

PAPER – 7 : DIRECT TAX LAWS
PART – III : QUESTIONS AND ANSWERS
QUESTIONS

Incomes which do not form part of total income

1. (a) Help All, a trust created on 1st January, 2014 for providing relief to the poor, applied for registration under section 12A on 1st March, 2014. On that date, its corpus fund comprised only of the initial contribution made by the trustees. The Commissioner denied registration solely on the ground that the trust had not commenced any charitable activity, due to which he could not satisfy himself about the genuineness of the trust. Is the ground for denial of registration by the Commissioner justified in this case? Discuss.
- (b) Educare, a trust created with the objective of promoting primary education in rural areas, filed an application for registration under section 12A on 1st April, 2013. Since the application was not disposed of by the Commissioner on or before 31st October, 2013 as required under section 12AA(2), the trust contended that it was deemed to be registered as per the provisions of section 12AA(1). Examine the correctness of contention of the trust.

Profits and gains of business or profession

2. Discuss, with the aid of decided case laws, whether the following expenditure are **revenue** or **capital** in nature –
 - (a) Expenditure incurred on glow-sign boards displayed at dealer outlets;
 - (b) Share issue expenses incurred by a company, where the public issue could not ultimately materialize on account of non-clearance by SEBI; and
 - (c) Expenditure incurred for purchase of second-hand medical equipment for use as spare parts of existing equipment.
3. Ashiana Ltd., a company engaged in the business of manufacture of household equipments, furnishes the following particulars pertaining to P.Y. 2013-14. Compute the deduction allowable under section 32 and section 32AC for A.Y.2014-15, while computing its income under the head “Profits and gains of business or profession”. Also, compute the written down value of plant and machinery as on 1.4.2014.

	Particulars	₹ in crores
1.	Written down value of plant and machinery (15% block) as on 1.4.2013	27.00
2.	Sold plant and machinery on 14.7.2013 (15% block)	3.00
3.	Purchase of second hand machinery (15% block) on 5.8.2013 for business purpose (the machinery was put to use immediately)	18.00
4.	Purchased new air-conditioners for office use on 27.8.2013	0.15

5.	Purchased new computers (60% block) on 1.12.2013 for office use	0.35
6.	Purchased computer accessories and peripherals (UPS, printers and scanners) on 1.12.2013 for office use	0.05
7.	Acquired and installed new plant and machinery (15% block) on 24.6.2013 (₹ 38 crore) and on 9.11.2013 (₹ 72 crore)	110.00

Profits and gains of business or profession, Capital Gains, Income from other sources & Provisions concerning deduction of tax at source

4. Mr. Harish, Vice President of ABC Bank, sold his house property in Chennai as well as his rural agricultural land for a consideration of ₹ 60 lakh and ₹ 15 lakh, respectively, to Mr. Suresh, a retail trader, on 10.10.2013. Mr. Harish had purchased the house property and the land in the year 2011 for ₹ 40 lakh and ₹ 10 lakh, respectively. The stamp duty value on the date of transfer, i.e., 10.10.2013, is ₹ 85 lakh and ₹ 20 lakh for the house property and rural agricultural land, respectively.
- (a) Determine the tax implications in the hands of Mr. Harish and Mr. Suresh, if the date of agreement for sale of house property and rural agricultural land is 1.7.2013 and the stamp duty value on the said date was ₹ 75 lakh and ₹ 15 lakh, respectively. On the said date, Mr. Suresh made a cheque payment of ₹ 5 lakh to Mr. Harish for purchase of house property. Also, discuss the TDS implications, if any, in the hands of Mr. Suresh, assuming that both Mr. Harish and Mr. Suresh are resident Indians.
- (b) Would your answer be different if Mr. Harish is a property dealer and sold the house property in the course of his business?

Capital Gains

5. Mr. X was the owner of a residential house comprising of two floors. In April 2013, he entered into a collaboration agreement with Arihant Builders for developing the property. According to the terms of the agreement, Arihant Builders were to demolish the existing structure on the plot of land and develop, construct, and put up a building consisting of four independent floors - ground floor, first floor, second floor and third floor with terrace at its own cost. Mr. X handed over to Arihant Builders, the physical possession of the entire property, for the limited purpose of development. Arihant Builders was to get the third floor plus the undivided interest in the land to the extent of 25% for its exclusive enjoyment. The remaining floors (i.e., the ground, first and second) were to be handed over to Mr. X after construction.

The cost of construction of each floor was ₹ 1 crore, which was borne by Arihant Builders. In addition to the cost of construction incurred by Arihant Builders on development of the property, a further amount of ₹ 5 crore was payable by Arihant Builders to Mr. X as consideration against the rights of Mr. X.

You are required to discuss and resolve the following issues arising in the assessment of Mr. X as a result of the above transaction –

- (i) For computation of capital gains, what should be the full value of consideration accruing as a result of transfer of the capital asset?
- (ii) Is Mr. X eligible for exemption under section 54F?
- (iii) If the answer to (ii) is yes, whether exemption is to be restricted to the cost of construction of one independent floor, on the reasoning that the floors given to Mr. X contained independent residential units having separate entrances and therefore, cannot qualify as a single residential unit?

Income from other sources

6. (a) Discuss the applicability of the provisions of section 56(2)(viib) in respect of the shares issued by the following closely held companies to resident Indians –

Company	Consideration received for issue of a share (₹)	Face value of a share (₹)	Fair Market Value (FMV) of a share (₹)	Number of shares issued
Win (P) Ltd.	370	300	350	1,00,000
Gain (P) Ltd.	330	300	350	2,00,000
Profit (P) Ltd.	290	300	280	3,00,000
Top (P) Ltd.	310	300	275	4,00,000

- (b) 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. What can be some of the tests to determine “substantial part of the business” of lending company for the purpose of application of exclusion provision under section 2(22)?

Set-off and carry forward of losses

7. Mr. Arjun was a partner in M/s. XYZ & Co., which dissolved on 31st August, 2013. As per the dissolution deed of the partnership firm, Mr. Arjun took over the entire business of the partnership firm in his individual capacity including fixed assets, current assets and liabilities and the other partners were paid their dues. Mr. Arjun then ran the business as a sole proprietor with effect from 1st September, 2013. Relying upon the provisions section 78(2) and the decisions of the Supreme Court in *CIT v. Madhukant M. Mehta (2001) 247 ITR 805* and *Saroj Aggarwal v. CIT (1985) 156 ITR 497*, Mr. Arjun claimed the set-off of the losses suffered by the M/s. XYZ & Co. against his income earned as an individual proprietor for A.Y.2014-15 considering the case as inheritance of business. Discuss whether the claim of Mr. Arjun is tenable. In this regard, also examine whether there is any contradiction between the provisions of section 78(2) and section 170(1).

Deductions from Gross Total Income

8. From the following details, compute the total income of Mr. A, Mr. B and Mr. C for A.Y.2014-15 –

Particulars		Mr. A ₹	Mr. B ₹	Mr. C ₹
(i)	Salary (computed)	9,25,000	10,45,000	11,15,000
(ii)	Interest income (on fixed deposits)	75,000	85,000	95,000

Mr. A, Mr. B and Mr. C are new retail investors who have made the following investments in equity shares/units of equity oriented fund of Rajiv Gandhi Equity Savings Scheme, 2013 for the P.Y.2013-14:

Particulars		Mr. A ₹	Mr. B ₹	Mr. C ₹
(i)	Investment in listed equity shares	15,000	62,000	23,000
(ii)	Investment in units of equity-oriented fund	30,000	-	25,000

The particulars of their other investments/payments made during the P.Y.2013-14 are given hereunder -

	Particulars				₹
(1)	Deposit in Public Provident Fund (PPF) by Mr. A				80,000
(2)	Life insurance premium paid by Mr. C, the details of which are as follows -				

(3)	Payment of medical insurance premium by the following persons to insure their health:													
	<table> <tr> <th>Payer</th><th>Amount in ₹</th><th>Mode of payment</th></tr> <tr> <td>Mr. A (aged 55 years)</td><td>20,000</td><td>Account payee cheque</td></tr> <tr> <td>Mr. B (aged 52 years)</td><td>15,000</td><td>Cash</td></tr> <tr> <td>Mr. C (aged 48 years)</td><td>10,000</td><td>Crossed cheque</td></tr> </table>	Payer	Amount in ₹	Mode of payment	Mr. A (aged 55 years)	20,000	Account payee cheque	Mr. B (aged 52 years)	15,000	Cash	Mr. C (aged 48 years)	10,000	Crossed cheque	
Payer	Amount in ₹	Mode of payment												
Mr. A (aged 55 years)	20,000	Account payee cheque												
Mr. B (aged 52 years)	15,000	Cash												
Mr. C (aged 48 years)	10,000	Crossed cheque												
(4)	Mr. B paid interest on loan taken for the purchase of house in which he currently resides. He is claiming benefit of self-occupation under section 23(2) in respect of this house. He does not own any other house.	1,90,000												
	Repayment of principal amount of loan taken for purchase of the said house (The housing loan of ₹ 23 lakhs was sanctioned by HDFC on 3.4.2013 and disbursed in full on 10.4.2013, being the date of purchase of house property, the cost of which was ₹ 28 lakhs).	1,50,000												
(5)	Contribution by Mr.A by cheque to National Children's Fund during the year.	30,000												
(6)	Mr. B makes the following donations during the P.Y.2013-14 -													
	Donation to BJP by crossed cheque	50,000												
	Donation to Electoral trust by cash	50,000												

What would be the tax consequence if Mr. A and Mr. C sold their entire investment in units of equity oriented fund in May 2014?

Assessment of companies

9. Alpha Ltd. earned a net profit of ₹ 15,75,000 after debit/credit of the following items to its profit and loss account for the year ended on 31.3.2014:

(a)	Items debited to Profit and Loss Account	₹
	Provision for income-tax	1,75,000
	Interest on income-tax	9,000
	Dividend distribution tax	32,000
	Provision for deferred tax	21,000
	Securities Transaction Tax	11,000
	Transfer to General Reserve	32,000
	Provision for gratuity based on actuarial valuation	27,000
	Provision for diminution in the value of investment	17,000

	Proposed dividend	30,000
	Preference dividend	18,000
	Expenditure to earn agricultural income	12,000
	Expenditure to earn LTCG exempt under section 10(38)	7,000
	Expenditure to earn dividend income	4,500
	Depreciation (including depreciation of ₹ 14,000 on revaluation)	36,000
(b)	Items credited to Profit and Loss Account	
	Amount credited to P& L A/c from Special Reserve	24,000
	Amount credited to P& L A/c from Revaluation Reserve	18,000
	Agricultural income	27,000
	LTCG exempt under section 10(38)	19,000
	Dividend income	21,000

The company provides the following additional information:

Brought forward Business Loss/Unabsorbed Depreciation:

Assessment Year	Amount as per books	
	Loss	Depreciation
2011-12	40,000	70,000
2012-13	50,000	40,000
2013-14	30,000	Nil

You are required to examine the applicability of section 115JB of the Income-tax Act, 1961 and compute book profit and the tax credit, if any, to be carried forward, assuming that the total income computed as per the provisions of the Income-tax Act, 1961 is ₹ 10,00,000.

10. ABC Ltd., an Indian company, receives the following dividend income during the P.Y. 2013-14 -

- (1) from shares held in BCD Inc., a Danish company, in which it holds 25% of nominal value of equity share capital – ₹ 65,000;
- (2) from shares held in EFG Inc., an English company, in which it holds 31% of nominal value of equity share capital – ₹ 1,50,000.
- (3) from shares held in HIJ Inc., a Dutch company, in which it holds 62% of the nominal value of equity share capital - ₹ 1,07,000
- (4) from shares held in Indian subsidiaries, on which dividend distribution tax has been paid by such subsidiaries – ₹ 47,000.

ABC Ltd. has paid remuneration of ₹ 16,000 for realising dividend, the break up of which

is as follows –

- (1) ₹ 4,000 (BCD Inc.); (2) ₹ 7,000 (EFG Inc.); (3) ₹ 5,000 (Indian subsidiaries)

The business income of ABC Ltd. computed under the provisions of the Act is ₹ 48 lakh. Compute the total income and tax liability of ABC Ltd., ignoring MAT. Assuming that ABC Ltd. has distributed dividend of ₹ 4,20,000 in February, 2014, compute the additional income-tax payable by it under section 115-O. Ignore the provisions of double taxation avoidance agreement, if any, applicable in this regard.

Assessment of various entities

11. M/s. ABC & Co., a resident firm, has income of ₹ 95 lakh under the head “Profits and gains of business or profession”. It undertook two projects in Tamil Nadu - a highway project in East Coast Road (ECR) which involves expansion of existing roads by constructing additional lanes and a roadway project in Old Mahabalipuram Road (OMR), which involves relaying of existing roads. The profit from the highway project in ECR is ₹ 50 lakh and roadway project in OMR is ₹ 30 lakh. The firm is also engaged in cement trading, the profit from which is ₹15 lakh. The trading unit transferred cement worth ₹ 5 lakh to the ECR project at ₹ 2 lakh. Compute the tax payable by M/s. ABC & Co. for A.Y.2014-15, assuming that it has no other income during the P.Y.2013-14.
12. A securitization trust distributes income of ₹ 6,50,000 on 17th August, 2013 to its investors comprising of -

	Category of investor	Income distributed (₹)
(i)	Mutual funds exempt under section 10(23D)	1,50,000
(ii)	Individuals and HUFs	1,00,000
(iii)	Companies	4,00,000

Compute the additional income-tax payable by the trust under section 115TA. Assuming that the additional income-tax payable as per section 115TA is paid to the credit of the Central Government on 7th November, 2013, compute the interest, if any payable, under section 115TB.

Assessment Procedure

13. (a) The assessment of Ashiana Pvt. Ltd. for the A.Y. 2012-13 was completed under section 143(3). On 25-3-2014, the Assessing Officer reopened the assessment on the ground 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 Ashiana Pvt. Ltd.
- (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.

14. Mr. Hari, aged 65 years, is a resident and ordinarily resident in India for the A.Y.2014-15. He owns a house property in Dubai, which he purchased on 30.4.2004, and he also has a bank account in the Bank of Dubai.
- (a) Mr. Hari contends that since his total income of ₹ 2,40,000 for the P.Y.2013-14, comprising of income from house property and bank interest, is less than the basic exemption limit, he need not file his return of income for A.Y.2014-15.
 - (b) Mr. Hari also contends that the notice issued by the Assessing Officer under section 148 in June, 2014 for A.Y.2005-06 is not valid due to the following reasons –
 - (i) There is no escaped income relating to that year; and
 - (ii) The time period prescribed in section 149 for issuing notice under section 148 for A.Y.2005-06 has since lapsed.

Discuss the correctness of the above contentions of Mr. Hari.

Appeals and Revision

15. Discuss the correctness or otherwise of the following statements with reference to the provisions of the Income-tax Act, 1961 –
- (i) An appeal before Appellate Tribunal cannot be decided in the event of difference of opinion between the Judicial member and the Accountant member on a particular ground;
 - (ii) The Appellate Tribunal is empowered to grant indefinite stay for the demand disputed in the appeals before it.

Deduction, Collection and Recovery of tax

16. Discuss the applicability of provisions for deduction of tax at source under section 194H in the following cases –
- (i) Discount given to stamp vendors on purchase of stamp papers;
 - (ii) Discount given on supply of SIM cards and recharge coupons by a telecom company to its distributors under a prepaid scheme.

Double Taxation Relief

17. Mr. Vallish, a resident Indian aged 36 years, earned a sum of ₹ 15 lakh during the P.Y.2013-14 from playing kabaddi matches in a country with which India does not have a double taxation avoidance agreement (DTAA). Tax of ₹ 3 lakh was levied on such income in the source country. In India, he earned a sum of ₹ 18 lakh during the P.Y.2013-14 from playing kabaddi matches. He has deposited ₹ 1 lakh in public

provident fund. He qualifies as a new retail investor under the Rajiv Gandhi Equity Savings Scheme, 2013 and has invested ₹ 50,000 in listed equity shares under the said scheme. He paid medical insurance premium of ₹ 18,000 to insure his health and ₹ 22,000 to insure the health of his father, aged 61 years, who is not dependent on him. Compute his income-tax liability for the A.Y.2014-15.

Transfer Pricing

18. Examine the following transactions and discuss whether the transfer price declared by the following assessee, who have exercised a valid option for application of safe harbour rules, can be accepted by the Income-tax Authorities –

	Assessee	International transaction	Aggregate value of transactions entered into in the P.Y.2013-14	Declared Operating Margin	Operating Expense
(1)	A Ltd., an Indian company	Provision of system support services to X Inc., which is a "specified foreign company" in relation to A Ltd.	₹ 600 crore	₹ 90 crore	₹ 450 crore
(2)	B Ltd., an Indian company	Provision of data processing services with the use of information technology to Y Inc., its foreign subsidiary.	₹ 400 crore	₹ 62 crore	₹ 300 crore
(3)	C & Co., a partnership firm registered under the Partnership Act, 1932	Provision of contract R & D services relating to development of internet technology, to XYZ & Co., a foreign firm, which holds 12% interest in C & Co.	₹ 100 crore	₹ 20 crore	₹ 70 crore
(4)	D Ltd., an Indian company	Provision of contract R & D services relating to generic pharmaceutical drug, to ABC Inc., a foreign company which guarantees 15% of the total borrowings of D Ltd.	₹ 50 crore	₹ 9 crore	₹ 30 crore
(5)	Sole proprietary concern of Mr.E, solely engaged in the original manufacture and export of	100% export of automobile transmission and steering parts to LMN LLP, a foreign LLP, controlled by Mr.E jointly with his relatives.	₹ 12 crore	₹ 1 crore	₹ 10 crore

	automobile transmission and steering parts.				
(6)	F Ltd. an Indian company, solely engaged in the original manufacture and export of non-core auto components.	100% export of non-core auto components to GKG Inc., a foreign company. F Ltd. appoints two-thirds of the Board of Directors of GKG Inc.	₹ 12 crore	₹ 1 crore	₹ 10 crore

In all the above cases, it may be assumed that the Indian entity which provides the services assumes insignificant risk. It may also be assumed that the foreign entities referred to above are non-resident in India.

Would your answer change, if in any of the cases mentioned above, the foreign entity is located in a notified jurisdictional area?

Wealth-tax

19. Mr. Sridhar, an individual, furnishes the following particulars of his assets and liabilities as on 31.3.2014:

Assets:	₹ in lakhs
Residential house at Mumbai	40
Residential house at Chennai	25
Plot of land comprising an area of 325 square meters at New Delhi	90
House at Calcutta exclusively used for carrying on his business	22
Commercial complex at Chennai	30
Residential house at Bangalore let out for 310 days during the relevant previous year	15
Motor cars used in business of running them on hire	12
Shares in private limited companies	7
Cash in hand	2
Gold jewellery	8
Liabilities:	
Loan borrowed for purchase of land at New Delhi	30
Loan borrowed for purchase of shares in private limited companies	5
Loan borrowed for purchase of gold jewellery	4

The amounts stated against assets, except cash in hand, are the values determined as per section 7 of the Wealth-tax Act, 1957 read with Schedule III thereto.

Compute the net wealth of Mr. Sridhar as on valuation date 31.3.2014.

State the reasons for inclusion or exclusion of the various items.

20. Mrs. Gauri owns two residential houses, one in Chennai and another in Pune. Both the houses are meant to be used for residential purposes by Gauri and her family. The particulars of the houses are as follows:
- (i) The house at Chennai was purchased by her in March, 1980 for ₹ 12 lacs. The house was occupied by her maternal aunt, Mrs. Jyothi, without rent for four months from 1st April, 2013 to 31st July, 2013. The value of the house as per Schedule III to the Wealth-tax Act, 1957 on 31st March, 2014 is ₹ 28 lacs. Its value on the same basis as on 31st March, 1980 was ₹ 15 lacs.
 - (ii) The house at Pune was purchased in February, 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, 2014 are ₹ 7 lacs and ₹ 10 lacs, respectively.

You are required to compute the value of each house for the purpose of computation of net wealth of Mrs. Gauri on the valuation date 31.03.2014.

SUGGESTED ANSWERS/HINTS

1. (a) The Karnataka High Court, in *DIT (Exemptions) v. Meenakshi Amma Endowment Trust (2013) 354 ITR 219*, opined that an application under section 12A for registration of the trust can be sought even within a week of its formation. The activities carried on by the trust are to be seen in a case where the registration is sought much later after formation of the trust.

The High Court further observed that the corpus fund included contribution made by the trustees only, which indicated that the trustees were contributing the funds by themselves in a humble way and were intending to commence charitable activities. The assessee-trust had not also collected any donation for the activities of the trust, by the time its application came up for consideration before them. When the application for registration was made, the trust, therefore, did not have sufficient funds for commencement of its activities.

The High Court observed that, with the money available with the trust, it cannot be expected to carry out activity of charity immediately. Consequently, in such a case, it cannot be concluded that the trust has not intended to do any activity of charity. In such a situation, where application is made shortly after formation of the trust, the objects of the trust as mentioned in the trust deed have to be taken into consideration by the authorities for satisfying themselves about the genuineness of the trust and not the activities carried on by it. Later on, if it is found from the subsequent returns filed by the trust, that it is not carrying on any charitable activity, it would be open to the concerned authorities to withdraw the registration granted or cancel the registration as per the provisions of section 12AA(3).

Applying the rationale of the above ruling, the Commissioner cannot deny registration solely on the ground that the trust had not commenced any charitable activity in this case, since the trust has applied for registration under section 12A within two months after its formation and the corpus fund comprised only of contribution made by the trustees. The Commissioner has to take into consideration the objects of the trust as mentioned in the trust deed to satisfy itself about the genuineness of the trust.

- (b) As per the provisions of section 12AA(2), every order granting or refusing registration under section 12AA(1)(b), **shall** be passed by the registering authority before the expiry of six months from the end of the month in which the application was received under section 12A(1)(a) or section 12A(1)(aa).

The Madras High Court, in *CIT v. Karimangalam Onriya Pengal Semipu Amaipu Ltd.* (2013) 354 ITR 483, noted the decision of the Orissa High Court, in *Srikhetra, A.C. Bhakti-Vedanta Swami Charitable Trust v. ACIT (2006) (II) OLR 75*, wherein it was held that the period of six months as provided under section 12AA(2) is not mandatory. In that case, the Orissa High Court observed that in order to ascertain whether a provision is mandatory or not, the expression 'shall' is not always decisive. The nature of the statutory provision, whether mandatory or directory, has to be ascertained not only from the wording of the statute, but also from the nature and design of the statute and the purpose sought to be achieved. Further, since the consequence for non-adherence of the time limit of six months is not spelt out in the statute, it cannot be said that passing the order within such time limit is mandatory in nature. The Orissa High Court also opined that in the absence of any clear statutory intent to the contrary, when public duty is to be performed by the public authorities, the time-limit which is granted by the statute is normally directory and not mandatory. Hence, though the word 'shall' has been used in section 12AA(2), the period of six months provided thereunder is not mandatory but directory in nature.

Accordingly, the Madras High Court held that the time frame mentioned in section 12AA(2) is only directory in nature and non-consideration of the registration application within the said time frame of six months would not amount to "deemed registration".

