.
- (iii) Out of provident fund contribution debited to profit and loss account, ₹ 10,000 is outstanding beyond the due date of filing of return.
- (iv) The firm purchased goods by issuing account payee drafts except in the case of one bill for ₹ 80,000 for which payment has been made by cash. This has been debited to trading account as part of purchases.

[Hints: Section 40(b), section 43B, section 40A(3) of the Income-tax Act, 1961]

Assessment of companies

10. "Dividend received by Indian companies from specified foreign companies would be subject to a concessional tax treatment" - Is this statement correct? Examine. How would you compute the income-tax payable by an Indian company, whose total income includes dividend received from a specified foreign company?

[Hints: Section 115BBD of the Income-tax Act, 1961]

11. Gravity Ltd earned a net profit of ₹ 44,74,000 after debit/credit of the following items to its profit and loss account for the year ended on 31.3.2012:

(a)	Items debited to Profit and Loss Account	₹
	Provision for income-tax	9,18,000
	Provision for diminution in the value of investment	72,000
	Wealth-tax	2,56,000
	Securities Transaction Tax	76,000

	Transfer to General Reserve	2,10,000
	Provision for gratuity based on actuarial valuation	1,20,000
	Provision for losses of subsidiary company	1,40,000
	Expenditure to earn agricultural income	50,000
	Expenditure to earn LTCG exempt under section 10(38)	40,000
	Depreciation (including depreciation of ₹ 1,50,000 on revaluation)	3,50,000
(b)	Items credited to Profit and Loss Account	
	Amount credited to P& L A/c from Special Reserve	1,00,000
	Amount credited to P& L A/c from Revaluation Reserve	1,80,000
	Agricultural income	2,50,000
	LTCG exempt under section 10(38)	1,60,000

The company provides the following additional information:

Brought forward Business Loss/Unabsorbed Depreciation:

Assessment Year	Amount as per books	
	Loss (₹)	Depreciation (₹)
2009-10	6,00,000	3,00,000
2010-11	2,00,000	Nil
2011-12	3,00,000	4,00,000

You are required to examine the applicability of section 115JB of the Income-tax Act, 1961, and compute book profit and the tax credit to be carried forward, assuming that the total income computed as per the other provisions of the Income-tax Act, 1961 is ₹ 25,00,000.

[Hints: Section 115JB, section 115JAA of the Income-tax Act, 1961]

Assessment Procedure

12. (a) The assessment of XYZ (P) Ltd. for the A.Y. 2010-11 was completed under section 143(3). On 25-3-2012, the Assessing Officer reopened the assessment in proper manner under section 147. The reason recorded was that certain expenditure which ought to have been disallowed under section 40(a) was not done and hence, there has been escapement of income. During the course of hearing, he wants to take up some other matter also, which is not covered by the reason recorded. The company objects to the same, contending that the same is not permissible as per the provisions of the Income-tax Act, 1961. Examine the correctness of contention of XYZ (P) Ltd.

[Hints: Section 147, section 148 of the Income-tax Act, 1961]

- (b) Can the Assessing Officer issue notice under section 148 to reopen the same assessment order on the same grounds for which the Commissioner had issued notice under section 263? Examine critically in the context of provisions of the Income-tax Act, 1961.

[Hints: Section 147, section 148, section 263 of the Income-tax Act, 1961]

Transfer Pricing

13. "The Finance Act, 2011 has expanded the scope of powers of the Transfer Pricing Officer" - Discuss the correctness or otherwise of this statement.

[Hints: Section 92CA of the Income-tax Act, 1961]

14. Geomatics Ltd., an Indian company, provides technical services to a company, MNC Inc., located in a Notified Jurisdictional Area (NJA) for a consideration of ₹ 40 lakhs in January, 2012. It charges ₹ 48 lakhs and ₹ 52 lakhs for similar services rendered to Alpha Inc. and Beta Inc., respectively, which are not located in a NJA. Alpha Inc. and Beta Inc. are not associated enterprises of Geomatics Ltd.

Assuming that the variation notified by the Central Government for such class of international transactions is 6% of the transaction price, discuss the tax implications under section 94A read with section 92C in respect of the above transaction of provision of technical services by Geomatics Ltd. to MNC Inc.

[Hints: Section 94A of the Income-tax Act, 1961]

Appeals and Revision

15. "The Appellate Tribunal can grant indefinite stay in any proceeding relating to an appeal" – Is this statement correct? Discuss.

[Hints: Section 254 of the Income-tax Act, 1961]

Settlement Commission

16. "The order of the Settlement Commission is final and conclusive and hence, the same cannot be rectified" – Discuss the correctness or otherwise of this statement.

[Hints: Section 245D of the Income-tax Act, 1961]

Deduction, Collection and Recovery of tax

17. Teleco Ltd., a telecom company, supplied SIM cards and recharge coupons to its distributors under a prepaid scheme. Teleco Ltd. was accountable to the ultimate subscribers for rendering prompt services pursuant to connections given by the distributors. Teleco Ltd. claimed that tax was not deductible on the discount given on supply of SIM cards and recharge coupons to the distributors since the transaction was a sale transaction. Examine, with the aid of a recent case law, whether the discount given on supply of SIM cards and recharge coupons by Teleco Ltd. to its distributors under the

prepaid scheme can be treated as commission to attract the TDS provisions under section 194H.

[Hints: Vodafone Essar Cellular Ltd. v. ACIT (TDS) (2011) 332 ITR 255 (Kerala)]

18. Fly High Airlines, an airline company, sold tickets to its agents at a minimum fixed commercial price. The agents were permitted to sell the tickets at a higher price, however, up to the maximum of published price. Commission@9% of published price was payable to the agents, on which the airline company deducted tax under section 194H. The Assessing Officer contended that the difference between the published price and the minimum fixed commercial price amounts to additional special commission in the hands of the agents and therefore, the airline company is also required to deduct tax on such additional special commission under section 194H. Discuss the correctness of the contention of the Assessing Officer, with the aid of a recent case law.

[Hints: CIT v. Qatar Airways (2011) 332 ITR 253 (Bom.)]

Wealth-tax

19. Sky Heights Limited furnishes the following data and requests you to compute its net wealth on the valuation date 31.3.2012,:
- (i) Land in urban area (Construction is not permitted as per Municipal Laws in force) ₹ 50,00,000
 - (ii) Motor-cars (used on hire by the company) ₹ 10,00,000
 - (iii) Jewellery (Investment) ₹ 22,00,000. Loan taken for purchasing the same ₹ 13,00,000
 - (iv) Cash Balance (as per books) ₹ 3,00,000
 - (v) Bank Balances ₹ 7,00,000
 - (vi) Guest House (situated in a place which is 30 kms away from the local limits of the municipality) ₹ 12,00,000
 - (vii) Residential flat occupied by the Managing Director ₹ 18,00,000. The Managing Director is on whole time appointment and is drawing remuneration of ₹ 10,00,000.
 - (viii) Residential house let out on hire for 230 days ₹ 16,00,000.

[Hints: Section 2(ea), 2(m) of the Wealth-tax Act, 1957]

20. Madan owns two residential houses, one in Calcutta and another in Bangalore. Both the houses are meant to be used for residential purposes by Madan and his family. The particulars of the houses are as follows:
- (i) The house at Calcutta was purchased by him in January, 1980 for ₹ 12 lacs. The house was occupied by his close relative, Kishan, without rent for four months from 1st April, 2011 to 31st July, 2011. The value of the house as per Schedule III to the

Wealth-tax Act, 1957 on 31st March, 2012 is ₹ 28 lacs. Its value on the same basis as on 31st March, 1980 was ₹ 15 lacs.

- (ii) The house at Bangalore was purchased in January, 2006 for ₹ 11 lacs. The values of the house as per Schedule III to the Wealth-tax Act, 1957, on 31st March, 2006 and 31st March, 2012 are ₹ 7 lacs and ₹ 10 lacs, respectively.

You are required to fix the value of each house for the purpose of computation of net wealth of Madan on the valuation date 31.03.2012.

[Hints: Section 2(ea), section 5(vi), section 7, Schedule III of the Wealth-tax Act, 1957]

SUGGESTED ANSWERS/HINTS

1. (a) The statement is not correct, since exemption is not available in respect of all allowances and perquisites but is restricted to such allowances and perquisites as may be notified by the Central Government in this behalf.

The Finance Act, 2011 has inserted new clause (45) in section 10 to exempt specified allowances and perquisites received by Chairman or any other member, including retired Chairman/member, of the Union Public Service Commission (UPSC). The exemption would be available in respect of such allowances and perquisites as may be notified by the Central Government in this behalf.

Accordingly, the Central Government has notified the following allowances and perquisites for serving Chairman and members of UPSC, for the purpose of exemption under section 10(45) -

- (i) the value of rent free official residence,
- (ii) the value of conveyance facilities including transport allowance,
- (iii) the sumptuary allowance and
- (iv) the value of leave travel concession.

In case of retired Chairman and retired members of UPSC, the following have been notified for exemption under section 10(45):

- (i) a sum of maximum ₹ 14,000 per month for defraying the service of an orderly and for meeting expenses incurred towards secretarial assistance on contract basis.
- (ii) the value of a residential telephone free of cost and the number of free calls to the extent of ₹ 1,500 per month (over and above free calls per month allowed by the telephone authorities).

- (b) In order to give a fillip to infrastructure and encourage inflow of long-term foreign funds to this sector, the Finance Act, 2011 has provided enabling power to the Central Government to notify any infrastructure debt fund which is set up in

accordance with the prescribed guidelines. Once notified, the income of such infrastructure debt fund would be exempt from tax under section 10(47).

Such infrastructure debt fund is required to furnish its return of income for the previous year in the prescribed form within the period specified under section 139(1), if its total income, without giving effect to the exemption under section 10(47), exceeds the basic exemption limit.

Interest income received by a non-resident or a foreign company from such fund would be subject to tax at a concessional rate of 5% under section 115A on the gross amount of such interest income as compared to tax @ 20% on other interest income of non-resident.

Accordingly, tax would be deductible @ 5% on interest paid/credited by such fund to a non-resident/foreign company. The person responsible for making the payment shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct income-tax @5%. This is provided for in new section 194LB.