Similar ruling was pronounced by the Madras High Court in the case of *CIT v. Sheela Christian Charitable Trust* (2013) 354 ITR 478, holding that there is no automatic or deemed registration if the application filed under section 12AA was not disposed of within the stipulated period of six months.

Applying the rationale of the Madras High Court ruling in the above cases, the contention that the trust is deemed to be registered, since its application for registration has not been disposed of within six months, is incorrect.

2. (a) Expenditure incurred on glow-sign boards displayed at dealer outlets

The Delhi High Court, in *CIT v. Orient Ceramics and Industries Ltd.* (2013) 358 ITR

49, noted the following observations of the Punjab and Haryana High Court, in *CIT v. Liberty Group Marketing Division (2009) 315 ITR 125*, while holding that such expenditure was revenue in nature -

- (i) The expenditure incurred by the assessee on glow sign boards does not bring into existence an asset or advantage for the enduring benefit of the business, which is attributable to the capital.
- (ii) The glow sign board is not an asset of permanent nature. It has a short life.
- (iii) The materials used in the glow sign boards decay with the effect of weather. Therefore, it requires frequent replacement. Consequently, the assessee has to incur expenditure on glow sign boards regularly almost every year.
- (iv) The assessee incurred expenditure on the glow sign boards with the object of facilitating the business operation and not with the object of acquiring an asset of enduring nature.

The Delhi High Court concurred with the above observations of the Punjab & Haryana High Court and held that such expenditure on glow sign boards displayed at dealer outlets is revenue in nature.

(b) Share issue expenses incurred by a company, where the public issue could not ultimately materialize on account of non-clearance by SEBI

The issue relating to the nature of such expenditure came up before the Madras High Court in *Mascon Technical Services Ltd. v. CIT (2013) 358 ITR 545*. In that case, the Court observed that the assessee had taken steps to go in for a public issue and incurred share issue expenses for the same. However, it could not go in for the public issue by reason of the orders issued by the SEBI just before the proposed issue.

The High Court observed that though the efforts were aborted, the fact remains that the expenditure incurred was only for the purpose of expansion of the capital base. The capital nature of the expenditure would not be lost on account of the abortive efforts. The expenditure, therefore, constitutes a capital expenditure.

(c) Expenditure incurred for purchase of second-hand medical equipment for use as spare parts of existing equipment

The Karnataka High Court, in *Dr. Aswath N. Rao v. ACIT (2010) 326 ITR 188*, held that since the second hand machinery purchased by the assessee was for use as spare parts for the existing old machinery, the same had to be allowed as revenue expenditure.

3. Computation of depreciation allowance under section 32 for the A.Y. 2014-15

Particulars	Plant & Machinery	
	15%	60%
	(₹ in crores)	
WDV as on 01.04.2013	27.00	-
Add: Plant and Machinery acquired during the year		
- Second hand machinery 18.00		
- New plant and machinery 110.00		
- Air conditioner installed in office 0.15		
	128.15	
Computers (including accessories, peripherals etc. acquired during the year) [See Note 1 below]	-	0.40
	155.15	0.40
Less: Asset sold during the year	3.00	Nil
WDV as on 31.3.2014 (before charging depreciation)	152.15	0.40
Less: Depreciation for the P.Y.2013-14 [See Working Note]	32.22	0.12
WDV as on 1.4.2014	119.93	0.28
Working Note : Computation of depreciation for the P.Y.2013-14		
Normal depreciation [Under section 32(1)(ii)]		
Depreciation@30% on computers put to use for less than 180 days (50% of 60% × ₹ 0.40 crore)	-	0.12
Depreciation on plant and machinery (15% block) (₹ 72 crore × 7.5%) + [(₹ 152.15 crore - ₹ 72 crore) × 15%]	17.42	
Additional depreciation [Under section 32(1)(ia)]		
- New plant and machinery installed on 24.6.2013 (₹ 38 crore × 20%) 7.60		
- on 9.11.2013 (₹ 72 crore × 10%) 7.20	14.80	Nil
Total depreciation	32.22	0.12

Computation of deduction under section 32AC for the A.Y.2014-15

Particulars	(₹ in crore)
15% of ₹ 110 crore, being aggregate investment in new plant and machinery acquired and installed during the P.Y.2013-14 [See Note 2 below]	16.50

Notes:

(1) The Delhi High Court, in CIT v. BSES Yamuna Powers Ltd. (2013) 358 ITR 47,

held that computer accessories and peripherals such as printers, scanners and server form an integral part of the computer system and they cannot be used without the computer. Consequently, they would be eligible for depreciation at 60%, being the rate applicable to computers including computer software. Also, in *CIT v. Orient Ceramics and Industries Ltd.* (2013) 358 ITR 49, the Delhi High Court held that depreciation on UPS is allowable@60%, being the eligible rate of depreciation on computers including computer software and not at the general rate of 15% applicable to plant and machinery.

- (2) For the A.Y.2014-15, the company would be entitled for deduction under section 32AC since the investment in new plant and machinery acquired and installed during the P.Y.2013-14 is ₹ 110 crores (i.e., more than ₹ 100 crores). The deduction under section 32AC would be in addition to the depreciation allowable under section 32 for that year. However, the deduction under section 32AC would not be reduced to arrive at the written down value of plant and machinery.

It may be noted that investment in second hand plant and machinery and air-conditioners and computers installed in office would neither be eligible for deduction under section 32AC nor for additional depreciation under section 32(1)(ia).

4. (a) Tax implications on sale of rural agricultural land and house property representing a capital asset in the hands of Mr. Harish, a salaried employee

(i)	<u>Tax implications in the hands of Mr. Harish, a salaried employee</u>
	Since rural agricultural land is not a capital asset, the gains arising on sale of such land is not taxable in the hands of Mr. Harish. However, capital gains would arise on sale of house property, being a capital asset. As per section 50C, the stamp duty value of house property (i.e., ₹ 85 lakh) would be deemed to be the full value of consideration arising on transfer of property. Therefore, ₹ 45 lakh (i.e., ₹ 85 lakh – ₹ 40 lakh, being the purchase price) would be taxable as short-term capital gains in the A.Y.2014-15. It may be noted that under section 50C, there is no option to adopt the stamp duty value on the date of agreement, even if the date of agreement is different from the date of registration and part of the consideration has been received on or before the date of agreement otherwise than by way of cash.
(ii)	<u>Tax implications in the hands of the buyer - Mr. Suresh, a retail trader</u>
	The house property purchased would be a capital asset in the hands of Mr. Suresh, who is a retail trader. The provisions of section 56(2)(vii) would be attracted in the hands of Mr. Suresh who has received immovable property, being a capital asset, for inadequate consideration. For the purpose of section 56(2)(vii), Mr. Suresh can take the stamp duty value on the date of agreement instead of the date of registration since he has paid a part of the

	consideration by a mode other than cash on the date of agreement. Therefore, ₹ 15 lakh, being the difference between the stamp duty value of the property on the date of agreement (i.e., ₹ 75 lakh) and the actual consideration (i.e., ₹ 60 lakh) would be taxable as per section 56(2)(vii) under the head "Income from other sources" in the hands of Mr. Suresh. Since rural agricultural land is not a capital asset, the provisions of section 56(2)(vii) are not attracted in respect of receipt of agricultural land for inadequate consideration, since the definition of "property" under section 56(2)(vii) includes only capital assets specified thereunder.
(iii)	<u>TDS implications in the hands of the buyer, Mr. Suresh</u> Since the sale consideration of house property exceeds ₹ 50 lakh, Mr. Suresh is required to deduct tax at source under section 194-IA. The tax to be deducted under section 194-IA would be ₹ 60,000, being 1% of ₹ 60 lakh. TDS provisions under section 194-IA are not attracted in respect of transfer of rural agricultural land.

(b) **Tax implications on sale of house property representing stock-in-trade in the hands of Mr. Harish, a property dealer**

(i)	<u>Tax implications in the hands of Mr. Harish for A.Y.2014-15</u> If Mr. Harish is a property dealer who has sold the house property in the course of his business, the provisions of section 43CA would be attracted, since the house property represents his stock-in-trade and he has transferred the same for a consideration less than the stamp duty value. For the purpose of section 43CA, Mr. Harish can take the stamp duty value on the date of agreement instead of the date of registration, since he has received part of the consideration by a mode other than cash on the date of agreement. Therefore, ₹ 35 lakh, being the difference between the stamp duty value on the date of agreement (i.e., ₹ 75 lakh) and the purchase price (i.e., ₹ 40 lakh), would be chargeable as business income in the hands of Mr. Harish.
(ii)	<u>TDS implications and taxability in the hands of Mr. Suresh for A.Y.2014-15</u> There would be no difference in the TDS implications or taxability in the hands of Mr. Suresh, whether Mr. Harish is a property dealer or a salaried employee. Therefore, the provisions of section 56(2)(vii) would be attracted in the hands of Mr. Suresh who has received house property, being a capital asset, for inadequate consideration. The TDS provisions under section 194-IA would also be attracted since the actual consideration for house property exceeds ₹50 lakh.

5. Applying the rationale of the Delhi High Court ruling in *CIT v. Gita Duggal (2013) 357 ITR 153*, wherein the facts are similar to the facts stated in the question -

- (i) The full value of consideration would include the amount of ₹ 5 crore received by Mr. X as consideration as well as the cost of construction incurred by Arihant Builders in relation to the three floors handed over to Mr. X. Therefore, the full value of consideration in this case is ₹ 8 crore, being ₹ 5 crore plus ₹ 3 crore representing the cost of construction of three floors handed over to Mr.X, the owner.
- (ii) Yes, Mr. X is eligible for exemption under section 54F. Since the cost of construction of the floors handed over to Mr.X has been included in the full value of consideration, the same would also represent investment by Mr.X in residential house. Hence, Mr. X is eligible for exemption under section 54F.
- (iii) Section 54F uses the expression "residential house" and not "residential unit". Section 54F requires the assessee to acquire a "residential house" and so long as the assessee acquires a building, which may be constructed, for the sake of convenience, in such a manner as to consist of several units which can, if the need arises, be conveniently and independently used as an independent residence, the requirement of the section should be taken to have been satisfied. There is nothing in the section which requires the residential house to be constructed in a particular manner. The only requirement is that it should be for residential use and not for commercial use. The physical structuring of the new building, whether lateral or vertical, should not come in the way of considering the building as a residential house.

The fact that the residential house consists of several independent units cannot be permitted to act as an impediment to the allowance of the exemption under section 54F. It is neither expressly nor by necessary implication prohibited. Therefore, Mr.X is entitled to exemption of capital gains in respect of investment of ₹ 3 crores in the residential house, comprising of independent residential units handed over to him.

6. (a) **Applicability of the provisions of section 56(2)(viib)**

Co.	Face value of shares (₹)	FMV of shares (₹)	Consideration received (₹)	Applicability of section 56(2)(viib)
Win (P) Ltd.	300	350	370	The provisions of section 56(2)(viib) are attracted in this case since the shares are issued at a premium (i.e., issue price exceeds the face value of shares). The excess of the issue price of the shares over the FMV would be taxable under section 56(2)(viib).i.e., ₹ 20 lakh, being ₹ 20 (₹ 370 - ₹ 350) per share ×

				1,00,000 shares, shall be treated as income in the hands of Win (P) Ltd.
Gain (P) Ltd.	300	350	330	The provisions of section 56(2)(viib) are attracted since the shares are issued at a premium. However, no sum shall be chargeable to tax under the said section in the hands of Gain (P) Ltd. as the shares are issued at a price less than the FMV of shares.
Profit (P) Ltd.	300	280	290	Section 56(2)(viib) is not attracted since the shares are issued at a discount, though the issue price is greater than the FMV.
Top (P) Ltd.	300	275	310	The provisions of section 56(2)(viib) are attracted in this case since the shares are issued at a premium. The excess of the issue price of the shares over the FMV would be taxable under section 56(2)(viib). Therefore, ₹ 140 lakh, being ₹ 35 (₹ 310 - ₹ 275) per share × 4,00,000 shares, shall be treated as income in the hands of Top (P) Ltd.

- (b) 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, may 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 may 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 may also be relevant to determine whether the part of the business constitutes a substantial part.

7. The facts of the case are similar to the facts of *Pramod Mittal v. CIT* (2013) 356 ITR 456, wherein the Delhi High Court observed that upon dissolution, the partnership firm ceased to exist. The partnership firm and the proprietorship concern are two separate and distinct units for the purpose of assessment.

As per section 170(1), the partnership firm shall be assessed as such from 1st April of the previous year till the date of dissolution (i.e., 31st August, 2013, in this case). Thereafter, the income of the sole-proprietorship shall be taxable in the hands of the assessee as an individual. Thus, section 170(1) provides as to who will be assessable in respect of the income of the previous year from business, when there is a change in the person carrying on business by succession.

Section 78(2), however, deals with carry forward of losses in case of succession of business. It provides that only the person who has incurred the losses, and no one else, would be entitled to carry forward the same and set it off. An exception provided thereunder is in the case of succession by inheritance.

Therefore, section 170(1) providing the person in whose hands income is assessable in case of succession and section 78(2) providing for carry forward of losses in case of succession of business, deal with different situations and resultantly, there is no contradiction between these sections.

The income earned by the sole proprietor would include his share of loss as an individual but not the loss suffered by the erstwhile partnership firm in which he was a partner. The exception given in section 78(2), permitting carry forward of losses by the successor in case of inheritance, is not applicable in the present case since the partnership firm was dissolved and ceased to continue. Taking over of business by a partner cannot be considered as a case of inheritance due to death as per the law of succession. The Delhi High Court opined that the decision in *Madhukant M. Mehta's case* and *Saroj Aggarwal's case* cannot be applied since this is not a case of succession by inheritance. Therefore, the Court held that loss suffered by the erstwhile partnership firm before dissolution of the firm cannot be carried forward by the successor sole-proprietor, since it was not a case of succession by inheritance.

Applying the rationale of the Delhi High Court ruling to the case on hand, Mr. Arjun is not entitled to set-off the loss of the erstwhile partnership firm M/s. XYZ & Co. against the income earned by him as a sole-proprietor, since succession of a partnership firm by a sole-proprietor, being an erstwhile partner, is not a case of inheritance.

8. Computation of total income for A.Y.2014-15

Particulars		Mr. A ₹	Mr. B ₹	Mr. C ₹
(A)	Salary	9,25,000	10,45,000	11,15,000
	Income from house property [See Note 4]		(1,50,000)	
	Income from other sources (Interest)	75,000	85,000	95,000
	Gross total income	10,00,000	9,80,000	12,10,000
	Less: Deductions under Chapter VIA			
	<u>Under section 80C</u>			
	Deposit in PPF	80,000		
	LIC premium paid [See Note 1]			62,500
	Principal repayment of housing loan (restricted to maximum ₹1,00,000) [See Note 4]		1,00,000	
	<u>Under section 80CCG</u>			
(B)	Investment in listed equity shares/ units of equity oriented fund of Rajiv Gandhi Equity Savings Scheme [See Note 2]	22,500	25,000	Nil
	<u>Under section 80D</u>			
	Medical insurance premium [See Note 3]	15,000	Nil	10,000
	<u>Under section 80EE</u>			
	Interest on housing loan [See Note 4]		40,000	
	<u>Under section 80G</u>			
	Contribution to National Children's Fund [See Note 5]	30,000		
	<u>Under section 80GGC [See Note 6]</u>			
	Donation to BJP by crossed cheque		50,000	
	Cash donation to Electoral Trust		Nil	
(B)	Total deduction under Chapter VIA	1,47,500	2,15,000	72,500
(C)	Total Income (A) – (B)	8,52,500	7,65,000	11,37,500

Notes:

(1)	Deduction u/s 80C in respect of life insurance premium paid by Mr. C					
	Date of issue of policy	Person insured	Actual capital sum assured	Insurance premium paid during 2013-14	Restricted to % of sum assured	Deduction u/s 80C
	14/5/2011	Self	1,00,000	25,000	20%	20,000
	11/6/2012	Spouse	1,25,000	15,000	10%	12,500
	31/7/2013	Handicapped Son (section 80U disability)	2,00,000	40,000	15%	30,000
				Total		62,500
(2)	Deduction under section 80CCG in respect of investment made as per the Rajiv Gandhi Equity Savings Scheme					
	Particulars			Mr. A	Mr. B	
				₹	₹	
	(i)	Investment in listed equity shares	15,000	62,000		
	(ii)	Investment in units of equity-oriented fund	30,000			
	Total investment		45,000	62,000		
	50% of the above		22,500	31,000		
	Deduction under section 80CCG (restricted to a maximum of ₹25,000)		22,500	25,000		
	Mr. C is not eligible for deduction under section 80CCG since his gross total income exceeds ₹12 lakh.					
	(3)	Medical Insurance Premium				
(i)		Medical insurance premium of ₹ 20,000 paid by account payee cheque by Mr. A is allowed as a deduction under section 80D, subject to a maximum of ₹ 15,000.				
(ii)		Medical insurance premium paid by cash is not allowable as deduction. Hence, Mr. B is not eligible for deduction under section 80D in respect of medical insurance premium of ₹ 15,000 paid in cash.				
(iii)		Mr. C is eligible for deduction of ₹ 10,000 under section 80D in respect of medical insurance premium paid by crossed cheque.				
(4)	Deduction in respect of interest and principal repayment of housing loan					
	Mr. B is eligible for a maximum deduction of ₹ 1.50.000 under section 24 in					

	respect of interest on housing loan taken in respect of a self-occupied property, for which he is claiming benefit of "Nil" annual value. Therefore, ₹ 1,50,000 would represent his loss from house property. Mr. B is eligible for deduction of ₹ 40,000 under section 80EE, in respect of the balance interest on housing loan (₹ 1,90,000 – ₹ 1,50,000), since the following conditions are satisfied – (i) The loan is sanctioned by HDFC, a financial institution, during the period between 1.4.2013 and 31.3.2014; (ii) The loan amount sanctioned is less than ₹ 25 lakh; (iii) The value of the house property is less than ₹ 40 lakh; (iv) He does not own any other house property. Further, he is eligible for deduction in respect of principal repayment of housing loan subject to a maximum of ₹1 lakh under section 80C.
(5)	Contribution to National Children's Fund qualifies for 100% deduction under section 80G with effect from A.Y.2014-15. Therefore, Mr. A is entitled to 100% deduction of the sum of ₹ 30,000 contributed by him by way of cheque to National Children's Fund.
(6)	Mr. B is eligible for deduction under section 80GGC in respect of donation to a political party made otherwise than by way of cash. However, cash donation to electoral trust would not qualify for deduction under section 80GGC with effect from A.Y.2014-15.

Note – In case Mr. A sells all the units of equity oriented fund in May 2014, the amount of ₹ 15,000 (i.e., 50% of ₹ 30,000), being deduction allowed to him under section 80CCG in A.Y.2014-15, would be subject to tax in the A.Y.2015-16, since the condition of the minimum fixed lock-in period of one year from the end of P.Y.2013-14 stipulated under the Rajiv Gandhi Equity Scheme, 2013, has been violated in this case. However, in the case of Mr. C, since deduction under section 80CCG was not allowed during the A.Y.2014-15 on account of his gross total income exceeding ₹ 12 lakh, no amount relating to that year can be subject to tax in the A.Y.2015-16, being the year of violation of condition.

9. Computation of Book Profit of Alpha Ltd. under section 115JB

Particulars	₹	₹
Net Profit as per Profit & Loss Account		15,75,000
Add: Net Profit to be increased by the following amounts as per Explanation 1 to section 115JB		
Income-tax paid or payable or provision therefor		
Provision for income-tax	1,75,000	
Interest on income-tax	9,000	
Dividend distribution tax	32,000	2,16,000

Provision for deferred tax	21,000	
Transfer to General Reserve	32,000	
Provision for diminution in the value of investment	17,000	
Dividend paid or proposed		
Proposed dividend 30,000		
Preference dividend 18,000	48,000	
Expenditure to earn income exempt u/s 10 [except section 10(38)]		
Expenditure to earn agricultural income [exempt u/s 10(1)] 12,000		
Expenditure to earn dividend income [exempt u/s 10(34)] 4,500	16,500	
Depreciation	36,000	3,86,500
		19,61,500
Less: Net Profit to be reduced by the following amounts as per Explanation 1 to section 115JB		
Amount credited to profit and loss account from Special Reserve	24,000	
Depreciation (excluding depreciation on account of revaluation of fixed assets) (i.e. ₹ 36,000 – ₹ 14,000)	22,000	
Amount credited to profit and loss account from revaluation reserve (to the extent of depreciation on revaluation)	14,000	
Brought forward business loss or unabsorbed depreciation as per books of account, whichever is less taken on cumulative basis	1,10,000	
Income exempt u/s 10 [except section 10(38)]		
Agricultural Income [since it is exempt under section 10(1)]	27,000	
Dividend income [since it is an income exempt under section 10(34)]	21,000	2,18,000
Book Profit		17,43,500
18.5% of book profit		3,22,548
Add: Education cess @ 2%	6,451	
Secondary and higher education cess @ 1%	3,225	9,676
Tax liability under section 115JB		3,32,224
Total income computed as per the provisions of the Income-tax Act, 1961	10,00,000	
Tax payable @ 30%		3,00,000

Add: Education cess @ 2%	6,000	
Secondary and higher education cess @ 1%	3,000	9,000
Tax Payable as per the Income-tax Act, 1961		3,09,000

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 18.5% of book profit, the book profit shall be deemed as the total income and the tax payable on such total income shall be 18.5% 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 18.5% of book profit, the book profit of ₹ 17,43,500 is deemed to be the total income and income-tax is payable @ 18.5% thereof plus education cess @2% and secondary and higher education cess @1%. The tax liability, therefore, works out to ₹ 3,32,224.

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, 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	3,32,224
Less: Tax on total income computed as per the other provisions of the Act	3,09,000
Tax credit to be carried forward	23,224

Notes:

1. Securities transaction tax does 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.

10. Computation of total income of ABC Ltd. for A.Y. 2014-15

Particulars	₹
Profits and gains of business or profession	48,00,000
Income from other sources (<i>See Note below</i>)	<u>3,18,000</u>
Total income	<u>51,18,000</u>

Note – Dividend income taxable under “Income from other sources”

Particulars	₹
From BCD Inc., a Danish company, – net dividend (i.e., ₹ 65,000 – ₹ 4,000) is taxable at normal rates	61,000
From EFG Inc., an English company – gross dividend is taxable@15% under section 115BBD [no deduction is allowable in respect of any expenditure as per section 115BBD(2)]	1,50,000
From HIJ Inc., a Dutch company – gross dividend is taxable@15% under section 115BBD [no deduction is allowable in respect of any expenditure as per section 115BBD(2)]	1,07,000
From shares in Indian subsidiaries ₹ 47,000 – exempt under section 10(34) since dividend distribution tax has been paid under section 115-O [As per section 14A, no deduction is allowable in respect of expenditure incurred to earn exempt income]	Nil
	<u>3,18,000</u>

Computation of tax liability of ABC Ltd. for the A.Y.2014-15

Particulars	₹
Tax@15% under section 115BBD on ₹ 2,57,000 (gross dividend)	38,550
Tax@30% on balance income of ₹ 48,61,000	<u>14,58,300</u>
	14,96,850
Add: Education cess@2% and Secondary and higher education cess@1%	<u>44,906</u>
Tax liability	<u>15,41,756</u>

Computation of additional income-tax payable by ABC Ltd. under section 115-O	
Particulars	₹
Amount distributed by way of dividend	4,20,000
Less: Dividend received from Indian subsidiaries, on which DDT payable under section 115-O has been paid	47,000
Dividend received from foreign subsidiary, HIJ Inc., on which tax is payable under section 115BBD	<u>1,07,000</u>
	<u>1,54,000</u>
	<u>2,66,000</u>
Additional income-tax@15%	39,900
Add: Surcharge@10%	<u>3,990</u>
	43,890
Add: Education cess@2% and Secondary and higher education cess@1%	<u>1,317</u>
Additional income-tax payable under section 115-O	<u>45,207</u>

11. Computation of total income and tax liability of M/s. ABC & Co. for A.Y.2014-15

Particulars	₹
Profit from ECR project	50,00,000
Profit from OMR project	30,00,000
Profit from trading unit	<u>15,00,000</u>
Business income/Gross Total Income	95,00,000
Less: Deduction under section 80-IA (See Notes 1 & 2 below)	<u>47,00,000</u>
Total Income	<u>48,00,000</u>
Income-tax @30%	14,40,000
Add: Education cess@2% and SHEC@1%	<u>43,200</u>
Total tax liability under the regular provisions of the Act	<u>14,83,200</u>

The provisions of Chapter XII-BA on Alternate Minimum Tax shall apply to M/s. ABC & Co., since the firm has claimed deduction under section 80-IA.