2. (i) As the main object of the institution is “advancement of object of general public utility”, it will lose its status as a “charitable institution” for the P.Y.2011-12, since it has received ₹ 50 lakhs from an activity in the nature of trade. The application of 100% of such receipt for its main object during the year would not help in retaining its status as a “charitable institution” for that year.
- (ii) If the institution receives only ₹ 25 lakhs in aggregate from an activity in the nature of trade during the P.Y.2011-12, then it will not lose its status as a “charitable institution” since receipt of up to ₹ 25 lakhs in a year from such activity is permissible as per the amendment by the Finance Act, 2011. The institution can claim exemption subject to fulfilment of other conditions under sections 11 to 13.
- (iii) The restriction regarding carrying on of a trading activity for a cess, fee or other consideration will not apply if the main object of the institution is “preservation of environment”. Therefore, receipt of ₹ 50 lakhs from a trading activity by such an institution will not affect its status as a “charitable institution”. The institution can claim exemption subject to fulfilment of other conditions under sections 11 to 13.
3. At present, investment-linked tax incentive under section 35AD is available in respect of certain specified businesses which, *inter alia*, include building and operating a hotel of two-star or above category, anywhere in India. 100% of the capital expenditure incurred during the previous year, wholly and exclusively for the above businesses would be allowed as deduction from the business income. However, expenditure incurred on acquisition of any land, goodwill or financial instrument would not be eligible for deduction. Further, the expenditure incurred, wholly and exclusively, for the purpose of specified business prior to commencement of operation would be allowed as deduction

during the previous year in which the assessee commences operation of his specified business. A condition has been inserted that such amount incurred prior to commencement should be capitalized in the books of account of the assessee on the date of commencement of its operations.

Further, in respect of the business of hotels and hospitals, the word “new” has been removed from the definition of “specified business”. Therefore, “specified business”, in relation to hotels and hospitals, would now mean the business of building and operating, anywhere in India, -

- (1) a hotel of two-star or above category as classified by the Central Government;
- (2) a hospital with at least one hundred beds for patients.

Consequently, the loss of an assessee claiming deduction under section 35AD in respect of a specified business can be set-off against the profit of another specified business under section 73A, irrespective of whether the latter is eligible for deduction under section 35AD. As assessee can, therefore, set-off the losses of a hospital or hotel which begins to operate after 1st April, 2010 and which is eligible for deduction under section 35AD, against the profits of the existing business of operating a hospital (with atleast 100 beds for patients) or a hotel (of two-star or above category), even if the latter is not eligible for deduction under section 35AD.

Particulars	₹
Profits from the specified business of new hotel in Pune (before providing deduction under section 35AD)	15 lakh
Less: Deduction under section 35AD	
Capital expenditure incurred during the P.Y.2011-12 (excluding the expenditure incurred on acquisition of land) = ₹ 75 lakh – ₹ 35 lakh	40 lakh
Capital expenditure incurred prior to 1.4.2011 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2011	<u>25 lakh</u>
Total deduction under section 35AD for A.Y.2012-13	<u>65 lakh</u>
Loss from the specified business of new hotel in Pune	(50 lakh)
Profit from the existing business of running a hotel in Nagpur	<u>80 lakh</u>
Net profit from business after set-off of loss of specified business against profits of another specified business under section 73A	<u>30 lakh</u>

4. (a) Under section 40A(3), disallowance is attracted in the computation of income in a case where a payment or aggregate of payments exceeding ₹ 20,000 is made to a person in a day, otherwise than by an account payee cheque drawn on a bank or an account payee bank draft.

However, payment made otherwise than by an account payee cheque drawn on a

bank or by an account payee bank draft exceeding ₹ 20,000 does not attract the aforesaid disallowance in certain circumstances as prescribed under Rule 6DD of the Income-tax Rules, 1962. Such exceptions, *inter-alia*, refer to payment made to the producer for the purchase of fish or fish products under sub-clause (iii) of clause (e) of Rule 6DD.

With regard to this sub-clause, the CBDT has, vide *Circular 10/2008 dated 5.12.2008*, issued the following clarifications –

- (i) The expression 'fish or fish products' would include 'other marine products such as crab, lobster etc.'.
- (ii) The 'producers' of fish or fish products would include, besides the fishermen, any headman of fishermen, who sorts the catch of fish brought by fishermen from the sea, at the sea shore itself and then sells the fish or fish products to traders, exporters etc.

In view of the above circular, cash payment of ₹ 40,000 made to local fishermen for supply of lobsters and crabs, would not be hit by the provisions of section 40A(3).

However, the above exception will not be available in respect of payment for the purchase of fish or fish products from a person who is not proved to be a 'producer' of these goods and is only a trader, broker or any other middleman, by whatever name called.

Therefore, the disallowance under section 40A(3) would be attracted if such cash payment of ₹ 40,000 on a single day is made to a trader who supplies lobsters and crabs.

- (b) Section 44BBA incorporates special provisions for computing profits and gains of the business of operation of aircraft in the case of non-residents. Section 44BBA starts with a non-obstante clause. Therefore, section 44BBA overrides the provisions contained in sections 28 to 43A. As such, the business income of Mr. Vallish is required to be computed in accordance with the provisions of section 44BBA.

Under section 44BBA(1), a sum equal to 5% of the aggregate of the amounts specified in sub-section (2) is deemed to be the profits and gains chargeable to tax under the head "Profits and gains of business or profession". Sub-section (2) specifies the following amounts -

- (a) the amount paid or payable, whether in or out of India, to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place in India; and
- (b) the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods from any place outside India.

Keeping in view the provisions of section 44BBA, the income of Mr. Vallish chargeable to tax in India under the head "Profits and gains of business or profession" is worked out hereunder -

Particulars	₹
Amount received in India on account of carriage of passengers from Mumbai	4,00,00,000
Amount received in India on account of carriage of goods from Mumbai	2,00,00,000
Amount received in India on account of carriage of passengers from Hong Kong	3,00,00,000
Amount received in Hong Kong on account of carriage of passengers from Mumbai	1,00,00,000
	10,00,00,000

Income from business under section 44BBA at 5% of ₹ 10,00,00,000 is ₹ 50,00,000, which is the income of Mr. Vallish chargeable to tax in India under the head "Profits and gains of business or profession" for the A.Y.2012-13.

5. (i) Sridhar inherited the house property with the liability to discharge the mortgage debt. He can, therefore, claim the amount paid to the mortgagee as cost of improvement while computing the capital gain on sale of the said property. The decision of the Supreme Court in *RM. Arunachalam v. CIT (1997) 227 ITR 222* supports this view.
- (ii) Ganesh has himself created the mortgage in respect of his house property. It is a self-created mortgage. Therefore, the debt discharged by Ganesh on the property under mortgage created by him does not form part of cost of acquisition. The decision of the Supreme Court in *V.S.M.R. Jagadish Chandran v. CIT (1997) 227 ITR 240* supports this view. Therefore, capital gain on sale of the property cannot be computed on the basis of the claim made by him.

Note – This question can also be answered with reference to the Bombay High Court ruling in *CIT v. Roshanbabu Mohammed Hussein Merchant (2005) 144 Taxman 720 / 275 ITR 0231*. This case highlights the difference in tax treatment in respect of allowability of the expenditure incurred on removing an encumbrance in two different cases, namely –

- (i) In a case where the mortgage is created by the previous owner and
- (ii) In a case where the mortgage is created by the assessee himself.

The Bombay High Court pointed out that there is a distinction between the obligation to discharge the mortgage debt created by the previous owner and the obligation to discharge the mortgage debt created by the assessee himself. Where the property

acquired by the assessee is subject to the mortgage created by the previous owner, the assessee acquires absolute interest in that property only after the discharge of mortgage debt. In such a case, the expenditure incurred by the assessee to discharge the mortgage debt created by the previous owner to acquire absolute interest in the property is treated as 'cost of acquisition' and is deductible from the full value of consideration received by the assessee on transfer of that property. However, where the assessee acquires property which is unencumbered, the assessee gets absolute interest in that property on acquisition. When the assessee transfers that property, he is liable for capital gains tax on the full value realized, even if he has himself created an encumbrance on that property. The assessee is under an obligation to remove that encumbrance for effectively transferring the property. In other words, the expenditure incurred by the assessee to remove the encumbrance created by the assessee himself on the property (which was acquired by him without any encumbrance) is not an allowable deduction under section 48.

6. This question came up before the Bombay High Court in *CIT v. Parle Plastics Ltd. (2011) 332 ITR 63*. The Bombay High Court observed that under section 2(22), dividend does not include, *inter alia*, any advance or loan made to a shareholder by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company.

In that case, 42% of the total assets of the lending company were deployed by it by way of loans and advances. Further, if the income earned by way of interest is excluded, the other business had resulted in a net loss. These factors were considered in concluding that lending of money was a substantial part of the business of the company. Since lending of money was a substantial part of the business of the lending company, the money given by it by way of advance or loan to the assessee could not be regarded as a dividend, as it had to be excluded from the definition of "dividend" by virtue of the specific exclusion in section 2(22).

The expression used in the exclusion provision of section 2(22) is "substantial part of the business". Sometimes a portion which contributes a substantial part of the turnover, though it contributes a relatively small portion of the profit, would be termed as a substantial part of the business. Similarly, a portion which is relatively small as compared to the total turnover, but generates a large portion, say more than 50% of the total profit of the company, would also be a substantial part of its business.

Percentage of turnover in relation to the whole as also the percentage of the profit in relation to the whole and sometimes even percentage of manpower used for a particular part of the business in relation to the total manpower or work force of the company would be required to be taken into consideration for determining the substantial part of business.

The capital employed for a specific division of a company in comparison to total capital employed would also be relevant to determine whether the part of the business constitutes a substantial part.