Computation of Alternate Minimum Tax (AMT)

Particulars	₹
Total Income as per the Income-tax Act, 1961	48,00,000
Add: Deduction under section 80-IA	<u>47,00,000</u>
Adjusted Total Income	<u>95,00,000</u>
AMT = 18.5% × 95,00,000 =	<u>17,57,500</u>

Since the regular income-tax payable as per the provisions of the Act is less than the AMT, the adjusted total income of ₹ 95,00,000 would be deemed to be the total income of M/s. ABC & Co. and it would be liable to pay tax@18.5% thereof. The tax payable by M/s. ABC & Co. for the A.Y.2014-15 would, therefore, be ₹ 17,57,500 plus education cess@2% and secondary and higher education cess@1%, totaling ₹ 18,10,225.

M/s. ABC & Co. would be eligible for credit of ₹ 3,27,025, being the difference between the AMT of ₹ 18,10,225 and tax of ₹ 14,83,200 on total income computed under the regular provisions of the Act. Such credit can be set-off in the year in which tax on total income computed under the regular provisions of the Act exceeds the AMT. Such credit can be carried forward for succeeding ten assessment years.

Notes:

- (1) Section 80-IA(1) provides for 100% deduction of profits derived by an undertaking or an enterprise from an eligible business referred to in sub-section (4) for ten consecutive assessment years. Clause (i) of sub-section (4) provides that the deduction under section 80-IA would be applicable to any enterprise carrying on the business of developing or operating and maintaining or developing, operating and maintaining any infrastructure facility fulfilling the conditions mentioned therein. The *Explanation* to this clause defines “infrastructure facility” to include, *inter alia*, -

- (a) a road, including a toll road, a bridge or a rail system and
- (b) a highway project including housing or other activities being an integral part of the highway project.

The CBDT has, vide *Circular No.4/2010 dated 18.5.2010*, clarified that widening of an existing road by constructing additional lanes as a part of a highway project by an undertaking would be regarded as a new infrastructure facility for the purpose of section 80-IA(4)(i). However, simply relaying of an existing road would not be classifiable as a new infrastructure facility for this purpose.

Therefore, ABC & Co. would be eligible for deduction under section 80-IA in respect of the profits from ECR highway project, since it involves expansion of existing roads by constructing additional lanes as a part of the highway project. However, it would not be eligible for deduction under section 80-IA in respect of profits from the OMR project, which involves only relaying of existing roads.

- (2) The ECR project is eligible for deduction@100% of the profits derived from its eligible business (i.e., the business of developing an infrastructure facility, being a highway project) under section 80-IA. However, the Trading Unit is not an “eligible business” and its profits are not eligible for deduction under section 80-IA. Since the trading unit has transferred cement worth ₹ 5 lakh to the ECR project at ₹ 2 lakh, i.e., a price lower than the fair market value, it is an inter-Unit transfer of goods between eligible business and other business, where the consideration for

transfer does not correspond with the market value of goods. As per section 80-IA(8), the profits of eligible business (i.e., ECR project) has to be computed as if the transfer has been made at market value i.e., at ₹ 5 lakh, for the purpose of deduction under section 80-IA. Therefore, the profits of the eligible business (i.e., ECR project), for the purpose of deduction under section 80-IA, would be ₹ 47 lakh (i.e., ₹ 50 lakh – ₹ 5 lakh + ₹ 2 lakh).

12. Computation of additional income-tax payable under section 115TA

	Category of investor	Income distributed (₹)	Rate of tax	Amount of tax (₹)
(i)	Mutual funds exempt under section 10(23D)	1,50,000	Nil	Nil
(ii)	Individuals and HUFs	1,00,000	28.325%	28,325
(iii)	Companies	4,00,000	33.99%	<u>1,35,960</u>
				<u>1,64,285</u>

The additional income-tax is payable on or before 31st August, 2013. However, the same was paid only on 7th November 2013.

Consequently, interest@1% per month or part of month is leviable under section 115TB, as follows –

Period	No. of months/ part of a month
1 st September, 2013 – 30 th September, 2013 (whole of first month)	1
1 st October – 31 st October, 2013 (whole of second month)	1
1 st November – 7 th November, 2013 (part of third month)	1
No. of months for which interest is leviable u/s 115TB	3

Interest under section 115TB is payable @1% per month for 3 months on the amount of additional tax payable i.e., ₹ 1,64,285. Therefore, interest payable under section 115TB is ₹ 4,929.

Notes:

- As per section 115TTA, the securitisation trust will be liable to pay additional income-tax on income distributed to its investors.
- The rates of additional income-tax and the effective rate of tax (i.e., including surcharge@10% and cess@3%) in respect of each category are shown hereunder –

	Category of investors to whom income is distributed	Rate	Effective rate of tax
(1)	Persons, in whose case, income, irrespective of its nature and source, is exempt from tax under the Income-tax Act, 1961 [for example, mutual funds exempt under section 10(23D)]	Nil	Nil
(2)	Individuals and HUFs	25%	28.325%
(3)	Other Investors [i.e., investors other than mentioned in (1) and (2) above]	30%	33.99%

- (iii) Such tax has to be paid within 14 days from the date of distribution or payment of such income, whichever is earlier.
- (iv) The securitisation trust will be liable to pay simple interest on the amount of additional income-tax not paid within the specified time i.e., within 14 days from the date of distribution or payment of such income, whichever is earlier. Such interest is leviable at the rate of 1% for every month or part of the month on the amount of such tax not paid or short paid, as the case may be, for the period beginning on the date immediately after the last date on which such tax was payable and ending with the date on which the tax is actually paid [Section 115TB].

13. (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), and such issue 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 Ashiana Pvt. 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 third 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.

14. (a) The first contention of Mr. Hari is not correct.

Section 139(1) requires every resident and ordinarily resident having any asset (including financial interest in any entity) located outside India or signing authority in any account located outside India to file a return of income compulsorily whether or not he has income chargeable to tax. Mr. Hari has a house property in Dubai and a bank account in the Bank of Dubai. Therefore, Mr. Hari has to file his return of income mandatorily for the A.Y.2014-15, even though his total income of ₹ 2,40,000, comprising solely of income from house property and bank interest, is less than the basic exemption limit of ₹ 2,50,000 applicable to a senior citizen.

- (b) Mr. Hari's second contention is also not correct.

Income chargeable to tax shall be deemed to have escaped assessment for the purpose of section 147, where a person is found to have any asset (including financial interest in any entity) located outside India. Accordingly, the Assessing Officer can serve a notice under section 148 on such assessee requiring him to furnish a return of income within the specified period, for the purpose of making an assessment, reassessment or re-computation under section 147.

Further, section 149 prescribes an extended time limit of sixteen years for issue of notice under section 148, in case income in relation to such assets located outside India has escaped assessment.

In this case, since Mr. Hari has a house property located outside India in the P.Y.2004-05, income is deemed to have escaped assessment for A.Y.2005-06. Notice under section 148 issued to Mr. Hari in June 2014 in respect of A.Y.2005-06 is valid, since the extended time limit of sixteen years from the end of the relevant assessment year has not expired.

15. (a) **The statement is not correct**

The statement given is not correct. As per the provisions of section 255, in the event of difference in opinion between the members of the Bench of the Income-tax Appellate Tribunal, the matter shall be decided on the basis of the opinion of the majority of the members. In case the members are equally divided, they shall state the point or points of difference and the case shall be referred by the President of the Tribunal for hearing on such points by one or more of the other members of the Tribunal. Such point or points shall be decided according to the opinion of majority of the members of the Tribunal who heard the case, including those who had first heard it.

- (b) **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 off within this period and the delay in disposing the appeal is not attributable to the assessee, the Appellate Tribunal can further extend the period of stay originally allowed. However, the aggregate 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. (i) The issue as to whether discount given to stamp vendors on purchase of stamp papers can be treated as "commission or brokerage" to attract the provisions for tax deduction at source came up before the Supreme Court in *CIT v. Ahmedabad Stamp Vendors Association (2012) 348 ITR 378*.

The principal issue in that case was whether stamp vendors were agents of the State Government who were being paid commission or brokerage or whether the sale of stamp papers by the Government to the licensed vendors was on "principal-to-principal" basis involving a "contract of sale".

On this issue, the Gujarat High Court had observed that the crucial question is whether the ownership in the stamp papers passes to the stamp vendor when the treasury officer delivers stamp papers on payment of price less discount. The Gujarat Stamp Supply and Sales Rules contemplate that the licensed vendor, while taking delivery of the stamp papers from the Government offices, is purchasing the stamp papers. The Rules also indicate that the discount which the licensed vendor has obtained from the Government is on purchase of the stamp papers.

If the licensed stamp vendors were mere agents of the State Government, no sales tax would have been leviable when the stamp vendors sell the stamp papers to the customers, because it would have been sale by the Government "through" stamp vendors. However, entry 84 in Schedule I to the Gujarat Sales Tax Act, 1969 specifically exempts sale of stamp papers by the licensed vendors from sales-tax. The very basis of the State Legislature enacting such exemption provision in respect of sale of stamp papers by the licensed vendors makes it clear that the sale of stamp papers by the licensed vendors to the customers would have, but for such exemption, been subject to sales tax levy. The question of levy of sales tax arises only because the licensed vendors themselves sell the stamp papers on their own and not as agents of the State Government. Had they been treated as agents of the State Government, there would be no question of levy of sales tax on sale of stamp papers by them, and consequently, there would have been no necessity for any

exemption provision in this regard.

Therefore, although the Government has imposed a number of restrictions on the licensed stamp vendors regarding the manner of carrying on the business, the stamp vendors are required to purchase the stamp papers on payment of price less discount on "principal to principal" basis and there is no "contract of agency" at any point of time. The definition of "commission or brokerage" under clause (i) of the *Explanation* to section 194H indicates that the payment should be received, directly or indirectly, by a person acting on behalf of another person, *inter alia*, for services in the course of buying or selling goods. Therefore, the element of agency is required in case of all services and transactions contemplated by the definition of "commission or brokerage" under *Explanation (i)* to section 194H. When the licensed stamp vendors take delivery of stamp papers on payment of full price less discount and they sell such stamp papers to the retail customers, neither of the two activities (namely, buying from the Government and selling to the customers) can be termed as service in the course of buying and selling of goods. The High Court, therefore, held that discount on purchase of stamp papers does not fall within the expression "commission or brokerage" to attract the provisions of tax deduction at source under section 194H.

The Supreme Court affirmed the above decision of the High Court holding that the said transaction is a sale and the discount given to stamp vendors for purchasing stamps in bulk quantity is in the nature of cash discount and consequently, section 194H has no application in this case.

- (ii) The issue as to whether discount given on supply of SIM cards and recharge coupons by a telecom company to its distributors under a prepaid scheme would be treated as commission to attract the provisions of section 194H 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 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.

17. Deduction under section 91 is allowable subject to satisfaction of the following conditions :-

- (a) He is a resident in India during the relevant previous year.
- (b) The income accrues or arises to him outside India during that previous year.
- (c) Such income is not deemed to accrue or arise in India during the previous year.
- (d) The income in question has been subjected to income-tax in the foreign country in the hands of Mr. Vallish and he has paid tax on such income in the foreign country.
- (e) There is no agreement under section 90 for the relief or avoidance of double taxation between India and the other country where the income has accrued or arisen.

In this case, Mr. Vallish satisfies all the above conditions, and therefore, he is eligible for deduction under section 91.

Computation of tax liability of Mr. Vallish for the A.Y.2014-15

Particulars	₹	₹
Indian income		18,00,000
Foreign income		<u>15,00,000</u>
Gross Total Income		33,00,000
Less: Deductions under Chapter VI-A		
<u>Deduction under section 80C</u>		
PPF Contribution	1,00,000	
<u>Deduction under section 80CCG</u>		
Investment in listed equity shares under Rajiv Gandhi Equity Savings Scheme, 2013 (Since his gross total income exceeds ₹ 12 lakh, he is not eligible for deduction under section 80CCG even though he qualifies as a new retail investor)	Nil	
<u>Deduction under section 80D</u>		
Premium for insuring his health, restricted to	15,000	
Premium for insuring health of father, being a senior citizen, restricted to	<u>20,000</u>	
	<u>35,000</u>	<u>1,35,000</u>
Total Income		<u>31,65,000</u>
Tax on total income		7,79,500
Add: Education Cess @ 2%		15,590
Secondary and higher education cess @ 1%		<u>7,795</u>
		8,02,885

Less: Rebate under section 91 on doubly taxed income of ₹ 15,00,000 @ 20%, being the lower of average Indian tax rate and average rate of tax in the foreign country (See Note below)		<u>3,00,000</u>
Net tax liability		<u>5,02,885</u>

Note – Calculation of Average Rate of Tax

- | | |
|---|--------|
| (i) Average rate of tax in India
[i.e. ₹ 8,02,885/₹ 31,65,000 x 100] | 25.37% |
| (ii) Average rate of tax in the foreign country
[i.e. ₹ 3,00,000/ ₹ 15,00,000 x 100] | 20% |

Lower of the above, i.e., 20% has to be applied on the doubly taxed income of ₹ 15,00,000 to compute rebate under section 91

- 18.** Section 92CB(1) provides that the determination of arm's length price under section 92C or section 92CA shall be subject to safe harbour rules. Safe harbour means circumstances in which the income tax authorities shall accept the transfer price declared by the assessee. Section 92CB(2) empowers the CBDT to prescribe such safe harbour rules or circumstances under which the transfer price declared by the assessee shall be accepted by the Income-tax Authorities.

Accordingly, in exercise of the powers conferred by section 92CB read with section 295 of the Income-tax Act, 1961, the CBDT has, vide Notification No.73/2013 dated 18.9.2013, prescribed safe harbour rules. Rule 10TD provides that where an eligible assessee has entered into an eligible international transaction and the option exercised by the said assessee is not held to be invalid under Rule 10TE, the transfer price declared by the assessee in respect of such transaction shall be accepted by the income-tax authorities, if it is in accordance with the circumstances set out thereunder.

An eligible assessee is a person who has exercised a valid option for application of safe harbour rules and is engaged in, *inter alia*, providing the following services, with insignificant risk, to a non-resident associated enterprise –

- (i) software development services; or
- (ii) information technology enabled services; or
- (iii) knowledge process outsourcing services; or
- (iv) contract R & D services wholly or partly relating to software development; or
- (v) contract R & D services wholly or partly relating to generic pharmaceutical drugs.

A person who is engaged in the manufacture and export of core or non-core auto components and where 90% or more of total turnover during the relevant previous year is

in the nature of original equipment manufacturer sales also falls within the definition of eligible assessee if he has exercised a valid option for application of safe harbour rules.

- (1) X Inc. is a specified foreign company in relation to A Ltd. Therefore, the condition of A Ltd. holding shares carrying not less than 26% of the voting power in X Inc is satisfied. Hence, X Inc. and A Ltd. are deemed to be associated enterprises. Therefore, provision of systems support services by A Ltd., an Indian company, to X Inc., a foreign company, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

Systems support services falls within the definition of “software development services”, and hence, is an eligible international transaction. Since A Ltd. is providing software development services to a non-resident associated enterprise and has exercised a valid option for safe harbour rules, it is an eligible assessee.

Since the aggregate value of transactions entered into in the P.Y.2013-14 exceed ₹ 500 crore, A Ltd. should have declared an operating profit margin of not less than 22% in relation to operating expense, to be covered within the safe harbour rules. However, since A Ltd. has declared an operating profit margin of only 20% (i.e.,

$$\frac{90}{450} \times 100), \text{ the same is not in accordance with the circumstance mentioned in Rule}$$

10TD. Hence, it is not binding on the income-tax authorities to accept the transfer price declared by A Ltd.

- (2) Y Inc., a foreign company, is a subsidiary of B Ltd., an Indian company. Hence, Y Inc. and B Ltd. are associated enterprises. Therefore, provision of data processing services by B Ltd., an Indian company, to Y Inc., a foreign company, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

Data processing services with the use of information technology falls within the definition of “information technology enabled services”, and is hence, an eligible international transaction. Since B Ltd. is providing data processing services to a non-resident associated enterprise and has exercised a valid option for safe harbour rules, it is an eligible assessee.

Since the aggregate value of transactions entered into in the P.Y.2013-14 does not exceed ₹ 500 crore, B Ltd. should have declared an operating profit margin of not less than 20% in relation to operating expense, to be covered within the scope of safe harbour rules. In this case, since B Ltd. has declared an operating profit

$$\text{margin of } 20.67\% \text{ (i.e., } \frac{62}{300} \times 100), \text{ the same is in accordance with the}$$

circumstance mentioned in Rule 10TD. Hence, the income-tax authorities shall accept the transfer price declared by B Ltd in respect of such international transaction.

- (3) XYZ & Co., a foreign firm holds 12% interest in C & Co., an Indian firm. Therefore, the condition of one enterprise, being a foreign firm, holding not less than 10% interest in another enterprise, being an Indian firm, is satisfied. Hence, XYZ & Co. and C & Co. are deemed to be associated enterprises. Therefore, provision of contract R & D services relating to software development by C & Co., an Indian firm, to XYZ & Co., a foreign firm, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

Development of internet technology falls within the meaning of “contract R&D services wholly or partly relating to software development”, and hence, is an eligible international transaction. Since C & Co., an Indian firm, is providing contract R & D services to a non-resident associated enterprise and has exercised a valid option for safe harbour rules, it is an eligible assessee.

Irrespective of the aggregate value of transactions entered into in the P.Y.2013-14, C & Co. should have declared an operating profit margin of not less than 30% in relation to operating expense, to be covered within the safe harbour rules. However, since C & Co. has declared an operating profit margin of only 28.57%

(i.e., $\frac{20}{70} \times 100$), the same is not in accordance with the circumstance mentioned in

Rule 10TD. Hence, it is not binding on the income-tax authorities to accept the transfer price declared by C & Co.

- (4) ABC Inc., a foreign company, guarantees 15% of the total borrowings of D Ltd., an Indian company. Since ABC Inc. guarantees not less than 10% of the total borrowings of D Ltd., ABC Inc. and D Ltd. are deemed to be associated enterprises. Therefore, provision of contract R & D services relating to generic pharmaceutical drug by D Ltd., an Indian company, to ABC Inc., a foreign company, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

Provision of contract R& D services in relation to generic pharmaceutical drug is an eligible international transaction. Since D Ltd. is providing such services to a non-resident associated enterprise and has exercised a valid option for safe harbour rules, it is an eligible assessee.

Irrespective of the aggregate value of transactions entered into in the P.Y.2013-14, D Ltd. should have declared an operating profit margin of not less than 29% in relation to operating expense, to be covered within the scope of safe harbour rules. In this case, since D Ltd. has declared an operating profit margin of 30% (i.e.,

$\frac{9}{30} \times 100$), the same is in accordance with the circumstance mentioned in Rule

10TD. Hence, the income-tax authorities shall accept the transfer price declared by D Ltd in respect of such international transaction.

- (5) LMN LLP, a foreign LLP, is controlled by Mr.E jointly with his relatives. Mr. E also has control over his own sole proprietorship concern. Therefore, the sole proprietorship concern of Mr.E in India and LMN LLP are deemed to be associated enterprises.

Automobile transmission and steering parts fall within the meaning of “core auto components”, and hence, 100% export of all such parts originally manufactured by the sole proprietorship concern of Mr.E is an eligible international transaction. Since the sole proprietorship concern of Mr.E is solely engaged in the original manufacture and 100% export of such parts and has exercised a valid option for safe harbour rules, it is an eligible assessee.

Irrespective of the aggregate value of transactions entered into in the P.Y.2013-14, the sole-proprietorship concern of Mr.E should have declared an operating profit margin of not less than 12% in relation to operating expense, to be covered within the safe harbour rules. However, since A Ltd. has declared an operating profit margin of only 10% (i.e., $\frac{1}{10} \times 100$), the same is not in accordance with the circumstance mentioned in Rule 10TD. Hence, it is not binding on the income-tax authorities to accept the transfer price declared by Mr.E.

- (6) F Ltd. and GKG Inc. are deemed to be associated enterprises since F Ltd. appoints more than half of the Board of Directors of GKG Inc. Manufacture and export of non-core auto components is an eligible international transaction. Since F Ltd. is engaged in original manufacture of non-core auto components and 100% export of the same, it is an eligible assessee.

Irrespective of the aggregate value of transactions entered into in the P.Y.2013-14, F Ltd. should have declared an operating profit margin of not less than 8.5% in relation to operating expense, to be covered within the scope of safe harbour rules. In this case, since F Ltd. has declared an operating profit margin of 10% (i.e., $\frac{1}{10} \times 100$), the same is in accordance with the circumstance mentioned in Rule 10TD. Hence, the income-tax authorities shall accept the transfer price declared by F Ltd in respect of such international transaction.

The safe harbour rules shall not apply in respect of eligible international transactions entered into with an associated enterprise located in a notified jurisdictional area. Therefore, if in any of the cases mentioned above, the foreign entity is located in a NJA, the safe harbour rules shall not be applicable, irrespective of the operating profit margin declared by the assessee.