7. (a) The Supreme Court, in *Liberty India v. CIT* [2009] 317 ITR 218, observed that section 80-IB provides for deduction in respect of profits and gains “derived from the business” of the assessee and accordingly, the Parliament intended to cover sources of profits and gains not beyond the first degree. There should be a direct nexus between the generation of profits and gains and the source of profits and gains, the latter being directly relatable to the business of the assessee. Any other source, not falling within the first degree, can only be considered as ancillary to the business of the assessee.
- (i) The issue of whether income derived from sale of export incentive would qualify for deduction under section 80-IB came up recently before the Punjab & Haryana High Court in *CIT v. Jaswand Sons* (2010) 328 ITR 442, wherein the High Court held income derived from sale of export incentive cannot be said to be income “derived from” the industrial undertaking and therefore, such income is not eligible for deduction under section 80-IB.
 - (ii) In *CIT v. Meghalaya Steels Ltd.* (2011) 332 ITR 91, the Gauhati High Court observed that the transport and interest subsidies were revenue receipts which were granted after setting up of the new industries and after commencement of production. The transport subsidy would have the effect of reducing the inward and outward transport costs for the purposes of determining the cost of production as well as for sales. However, the subsidy had no direct nexus with the profits or gains derived by the assessee from its industrial activity and the benefit to the assessee was only ancillary to its industrial activity. The subsidies were not directly relatable to the industrial activity of the assessee, and hence they did not fall within the first degree contemplated by the Act. Therefore, the subsidies could not be taken into account for purposes of deduction under section 80-IB.
 - (iii) The payment of Central excise duty, however, has a direct nexus with the manufacturing activity and similarly, the refund of the Central excise duty also had a direct nexus with the manufacturing activity, being a profit-linked incentive, since payment of the Central excise duty would not arise in the absence of any industrial activity. Therefore, the refund of excise duty had to be taken into account for purposes of section 80-IB.
- (b) As regards the issue of whether an assessee who has not claimed deduction under section 80-IB in the initial years can claim the said deduction for the remaining

years during the period of eligibility, the Delhi High Court, in *Praveen Soni v. CIT (2011) 333 ITR 324*, held that the provisions of section 80-IB nowhere stipulated a condition that the claim for deduction under this section had to be made from the first year of qualification of deduction failing which the claim will not be allowed in the remaining years of eligibility. Therefore, the deduction under section 80-IB should be allowed to the assessee for the remaining years up to the period for which his entitlement would accrue, provided the conditions mentioned under section 80-IB are fulfilled.

8. The Finance Act, 2011 has introduced the concept of "Alternate Minimum Tax" on limited liability partnerships (LLPs). Accordingly, LLPs would be subject to Alternate Minimum Tax @ 18.5%. Though the concept of Alternate Minimum Tax (AMT) is similar to MAT in case of corporates, however, the tax base in the case of LLPs would be the adjusted total income computed as per the Income-tax Act, 1961 and not the book profit computed after making the specified adjustments to the profit as per the profit and loss account prepared in accordance with Schedule VI to the Companies Act, 1956, as in the case of companies.

Where the regular income-tax payable by an LLP for a previous year computed as per the provisions of the Income-tax Act, 1961 (other than Chapter XII-BA) is less than the AMT payable for such previous year, the adjusted total income shall be deemed to be the total income of the LLP. The LLP shall be liable to pay income-tax on the adjusted total income @ 18.5%.

"Adjusted total income" would mean the total income before giving effect to Chapter XII-BA as increased by the deductions claimed under –

- (1) any section included in Chapter VI-A under the heading "C – Deductions in respect of certain incomes"; and
- (2) section 10AA.

Such LLPs to which this section applies should obtain a report in the prescribed form from a Chartered Accountant certifying that the adjusted total income and the AMT have been computed in accordance with the provisions of this Chapter. The LLP has to furnish such report on or before the due date of filing of return under section 139(1).

Section 115JE specifically provides that "save as otherwise provided in this Chapter, all other provisions of this Act shall apply to a LLP referred to in this Chapter". Hence, all other provisions relating to advance tax, interest under sections 234A, 234B and 234C, penalty etc. would also apply to a LLP which is subject to AMT.

Further, AMT paid in excess of income-tax payable under the normal provisions of the Income-tax Act, 1961 for any year would be eligible for credit to be carried forward and set-off against income-tax payable in the later year to the extent of excess of income-tax payable under the regular provisions over the AMT payable in that year. The balance tax credit, if

any, shall be carried forward to the next year for set-off in that year in a similar manner.

AMT credit can be carried forward for set-off upto a maximum period of 10 assessment years succeeding the assessment year in which the credit becomes allowable. No interest shall, however, be payable on such tax credit. If the amount of regular income-tax or AMT is reduced or increased as a result of any order passed under the Income-tax Act, 1961, the amount of tax credit allowed under section 115JD would also vary accordingly.

9. Computation of business income of M/s. LMN for the A.Y 2012-13

Particulars	₹	₹
Net profit as per profit and loss account		1,00,000
Add : Remuneration to partners (considered separately)		<u>2,50,000</u>
		3,50,000
Add: Inadmissible expenses :		
Interest [54,000 – 36,000 (calculated@12%)]	18,000	
Provident fund payment outstanding as on due date of filing of return - disallowed under section 43B	10,000	
Cash purchases [disallowed under section 40A(3)]	<u>80,000</u>	<u>1,08,000</u>
		4,58,000
Less: Amount credited but exempt		
Dividend from Indian company[Exempt under section 10(34)]		<u>8,000</u>
Book Profit		4,50,000
Less: Remuneration to partners deductible (See note below)		<u>2,50,000</u>
Taxable business income		<u>2,00,000</u>

Note - Computation of remuneration allowable as deduction as per 40(b)(v)

Particulars	Percentage allowable	₹
On first 3,00,000 of book profit	90%	2,70,000
On the balance book profit of ₹ 1,50,000	60%	<u>90,000</u>
Remuneration allowable as per 40(b)(v)		<u>3,60,000</u>

Since the actual remuneration of ₹ 2,50,000 is less than the allowable limit of ₹ 3,60,000, the entire remuneration of ₹ 2,50,000 is deductible.

10. The statement is correct.

New section 115BBD has been introduced by the Finance Act, 2011 to provide for a concessional rate of tax on dividends received by Indian companies from specified foreign companies. Specified foreign company has been defined to mean a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital of the company.

Dividends received by Indian companies from specified foreign companies to be subject to a concessional rate of 15% as against the existing rate of 30%. This rate of 15% would be applied on gross dividend, in the sense, that no expenditure would be allowable in respect of such dividend. However, this concessional rate would not be applicable in respect of dividend received from a foreign company in which the holding of the Indian company is less than 26% of the nominal value of the equity share capital.

Therefore, if the total income of an Indian company, includes income by way of dividend declared, distributed or paid by a specified foreign company, the income tax payable would be the aggregate of –

- (a) Income-tax @15% on gross dividend from such specified foreign company; and
- (b) Income-tax with which the assessee would have been chargeable had its total income been reduced by such dividend.

11. Computation of Book Profit under section 115JB

Particulars	₹	₹
Net profit as per profit and loss account		44,74,000
<i>Add:</i> Net Profit to be increased by the following amounts as per <i>Explanation 1</i> to section 115JB		
Provision for income-tax	9,18,000	
Provision for diminution in the value of investment	72,000	
Transfer to General Reserve	2,10,000	
Provision for losses of subsidiary company	1,40,000	
Expenditure to earn agricultural income [exempt u/s 10(1)]	50,000	
Depreciation	3,50,000	17,40,000
		62,14,000
<i>Less:</i> Net Profit to be reduced by the following amounts as per <i>Explanation 1</i> to section 115JB		
Amount credited to profit and loss account from Special Reserve	1,00,000	
Depreciation (excluding depreciation on account of revaluation of fixed assets) (i.e. ₹ 3,50,000 – ₹ 1,50,000)	2,00,000	
Amount credited to profit and loss account from Revaluation Reserve (to the extent of depreciation on revaluation)	1,50,000	
Brought forward business loss or unabsorbed depreciation as per books of account, whichever is less, taken on cumulative basis	7,00,000	

Agricultural Income [since it is exempt under section 10(1)]	2,50,000	
		14,00,000
Book Profit		48,14,000
18.50% of book profit		8,90,590
Add: Education cess @ 2%	17,812	
Secondary and higher education cess @ 1%	8,906	26,718
Tax liability under section 115JB		9,17,308
Total income computed as per the provisions of the Income-tax Act, 1961	25,00,000	
Tax payable @ 30%		7,50,000
Add: Education cess @ 2%	15,000	
Secondary and higher education cess @ 1%	7,500	22,500
Tax Payable as per the Income-tax Act, 1961		7,72,500

In case of a company, it has been provided that where income-tax payable on total income computed as per the provisions of the Act is less than 18.50% of book profit, the book profit shall be deemed as the total income and the tax payable on such total income shall be 18.50% thereof plus education cess @ 2% and secondary and higher education cess @ 1%. Accordingly, in this case, since income-tax payable on total income computed as per the provisions of the Act is less than 18.50% of book profit, the book profit of ₹ 48,14,000 is deemed to be the total income and income-tax is payable @ 18.50% thereof plus education cess @ 2% and secondary and higher education cess @ 1%. The tax liability, therefore, works out to ₹ 9,17,308.

Section 115JAA provides that where tax is paid in any assessment year in relation to the deemed income under section 115JB(1), the excess of tax so paid, over and above the tax payable under the other provisions of the Income-tax Act, 1961, will be allowed as tax credit in the subsequent years. The tax credit is, therefore, the difference between the tax paid under section 115JB(1) and the tax payable on the total income computed in accordance with the other provisions of the Act. This tax credit is allowed to be carried forward for ten assessment years succeeding the assessment year in which the credit became allowable. Such credit is allowed to be set off against the tax payable on the total income in an assessment year in which the tax is computed in accordance with the provisions of the Act, other than section 115JB, to the extent of excess of such tax payable over the tax payable on book profits in that year.

Particulars	₹
Tax on book profit under section 115JB	9,17,308
Less: Tax on total income computed as per the other provisions of the Act	7,72,500
Tax credit to be carried forward	1,44,808

Notes:

- (1) Wealth-tax and securities transaction tax do not form part of income-tax and hence, should not be added back to net profit for computing book profit.
- (2) Provision for gratuity based on actuarial valuation is a provision for meeting an ascertained liability. Therefore, it should not be added back for computing book profit.
- (3) Long-term capital gains on sale of equity shares through a recognized stock exchange on which securities transaction tax (STT) is paid is exempt under section 10(38). One of the adjustments to the book profit is that exempt income under section 10, which is credited to profit and loss account, would be deducted in arriving at the book profit.

However, deduction of such long-term capital gains is not allowed for computing book profit. Consequently, expenditure to earn such income should not be added back to arrive at the book profit. Section 10(38) also provides that such long term capital gain of a company shall be taken into account in computing the book profit and income-tax payable under section 115JB.

- 12. (a)** The Assessing Officer may, in course of proceeding under section 147, assess or reassess any other income which has escaped assessment and which comes to his notice subsequently in the course of such proceeding.