19. Computation of net wealth of Sridhar as on valuation date 31.03.2014

	Particulars	Amount in ₹
(a)	Residential house at Mumbai	40,00,000

(b)	Residential house at Chennai	25,00,000
(c)	Plot of land comprising an area of 325 square meters at New Delhi is an asset but exempt under section 5(vi)	Nil
(d)	House at Calcutta exclusively used for carrying on his business - not an asset under section 2(ea)	Nil
(e)	Commercial complex at Chennai - not an asset under section 2(ea)	Nil
(f)	Residential house at Bangalore let out for 310 days during the relevant previous year - not an asset under section 2(ea)	Nil
(g)	Motor cars used in the business of running them on hire - not an asset under section 2(ea)	Nil
(h)	Shares in private limited companies - not an asset under section 2(ea)	Nil
(i)	Cash in hand in excess of ₹ 50,000	1,50,000
(j)	Gold jewellery	8,00,000
		74,50,000
	Less: Debts incurred in relation to assets	
(k)	Loan borrowed for purchase of land at New Delhi (not deductible since exemption under section 5(vi) has been claimed in respect of the said land)	Nil
(l)	Loan borrowed for purchase of shares in private limited companies (not deductible since shares are not included in net wealth)	Nil
(m)	Loan borrowed for purchase of gold jewellery	4,00,000
Net Wealth		70,50,000

Reasons for inclusion or exclusion of the various items are furnished below:

- (a) Residential house at Mumbai is included in net wealth, as residential house is an "asset" within the meaning of section 2(ea) of the Wealth-tax Act, 1957. Exemption under section 5(vi) is not claimed in respect of this house as it is more beneficial for the assessee to claim exemption in respect of plot of land at New Delhi whose value is higher.
- (b) Residential house at Chennai is an asset under section 2(ea) and, therefore, included in the net wealth.
- (c) Plot of land measuring 325 square metres at New Delhi is exempt under section 5(vi) and, therefore, does not form part of net wealth. One house or part thereof or a plot of land, not exceeding 500 square metres, belonging to an individual or a Hindu Undivided Family is exempt under section 5(vi) without any monetary ceiling.
- (d) House at Calcutta, occupied for own business purposes, is not an asset by virtue of the specific exclusion under item (3) of section 2(ea)(i). Hence, the same does not form part of net wealth.

- (e) Commercial complex at Chennai is not an asset by virtue of the specific exclusion under item (5) of section 2(ea)(i).
 - (f) Any residential property let out for a minimum period of 300 days in the previous year is not an asset due to the specific exclusion under item (4) of section 2(ea)(i). Residential house at Bangalore let out for more than 300 days is, therefore, not includible in net wealth.
 - (g) Motor cars used in business of running them on hire are not assets as per section 2(ea)(ii) and, therefore, excluded from net wealth.
 - (h) Shares in private limited companies are not included in the definition of “asset” under section 2(ea). Therefore, they do not form part of net wealth.
 - (i) In case of individuals, cash in hand in excess of ₹ 50,000 constitutes an asset. Therefore, ₹ 1,50,000, being cash in hand in excess of ₹ 50,000, is included in Mr. Sridhar’s net wealth.
 - (j) Gold jewellery constitutes an asset as per section 2(ea)(iii) and is, hence, includible in net wealth.
 - (k) Debts incurred in relation to an exempted asset are not deductible in computing net wealth. Loan borrowed for purchase of land at New Delhi is not deductible as exemption under section 5(vi) has been claimed in respect of the said land.
 - (l) Loan borrowed for purchase of shares in private limited companies is not deductible while computing net wealth, as shares are not included in net wealth.
 - (m) Gold jewellery, being an asset, has been included in the net wealth. Therefore, loan borrowed for purchase thereof is deductible in computing net wealth.
- 20.** In the given case, Mrs. Gauri is the owner of two residential houses for self-occupation, one at Chennai and another at Pune.

The value of any one house can be claimed as exempt under section 5(vi) of the Wealth-tax Act, 1957. Mrs. Gauri 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 Mrs. Gauri and exclusively used by her for residential purposes throughout the period of 12 months immediately preceding the valuation date, may, at her option, 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 she 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 Mrs. Gauri 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 Chennai since the house was occupied by the Gauri's relative for a part of the year. The Schedule III value of the flat at Chennai as on the valuation date 31st March, 2014, 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. Therefore, ₹ 28 lacs is the value of the Chennai house for wealth-tax purpose.

The benefit of pegging down of value can be opted for the flat situated at Pune, as it was self-occupied by Mrs. Gauri throughout the 12 months immediately preceding the valuation date of 31st March, 2014 for her residential purposes. In case of the house at Pune, the Schedule III value as on 31st March, 2006, being the first valuation date after she 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 Pune house for wealth-tax purposes.

It would be more beneficial for Mrs. Gauri to claim exemption under section 5(vi) in respect of the Chennai house since the value of the Chennai house (₹ 28 lacs) is higher than the value of the Pune house (₹ 7 lacs) as on the valuation date 31st March, 2014.

**Applicability of Legislative Amendments/Circulars etc.
for November, 2014 – Final Examination**

Paper 7 : Direct Tax Laws & Paper 8 : Indirect Tax Laws

Applicability of the Finance Act, Assessment Year etc. for November, 2014 Examination

The provisions of direct and indirect tax laws, as amended by the Finance Act, 2013, including notifications and circulars issued upto 30th April, 2014. The applicable assessment year for Direct Tax Laws is A.Y. 2014-15.

ANNEXURE

Part I: Statutory Update - Direct Tax Laws

Significant Notifications and Circulars issued between 1.5.2013 and 30.4.2014

I NOTIFICATIONS

1. **Notification No. 38/2013 dated 30.05.2013 (as amended by Notification No. 18/2014 dated 21.03.2014)**

Approval of Agricultural Extension Project under section 35CCC: Conditions and Guidelines

In order to incentivize the business entities to provide better and effective agriculture extensive services, section 35CCC was inserted to provide weighted deduction of a sum equal to 150% of expenditure incurred by **an assessee** on agricultural extension project in accordance with the prescribed guidelines.

Accordingly, the CBDT in exercise of the powers conferred by section 295 read with section 35CCC(1) of the Income tax Act, 1961, vide Notification No. 38/2013 dated 30.05.2013, prescribed rule 6AAD and 6AAE that contains the guidelines and conditions, for approval of the agricultural extension project. Rule 6AAD has been substituted and Rule 6AAE has been amended by this notification.

(a) Conditions to be fulfilled for approval of agricultural extension project under section 35CCC [Rule 6AAD]:

The agricultural extension project shall be considered for notification if it fulfils **all** of the following conditions, namely :—

- (i) the project shall be undertaken by an assessee for training, education and guidance of farmers;
- (ii) the project shall have prior approval of the Ministry of Agriculture, Government of India; and
- (iii) an expenditure (not being expenditure in the nature of cost of any land or building) exceeding the amount of twenty-five lakh rupees is expected to be incurred for the project.

An assessee shall make an application in Form 3C-O to the Member(IT), CBDT for notification of such project under section 35CCC.

(b) Conditions to be fulfilled for claiming weighted deduction [Rule 6AAE]:

- (i) The assessee undertaking agricultural extension project shall maintain separate books of account of such agricultural extension project and get such books of account audited by an Accountant.
- (ii) The audit report shall include the comments of the auditor on the true and fair view of the books of account maintained for agricultural extension project, the genuineness of the activities of the agricultural extension project and fulfillment of the conditions specified in the relevant provisions of the Act or the rules.

- (iii) The assessee shall not accept an amount exceeding the amount as approved in the notification from the beneficiary under the eligible agricultural extension project for training, education, guidance or any material distributed for the purposes of such training, education or guidance.
- (iv) The assessee shall not get any direct or indirect benefit from the notified agricultural extension project except the deduction of the eligible expenditure in accordance with the provisions of section 35CCC of the Act and prescribed rules.
- (v) All expenses (not being expenditure in the nature of cost of any land or building), as reduced by the amount received from beneficiary, if any, incurred wholly and exclusively for undertaking an eligible agricultural extension project shall be eligible for deduction under section 35CCC.

However, expenditure incurred on the agricultural extension project which is reimbursed or reimbursable to the assessee by any person, whether directly or indirectly, shall not be eligible for deduction under section 35CCC.

- (vi) The assessee shall, on or before the due date of furnishing the return of income under section 139(1), furnish the following to the Commissioner of Income-tax or the Director of Income-tax, as the case may be, namely:—

(a)	the audited statement of accounts of the agricultural extension projects for the previous year along with the audit report and amount of deduction claimed under section 35CCC(1).
(b)	a note on the agricultural extension project undertaken by it during the previous year and the programme of agricultural extension project to be undertaken during the current year and the financial allocation for such programme; and
(c)	a certificate from the Ministry of Agriculture, Government of India, regarding the genuineness of the agricultural extension project undertaken by the assessee during the previous year.

2. Notification No. 39/2013 dated 31.05.2013

Time and mode of payment of tax deducted at source under section 194-IA to the credit of Central Government, furnishing challan-cum-statement and TDS Certificate [Rules 30, 31A & 31]

New section 194-IA has been inserted by Finance Act, 2013, requiring every transferee responsible for paying any sum as consideration for transfer of immovable property (land, other than agricultural land, or building or part of building) to deduct tax, at the rate 1% of such sum, at the time of credit of such sum to the account of the resident transferor or at the time of payment of such sum to a resident transferor, whichever is earlier.

Accordingly, the time and mode of, payment of tax deducted at source under section 194-IA, furnishing Challan-cum-statement and TDS Certificate have been provided, by amending Rules 30, 31A & 31, respectively -

- (i) Such sum deducted under section 194-IA shall be paid to the credit of the Central Government within a period of seven days from the end of the month in which the deduction is made and shall be accompanied by a challan-cum-statement in Form No.26QB [Rule 30].
- (ii) The amount so deducted has to be deposited to the credit of the Central Government by electronic remittance within the above mentioned time limit, into RBI, SBI or any authorized bank [Rule 30].
- (iii) Every person responsible for deduction of tax under section 194-IA shall also furnish to the DGIT (Systems) or any person authorized by him, a challan-cum-statement in Form No.26QB electronically within seven days from the end of the month in which the deduction is made [Rule 31A].
- (iv) Every person responsible for deduction of tax under section 194-IA shall furnish the TDS certificate in Form No.16B to the payee within 15 days from the due date for furnishing the challan-cum-statement in Form No.26QB under Rule 31A, after generating and downloading the same from the web portal specified by the DGIT (Systems) or the person authorized by him [Rule 31].

3. Notification No. 40/2013 dated 6.06.2013

Notification of Cost Inflation Index for F.Y.2013-14

Clause (v) of *Explanation* to section 48 defines “Cost Inflation Index”, in relation to a previous year, to mean such Index as the Central Government may, by notification in the Official Gazette, specify in this behalf, having regard to 75% of average rise in the Consumer Price Index for urban non-manual employees.

Accordingly, the Central Government has, in exercise of the powers conferred by clause (v) of *Explanation* to section 48, specified the Cost Inflation Index for the financial year 2013-14 as 939.

S. No.	Financial Year	Cost Inflation Index	S. No.	Financial Year	Cost Inflation Index
1.	1981-82	100	18.	1998-99	351
2.	1982-83	109	19.	1999-2000	389
3.	1983-84	116	20.	2000-01	406
4.	1984-85	125	21.	2001-02	426
5.	1985-86	133	22.	2002-03	447
6.	1986-87	140	23.	2003-04	463
7.	1987-88	150	24.	2004-05	480
8.	1988-89	161	25.	2005-06	497
9.	1989-90	172	26.	2006-07	519
10.	1990-91	182	27.	2007-08	551

11.	1991-92	199	28.	2008-09	582
12.	1992-93	223	29.	2009-10	632
13.	1993-94	244	30.	2010-11	711
14.	1994-95	259	31.	2011-12	785
15.	1995-96	281	32.	2012-13	852
16.	1996-97	305	33.	2013-14	939
17.	1997-98	331			

4. Notification No. 41/2013 dated 10.06.2013

Transfer Pricing Rules made applicable to Specified Domestic Transactions as well

With effect from A.Y 2013-14, the transfer pricing provisions have been extended to Specified Domestic Transactions. Accordingly, the transfer pricing rules prescribed for international transactions have been suitably amended to make the same applicable for specified domestic transactions, as well.

Rule No.	Particulars	Amendment
10A	Meaning of expressions used in computation of Arm's length price	<u>Definition of "associated enterprise" and "enterprise" included</u> "Associated Enterprise" shall - (i) have the same meaning as assigned to it in section 92A; and (ii) in relation to a specified domestic transaction entered into by an assessee, include -- (A) the persons referred to in section 40A(2)(b) in respect of a transaction referred to in section 40A(2)(a); (B) other units or undertakings or businesses of such assessee in respect of a transaction referred to in section 80A or section 80-IA(8); (C) any other person referred to in section 80-IA(10) in respect of a transaction referred to therein; (D) other units, undertakings, enterprises or business of such assessee, or other person referred to in section 80-IA(10) or in respect of a transaction referred to in section 10AA or the transactions referred to in Chapter VI-A to which the provisions of section 80-IA(8) or section 80-IA(10) are applicable; "Enterprise" shall have the same meaning as assigned to it in clause (iii) of section 92F and shall, for the

		purposes of a specified domestic transaction, include a unit, or an enterprise, or an undertaking or a business of a person who undertakes such transaction.
10AB	Other methods of determination of ALP	This Rule provides that for the purpose of section 92C(1)(f), the other method for determination of the arm's length price in relation to an international transaction shall be any method which takes into account the price which has been charged or paid or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts. This Rule has now been made applicable to specified domestic transactions as well.
10B	Determination of ALP under section 92C	The methods for determination of arm's length price specified in this Rule for the purpose of section 92C(2) in relation to an international transaction shall also be made applicable in respect of specified domestic transactions.
10C	Most appropriate method	Sub-rule (1) provides that, for the purposes of section 92C(1), the most appropriate method shall be the method which is best suited to the facts and circumstances of each particular international transaction, and which provides the most reliable measure of an arm's length price in relation to an international transaction. Sub-rule (2) specifies the factors to be taken into account in selecting the most appropriate method. This Rule is now made applicable in respect of a specified domestic transaction as well.
10D	Information and documents to be kept and maintained under section 92D	Sub-rule (1) requires every person who has entered into an international transaction to maintain the requisite information and documents as detailed thereunder. As per sub-rule (2), maintenance of information and documents shall not apply where the aggregate value of international transactions does not exceed 1 crore rupees. However, sub-rule (1) shall be applicable for every specified domestic transaction irrespective of its value.

10E	Report from an accountant to be furnished under section 92E	This rule provides for submission of audit report from a chartered accountant by every person who has entered into an international transaction. This provision would now apply to a person entered into a specified domestic transaction as well.
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5. Notification No. 54/2013, dated 15.07.2013

Approval of skill development project under section 35CCD: Conditions and Guidelines

In order to encourage **companies** to invest on skill development projects, section 35CCD was inserted, to provide for weighted deduction of a sum equal to 150% of the expenditure (not being expenditure in the nature of cost of any land or building) incurred on skill development project notified by the CBDT, in accordance with the prescribed guidelines.

Accordingly, the CBDT has, in exercise of the powers conferred by section 295 read with section 35CCD(1) of the Income-tax Act, 1961, laid down the guidelines and conditions for approval of a skill development project under section 35CCD.

S. No.	Particulars														
(1)	<u>Guidelines for approval of Skill Development Project under section 35CCD:</u> A skill development project shall be considered for notification if it is undertaken by an eligible company and the project is undertaken in separate facilities in a training institute [Rule 6AAF(1)]														
(i)	"Eligible company" means a company, which is - - engaged in the business of manufacture or production of any article or thing specified in the Eleventh Schedule; not being beer, wine and other alcoholic spirits and tobacco & tobacco preparations such as cigars and cheroots, cigarettes, biris, smoking mixtures for pipes and cigarettes, chewing tobacco and snuff or - engaged in providing the following services <table> <tr> <th>S. No.</th><th>Particulars</th></tr> <tr> <td>1.</td><td>Accounting services</td></tr> <tr> <td>2.</td><td>Architect services</td></tr> <tr> <td>3.</td><td>Automobile repair or maintenance</td></tr> <tr> <td>4.</td><td>Banking, insurance and financial services including ATM installation, maintenance and operations or banking correspondents or insurance agents</td></tr> <tr> <td>5.</td><td>Beauty and cosmetology, including hair styling or manicurists or pedicurists</td></tr> <tr> <td>6.</td><td>Cable operators or Direct To Home (DTH) services</td></tr> </table>	S. No.	Particulars	1.	Accounting services	2.	Architect services	3.	Automobile repair or maintenance	4.	Banking, insurance and financial services including ATM installation, maintenance and operations or banking correspondents or insurance agents	5.	Beauty and cosmetology, including hair styling or manicurists or pedicurists	6.	Cable operators or Direct To Home (DTH) services
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		7.	Cargo Handling and stevedoring services
		8.	Construction including painting or woodwork or plumbing or flooring or electrical wiring or installation or maintenance of lifts
		9.	Courier services
		10.	Design services including fashion or gems and jewellery or apparel or industrial designing
		11.	Event management
		12.	Facilities management, housekeeping, cleaning services
		13.	Fire and safety services
		14.	Food processing or preservation services, including post harvesting and post farm gate skills
		15.	Health and Wellness services including spa or nutritionists or weight management or health instructors or yoga or gym trainers
		16.	Home decor services, landscaping
		17.	Hospital and Healthcare services, such as Lab technicians, nursing and other paramedical staff
		18.	Hospitality, including culinary skills or catering services
		19.	Logistics and Transportation by any mode, including by air, sea, road, rail or pipelines, and related services such as driving or operation of heavy machinery equipment, forwarding agents, packers and movers
		20.	Market research services
		21.	Media or film or advertising
		22.	Mining and extraction of mineral resources, including hydrocarbons
		23.	Packaging and Warehousing, including both ambient temperature storage and cold storage, operation of Internal Container Depots and Container Freight Stations
		24.	Port and maritime services such as dredging, piloting, tug boat operations, shipbuilding, ship scrapping, bunkering
		25.	Power Sector Services, including those required for erection or installation or maintenance of equipment or towers, etc. in generation, transmission or distribution sector projects
		26.	Private Security, including guards, supervisors, installation and maintenance of security equipment etc.
		27.	Refrigeration and air-conditioning
		28.	Repair and maintenance services, including Installation and servicing of household goods or white goods

		<table><tr><td>29.</td><td>Retail marketing, including shop floor assistants or merchandisers</td></tr><tr><td>30.</td><td>Telecom services, including erection and maintenance of towers</td></tr><tr><td>31.</td><td>Travel and tourism, including guides or ticketing or sales or cab drives</td></tr></table>	29.	Retail marketing, including shop floor assistants or merchandisers	30.	Telecom services, including erection and maintenance of towers	31.	Travel and tourism, including guides or ticketing or sales or cab drives
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	(ii)	“Training Institute” means a training institute set up by the Central or State Government or a local authority or a training institute affiliated to National Council for Vocational Training or State Council for Vocational Training. A skill development project in respect of existing employees of the company shall not be eligible for notification under section 35CCD(1), where the training of such employees commences after six months of their recruitment [Rule 6AAG(3)].						
(2)	<u>Application for approval of project [Rule 6AAF(2)]:</u> Such company, before undertaking any skill development project, shall : - make an application for notification of such project under section 35CCD(1), in duplicate, in Form No. 3CQ, to the National Skill Development Agency(NSDA); and - also send a copy of the application in Form No. 3CQ to the Commissioner of Income tax or the Director of the Income tax as the case may be, having jurisdiction over the case, accompanied by the acknowledgement receipt as evidence of having furnished the application form in duplicate to the NSDA.							
(3)	<u>Conditions laid down under Rule 6AAG:</u> (i) The Company which undertakes a skill development project shall maintain separate books of account of the skill development project and get such books of account audited by an Accountant. (ii) All expenses (not being expenditure in the nature of cost of any land or building), incurred wholly and exclusively for undertaking a notified skill development project shall be eligible for deduction under section 35CCD. However, the expenditure incurred on the skill development project which is reimbursed or reimbursable to the company by any person, whether directly or indirectly, shall not be eligible for deduction under section 35CCD. (iii) The company shall, on or before the due date of furnishing the return of income under section 139(1), furnish the audited statement of accounts of the skill development project for the previous year along with the audit report and amount of deduction claimed under section 35CCD(1) to the Commissioner of Income-tax or the Director of Income-tax, as the case may be.							

6. Notification No.57 / 2013 dated 01.08.2013**Documents and information, to be furnished by the assessee for claiming treaty benefits, prescribed**

For claiming treaty benefits, sections 90(4) and 90A(4) provide that a certificate issued by the Government of a foreign country would constitute proof of tax residency, without any further conditions regarding furnishing of “prescribed particulars” therein.

Further, sections 90(5) and 90A(5) require **an assessee to provide such other documents and information, as may be prescribed**, for claiming the treaty benefits, in addition to such certificate issued by the foreign Government.

Accordingly, the assessee shall provide the following information in Form No. 10F:

- (i) Status (individual, company, firm etc.) of the assessee;
- (ii) Nationality (in case of an individual) or country or specified territory of incorporation or registration (in case of others);
- (iii) Assessee's tax identification number in the country or specified territory of residence and in case there is no such number, then, a unique number on the basis of which the person is identified by the Government of the country or the specified territory of which the assessee claims to be a resident;
- (iv) Period for which the residential status, as mentioned in the certificate referred to in section 90(4) or section 90A(4), is applicable; and
- (v) Address of the assessee in the country or specified territory outside India, during the period for which the certificate, as mentioned in (iv) above, is applicable.

However, the assessee may not be required to provide the information or any part thereof, if the information or the part thereof, as the case may be, is already contained in the TRC referred to in section 90(4) or section 90A(4).

The assessee shall keep and maintain such documents as are necessary to substantiate the information provided. An income-tax authority may require the assessee to provide the said documents in relation to a claim by the said assessee of any relief under an agreement referred to in section 90(1) or section 90A(1), as the case may be.

7. Notification No. 64/2013, dated 19.08.2013**Notification of foreign company for claiming exemption under section 10(48)**

Income received by a foreign company in India in Indian currency from sale of crude oil, any other goods or rendering of services, as may be notified by the Central Government in this behalf, to any person in India is exempt under section 10(48). For this purpose,

the foreign company, as well as the arrangement or agreement, should be notified by the Central Government having regard to the national interest. The foreign company should not be engaged in any other activity in India, except receipt of income under such arrangement or agreement.

Accordingly, vide this notification, the Central Government, having regard to the national interest, has notified for the purposes of the said clause, the National Iranian Oil Company, as the foreign company and the Memorandum of Understanding entered between the Government of India in the Ministry of Petroleum and Natural Gas and the Central Bank of Iran on the 20th January, 2013, as the agreement subject to the condition that the said foreign company shall not engage in any activity in India, other than the receipt of income under the agreement aforesaid.

The Notification is deemed to be effective from 20th January, 2013.

8. Notification No. 67/2013 dated 02.09.2013

Furnishing of information by the person responsible for making any payment chargeable to tax to a non-corporate non-resident or to a foreign company

The CBDT has, vide this notification, inserted new Rule 37BB relating to furnishing of information by the person responsible for making any payment, including any interest or salary or any other sum chargeable to tax, to a non-corporate non-resident or to a foreign company.

Sub-rule (1) requires such person to furnish the following:

- (i) the information in Part A of Form No.15CA, if the amount of payment does not exceed ₹ 50,000 and the aggregate of such payments made during the financial year does not exceed ₹ 2,50,000;
- (ii) the information in Part B of Form No.15CA for payments other than the payments referred in clause (i), after obtaining-
 - (a) a certificate in Form No.15CB from an “accountant” as defined in the *Explanation* below section 288(2); or
 - (b) a certificate from the Assessing Officer under section 197; or
 - (c) an order from the Assessing Officer under section 195(2) or section 195(3).

Sub-rule (2) requires the information in Form No. 15CA to be furnished by the person electronically to the website designated by the Income-tax Department and the submission of the signed printout of the said form to the authorised dealer under section 10(1) of the Foreign Exchange Management Act, 1999, prior to remitting the payment.

Sub-rule (3) provides that an income-tax authority may require the authorised dealer to furnish the signed printout for the purposes of any proceedings under the Act.

Further, in respect of the payments of the nature described in the “Specified list” given in the said Notification (like Indian investment abroad in equity, debt securities, subsidiaries and associates, branches and wholly-owned subsidiaries, real estate, remittance towards business travel, personal gifts and donations, donations to charitable and religious institutions abroad etc.) no information is required to be furnished under sub-rule (1).

9. Notification No. 73/2013, dated 18.09.2013

Notification of Safe Harbour Rules

Section 92CB(1) provides that the determination of arm’s length price under section 92C or section 92CA shall be subject to safe harbour rules. Safe harbour means circumstances in which the income tax authorities shall accept the transfer price declared by the assessee.

Section 92CB(2) empowers the CBDT to prescribe such safe harbour rules or circumstances under which the transfer price declared by the assessee shall be accepted by the Income-tax Authorities.

Accordingly, in exercise of the powers conferred by section 92CB read with section 295 of the Income-tax Act, 1961, the CBDT has, vide this notification, prescribed safe harbour rules. These rules are explained hereunder:

1. Safe Harbour [Rule 10TD read with Rule 10TA, Rule 10TB and Rule 10TC]

Where an eligible assessee has entered into an eligible international transaction and the option exercised by the said assessee is not held to be invalid under Rule 10TE, the transfer price declared by the assessee in respect of such transaction shall be accepted by the income-tax authorities, if it is in accordance with the circumstances mentioned below:

S. No.	Eligible International Transaction ¹	Circumstances	Definition																				
	[Rule 10TC]	[Rule 10TD]	[Rule 10TA]																				
(i)	Provision of software development services	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to operating expense incurred is –<table><tr><td>Not less than the prescribed percentage</td><td>Where the aggregate value of such transactions entered into during the previous year</td></tr><tr><td>20%</td><td>does not exceed a sum of ₹ 500 crore;</td></tr><tr><td>22%</td><td>exceeds a sum of ₹ 500 crore.</td></tr></table>	Not less than the prescribed percentage	Where the aggregate value of such transactions entered into during the previous year	20%	does not exceed a sum of ₹ 500 crore;	22%	exceeds a sum of ₹ 500 crore.	“Software development services” means, -<table><tr><td>(i)</td><td>business application software and information system development using known methods and existing software tools;</td></tr><tr><td>(ii)</td><td>support for existing systems;</td></tr><tr><td>(iii)</td><td>Converting or translating computer languages;</td></tr><tr><td>(iv)</td><td>adding user functionality to application programmes;</td></tr><tr><td>(v)</td><td>debugging of systems;</td></tr><tr><td>(vi)</td><td>adaptation of existing software; or</td></tr><tr><td>(vii)</td><td>preparation of user documentation.</td></tr></table> It, however, does not include any R&D services whether or not in the nature of contract R&D services.	(i)	business application software and information system development using known methods and existing software tools;	(ii)	support for existing systems;	(iii)	Converting or translating computer languages;	(iv)	adding user functionality to application programmes;	(v)	debugging of systems;	(vi)	adaptation of existing software; or	(vii)	preparation of user documentation.
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(ii)	Provision of information technology enabled services	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to operating expense incurred is –	“Information technology enabled services” means the following business process outsourcing services provided mainly with the assistance or use of information technology, namely:-																				

¹ Eligible international transaction means an international transaction between the eligible assessee and its associated enterprise, either or both of whom are non-residents, and which comprises of the transactions described in column (2) of the above table.

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(iii)	Provision of knowledge process	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to	“Knowledge process outsourcing services” means the following business process outsourcing services provided mainly with the assistance or use of																																				

outsourcing services	operating expense is not less than 25%, irrespective of the aggregate value of the transactions entered into during the previous year.	<table><tr><td>(i)</td><td>geographic information system</td></tr><tr><td>(ii)</td><td>human resources services</td></tr><tr><td>(iii)</td><td>engineering and design services</td></tr><tr><td>(iv)</td><td>animation or content development and management</td></tr><tr><td>(v)</td><td>business analytics</td></tr><tr><td>(vi)</td><td>financial analytics</td></tr><tr><td>(vii)</td><td>market research</td></tr></table> It, however, does not include any R&D services whether or not in the nature of contract R&D services.	(i)	geographic information system	(ii)	human resources services	(iii)	engineering and design services	(iv)	animation or content development and management	(v)	business analytics	(vi)	financial analytics	(vii)	market research
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(vi)	financial analytics															
(vii)	market research															
(iv) Advancing of intra-group loans	<table><tr><td>Where the amount of loan does not exceed ₹ 50 crore.</td><td>The Interest rate declared in relation to the eligible international transaction is not less than the base rate of SBI as on 30th June of the relevant previous year + 1.5%.</td></tr><tr><td>Where the amount of loan exceeds ₹ 50 crore.</td><td>The Interest rate declared in relation to the eligible international transaction is not less than the base rate of SBI as on 30th June of the relevant previous year + 3%.</td></tr></table>	Where the amount of loan does not exceed ₹ 50 crore.	The Interest rate declared in relation to the eligible international transaction is not less than the base rate of SBI as on 30th June of the relevant previous year + 1.5% .	Where the amount of loan exceeds ₹ 50 crore.	The Interest rate declared in relation to the eligible international transaction is not less than the base rate of SBI as on 30th June of the relevant previous year + 3% .	“Intra-group loan” means loan advanced to wholly owned subsidiary being a non-resident, where the loan— <table><tr><td>(i)</td><td>is sourced in Indian rupees</td></tr><tr><td>(ii)</td><td>is not advanced by an enterprise, being a financial company including a bank or a financial institution or an enterprise engaged in lending or borrowing in the normal course of business; and</td></tr><tr><td>(iii)</td><td>does not include credit line or any other loan facility which has no fixed term for repayment;</td></tr></table>	(i)	is sourced in Indian rupees	(ii)	is not advanced by an enterprise, being a financial company including a bank or a financial institution or an enterprise engaged in lending or borrowing in the normal course of business; and	(iii)	does not include credit line or any other loan facility which has no fixed term for repayment;				
Where the amount of loan does not exceed ₹ 50 crore.	The Interest rate declared in relation to the eligible international transaction is not less than the base rate of SBI as on 30th June of the relevant previous year + 1.5% .															
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(i)	is sourced in Indian rupees															
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(iii)	does not include credit line or any other loan facility which has no fixed term for repayment;															

(v)	Providing corporate guarantee	<table><tr><td>Where the amount guaranteed -</td><td>The commission or fee declared in relation to the eligible international transaction is at the rate not less than -</td></tr><tr><td>does not exceed ₹ 100 crore.</td><td>2% p.a. on the amount guaranteed.</td></tr><tr><td>exceeds ₹ 100 crore and the credit rating of the associated enterprise done by an agency registered with the SEBI is of the adequate to the highest safety</td><td>1.75% p.a. on the amount guaranteed</td></tr></table>	Where the amount guaranteed -	The commission or fee declared in relation to the eligible international transaction is at the rate not less than -	does not exceed ₹ 100 crore.	2% p.a. on the amount guaranteed.	exceeds ₹ 100 crore and the credit rating of the associated enterprise done by an agency registered with the SEBI is of the adequate to the highest safety	1.75% p.a. on the amount guaranteed	“Corporate guarantee” means explicit corporate guarantee extended by a company to its wholly owned subsidiary being a non-resident in respect of any short-term or long-term borrowing. Explicit corporate guarantee, however, does not include _ <table><tr><td>(i)</td><td>letter of comfort;</td></tr><tr><td>(ii)</td><td>implicit corporate guarantee;</td></tr><tr><td>(iii)</td><td>performance guarantee; or</td></tr><tr><td>(iv)</td><td>any other guarantee of similar nature.</td></tr></table>	(i)	letter of comfort;	(ii)	implicit corporate guarantee;	(iii)	performance guarantee; or	(iv)	any other guarantee of similar nature.
Where the amount guaranteed -	The commission or fee declared in relation to the eligible international transaction is at the rate not less than -																
does not exceed ₹ 100 crore.	2% p.a. on the amount guaranteed.																
exceeds ₹ 100 crore and the credit rating of the associated enterprise done by an agency registered with the SEBI is of the adequate to the highest safety	1.75% p.a. on the amount guaranteed																
(i)	letter of comfort;																
(ii)	implicit corporate guarantee;																
(iii)	performance guarantee; or																
(iv)	any other guarantee of similar nature.																
(vi)	Provision of contract R&D services wholly or partly relating to software development.	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to operating expense incurred is not less than 30%, irrespective of the aggregate value of the transactions entered into during the previous year.	“Contract research and development (R&D) services wholly or partly relating to software development” means the following, namely:- <table><tr><td>(i)</td><td>R & D producing new theorems and algorithms in the field of theoretical computer science;</td></tr><tr><td>(ii)</td><td>development of information technology at the level of operating systems, programming languages, data</td></tr></table>	(i)	R & D producing new theorems and algorithms in the field of theoretical computer science;	(ii)	development of information technology at the level of operating systems, programming languages, data										
(i)	R & D producing new theorems and algorithms in the field of theoretical computer science;																
(ii)	development of information technology at the level of operating systems, programming languages, data																

(vii)	Provision of contract R&D services wholly or partly relating to generic pharmaceutical drugs	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to operating expense incurred is not less than 29%, irrespective of the aggregate value of the transactions entered into during the previous year.	“Generic pharmaceutical drug” means a drug that is comparable to a drug already approved by the regulatory authority in dosage form, strength, route of administration, quality and performance characteristics, and intended use.
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(viii)	Manufacture and export of core auto components	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to operating expense is not less than 12%, irrespective of the aggregate value of the transactions entered into during the previous year.	<table><tr><td></td><td>“Core auto components” means ,</td></tr><tr><td>(i)</td><td>engine and engine parts, including piston and piston rings, engine valves and parts cooling systems and parts and power train components;</td></tr><tr><td>(ii)</td><td>transmission and steering parts, including gears, wheels, steering systems, axles and clutches;</td></tr><tr><td>(iii)</td><td>suspension and braking parts, including brake and brake assemblies, brake linings, shock absorbers and leaf springs;</td></tr></table>		“Core auto components” means ,	(i)	engine and engine parts, including piston and piston rings, engine valves and parts cooling systems and parts and power train components;	(ii)	transmission and steering parts, including gears, wheels, steering systems, axles and clutches;	(iii)	suspension and braking parts, including brake and brake assemblies, brake linings, shock absorbers and leaf springs;
	“Core auto components” means ,										
(i)	engine and engine parts, including piston and piston rings, engine valves and parts cooling systems and parts and power train components;										
(ii)	transmission and steering parts, including gears, wheels, steering systems, axles and clutches;										
(iii)	suspension and braking parts, including brake and brake assemblies, brake linings, shock absorbers and leaf springs;										
(ix)	Manufacture and export of non-core auto components	The operating profit margin declared by the eligible assessee from the eligible international transaction in relation to operating expense is not less than 8.5%, irrespective of the aggregate value of the transactions entered into during the previous year.	“Non-core auto components” mean auto components other than core auto components.								
Notes:											
(1) The above provisions shall apply for A.Y. 2013-14 to A.Y. 2017-18.											
(2) The second proviso to section 92C(2) provides that if the variation between the arm's length price determined and the price at which the transaction has been undertaken does not exceed such percentage, not exceeding 3%, as may be notified by the Central Government in the Official Gazette, the price at which the transaction has actually been undertaken shall be deemed to be the arm's length price. However, no comparability adjustment and allowance under the second proviso to section 92C(2) shall be made to the transfer price declared by the eligible assessee and accepted under the Safe Harbour Rules given above.											
(3) Section 92D requiring every person who has entered into an international transaction to keep and maintain the prescribed information and documents and section 92E requiring such person to obtain a report from an accountant and furnish such report on or before the specified date in prescribed form and manner, shall apply irrespective of the fact that the assessee exercises his option for safe harbor in respect of such transaction.											

Meaning of certain terms used above

	Term	Meaning																
(i)	Operating expense [Rule 10TA]	The costs incurred in the previous year by the assessee in relation to the international transaction during the course of its normal operations including depreciation and amortisation expenses relating to the assets used by the assessee, but not including the following, namely, - <table><tr><td>(i)</td><td>interest expense;</td></tr><tr><td>(ii)</td><td>provision for unascertained liabilities;</td></tr><tr><td>(iii)</td><td>pre-operating expenses;</td></tr><tr><td>(iv)</td><td>loss arising on account of foreign currency fluctuations;</td></tr><tr><td>(v)</td><td>extraordinary expenses;</td></tr><tr><td>(vi)</td><td>loss on transfer of assets or investments;</td></tr><tr><td>(vii)</td><td>expense on account of income-tax; and</td></tr><tr><td>(viii)</td><td>other expenses not relating to normal operations of the assessee;</td></tr></table>	(i)	interest expense;	(ii)	provision for unascertained liabilities;	(iii)	pre-operating expenses;	(iv)	loss arising on account of foreign currency fluctuations;	(v)	extraordinary expenses;	(vi)	loss on transfer of assets or investments;	(vii)	expense on account of income-tax; and	(viii)	other expenses not relating to normal operations of the assessee;
(i)	interest expense;																	
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(v)	extraordinary expenses;																	
(vi)	loss on transfer of assets or investments;																	
(vii)	expense on account of income-tax; and																	
(viii)	other expenses not relating to normal operations of the assessee;																	
(ii)	Operating revenue [Rule 10TA]	The revenue earned by the assessee in the previous year in relation to the international transaction during the course of its normal operations but not including the following, namely, - <table><tr><td>(i)</td><td>interest income;</td></tr><tr><td>(ii)</td><td>income arising on account of foreign currency fluctuations;</td></tr><tr><td>(iii)</td><td>income on transfer of assets or investments;</td></tr><tr><td>(iv)</td><td>refunds relating to income-tax;</td></tr><tr><td>(v)</td><td>provisions written back;</td></tr><tr><td>(vi)</td><td>extraordinary incomes; and</td></tr><tr><td>(vii)</td><td>other incomes not relating to normal operations of the assessee;</td></tr></table>	(i)	interest income;	(ii)	income arising on account of foreign currency fluctuations;	(iii)	income on transfer of assets or investments;	(iv)	refunds relating to income-tax;	(v)	provisions written back;	(vi)	extraordinary incomes; and	(vii)	other incomes not relating to normal operations of the assessee;		
(i)	interest income;																	
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(iv)	refunds relating to income-tax;																	
(v)	provisions written back;																	
(vi)	extraordinary incomes; and																	
(vii)	other incomes not relating to normal operations of the assessee;																	
(iii)	Operating profit margin [Rule 10TA]	Operating profit margin, in relation to operating expense, means the ratio of operating profit, being the operating revenue in excess of operating expense, to the operating expense expressed in terms of percentage;																

(iv)	Eligible Assessee [Rule 10TB(1)]	A person who has exercised a valid option for application of safe harbor rules and -			
		(i)	is engaged in providing the following services with insignificant risk -		
			software development services; or	to a non-resident associated enterprise (i.e., foreign principal);	
			information technology enabled services; or		
			knowledge process outsourcing services		
		(ii)	has made any intra-group loan;		
		(iii)	has provided a corporate guarantee;		
		(iv)	is engaged in providing contract R & D services wholly or partly relating to software development, with insignificant risk ,	to a non-resident associated enterprise (i.e., foreign principal);	
		(v)	is engaged in providing contract research and development services wholly or partly relating to generic pharmaceutical drugs, with insignificant risk ,		
		(vi)	is engaged in the manufacture and export of core or non-core auto components and where 90% or more of total turnover during the relevant previous year is in the nature of original equipment manufacturer sales		

Factors to be considered for identifying an eligible assessee with insignificant risk, referred to in clauses of (i), (iv) & (v) of Rule 10TB(1) defining an “Eligible assessee” [Rule 10TB (2) & (3)]

	Particulars	Foreign Principal [For Clause (i)]	Foreign Principal [For Clauses (iv) & (v)]	Eligible Assessee [For clauses (i), (iv) & (v)]	Remark
(1)	Economically significant functions	Performs most of the economically significant functions involved either through its own	Performs most of the economically significant functions involved in research or product	Carries out the work assigned to it by the foreign principal.	Economically significant functions would include critical functions such as conceptualization and design

		employees or through its associated enterprises	development cycle either through its own employees or through its associated enterprises		of the product and providing the strategic direction and framework.
(2)	Funds, Capital and other economically significant assets	Provides funds/ capital and other economically significant assets including intangibles required	Provides funds/ capital and other economically significant assets including intangibles required for research or product development.	Does not assume or has no economically significant realized risks. Receives remuneration from the Foreign Principal for carrying out the work.	If a contract shows that the foreign principal is obligated to control the risk but the conduct shows that the eligible assessee is doing so, then the contractual terms are not the final determinant.
(3)	Supervision and control	Has not only the capability to control or supervise but also actually controls or supervises the activities carried out through its strategic decisions to perform core functions as well as monitor activities on regular basis.	Has not only the capability to control or supervise but also actually controls or supervises the research or product development through its strategic decisions to perform core functions as well as monitor activities on regular basis.	Works under the direct supervision of the foreign principal or its associated enterprise	
(4)	Ownership rights	Has ownership right on any intangible generated or on the outcome of intangible generated or arising during the course of rendering of services.	Has ownership right on the outcome of the research	Has no ownership right (legal or economic).	This fact should be evident from the contract as well as from the conduct of the parties.

Procedure [Rule 10TE]**(1) Furnishing Form 3CEFA**

- (i) For exercising the option for safe harbor, the assessee has to furnish Form 3CEFA, complete in all respects, to the Assessing Officer on or before the due date specified in *Explanation 2* below section 139(1), for furnishing return of income for –

the relevant assessment year	In case the option is exercised only for that assessment year
the first of the assessment years	In case the option is exercised for more than one assessment year.

- (ii) The return of income for the relevant assessment year or the first of the relevant assessment years, as the case may be, has to be furnished by the assessee on or before the date of furnishing Form 3CEFA.
- (iii) In respect of the assessment year or years following the initial assessment year, the assessee has to furnish a statement to the Assessing Officer before furnishing return of income of that year, providing –
- details of eligible transactions,
 - their quantum and
 - the profit margins or the rate of interest or commission.

(2) Period for which the option for safe harbor shall remain in force

- (i) The period specified in Form 3CEFA or a period of five years, whichever is less.
- (ii) The option for safe harbor shall not remain in force in respect of any assessment year following the initial assessment year, if -
- (1) the option is held to be invalid for the relevant assessment year by the Transfer Pricing Officer or by the Commissioner in respect of an objection filed by the assessee against the order of the Transfer Pricing Officer, as the case may be; or
 - (2) the eligible assessee opts out of the safe harbour, for the relevant assessment year, by furnishing a declaration to that effect, to the Assessing Officer.

(3) Circumstances requiring determination of ALP as per sections 92C and 92CA

In the following cases, the arm's length price in relation to an international transaction shall be determined in accordance with the provisions of sections 92C and 92CA without having regard to the profit margin or the rate of interest or commission as specified rule 10TD -

- (i) Where no option for safe harbour has been exercised by an eligible assessee in respect of an eligible international transaction entered into by the assessee; or
- (ii) Where the option exercised by the assessee is held to be invalid

Non-applicability of Safe Harbour Rules in certain cases [Rule 10TF]

The rules for safe harbor, contained in Rules 10TA, 10TB, 10TC, 10TD or 10TE, shall **not** apply in respect of eligible international transactions entered into with an associated enterprise located in –

- (i) any country or territory notified under section 94A [a Notified Jurisdictional Area (NJA)]; or
- (ii) a no tax or low tax country or territory.

“No tax or low tax country or territory” means a country or territory in which the maximum rate of income-tax is less than 15%.

No recourse to MAP [Rule 10TG]

Where transfer price in relation to an eligible international transaction declared by an eligible assessee is accepted by the income tax authorities under section 92CB, the assessee shall not be entitled to invoke Mutual Agreement Procedure (MAP) under an agreement for avoidance of double taxation entered into with a country or specified territory outside India as referred to in sections 90 or 90A.

10. Notification No.79/2013 dated 07.10.2013**Reverse Mortgage Scheme amended to include within its scope, disbursement to an annuity sourcing institution for periodic payments by way of annuity to the Reverse Mortgagor**

The Central Government had notified the Reverse Mortgage Scheme, 2008 in exercise of the powers conferred by clause (xvi) of section 47 of the Income-tax Act, 1961. Reverse Mortgage means mortgage of a capital asset by an eligible person against a loan obtained by him from an approved lending institution. Such kind of a transaction is not regarded as transfer under section 47(xvi) and amounts received by the Reverse Mortgagor as loan, either in lump-sum or in installment, are exempt under section 10(43).

The Central Government has, vide this notification, amended the Reverse Mortgage Scheme, 2008, to include within its scope, disbursement of loan by an approved lending institution, in part or in full, to the annuity sourcing institution, for the purposes of periodic payments by way of annuity to the reverse mortgagor. This would be an additional mode of disbursement i.e., in addition to direct disbursements by the approved lending institution to the Reverse Mortgagor by way of periodic payments or lump sum payment in one or more tranches.

An annuity sourcing institution has been defined to mean Life Insurance Corporation of India or any other insurer registered with the Insurance Regulatory and Development Authority.

Maximum Period of Reverse Mortgage Loan

	Mode of disbursement	Maximum period of loan
(a)	Where the loan is disbursed directly to the Reverse Mortgagor	20 years from the date of signing the agreement by the reverse mortgagor and the approved lending institution.
(b)	Where the loan is disbursed, in part or in full, to the annuity sourcing institution for the purposes of periodic payments by way of annuity to the Reverse mortgagor	The residual life time of the borrower.

11. Notification No. 86/2013 dated 01.11.2013**Notification of Cyprus as a Notified Jurisdictional Area under section 94A**

In order to discourage assesseees from entering into transactions with persons located in countries or territories outside India which do not have effective information exchange mechanism with India, section 94A empowers the Central Government to notify such country or territory outside India as a notified jurisdictional area (NJA).

Accordingly, in exercise of the powers conferred by section 94A(1), the Central Government has specified 'Cyprus' as a NJA for the purposes of the said section. The tax consequences of notifying Cyprus as a NJA under section 94A are as follows –

- (i) A transaction where one of the parties thereto is a person located in Cyprus would be deemed to be an international transaction and all parties to the transaction would be deemed as associated enterprises. Accordingly, all the provisions of transfer pricing would be attracted in respect of such transaction. However, the benefit of permissible variation between the arm's length price and the transfer price [provided in the second proviso to section 92C(2)] based on the rate notified by the Central Government would not be available in respect of such transaction.
- (ii) Person located in Cyprus shall include a person who is a resident of Cyprus and a person, not being an individual, which is established in Cyprus. It would also include a permanent establishment of any other person in Cyprus.
- (iii) Payments made to any financial institution located in Cyprus would not be allowed as deduction unless the assessee authorizes the CBDT or any other income-tax authority acting on its behalf to seek relevant information from the financial institution on behalf of the assessee.
- (iv) No deduction in respect of any other expenditure or allowance, including depreciation, arising from the transaction with a person located in Cyprus would be allowed unless the assessee maintains the prescribed documents and furnishes the prescribed information.
- (v) Any sum credited or received from a person located in Cyprus would be deemed to be the income of the recipient-assessee if he does not explain satisfactorily the source of such money in the hands of such person or in the hands of the beneficial owner, if such person is not the beneficial owner.
- (vi) The rate of TDS in respect of any payment made to a person located in Cyprus, on which tax is deductible at source, will be the higher of the following rates –
 - (1) rates specified in the relevant provision of the Income-tax Act, 1961; or
 - (2) rate or rates in force; or
 - (3) 30%.