Explanation 3 to section 147 clarifies that the Assessing Officer may assess or reassess the income in respect of any issue (which has escaped assessment) which comes to his notice subsequently in the course of proceedings under section 147, even though the reason for such issue does not form part of the reasons recorded under section 148(2).

Therefore, the contention of XYZ (P) Ltd. is not correct.

- (b)** The Assessing Officer cannot issue notice under section 148 to reopen the same assessment order on the same grounds for which the Commissioner had issued notice under section 263 of the Income-tax Act, 1961, since the second proviso to section 147 specifically provides 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. Therefore, if the income relates to a matter which is the subject matter of revision under section 263, then the Assessing Officer cannot issue notice under section 148 to reopen the assessment order.

- 13.** This statement is correct.

The Finance Act, 2011 has expanded the powers of the Transfer Pricing Officer under section 92CA to empower him to -

- (i) determine the arm's length price of other international transactions, identified subsequently in course of proceedings before him. So far, his powers were restricted to determining the arm's length price of international transactions referred to him by the Assessing Officer.
- (ii) conduct a survey by exercising the powers conferred upon an income-tax authority under section 133A for the purpose of determining the arm's length price.

- 14.** Since MNC Inc. is located in a notified jurisdictional area (NJA), the transaction of provision of technical services by the Indian company, Geomatics Ltd., would be deemed to be an international transaction and MNC Inc. and Geomatics Ltd. would be deemed to be associated enterprises. Therefore, the provisions of transfer pricing would be attracted in this case.

The prices of ₹ 48 lakhs and ₹ 52 lakhs charged for similar services from Alpha Inc and Beta Inc, respectively, being independent entities located in non-NJA countries, can be taken into consideration for determining the arm's length price (ALP) under Comparable Uncontrolled Price (CUP) Method.

Since more than one price is determined by the CUP Method, the ALP would be the arithmetical mean of such prices.

Therefore, the ALP = ₹ 50,00,000 i.e., $(48,00,000 + 52,00,000) / 2$

Transfer price = ₹ 40,00,000

Since the ALP is more than the transfer price, the ALP of ₹ 50 lakhs would be considered as the income arising from the international transaction between Geomatics Ltd. and MNC Inc.

It may be noted that the benefit of permissible variation between the ALP and the transfer price at the rate notified by the Central Government for a particular class of international transaction would not be available where transfer pricing provisions are attracted under section 94A. Therefore, it is not necessary to determine the impact, if any, of such permissible variation.

- 15.** The statement is not correct.

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.

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 of the appeal within this period of stay.

Where the appeal has not been disposed of 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 even if the delay in disposing of the appeal is not attributable to the assessee. The Appellate Tribunal is required to dispose of the appeal within this extended period. 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.

Therefore, the statement given in the question is not correct.

16. The statement is not correct.

Section 245D(4) stipulates that the Settlement Commission shall pass an order after giving an opportunity of being heard to the applicant and the Commissioner. Under section 245F(1), the Settlement Commission has been conferred all the powers which are vested in an income-tax authority under the Act. Under section 154, an income-tax authority has the power to amend any order passed by it in order to rectify any mistake apparent from the record. However, there are High Court rulings holding that the order made by the Settlement Commission is conclusive and final and therefore, the same cannot be rectified under section 154. This view, however, does not convey the true legislative intent.

Therefore, in order to reflect the correct intention of the legislature, sub-section (6B) has been inserted in section 245D by the Finance Act, 2011 to specifically provide that the Settlement Commission may amend any order passed by it under section 245D(4) to rectify any mistake apparent from the record. However, the time limit for effecting such amendment is within six months from the date of its order, as against the permissible time limit of four years provided for under section 154(7).

Further, the Settlement Commission should not make a rectification which has the effect of modifying the liability of the applicant, without –

- (1) giving a notice to the applicant and the Commissioner of its intention to do so; and
- (2) allowing the applicant and the Commissioner an opportunity of being heard.

17. This issue came up before the Kerala High Court in *Vodafone Essar Cellular Ltd. v. ACIT (TDS)* (2011) 332 ITR 255

On this issue, the Kerala High Court observed that it was the SIM card which linked the mobile subscriber to the assessee's network. Therefore, supply of SIM card by the assessee-telecom company was only for the purpose of rendering continued services to the subscriber of the mobile phone. The position was the same so far as recharge coupons or e-top ups were concerned which were only air time charges collected from the subscribers in advance under a prepaid scheme.

There was no sale of any goods involved as claimed by Teleco Ltd. and the entire charges collected by Teleco Ltd. from the distributors at the time of delivery of SIM cards or recharge

coupons were only for rendering services to ultimate subscribers. Teleco Ltd. was accountable to the subscribers for failure to render prompt services pursuant to connections given by the distributor. Therefore, the distributor only acted as a middleman on behalf of Teleco Ltd. for procuring and retaining customers and therefore, the discount given to him was within the meaning of commission under section 194H on which tax was deductible.

18. The issue under consideration in this case is whether the difference between the published price and the minimum fixed commercial price amounts to additional special commission in the hands of the agents to attract the provisions of section 194H.