12. Notification No. 94/2013, dated 18.12.2013

Notification of "Rajiv Gandhi Equity Savings Scheme, 2013" for the purpose of deduction under section 80CCG

The Finance Act, 2012 had inserted section 80CCG in the Income-tax Act, 1961 to provide for a one-time deduction for A.Y.2013-14 to a resident individual who acquires listed equity shares in a previous year in accordance with a scheme notified by the Central Government, to encourage flow of savings in financial instruments and improve the depth of domestic capital market. However, only a resident individual, being a new retail investor, whose gross total income did not exceed Rs.10 lakh was eligible for the benefit of deduction. The deduction was 50% of amount invested in such equity shares or Rs.25,000, whichever is lower. The maximum deduction of Rs.25,000 was available on investment of Rs.50,000 in such listed equity shares.

The Finance Act, 2013 has amended the provisions of section 80CCG w.e.f. A.Y.2014-15 so that the benefit of deduction under this section is available to a new retail investor, being a resident individual with gross total income of up to ₹ 12 lakh, for investment in listed equity shares or listed units of equity oriented fund, in accordance with a notified scheme. Further, the deduction shall be allowed for three consecutive assessment years, beginning with the assessment year relevant to the previous year in which the listed equity shares or listed units of equity oriented fund were first acquired. The quantum of deduction would continue to remain the same.

Accordingly, the Central Government has, in exercise of the powers conferred by section 80CCG(1), notified the Rajiv Gandhi Equity Savings Scheme, 2013. The said scheme provides for eligibility criteria, procedure for investment, period of holding and other conditions.

S. No.	Particulars	Content					
1.	Eligibility	The deduction under this scheme shall be available to a new retail investor who complies with the conditions of the Scheme and whose gross total income for the financial year in which the investment is made under the Scheme is less than or equal to ₹12 lakh. <table><tr><td> New retail investor means a resident individual,: (i) who has not opened a demat account and has not made any transactions in the derivative segment before - - the date of opening of a demat account; or - the first day of the initial year, However, an individual who is not the first account holder of an existing joint demat account shall be deemed to have not opened a demat account for the purposes of this Scheme; (ii) who has opened a demat account but has not made any transactions in the equity segment or the derivative segment before – - the date he designates his existing demat account for the purpose of availing the benefit under the Scheme; or - the first day of the initial year. </td><td> } whichever is later } whichever is later </td></tr><tr><td colspan="2"></td><td> Initial year means - (a) the financial year in which the investor designates his demat account as Rajiv Gandhi Equity Savings Scheme account and makes investment in the eligible securities for availing deduction under the Scheme; or </td></tr></table>	New retail investor means a resident individual,: (i) who has not opened a demat account and has not made any transactions in the derivative segment before - - the date of opening of a demat account; or - the first day of the initial year, However, an individual who is not the first account holder of an existing joint demat account shall be deemed to have not opened a demat account for the purposes of this Scheme; (ii) who has opened a demat account but has not made any transactions in the equity segment or the derivative segment before – - the date he designates his existing demat account for the purpose of availing the benefit under the Scheme; or - the first day of the initial year.	} whichever is later } whichever is later			Initial year means - (a) the financial year in which the investor designates his demat account as Rajiv Gandhi Equity Savings Scheme account and makes investment in the eligible securities for availing deduction under the Scheme; or
New retail investor means a resident individual,: (i) who has not opened a demat account and has not made any transactions in the derivative segment before - - the date of opening of a demat account; or - the first day of the initial year, However, an individual who is not the first account holder of an existing joint demat account shall be deemed to have not opened a demat account for the purposes of this Scheme; (ii) who has opened a demat account but has not made any transactions in the equity segment or the derivative segment before – - the date he designates his existing demat account for the purpose of availing the benefit under the Scheme; or - the first day of the initial year.	} whichever is later } whichever is later						
		Initial year means - (a) the financial year in which the investor designates his demat account as Rajiv Gandhi Equity Savings Scheme account and makes investment in the eligible securities for availing deduction under the Scheme; or					

		(b) the financial year in which the investor makes investment in eligible securities for availing deduction under the Scheme for the first time, if the investor does not make any investment in eligible securities in the financial year in which the account is so designated.
2.	Procedure for investment under the Scheme	A new retail investor shall make investments under the Scheme in the following manner, namely:- 1. the new retail investor may invest in one or more financial years in a block of three consecutive financial years beginning with the initial year; 2. the new retail investor may make investment in eligible securities in one or more than one transaction during any financial year during the three consecutive financial years beginning with the initial year in which the deduction has to be claimed; 3. the new retail investor may make any amount of investment in the demat account but the amount eligible for deduction under the Scheme shall not exceed fifty thousand rupees in a financial year; 4. the new retail investor shall be eligible for the tax benefit under the Scheme only for three consecutive financial years beginning with the initial year, in respect of the investment made in each financial year; 5. if the new retail investor does not invest in any financial year following the initial year, he may invest in the subsequent financial year, within the three consecutive financial years beginning with the initial year, in accordance with the Scheme; 6. the new retail investor who has claimed a deduction under sub-section (1) of section 80CCG of the Act in any assessment year shall not be allowed any deduction under the Scheme for the same investment for any other assessment year; 7. the new retail investor shall be permitted a grace period of seven trading days from the end of the financial year so that the eligible securities purchased on the last trading day of the financial year also get credited in the demat account and such securities shall be deemed to have been acquired in the financial year itself; 8. the new retail investor can make investments in securities other than the eligible securities covered under the Scheme and such investments shall not be subject to the conditions of the Scheme nor shall they be counted for availing the benefit under the Scheme;

		9. the deduction claimed shall be withdrawn if the lock-in period requirements of the investment are not complied with or any other condition of the Scheme is contravened by the new retail investor.									
3.	Period of holding	The period of holding of eligible securities invested in each financial year shall be under a lock-in period of three years to be counted in the following manner: <table> <tr> <th>Type of lock-in</th><th>Meaning</th><th>Condition</th></tr> <tr> <td>Fixed lock-in period</td><td>The period commencing from the date of purchase of eligible securities in the relevant financial year and ending on 31st March of the year immediately following the relevant financial year.</td><td>The new retail investor shall hold eligible securities for fixed lock-in period. He shall not be permitted to sell, pledge or hypothecate any eligible security during the fixed lock-in period.</td></tr> <tr> <td>Flexible lock-in period</td><td>The period of two years beginning immediately after the end of the fixed lock-in period shall be called the flexible lock-in period.</td><td> The new retail investor shall be permitted to trade the eligible securities after the completion of the fixed lock-in period subject to the conditions prescribed under the scheme. The demat account should be compliant for a cumulative period of a minimum of 270 days during each of the two years of the flexible lock-in period. The demat account shall be considered as compliant for the number of days for which the value of the investment portfolio of eligible securities (other than those which are in fixed lock-in) is equal to or higher than the corresponding investment claimed as eligible for the purpose of deduction under section 80CCG. </td></tr> </table>	Type of lock-in	Meaning	Condition	Fixed lock-in period	The period commencing from the date of purchase of eligible securities in the relevant financial year and ending on 31st March of the year immediately following the relevant financial year.	The new retail investor shall hold eligible securities for fixed lock-in period. He shall not be permitted to sell, pledge or hypothecate any eligible security during the fixed lock-in period.	Flexible lock-in period	The period of two years beginning immediately after the end of the fixed lock-in period shall be called the flexible lock-in period.	The new retail investor shall be permitted to trade the eligible securities after the completion of the fixed lock-in period subject to the conditions prescribed under the scheme. The demat account should be compliant for a cumulative period of a minimum of 270 days during each of the two years of the flexible lock-in period. The demat account shall be considered as compliant for the number of days for which the value of the investment portfolio of eligible securities (other than those which are in fixed lock-in) is equal to or higher than the corresponding investment claimed as eligible for the purpose of deduction under section 80CCG.
Type of lock-in	Meaning	Condition									
Fixed lock-in period	The period commencing from the date of purchase of eligible securities in the relevant financial year and ending on 31st March of the year immediately following the relevant financial year.	The new retail investor shall hold eligible securities for fixed lock-in period. He shall not be permitted to sell, pledge or hypothecate any eligible security during the fixed lock-in period.									
Flexible lock-in period	The period of two years beginning immediately after the end of the fixed lock-in period shall be called the flexible lock-in period.	The new retail investor shall be permitted to trade the eligible securities after the completion of the fixed lock-in period subject to the conditions prescribed under the scheme. The demat account should be compliant for a cumulative period of a minimum of 270 days during each of the two years of the flexible lock-in period. The demat account shall be considered as compliant for the number of days for which the value of the investment portfolio of eligible securities (other than those which are in fixed lock-in) is equal to or higher than the corresponding investment claimed as eligible for the purpose of deduction under section 80CCG.									

4.	Other Conditions	(i) While making initial investments up to Rs.50,000, the total cost of acquisition of eligible securities shall not include brokerage charges, securities transaction tax, stamp duty, service tax and any other tax, which may appear in the contract note. (ii) Where the investment of the new retail investor undergoes a change as a result of involuntary corporate actions including demerger of companies, amalgamation and such other actions, as may be notified by SEBI, resulting in debit or credit of securities covered under the Scheme, the deduction claimed by such investor shall not be affected. (iii) In the case of voluntary corporate actions, including buy-back resulting only in debit of securities where new retail investor has the option to exercise his choice, the same shall be considered as a sale transaction for the purpose of the Scheme.
5.	Consequence of failure to comply with the prescribed conditions	If the new retail investor fails to fulfill any of the provisions of the Scheme, the deduction originally allowed to him under section 80CCG(1) for any previous year, shall be deemed to be the income of the assessee of the previous year in which he fails to comply with the provisions of the Scheme and shall be liable to tax for the assessment year relevant to such previous year.
6.	Savings	A new retail investor who has invested in accordance with the Rajiv Gandhi Equity Savings Scheme, 2012 shall continue to be governed by the provisions of that Scheme to the extent it is not in contravention of the provisions of this Scheme and such investor shall also be eligible for the benefit of investment made in accordance with this Scheme for the financial years 2013-14 and 2014-15.

13. Notification No.6/2014 dated 15.01.2014

Contributory Health Service Scheme of the Department of Space notified under section 80D

Section 80D(2)(a) provides for deduction in respect of medical insurance premium paid or for contribution made by an individual to the Central Government Health Scheme **or such other scheme as may be notified by the Central Government.** Accordingly, the Central Government has notified the Contributory Health Service Scheme of the Department of Space, contribution to which would be eligible for deduction under section 80D.

Therefore, any contribution made by an individual towards the Contributory Health Service Scheme of the Department of Space would be eligible for deduction under section 80D, subject to the overall limit of Rs.15,000 or Rs. 20,000, as the case may be.

14. Notification No. 9/2014 dated 22.01.2014**Foreign Institutional Investors notified as per section 115AD**

Section 115AD contains the special provisions for taxation of income of foreign institutional investors (FIIs) from securities or capital gains arising from transfer of securities. As per clause (a) of *Explanation* to section 115AD, the expression “Foreign Institutional Investor” means such investor as the Central Government may, by notification in the Official Gazette, specify in this behalf.

Accordingly, the Central Government has specified Foreign Portfolio Investors (FPIs) registered under the Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2014, as FII for the purposes of section 115AD. Hence, the special provisions for taxation of income of FIIs from securities and capital gains arising from transfer of securities, as contained in section 115AD, would apply to such income of Foreign Portfolio Investors registered under SEBI (FPI) Regulations, 2014.

15. Notification No. 24/2014 dated 01.04.2014**Notification of Income-tax Return Forms for the AY 2014-15**

Rule 12 of Income-tax Rules, 1962 prescribing income-tax return forms applicable in respect of different categories of persons has been amended to make the same applicable for assessment year 2014-15. Further, new income-tax return forms – SAHAJ (ITR-1), ITR-2, SUGAM (ITR-4S) and ITR-V for the Assessment year 2014-15 have been substituted in the place of the existing return forms. However, there are no changes in the applicability of return forms.

Applicability of income-tax return forms to various categories of persons [Rule 12(1)]

Form No.	Applicability
ITR-1 SAHAJ	A person, being an individual, whose has - (a) Income under the head “Salaries” or family pension; (b) Income from One House Property (excluding cases where loss is brought forward from previous years); or (c) Income from Other Sources (excluding Winnings from Lottery and Income from Race Horses). He should, however, not have any loss under this head. However, the following persons cannot file their return in Form ITR-1, even if they have only income falling under the above categories – (1) A resident, other than not-ordinarily resident in India, who has an asset (including financial interest in any entity) located outside India or signing authority in any account located outside India; or

	(2) A person who has claimed any relief under section 90 or 90A or deduction under section 91; or (3) A person who has income not chargeable to tax, exceeding Rs.5,000.
ITR-2	A person, being an individual (not being an individual eligible to file return in ITR-1) or HUF, not having income from business or profession.
ITR-3	A person, being an individual or a HUF, who is a partner in a firm and whose income chargeable under the head "Profits and gains of business or profession" includes only income by way of interest, salary, bonus, commission or remuneration due to or received by him from such firm.
ITR-4S SUGAM	A person, being an individual or a HUF, deriving business income and such income is computed in accordance with special provisions referred to in section 44AD and 44AE. However, the following persons cannot file their return in Form ITR-4S, even if they have only business income computed as per the provisions of section 44AD or section 44AE – (1) A resident, other than not-ordinarily resident in India, who has an asset (including financial interest in any entity) located outside India or signing authority in any account located outside India; or (2) A person who has claimed any relief under section 90 or 90A or deduction under section 91; or (3) A person who has income not chargeable to tax, exceeding Rs.5,000.
ITR-4	A person, being an individual or HUF, other than those to whom ITR-1, ITR-2, ITR-3 and ITR-4S are applicable, and having income from a proprietary business or profession.
ITR-5	A person, not being an individual or a HUF or a company or a person who is required to file return in Form ITR-7. In effect, ITR-5 is applicable in case of a firm, LLP, AOP, BOI, artificial juridical person referred to in section 2(31)(vii), co-operative society and local authority. However, persons required to file return in Form ITR-7 cannot use this form.
ITR-6	A company, other than a company claiming exemption under section 11. A company required to file its return in Form ITR-7, therefore, cannot use this form.
ITR-7	A person, including a company, whether or not registered under section 25 of the Companies Act, 1956, required to furnish return under section 139(4A) or section 139(4B) or section 139(4C) or section 139(4D)
ITR V	Verification of return filed electronically without digital signature or in paper form or in bar-coded form.

Filing of annexure-less return [Rule 12(2)]

The return forms (ITR-1, ITR-2, ITR-3, ITR-4, ITR-4S, ITR-5 & ITR-6) shall not be accompanied by any annexure such as statement showing the computation of tax, TDS certificates, challan etc.. However, where an assessee is required to furnish a report of audit under section 44AB, 92E, or 115JB, the same shall be furnished electronically. ***Likewise, the notice in writing given to the Assessing Officer under section 11(2)(a) mentioning the purpose for which the income is being accumulated or set apart by a charitable trust/institution and the period thereof, is also required to be furnished electronically.***

Manner of filing return of income [Rule 12(3)]

The return of income may be furnished in any of the following manners:

- (i) in paper form; or
- (ii) electronically under digital signature; or
- (iii) electronically without digital signature [followed by submission of the verification of the return in Form ITR-V]; or
- (iv) bar coded return in paper form

The following persons are required to furnish the return of income electronically, but have the option to furnish the same with or without digital signature, for A.Y.2014-15:

- (i) A person, other than a company and persons required to furnish the return in Form ITR-7, whose total income exceeds Rs.5 lakh.
- (ii) An individual or HUF, being a resident other than not-ordinarily resident in India, having assets (including financial interest in any entity) located outside India or signing authority in any account located outside India and required to furnish the return in Form ITR-2, ITR-3 or ITR-4.
- (iii) A person claiming relief of tax under section 90 or 90A or deduction of tax under section 91.
- (iv) A person required to furnish return in ITR-5, other than a firm to which provisions of section 44AB are applicable.***
- (v) A person, other than political party referred to in section 139(4B), required to furnish the return in Form ITR -7. Such person also has the option to furnish return in paper form.

The following persons are required to furnish the return of income electronically under digital signature:

- (i) a company required to furnish its return in ITR-6;

- (ii) a firm required to furnish return in ITR-5 or an individual or HUF required to furnish return in ITR 4 and to whom the provisions of section 44AB are applicable;

(iii) a political party referred to in section 139(4B), required to furnish return in ITR 7.

Note – The portion marked in **bold italics** above represent the changes/additions made by Notification No.24/2014 dated 1.4.2014.

II. CIRCULARS

1. Circular No.06/2013 dated 29.6.2013

Clarifications on Functional Profile of Development Centres engaged in contract R&D Services with insignificant risk – Conditions relevant to identify such Development Centres

There exists divergent views amongst the field officers and taxpayers regarding the functional profile of development centres engaged in contract R & D services for the purposes of determining arm's length price/transfer pricing. In some cases, while taxpayers insist that they are contract R & D service providers with insignificant risk, the TPOs treat them as full or significant risk-bearing entities and make transfer pricing adjustments accordingly.

The CBDT has, vide this Circular, addressed this issue by classifying the Research and Development Centres set up by foreign companies into three broad categories based on functions, assets and risk assumed by the centre established in India. While the three categories are not water-tight compartments, it is possible to distinguish them based on functions, assets and risk, as shown hereunder -

	Categories of R&D Centres	Nature of functions performed and level of risks assumed by the corresponding category of the Development Centre
(1)	Centres which are entrepreneurial in nature	Performs significantly important functions and assumes substantial risks
(2)	Centres which are based on cost-sharing arrangements	Performs functions which are of relatively lesser significance and assumes moderate risks.
(3)	Centres which undertake contract research and development	Performs functions which are of low significance and assumes minimal risks

The assessees, largely, tend to claim that the Development Centre in India is a contract R&D service provider with insignificant risk, and consequently, adopt the Transactional Net Margin Method (TNMM) as the most appropriate method.

The CBDT, after due consideration, has laid down the following guidelines for identifying the Development Centre as a contract R & D service provider with insignificant risk –

	Foreign Principal	Indian Development Centre	Remark
(1)	Performs most of the economically significant functions involved in research or product development cycle either through its own employees or through its associated enterprises.	Carries out the work assigned to it by the foreign principal.	Economically significant functions would include critical functions such as conceptualization and design of the product and providing the strategic direction and framework.
(2)	Provides funds/ capital and other economically significant assets including intangibles for research or product development. Provides remuneration to the Indian Development Centre for the work carried out by the latter.	Does not assume or has no economically significant realized risks	If a contract shows that the foreign principal is obligated to control the risk but the conduct shows that the Indian Development Centre is doing so, then the contractual terms are not the final determinant of actual activities.
(3)	Has not only the capability to control or supervise but also actually controls or supervises research or product development through its strategic decisions to perform core functions as well as monitor activities on regular basis.	Works under the direct supervision of the foreign principal or its associated enterprise	
(4)	Has ownership right on the outcome of the research	Has no ownership right (legal or economic) on the outcome of the research	This fact should be evident from the contract as well as from the conduct of the parties.

In the case of a foreign principal being located in a country/territory widely perceived as a low or no tax jurisdiction, it will be presumed that the foreign principal is not controlling the risk. However, the Indian Development Centre may rebut this presumption to the satisfaction of the revenue authorities. Low tax jurisdiction shall mean any country or

territory notified in this behalf under section 94A of the Act or any other country or territory that may be notified for the purpose of Chapter X of the Act;

The Assessing Officer or the Transfer Pricing Officer, as the case may be, shall have regard to the guidelines above and shall take a decision based on the totality of the facts and circumstances of the case. In doing so, the Assessing Officer or the Transfer Pricing Officer, as the case may be, shall be guided by the conduct of the parties and not merely by the terms of the contract.

The Assessing Officer or the Transfer Pricing Officer, as the case may be, shall bear in mind the provisions of section 92C of the Income-tax Act, 1961 and Rule 10A to Rule 10C of the Income-tax Rules, 1962. He has to apply the guidelines laid down in the Circular and select the 'most appropriate method'.

2. Circular No.05/2013 dated 29.06.2013

Withdrawal of Circular No.2/2013, dated 26-3-2013 on application of Profit Split Method for computation of Arm's Length Price

The Circular No. 2/2013 listed the factors to be taken into account for selection and application of the profit split method as the most appropriate method for computation of arm's length price.

Since the Circular appeared to give the impression that there was a hierarchy among the six methods listed in section 92C and that Profit Split Method (PSM) was the preferred method in the case involving unique intangible or in multiple interrelated international transactions, the CBDT has, consequently, withdrawn the said Circular (i.e., Circular No. 2/2013 dated 26th March 2013), with immediate effect.

3. Circular No.10/2013, dated 16.12.2013

Disallowance of interest etc. paid to a resident at any time during the previous year without deduction of tax under section 40(a)(ia)

Section 40(a)(ia) provides for disallowance of any interest, commission or brokerage, rent, royalty, fees for professional services or fees for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in section 139(1).

There have been conflicting interpretations by judicial authorities regarding the applicability of provisions of section 40(a)(ia), with regard to the amount not deductible in computing the income chargeable under the head 'Profits and gains of business or profession'. Some court rulings have held that the provisions of disallowance under section 40(a)(ia) apply only to the amount which remained payable at the end of the relevant financial year and would not be invoked to disallow the amount which had actually been paid during the previous year without deduction of tax at source.

Departmental View: The CBDT's view is that the provisions of section 40(a)(ia) would cover not only the amounts which are payable as on 31st March of a previous year but also amounts which are payable at any time during the year. The statutory provisions are amply clear and in the context of section 40(a)(ia), the term "payable" would include "amounts which are paid during the previous year".

The Circular has further clarified that where any High Court decides an issue contrary to the above "Departmental View", the "Departmental View" shall not be operative in the area falling in the jurisdiction of the relevant High Court.

4. Circular No. 1/2014, dated 13.1.2014

Non-deduction of tax at source on the service tax component comprised in payments made to residents, if the service-tax component is indicated separately

The CBDT had issued Circular No.4/2008 dated 28.4.2008 clarifying that tax is to be deducted at source under section 194-I, on the amount of rent paid/payable without including the service tax component. However, this Circular was silent regarding deduction of tax at source on the service tax component of other payments on which TDS provisions are applicable.

Accordingly, in exercise of the powers conferred under section 119, the Board has, vide this Circular, clarified that wherever in terms of the agreement/contract between the payer and the payee, the service tax component comprised in the amount payable to a resident is indicated separately, tax shall be deducted at source under Chapter XVII-B on the amount paid/payable without including such service tax component.

5. Circular No. 2/2014 dated 20.01.2014

Taxability of Awards received by a Sportsman

The CBDT had issued Circular No.447 on 22nd January, 1986 clarifying that awards received by a sportsman, who is not a professional, will not be liable to tax in his hands as the award will be in the nature of a gift and/or personal testimonial. This Circular was applicable when the gift was not taxable in the hands of the recipient. Thereafter, in the year 2005, there was a fundamental change in the manner of treatment of gift through insertion of sub-clauses (xiii), (xiv) and (xv) of section 2(24). Corresponding amendments were also made in section 56(2) by insertion of clauses (v), (vi) and (vii), thereby making an amount of money or immovable property received without consideration taxable subject to provisions of these clauses. Consequently, the CBDT has, through this Circular, clarified that *Circular No.447* had become inapplicable w.e.f. 1-4-2005, since the statutory provisions have overridden the same.

It may however be noted that, in terms of provisions of section 10(17A), Central Government approves awards instituted by Central Government, State Government or other bodies as also the purposes for rewards instituted by Central Government or State

Government from time to time. Tax exemption can be sought by eligible persons in respect of awards or rewards covered by such approvals.

6. Circular No. 5/2014, dated 11.2.2014

Clarification regarding disallowance of expenses under section 14A in cases where corresponding exempt income has not been earned during the financial year

The Finance Act, 2001 had introduced section 14A, with retrospective effect from 1st April, 1962, to provide that no deduction shall be allowed in respect of expenditure incurred relating to income which does not form part of total income. A controversy has arisen as to whether disallowance can be made by invoking section 14A even in those cases where no income has been earned by an assessee, which has been claimed as exempt during the financial year.

The CBDT has, through this Circular, clarified that the legislative intent is to allow only that expenditure which is relatable to earning of income. Therefore, it follows that the expenses which are relatable to earning of exempt income have to be considered for disallowance, irrespective of the fact whether such income has been earned during the financial year or not.

The above position is clarified by the usage of the term “includible” in the heading to section 14A [Expenditure incurred in relation to income not includible in total income] and Rule 8D [Method for determining amount of expenditure in relation to income not includible in total income], which indicates that it is not necessary that exempt income should necessarily be included in a particular year’s income, for triggering disallowance. Also, the terminology used in section 14A is “income under the Act” and not “income of the year”, which again indicates that it is not material that the assessee should have earned such income during the financial year under consideration.

In effect, section 14A read along with Rule 8D provides for disallowance of expenditure even where the taxpayer has not earned any exempt income in a particular year.

7. Circular No. 6/2014, dated 11.2.2014

Clarification regarding scope of additional income-tax on distributed income under section 115R

Section 115R provides for levy of additional tax on distributed income to unit holders. Some Assessing Officers have taken a view that mutual funds/specified companies are required to pay additional income-tax under section 115R not only on income distributed by way of dividend but also on payments made at the time of redemption/repurchase of units as well as at the time of allotment of bonus units to existing investors.

On these issues, the CBDT has clarified the following –

- (i) Section 115R(2) requires payment of additional income-tax at the rates prescribed thereunder in respect of any amount distributed by a specified company or a mutual fund to its unit holders. The income so distributed by such entities constitutes dividend paid to the unit holders and is liable to tax thereunder. However, **redemption of units or repurchase of units would not attract levy of tax under**

section 115R(2) as such income is not in the nature of income “distributed” to the unit holders and hence, lies outside the purview of this section.

- (ii) Further, the income so distributed by the mutual fund or the specified company is specifically exempt from tax under section 10(35) in the hands of the recipient unit holders. As per the proviso to section 10(35), exemption of income thereunder is not applicable to those cases where transfer of units take place. The recipient of income is, therefore, liable to pay capital gains tax, if applicable, as per the relevant provisions of the Act, on transfer of such units.
- (iii) Also, since issue of bonus units is not akin to distribution of income by way of dividend, the same would not be subject to additional income tax under section 115R. This inference can be drawn from the provisions of section 55, prescribing “cost of acquisition” of bonus shares as Nil for the purposes of computation of capital gains tax.

Thus, in view of the above position, the CBDT has, in exercise of its powers under section 119, clarified that additional income-tax under section 115R(2) is to be levied on income distributed by way of dividend to unit-holders of mutual fund or specified companies. Further, it is specifically clarified that receipts from redemption/repurchase of units or allotment of additional units by way of bonus units would **not** be subject to levy of additional income-tax thereunder.

8. Circular No. 8/2014 dated 31.03.2014

Taxability of partner's share, where the income of the firm is exempt under Chapter III / deductible under Chapter VI-A

Section 10(2A) provides that a partner's share in the total income of a firm which is separately assessed as such shall not be included in computing the total income of the partner. In effect, a partner's share of profits in such firm is exempt from tax in his hands.

Sub-section (2A) was inserted in section 10 by the Finance Act, 1992 with effect from 1.4.1993 consequent to change in the scheme of taxation of partnership firms. Since A.Y.1993-94, a firm is assessed as such and is liable to pay tax on its total income. A partner is, therefore, not liable to tax once again on his share in the said total income.

An issue has arisen as to the amount which would be exempt in the hands of the partners of a partnership firm, in cases where the firm has claimed exemption/deduction under Chapter III or Chapter VI-A.

The CBDT has clarified that the income of a firm is to be taxed in the hands of the firm only and the same can under no circumstances be taxed in the hands of its partners. Therefore, the entire profit credited to the partners' accounts in the firm would be exempt from tax in the hands of such partners, even if the income chargeable to tax becomes Nil

in the hands of the firm on account of any exemption or deduction available under the provisions of the Act.

9. Circular No. 09/2014, dated 23.04.2014

Clarification regarding treatment of expenditure incurred for development of roads/highways in Build-Operate-Transfer (BOT) agreements under the Income-tax Act, 1961

The CBDT has, vide this Circular, clarified the tax treatment of expenditure incurred on development and construction of infrastructural facilities like roads/highways on Build-Operate-Transfer (BOT) basis with right to collect toll - whether the same is entitled to depreciation under section 32(1)(ii) or can be amortized by treating it as an allowable business expenditure under the relevant provisions of the Income- tax Act, 1961.

Generally, the BOT basis projects are entered into between the developer and the government or the notified authority, on the following terms:

- (i) In such projects, the developer, in terms of concessionaire agreement with Government or its agencies, is required to construct, develop and maintain the infrastructural facility of roads/highways which, *inter alia*, includes laying of road, bridges, highways, approach roads, culverts, public amenities etc. at its own cost and its utilization thereof for a specified period.
- (ii) The possession of land is handed over to the assessee (i.e., the developer) by the Government/ notified authority for the purpose of construction of the project without any actual transfer of ownership. The assessee, therefore, has only a right to develop and maintain such asset. It also enjoys the benefits arising from the use of asset through collection of toll for a specified period, without having actual ownership over such asset. Therefore, the rights in the land remain vested with the Government/notified agencies.
- (iii) Since the assessee does not hold any rights in the project except recovery of toll fee to recoup the expenditure incurred, it cannot be treated as an owner of the property, either wholly or partly, for purposes of allowability of depreciation under section 32(1)(ii). Thus, claim of depreciation on tollways is not allowable due to non-fulfillment of ownership criteria in such cases.
- (iv) Where the assessee incurs expenditure on a project for development of roads/highways, it is entitled to recover cost incurred towards development of such facility (comprising of construction cost and other pre-operative expenses) during construction period. Further, expenditure incurred by the assessee on such BOT projects brings to it an enduring benefit in the form of right to collect the toll during the period of agreement.

The Supreme Court, in *Madras Industrial Investment Corporation Ltd. vs. CIT* 225 ITR 802, allowed the spreading over of liability over a number of years on the ground that there was continuing benefit to the company over a period. Therefore, analogously, expenditure incurred on an infrastructure project for development of roads/highways under BOT agreement may be treated as having been made/incurred for the purposes of

business or profession of the assessee and same shall be allowed to be spread during the tenure of concessionaire agreement.

In view of the above, the CBDT, in exercise of the powers conferred under section 119, clarifies that the cost of construction on development of infrastructure facility, being roads/highways under BOT projects, may be amortized and claimed as allowable business expenditure under the Act in the following manner:

- (i) The amortization allowable may be computed at the rate which ensures that the whole of the cost incurred in creation of infrastructural facility of road/highway is amortised evenly over the period of concessionaire agreement after excluding the time taken for creation of such facility.
- (ii) Where an assessee has claimed any deduction out of initial cost of development of infrastructure facility of roads/highways under BOT projects in earlier years, the total deduction so claimed for the assessment years prior to assessment year under consideration may be deducted from the initial cost of infrastructure facility of roads/highways and the cost so reduced shall be amortised equally over the remaining period of toll concessionaire agreement.

The clarification given in this Circular is applicable only to those infrastructure projects for development of road/highways on BOT basis where ownership is not vested with the assessee under the concessionaire agreement.

Part II : Judicial Update – Direct Tax Laws

Significant Legal Decisions

Basic Concepts

1. Can waiver of loan or advance taken for the purpose of relocation of office premises be treated as a revenue receipt liable to tax?

CIT v. Softworks Computers P. Ltd. (2013) 354 ITR 16 (Bom.)

Facts of the case:

In the present case, the assessee-company worked as a dedicated software development centre for Speedwing British Airways (Speedwing BA). It provided transaction processing facilities and airline control system services to Speedwing BA. The assessee-company was located in the same premises as that of Speedwing BA. As a matter of arrangement, it was decided that the assessee-company should relocate itself to an independent location, for which purpose, Speedwing BA provided an advance of one lakh pounds to the assessee-company. Later, Amadeus Global Travel stepped into the shoes of Speedwing BA and assumed its rights and liabilities. Consequently, a new agreement was signed between the assessee-company and Amadeus Global Travel which, *inter alia*, relieved the assessee-company of its liability to repay the advance of one lakh pounds.

Assessee's view vs. Assessing Officer's view:

The assessee-company claimed that such waiver, being capital in nature, was not taxable and hence, did not include the same while computing its taxable income. The Assessing Officer, however, opined that such waiver of loan was a revenue receipt, and so he added the same to the income of the assessee-company.

High Court's decision:

On appeal, the Bombay High Court held that since the advance taken by the assessee-company was utilized by it for the purpose of relocating its office premises i.e., for acquisition of a capital asset, namely, a new office, the waiver of the same cannot be said to be waiver or remission of trading liability to attract taxability under the Act. Waiver of such advance, being capital in nature, is not taxable under the Act.

2. What is the nature of grant received by a subsidiary company from its holding company to recoup the losses incurred year after year and to enable it to meet its liabilities - Capital or Revenue?

CIT v. Handicrafts and Handlooms Export Corporation of India Ltd. (2014) 360 ITR 0130 (Delhi)

Facts of the case:

The assessee, a Government company, operates a channelising agency for sale of handicrafts and handlooms abroad. In the relevant previous year, it received a grant of ₹

25 lakh from its holding company, the State Trading Corporation of India (STC). The Assessing Officer opined that the said amount was a revenue receipt chargeable to tax.

Tribunal's view:

The Appellate Tribunal held that the grant received was not taxable as revenue receipt since the said grant was given to recoup the losses incurred by the assessee and was hence, in the nature of capital contribution.

High Court's Observations:

The High Court examined the judgment of the Supreme Court in *Sahney Steel and Press Works Ltd. v. CIT* (1997) 228 ITR 253, which laid down the test for determining whether subsidy received by an assessee is taxable as capital or revenue receipt. As per the said test, if any subsidy is given, the character of the subsidy in the hands of the recipient - whether revenue or capital - will have to be determined by having regard to the purpose for which the subsidy is given. The point of time, the source and the form of subsidy are immaterial. The object for which the subsidy is given, would, thus determine the nature of subsidy. If it is given by way of assistance to the assessee in carrying on of his trade or business, it has to be treated as trading receipt.

The High Court observed that, in this case, ₹ 25 lakhs was not paid by a third party or by a public authority but by the holding company. It was not on account of any trade or commercial transaction between the subsidiary and holding company. The intention and purpose behind the said payment was to secure and protect the capital investment made by STC Ltd. The payment of grant by STC Ltd. and receipt thereof by the assessee was not during the course of trade or performance of trade, and thus, could not partake the character of a trading receipt. The same was in the nature of a capital grant.

The High Court observed the difference between Government Grant and payment made by STC, as pointed out by the Division Bench in *Handicrafts and Handlooms Corporation Ltd. v. CIT* (1983) 140 ITR 532. The grants given were specific amounts paid by STC to the assessee, in order to enable the assessee, which was its subsidiary and was incurring losses year after year, to recoup these losses and to enable it to meet its liabilities. These amounts, therefore, cannot form part of the trading receipts of the assessee since these were not in the nature of grants received from an outsider or the Government on general grounds such as for carrying on of trade.

High Court's Decision:

The High Court, in this case, observed that in all the years, it was the case of a 100% holding company coming to the rescue of its subsidiary. Applying the rationale of Apex Court decision in the case of *Sahney Steel [1997] 228 ITR 253 (SC)*, which requires the nature of subsidy to be decided on the basis for which the subsidy was given, the High Court held that grant given by the holding company in this case is in the nature of capital receipt since its purpose is to secure and protect the capital investment made in the subsidiary company.

Incomes which do not form part of total income

3. In a case where the application for registration of a charitable trust is not disposed of within the period of 6 months as required under section 12AA(2), can the trust be deemed to have been registered as per provisions of section 12AA?

CIT v. Karimangalam Onriya Pengal Semipu Amaipu Ltd. (2013) 354 ITR 483 (Mad)

High Court's Observations:

On this issue, the Madras High Court observed that as per the provisions of section 12AA(2), every order granting or refusing registration under section 12AA(1)(b), **shall** be passed by the registering authority before the expiry of six months from the end of the month in which the application was received under section 12A(1)(a) or section 12A(1)(aa).

The Madras High Court observed the decision of the Orissa High Court, in *Srikhetra, A.C. Bhakti-Vedanta Swami Charitable Trust v. ACIT (2006) (II) OLR 75*, wherein it was held that the period of six months as provided under section 12AA(2) is not mandatory. In that case, the Orissa High Court observed that in order to ascertain whether a provision is mandatory or not, the expression 'shall' is not always decisive. The nature of the statutory provision, whether mandatory or directory, has to be ascertained not only from the wording of the statute, but also from the nature and design of the statute and the purpose sought to be achieved. Further, since the consequence for non-adherence of the time limit of six months is not spelt out in the statute, it cannot be said that passing the order within such time limit is mandatory in nature. The Orissa High Court also opined that in the absence of any clear statutory intent to the contrary, when public duty is to be performed by the public authorities, the time-limit which is granted by the statute is normally directory and not mandatory. Hence, though the word 'shall' has been used in section 12AA(2), the period of six months provided thereunder is not mandatory but directory in nature.

High Court's decision:

Accordingly, in the present case, the Madras High Court held that the time frame mentioned in section 12AA(2) is only directory in nature and non-consideration of the registration application within the said time frame of six months would not amount to "deemed registration".

Note - Similar ruling was pronounced by the Madras High Court in the case of *CIT v. Sheela Christian Charitable Trust (2013) 354 ITR 478*, holding that there is no automatic or deemed registration if the application filed under section 12AA was not disposed of within the stipulated period of six months.

4. Where a charitable trust applied for issuance of registration under section 12A within a short time span (nine months, in this case) after its formation, can registration be denied by the concerned authority on the ground that no charitable activity has been commenced by the trust?

DIT (Exemptions) v. Meenakshi Amma Endowment Trust (2013) 354 ITR 219 (Kar.)

Facts of the case:

In the present case, the assessee, being a trust, made an application under section 12A for issuance of registration within nine months of its formation. The registration authority issued a show cause notice to the assessee-trust to furnish its audited accounts as also material indicating the actual activities undertaken by the trust. In response to the said notice, the assessee-trust furnished the details, wherein it indicated that it has not yet commenced any charitable activity. The concerned registration authority, not being satisfied with the reply, refused to grant registration to the trust on the ground that it has not commenced any charitable activity.

Issue:

The issue under consideration is whether registration under section 12AA can be denied on the ground of non-commencement of charitable activity, where an application for registration has been made within a short-time span after the formation of the trust.

High Court's observations:

On this issue, the Karnataka High Court opined that an application under section 12A for registration of the trust can be sought even within a week of its formation. The activities carried on by the trust are to be seen in case the registration is sought much later after formation of the trust.

The High Court further observed that, in this case, the corpus fund included contribution made by the trustees only, which indicated that the trustees were contributing the funds by themselves in a humble way and were intending to commence charitable activities. Also, it was not the Revenue's contention that the assessee-trust had collected lots of donations for the activities of the trust, by the time its application came up for consideration before them. When the application for registration was made, the trust, therefore, did not have sufficient funds for commencement of its activities.

High Court's decision:

The High Court observed that, with the money available with the trust, it cannot be expected to carry out activity of charity immediately. Consequently, in such a case, it cannot be concluded that the trust has not intended to do any activity of charity. In such a situation, the objects of the trust as mentioned in the trust deed have to be taken into consideration by the authorities for satisfying themselves about the genuineness of the trust and not the activities carried on by it. Later on, if it is found from the subsequent returns filed by the trust, that it is not carrying on any charitable activity, it would be open to the concerned authorities to withdraw the registration granted or cancel the registration as per the provisions of section 12AA(3).

Income from house property

5. Whether the rental income derived from the unsold flats which are shown as stock-in-trade in the books of the assessee would be taxable under the head 'Profits and gains from business and profession' or under the head 'Income from house

property', where the actual rent receipts formed the basis of computation of income?

New Delhi Hotels Ltd. v. ACIT (2014) 360 ITR 0187 (Delhi)

On this issue, in *CIT v. Ansal Housing Finance and Leasing Co. Ltd.* (2013) 354 ITR 180, where the deemed rent (i.e., annual letting value) formed the basis of computation of income from unsold flats held as stock-in-trade, the Delhi High Court held that such rent was taxable under the head "Income from house property". Further, in *CIT v. Discovery Estates Pvt. Ltd.* and *CIT v. Discovery Holding Pvt. Ltd.* (2013) 356 ITR 159, the same issue emerged when the actual rent formed the basis of computation of income from unsold flats held as stock-in-trade. In that case also, the Delhi High Court held that the income was taxable under the head "Income from house property".

High Court's Decision:

In this case, the Delhi High Court followed its own decision in the case of *CIT vs. Discovery Estates Pvt. Ltd / CIT vs. Discovery Holding Pvt. Ltd.*, wherein it was held that rental income derived from unsold flats which were shown as stock-in-trade in the books of the assessee should be assessed under the head "Income from house property" and not under the head "Profits and gains from business and profession".

Note – In effect, irrespective of whether it is the deemed rent or actual rent which forms the basis of computing income from unsold flats held as stock-in-trade, the head under which the income is taxable would be "Income from house property".

Profits and Gains of Business or Profession

6. Is ***Circular No. 5/2012 dated 01.08.2012*** disallowing the expenditure incurred on freebies provided by pharmaceutical companies to medical practitioners, in line with ***Explanation to section 37(1)***, which disallows expenditure which is prohibited by law?

Confederation of Indian Pharmaceutical Industry (SSI) v. CBDT (2013) 353 ITR 388 (H.P.)

High Court's observations:

On this issue, the Himachal Pradesh High Court observed that as per Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002, every medical practitioner and his or her professional associate is prohibited from accepting any gift, travel facility, hospitality, cash or monetary grant from any pharmaceutical and allied health sector industries. This is a salutary regulation in the interest of the patients and the public, considering the increase in complaints against the medical practitioners prescribing branded medicines instead of generic medicines, solely in lieu of gifts and other freebies granted to them by some particular pharmaceutical industries.

The CBDT, considering the fact that the claim of any expense incurred in providing freebies to medical practitioners is in violation of the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002, has, *vide Circular*

No.5/2012 dated 1.8.2012, clarified that the expenditure so incurred shall be inadmissible under section 37(1). The disallowance shall be made in the hands of such pharmaceutical or allied health sector industry or other assessee which has provided aforesaid freebies and claimed it as a deductible expense in its accounts against income.

High Court's decision:

The High Court opined that the contention of the assessee that the above mentioned Circular goes beyond section 37(1) was not acceptable. As per *Explanation* to section 37(1), it is clear that any expenditure incurred by an assessee for any purpose which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession. The sum and substance of the circular is also the same. Therefore, the circular is totally in line with the *Explanation* to section 37(1).

However, if the assessee satisfies the assessing authority that the expenditure incurred is not in violation of the regulations framed by the Medical Council then it may legitimately claim a deduction, but it is for the assessee to satisfy the Assessing Officer that the expense is not in violation of the Medical Council Regulations.

7. **Can the amount of employees' contribution towards provident fund, deducted and credited to the employee's PF account by the employer-assessee after the "due date" under the EPF & Miscellaneous Provisions Act, 1952, but before the due date of filing return of income under the Income-tax Act, 1961, be allowed as deduction while computing business income of the employer-assessee?**

CIT v. Kichha Sugar Co. Ltd. (2013) 356 ITR 351 (Uttarakhand)

High Court's observations:

On this issue, the Uttarakhand High Court observed that the "due date" referred to in section 36(1)(va) must be read in conjunction with the "due date" referred to in the first proviso to section 43B. A combined reading of both the sections would make it clear that the due date referred to in section 36(1)(va) is the due date as mentioned in section 43B i.e., the due date of filing of return of income. Therefore, any amount of employees' contribution paid by the employer-assessee to the provident fund authorities after the due date under the Employees Provident Fund & Miscellaneous Provisions Act, 1952 (EPF & MP Act) but before the due date of filing the return for the previous year, shall be allowable as deduction in the hands of the employer-assessee.

The High Court opined that the Assessing Officer had committed an error in disallowing the said payment on account of delay in depositing the same to the credit of the account of the employee maintained with the provident fund authorities, taking a view that the due date mentioned in section 36(1)(va) is the due date fixed by the provident fund authorities under the EPF & MP Act, without considering the provisions of section 43B. The High Court concurred with the opinion of the previous appellate authority/ies that the amount paid was no longer in the hands of the employer and thus, cannot be taken as income in the hands of the employer-assessee.

High Court's decision:

Therefore, the employees' contribution to provident fund, deducted from the salaries of the employees of the assessee, shall be allowed as deduction from the income of the employer-assessee, if the same is deposited by the employer-assessee with the provident fund authority on or before the due date of filing the return for the previous year.

Note - As per provisions of section 2(24)(x), any sum received by the assessee from his employees as a contribution towards, inter alia, any provident fund, shall be included in the income of the assessee.

Section 36(1)(va) provides for deduction, while computing income under the head 'Profit and gains of business or profession', of any sum received by the assessee from any of its employees to which provisions of section 2(24)(x) apply, provided the same is credited by the assessee to the employee's account in the relevant fund on or before the due date. Explanation to section 36(1)(va) clarifies that the "due date" referred to therein is the date by which the assessee is required as an employer to credit an employee's contribution to the employee's account in the relevant fund (i.e., Provident Fund, in this case) under any Act (i.e., EPF & MP Act, in this case).