This issue came up before *CIT v. Qatar Airways (2011) 332 ITR 253*, where the Bombay High Court observed that the difference between the published price and minimum fixed commercial price cannot be taken as additional special commission in the hands of the agents, since the published price was the maximum price and the airline company had granted permission to the agents to sell the tickets at a price lower than the published price. In order to deduct tax at source, the exact income in the hands of the agents must necessarily be ascertainable by the airline company. However, the airline company would have no information about the exact rate at which the tickets were ultimately sold by its agents, since the agents had been given the discretion to sell the tickets at any rate between the minimum fixed commercial price and the published price. It would be impracticable and unreasonable to expect the airline company to get a feedback from its numerous agents in respect of each ticket sold.

Thus, tax was not deductible at source on the difference between the actual sale price and the minimum fixed commercial price, even though the amount earned by the agent over and above minimum fixed commercial price would be taxable as income in his hands.

19. **Computation of net wealth of Sky Heights Limited as on 31.3.2012**

	Particulars	Note No.	₹ in lacs
(i)	Land in urban area	(1)	Nil
(ii)	Motor-cars used on hire	(2)	Nil
(iii)	Jewellery	(3)	22
(iv)	Cash balance	(4)	Nil
(v)	Bank balance	(5)	Nil
(vi)	Guest house	(6)	12
(vii)	Residential flat occupied by the Managing Director	(7)	18
(viii)	Residential house let out for 230 days	(8)	16
			68
	Less: Loan obtained for purchasing jewellery	(9)	13
	Net wealth as on 31.3.2012		55

Notes:

- (1) Land in urban area on which the construction is not permitted as per municipal laws in force is not an asset within the meaning of "asset" as defined under section 2(ea) and as such is excluded from taxability.

- (2) Motor car held as stock in trade or used on hire is not taxable.
 - (3) Jewellery is taxable unless the same is held as stock in trade.
 - (4) In case of a company, cash on hand is not taxable to the extent reflected in the books of account. In this case, since cash balance of ₹ 3,00,000 is as per books of the company, it is not taxable.
 - (5) Bank balance is not an asset within the meaning of "asset" as defined in section 2(ea).
 - (6) Guest house situated 30 kms away from the local limits of the municipality is an asset and is, therefore, taxable. Only in the case of farm house situated beyond 25 kms from the local limits of any municipality, the taxability would not arise.
 - (7) Residential flat which is allotted by a company to an employee or an officer or a director who is in whole time employment, having gross annual salary of ₹ 5 lacs or more is an asset within the meaning of "asset" as defined in section 2(ea). Accordingly, the residential flat occupied by the Managing Director is taxable since his annual remuneration is ₹ 10 lacs.
 - (8) Any residential property which is let out for a minimum period of 300 days in the previous year is not an asset. In the given case, the residential house is taxable since it has been let out for only 230 days (i.e. less than 300 days during the previous year).
 - (9) Debts incurred in relation to assets chargeable to wealth tax shall be allowed as deduction in the computation of net wealth. Accordingly, loan obtained for purchase of jewellery shall be allowed as deduction since jewellery is assessable to wealth tax.
- 20.** In the given case, Madan is the owner of two residential houses for self-occupation, one at Calcutta and another at Bangalore.

The value of any one house can be claimed as exempt under section 5(vi) of the Wealth-tax Act, 1957. Madan should first determine the value to be adopted for wealth-tax purpose and then should select the house with the higher value for availing such exemption.

As per section 7(2) of the Wealth-tax Act, 1957, the value of a house belonging to the assessee and exclusively used by him for residential purposes throughout the period of 12 months immediately preceding the valuation date, may, at the option of the assessee, be taken to be the value determined in the manner laid down in Schedule III as on the valuation date next following the date on which he became the owner of the house or the valuation date relevant to the assessment year commencing on 1st April, 1971, whichever valuation date is later.

This benefit of pegging down of value is available only if the house is self-occupied by the assessee throughout the period of 12 months immediately preceding the valuation date. Therefore, such benefit of pegging down of value cannot be availed for the house situated at Calcutta since the house was occupied by the Madan's relative for a part of the year. The value of such house would be the Schedule III value as on 31st March, 2012 or the cost

of acquisition, whichever is higher. Therefore, the Schedule III value of the flat at Calcutta as on the valuation date 31st March, 2012, being ₹ 28 lacs, or the cost of acquisition of ₹ 12 lacs, whichever is higher, is to be adopted as the value for wealth-tax purpose. Accordingly, ₹ 28 lacs is the value of the Calcutta house for wealth-tax purpose.

The benefit of pegging down of value can be opted for the flat situated at Bangalore, as it was self-occupied by Mr. Madan throughout the 12 months immediately preceding the valuation date of 31st March, 2012 for his residential purposes. In case of the house at Bangalore, the Schedule III value as on 31st March, 2006, being the first valuation date after he became the owner, i.e. ₹ 7 lacs can be adopted, since its cost of acquisition does not exceed ₹ 50 lacs. Therefore, ₹ 7 lacs is the value of the Bangalore house for wealth-tax purposes.

It would be more beneficial for Mr. Madan to claim exemption under section 5(vi) in respect of the Calcutta house since the value of the Calcutta house (₹ 28 lacs) is higher than the value of the Bangalore house (₹ 7 lacs) as on the valuation date 31st March, 2012.