Section 43B provides for certain deductions only on actual payment. The first proviso to section 43B permits such payments to be made on or before the due date of filing of return under section 139(1), for the purpose of admissibility of deduction. The payments covered under section 43B include, inter alia, any sum payable by the assessee as an employer by way of contribution to any provident fund.

Thus, whereas section 43B permits payment of employer's contribution to PF on or before the due date of filing of return to qualify for deduction, section 36(1)(va) provides a time limit upto the due date specified under the EPF & MP Act for credit of employee's contribution to the employee's PF account, for claiming deduction under that section.

In this case, the High Court has concluded that the extended time limit upto the due date of filing of return under section 43B is also available for credit of employee's contribution to his PF Account, even though Explanation to section 36(1)(va) requires such payment to be made on or before the due date under the EPF & MP Act to qualify for deduction.¹

8. What is the nature of expenditure incurred on glow-sign boards displayed at dealer outlets - capital or revenue?

CIT v. Orient Ceramics and Industries Ltd. (2013) 358 ITR 49 (Delhi)

¹ Recently, the Gujarat High Court, in CIT v. Gujarat State Road Transport Corporation (2014) 223 Taxmann 398, held that employees contribution to provident fund, deposited by an employer after the due date under the EPF & MP Act but before the due date of filing of return for the relevant assessment year, is not allowable as deduction under section 36(1)(va).

High Court's observations:

On this issue, the Delhi High Court noted the following observations of the Punjab and Haryana High Court in *CIT v. Liberty Group Marketing Division* [2009] 315 ITR 125, while holding that such expenditure was revenue in nature -

- (i) The expenditure incurred by the assessee on glow sign boards does not bring into existence an asset or advantage for the enduring benefit of the business, which is attributable to the capital.
- (ii) The glow sign board is not an asset of permanent nature. It has a short life.
- (iii) The materials used in the glow sign boards decay with the effect of weather. Therefore, it requires frequent replacement. Consequently, the assessee has to incur expenditure on glow sign boards regularly in almost each year.
- (iv) The assessee incurred expenditure on the glow sign boards with the object of facilitating the business operation and not with the object of acquiring asset of enduring nature.

High Court's decision:

The Delhi High Court concurred with the above observations of the P & H High Court and held that such expenditure on glow sign boards displayed at dealer outlets was revenue in nature.

9. What is the eligible rate of depreciation in respect of computer accessories and peripherals under the Income-tax Act, 1961?

CIT v. BSES Yamuna Powers Ltd (2013) 358 ITR 47 (Delhi)

Assessee's contention vs. Department's contention:

The assessee claimed depreciation on computer accessories and peripherals at the rate of 60%, being the eligible rate of depreciation on computers including computer software. However, the Revenue contended that computer accessories and peripherals cannot be treated at par with computers and computer software, and hence were eligible for depreciation at the general rate applicable to plant and machinery, i.e., 15%.

High Court's decision:

The High Court observed that computer accessories and peripherals such as printers, scanners and server etc. form an integral part of the computer system and they cannot be used without the computer. Consequently, the High Court held that since they are part of the computer system, they would be eligible for depreciation at the higher rate of 60% applicable to computers including computer software.

Note - The Delhi High Court, in *CIT v. Orient Ceramics and Industries Ltd.* [2013] 358 ITR 0049, following its own judgment in the above case, held that depreciation on UPS is allowable @ 60%, being the eligible rate of depreciation on computers including computer software, and not at the general rate of 15% applicable to plant and machinery.

10. Can share issue expenses incurred by a company be treated as capital in nature, if the public issue could not ultimately materialize on account of non-clearance by SEBI?

Mascon Technical Services Ltd. v. CIT (2013) 358 ITR 545 (Mad.)

Facts of the case:

The assessee-company incurred share issue expenses of ₹ 35.39 lakh for its proposed public issue, which could not ultimately materialize due to non-clearance by the SEBI. It claimed such expenses as revenue in nature, on the ground that the same was incurred for augmenting its working capital. The claim of the assessee was, however, rejected by the Assessing Officer.

Assessee's contention vis-à-vis Tribunal's contention:

On appeal to the Tribunal, the assessee contended that the expenditure incurred was only for the purpose of bettering the cash availability and the working capital of the company, and hence, the same should be allowed as a revenue expenditure. The assessee further contended that since incurring of share issue expenses did not result in increase in the share capital of the company on account of the reasons beyond its control, such expenditure should be allowed as revenue expenditure.

The Tribunal rejected the said contention of the assessee and took the view that the share issue expenditure was incurred *prima facie* for expansion of the capital base of the company and was, hence, in the nature of capital expenditure. The fact that the efforts had got frustrated later on would not alter the nature of the expenditure.

High Court's Decision:

The High Court noted that the assessee-company had taken steps to go in for a public issue and incurred share issue expenses for the same. However, it could not go in for the public issue by reason of the orders issued by the SEBI just before the proposed issue. Though the efforts were aborted, the fact remains that the expenditure incurred was only for the purpose of expansion of the capital base. The capital nature of the expenditure would not be lost on account of the abortive efforts. The expenditure, therefore, constitutes a capital expenditure.

11. Can depreciation under section 32 be allowed on the plant and machinery which is ready for use but could not be put to use at any time during the previous year due to some extraneous reason, for example, paucity of raw material?

CIT v. Chennai Petroleum Corporation Ltd. (2013) 358 ITR 314 (Mad.)

Facts of the case:

The assessee claimed depreciation on the gas sweetening plant, which was built during the relevant previous year, but was not put to use in that year on account of non-availability of raw material i.e., sour gas. In the earlier previous year, the plant was commissioned by running a test run for the first time and depreciation was allowed for

that year by the Department, considering the trial run as equivalent to putting the said plant to use. However, the assessment for the relevant previous year was reopened on the ground that the assessee had not disclosed the material fact that the plant was not in use for the whole of the said previous year

Assessee's contention vis-à-vis Assessing Officer's contention:

The assessee's contention was that the plant was ready for use for the year under consideration and the non-availability of raw material was an impediment to put the plant to use. The expression "used" in section 32(1) should be understood to include passive as well as active use. In this case, the asset was in good condition and ready for use. It could have been put to actual use in any minute, at any time during the relevant previous year, and hence the claim for depreciation cannot be denied.

The Assessing Officer, however, completed the assessment rejecting the assessee's claim on the ground that the asset had never been put to use during the whole of the relevant previous year i.e., the second year of installation of the plant.

Majority view of the Tribunal:

The Accountant Member of the Tribunal supported the assessee's view that once the plant was ready for use, it was entitled to depreciation. The Judicial Member, however, was of the view that unless the assets have been actually put to use, the claim of the assessee could not be granted. The Third Member i.e., the Vice President of the Appellate Tribunal agreed with the view taken by the Accountant Member in favour of the assessee.

High Court's observations:

The High Court referred to the Supreme Court ruling in *Liquidators of Pursa Ltd. v. CIT* (1954) 25 ITR 265 in context of the expression "used for the purpose of business" for claim of depreciation. The Court held that so long as the business was a going one and the machinery got ready for use but could not be put to use due to certain extraneous circumstances, depreciation under section 32 would be allowable.

High Court's decision:

The High Court confirmed the majority decision of the Tribunal holding that, in this case, the machinery was entitled to depreciation since the business was a going concern and the machinery, being ready for use, could not be actually put to use due to an extraneous reason, namely, raw material paucity.

Capital Gains

12. Where the stamp duty value under section 50C has been adopted as the full value of consideration, can the reinvestment made in acquiring a residential property, which is in excess of the actual net sale consideration, be considered for the purpose of computation of exemption under section 54F, irrespective of the source of funds for such reinvestment?

Gouli Mahadevappa v. ITO (2013) 356 ITR 90 (Kar.)**Facts of the case:**

In the present case, the assessee sold a plot of land for ₹ 20 lakhs and reinvested the sale consideration of ₹ 20 lakhs together with agricultural income of ₹ 4 lakhs, in construction of a residential house. The assessee claimed capital gains exemption under section 54F, taking into consideration the entire investment of ₹ 24 lakhs. The Assessing Officer, applying the provisions of section 50C, deemed the stamp duty value of ₹ 36 lakhs as the full value of consideration since the consideration received or accruing as a result of transfer of capital asset (i.e. ₹ 20 lakhs) was less than the value adopted by the stamp valuation authority (i.e., ₹ 36 lakhs). The same was not disputed by the assessee before the Assessing Officer.

Assessing Officer's contention vis-a-vis assessee's contention:

The Assessing Officer allowed exemption under section 54F, taking into consideration investment in construction of residential house, to the extent of actual net consideration of ₹ 20 lakhs. He did not consider the balance amount of ₹ 4 lakhs, invested in the construction of residential house, out of agricultural income, for computation of exemption under section 54F, even though the sale consideration adopted for the purpose of computation of capital gains i.e., stamp duty value of ₹ 36 lakhs, was more than the amount of ₹ 24 lakhs invested in the new house.

The assessee contended that the entire investment of ₹ 24 lakhs made in construction of the residential house should be considered for computation of exemption under section 54F, irrespective of the source of funds for such reinvestment. Further, the assessee also contended before the High Court that the registration value adopted under section 50C was excessive and disproportionate to the market value of the property.

High Court's observations:

On the issue of applicability of section 50C, the Karnataka High Court observed that section 50C(2) allows an opportunity to the assessee to contend, before the Assessing Officer, the correctness of the registration value fixed by the State Government. Had he done so, the assessing authority would have invoked the power of appointing a Valuation Officer for assessing the fair market value of the property. The High Court held that when the assessee had not disputed the registration value at that point of time, it is not permissible for the assessee to now contend, at this stage, that the registration value does not correspond to the market value. Hence, the value of ₹ 36 lakhs adopted under section 50C has to be deemed as the full value of consideration.

High Court's decision:

On the issue of exemption under section 54F, the High Court held that when capital gain is assessed on notional basis as per the provisions of section 50C, and the higher value i.e., the stamp duty value of ₹ 36 lakhs under section 50C has been adopted as the full value of consideration, the entire amount of ₹ 24 lakhs reinvested in the residential house within the prescribed period should be considered for the purpose of exemption under section 54F, irrespective of the source of funds for such reinvestment.

13. Where transfer of shares in a company has been effected, fulfilling all the requirements for claim of exemption under section 10(38), can such exemption be denied on the ground that the transaction is a colorable device, since the underlying asset transferred is, in effect, land, which is a short-term capital asset, on sale of which capital gains tax liability would have been attracted?

Bhoruka Engineering Inds. Ltd. v. DCIT (2013) 356 ITR 25 (Kar.)

Facts of the case:

Bhoruka Steel Ltd. (BSL), a group company of the assessee, was incorporated in the year 1969. It had a mini steel plant at Bangalore. It commenced commercial production in 1972 and set up a refractory plant at Bangalore. BSL was declared as a sick industrial company in 1996 and IDBI was appointed as the Operating Agency. The rehabilitation scheme formulated envisaged sale of the surplus assets of BSL, which included 30 acres of land. A decision was taken in the meeting held on 29th July, 2002, to offer the land first to the promoters/sister companies jointly or severally with the reserve price of ₹ 25 lakhs per acre on the condition that the dues of the secured creditors and the others as per the rehabilitation scheme were cleared by 31st December, 2002. Bhoruka Financial Services Ltd. (BFSL), a public limited company and a group company engaged in financial services, offered to purchase the 30 acres of land at a price of ₹ 25 lakhs per acre. The Committee approved the sale of 15 acres of land to BFSL at ₹ 3.75 crores. Accordingly, the land measuring 15 acres was sold to BFSL in June 2004 through registered sale deeds for ₹ 3.75 crores, the then prevailing market price which was accepted for the purpose of section 50C also.

The assessee-company is a limited company whose shares are quoted in the stock exchange. The assessee is holding shares in BFSL since October, 1984. The assessee, together with other promoter shareholders, held 98.73% shares in BFSL, the remaining being held by the public shareholders. In the financial year 2005-06, the assessee-company sold its shares to DLF Commercial Developers Ltd. (DLFCDL) for a net consideration of ₹ 20.29 crores. The other promoters also sold their shares to DLFCDL and the total net consideration, including that of the assessee, was ₹ 89.28 crores. The assessee claimed the capital gain arising on sale of such shares as exempt under section 10(38), since the shares, being a long-term capital asset, were sold in a recognized stock exchange and securities transaction tax has been paid on such sale.

Revenue's contention:

The Revenue contended that the substance of the above transaction was the transfer of land, which would attract short-term capital gains tax in the hands of BFSL. BSL had sold its immovable property to its associate concern, BFSL, for a nominal value of ₹ 3.75 crores. BFSL, never before doing any business other than financial services, purchases the land for ₹ 3.75 crores and immediately thereafter, the assessee-company and its entire group, holding 98.73% of shares in BFSL, sell their entire shareholding of BFSL to DLFCDL for a consideration of ₹ 89.28 crores, without attracting corresponding tax liability. This is made possible by getting away from Bangalore Stock Exchange and going to Magadh Stock Exchange to carry out the sale transaction and by paying securities transaction tax for claiming exemption from long-term capital gains arising on

sale of shares under section 10(38). The shares of BFSL were listed in Bangalore Stock Exchange, but hardly got traded. The last quoted value of the share was ₹ 5 in the year 1985. The promoters of BFSL sought permission from SEBI to exempt them from making public announcement in respect of sale of equity shares to DLFCDL.

Further, the promoters of BFSL had disposed of all the other assets held by BFSL except land, before the shares were sold to DLFCDL. BFSL was, in effect, reduced to a shell company, which was used to transfer a real asset and the promoters took the fruits of the transaction. The intention of the promoters was to transfer the underlying asset, being land to DLFCDL. The Revenue contended that DLFCDL could not have bought the shares of BFSL at a substantial rate of ₹ 4,490 per share. Since the area where the land was situated had high commercial value, DLFCDL had purchased the shares of BFSL keeping in mind the value of the underlying asset, being the land. The land had, in effect, been transferred to DLFCDL by way of the above circuitous transaction.

Appellate authorities' views:

The Commissioner (Appeals) concurred with the view of the assessing authority and held that the corporate veil had to be pierced and the substance of the transaction (i.e. sale of a short-term capital asset, being land, giving rise to taxable short-term capital gains), has to be considered. The Tribunal was of the view that the transaction in question was a colorable device to avoid payment of short-term capital gains tax. This view was further substantiated by applying the rationale of case of *Vodafone International Holdings B. V. v. Union of India* reported in (2012) 341 ITR 1 (SC).

High Court's observations:

The Karnataka High Court observed that in *Vodafone* case, it was also mentioned that 'Tax planning may be legitimate provided it is within the framework of law' and 'colorable devices cannot be a part of tax planning and it is wrong to encourage or entrain the belief that it is honorable to avoid the payment of tax by resorting to dubious methods'. Therefore, in that case, it was inferred that tax planning within the framework of law is legal. However, tax evasion through the use of colorable devices and by resorting to dubious methods and subterfuges is not allowed.

The High Court further observed that the assessee is entitled to manage its affairs within the four corners of law so as to attract minimum tax liability or no tax liability. However, the same should be real and genuine and not a sham or make-believe. He may legitimately claim the advantage of any express terms or of any omissions that he can find in his favour in taxing statutes in absence of any specific tax avoidance provision. Further, the intention of the legislature in a taxation statute is to be gathered from the language of the provisions particularly where the language is plain and unambiguous. In a taxing Act, it is not possible to assume any intention or governing purpose of the statute more than what is stated in the plain language.

If the transaction in question is sham or colorable and entered into with the sole intention of evading payment of tax, then such a transaction would not have any legitimacy. For determining whether a transaction is a valid transaction or a sham, each case should be seen on a standalone basis.

High Court's decision:

The Karnataka High Court observed that, in this case, the assessee-company was holding shares in BFSL from 1st October, 1984. Therefore, the shares represent a long-term capital asset. The transaction had taken place subsequent to 28th September, 2004. Hence, the second condition for claim of exemption is fulfilled. The transaction had taken place through the Magadh Stock Exchange and securities transaction tax has been paid on such sale. Where all the three conditions have been fulfilled, the assessee is entitled to exemption under section 10(38) in respect of long-term capital gains arising from such transfer. Merely because capital gains tax liability would have been attracted had a registered sale deed been executed by BFSL for selling land to DLFCDL, it cannot be concluded that the shareholders of BFSL transferring their shares after complying with the legal requirements would not be entitled to the benefit of exemption.

The High Court further noted that the companies involved in the transaction were existing companies. Thus, neither of the companies came into existence as a part of the scheme for purchase of immovable property or transfer of shares for the purpose of evading payment of tax. The event of transfer of shares happened in ordinary course of business and is legal. The transaction is, therefore, real, valuable consideration is paid, all legal formalities are complied with, and what is transferred is shares and not immovable property. Hence, it is a valid legal transaction and cannot be termed as a colorable device or sham transaction or an unreal transaction.

14. Where a building, comprising of several floors, has been developed and re-constructed, would exemption under section 54/54F be available in respect of the cost of construction of -

- (i) the new residential house (i.e., all independent floors handed over to the assessee); or
- (ii) a single residential unit (i.e., only one independent floor)?

CIT v. Gita Duggal (2013) 357 ITR 153 (Delhi)

Facts of the case:

In the present case, the assessee was the owner of property comprising the basement, ground floor, first floor and second floor. In the year 2006, she entered into a collaboration agreement with a builder for developing the property. According to the terms of the agreement, the builder was to demolish the existing structure on the plot of land and develop, construct, and/or put up a building consisting of basement, ground floor, first floor, second floor and third floor with terrace at its own costs and expenses. The assessee handed over to the builder, the physical possession of the entire property, along with 22.5% undivided interest over the land. The handing over of the entire property was, however, only for the limited purpose of development. The builder was to get the third floor plus the undivided interest in the land to the extent of 22.5% for his exclusive enjoyment. In addition to the cost of construction incurred by the builder on development of the property, a further amount of ₹ 4 crores was payable by the builder to the assessee as consideration against the rights of the assessee.

Assessee's contention vis-à-vis Assessing Officer's contention:

The assessee, in her return of income, showed only ₹ 4 crore as sales consideration. The Assessing Officer, however, took the view that the sale consideration for the transfer should include not only the amount of ₹ 4 crores received by the assessee in cash, but also the cost of construction amounting to ₹ 3.44 crore incurred by the developer in respect of the other floors, which were handed over to the assessee.

The assessee contended that if the cost of construction incurred by the builder is to be added to the sale price, then, the same should also correspondingly be considered as re-investment in the residential house for exemption under section 54.

However, the Assessing Officer rejected the claim for exemption under section 54 on the ground that the floors obtained by the assessee contained separate residential units having separate entrances and cannot qualify as a single residential unit. He contended that deduction under section 54F was allowable, and that too only in respect of cost of construction incurred in respect of one unit i.e., one floor.

Appellate authorities' views:

The Commissioner (Appeals), on the basis of the judgment in *CIT v. D. Ananda Basappa* [2009] 309 ITR 0329 (Kar.), took a contrary view. The Tribunal concurred with the view of the Commissioner (Appeals), observing that the words "a residential house" appearing in section 54/54F of the Act cannot be construed to mean a single residential house since under section 13(2) of the General Clauses Act, "singular" includes "plural".

High Court's observations:

The High Court observed that sections 54 and 54F use the expression "residential house" and not "residential unit" and it is the Assessing Officer who has introduced a new concept of "residential unit" into these sections. Sections 54 and 54F require the assessee to acquire a "residential house" and so long as the assessee acquires a building, which may be constructed, for the sake of convenience, in such a manner as to consist of several units which can, if the need arises, be conveniently and independently used as an independent residence, the requirement of the section should be taken to have been satisfied. There is nothing in these sections which requires the residential house to be constructed in a particular manner. The only requirement is that it should be for residential use and not for commercial use. The physical structuring of the new building, whether lateral or vertical, should not come in the way of considering the building as a residential house.

High Court's decision:

The High Court held that the fact that the residential house consists of several independent units cannot be permitted to act as an impediment to the allowance of the deduction under section 54 or section 54F. It is neither expressly nor by necessary implication prohibited. Therefore, the assessee is entitled to exemption of capital gains in respect of investment in the residential house, comprising of independent residential units handed over to the assessee.

15. In the case of an assessee, being a dealer in shares and securities, whose portfolio comprises of shares held as stock-in-trade as well as shares held as investment, is it permissible under law to convert a portion of his stock-in-trade into investment and if so, what would be the tax treatment on subsequent sale of such investment?

CIT v. Yatish Trading Co. Pvt. Ltd. (2013) 359 ITR 320 (Bom.)

Facts of the case:

The assessee, being a dealer in shares and securities, has a trading as well as an investment portfolio of shares and securities. On 1st April 2002 and 1st October 2004, the assessee converted certain shares and securities held as stock-in-trade into investments and thereafter, in the A.Y.2006-07, it transferred such converted shares and securities and declared income arising on such transfer under the head "Profits and gains of business or profession" and "Capital gains". The profits and gains up to the date of conversion was offered as business income (i.e., fair market value on the date of conversion minus the cost of acquisition). The profits and gains arising after conversion up to the date of sale was offered as capital gains (i.e., sale price minus the fair market value on the date of conversion). The Assessing Officer, however, assessed the entire income arising on transfer of such converted shares and securities as business income.

Appellate Authorities' findings & views:

The CIT (Appeals) opined that the view of the assessee was logical and reasonable. The Tribunal noted that the Department had accepted the conversion of stock-in-trade into investment while assessing the income of A.Y.2003-04 and A.Y.2005-06. Further, the books of account of the assessee showed such shares (on which the assessee offered income as capital gains) as investment. Also, the mere fact that the assessee-company was trading in the shares and securities cannot estop it from holding certain shares as investment and offering the gains on sale of such shares to tax under the head "Capital gains". It is open for a trader in shares to have a trading as well as an investment portfolio of shares and securities.

High Court's decision:

The High Court concurred with the Tribunal's ruling that the gains arising on sale of those shares held as investments by the dealer-assessee (i.e., the difference between the sale price and the fair market value on the date of conversion) were to be assessed under the head "Capital gains" and not under the head "Profits and gains of business or profession".

16. Where a leasehold property is purchased and subsequently converted into freehold property and then sold, should the period of holding be reckoned from the date of purchase or from the date of conversion for determining whether the resultant capital gains is short-term or long-term?

CIT v. Smt. Rama Rani Kalia (2013) 358 ITR 0499 (All.)

Facts of the case:

The assessee purchased a leasehold property on July 7, 1984. Such leasehold rights in the property were converted into freehold rights on March 29, 2004. She sold the property on March 31, 2004 and declared long-term capital gains on the transfer. The Assessing Officer opined that since the property was acquired by converting the leasehold right into freehold right on March 29, 2004, and was sold within three days on March 31, 2004, the resultant capital gains would be short-term.

Appellate Authorities' views:

The Commissioner (Appeals) opined that the conversion of leasehold property into freehold property was nothing but improvement of the title over the property, as the assessee was the owner prior to conversion. The Tribunal affirmed this view of the Commissioner (Appeals) and held that the gains were long-term capital gains, as the assessee was the owner of the property even prior to conversion.

High Court's observations:

The High Court observed that the difference between "short-term capital asset" and "long-term capital asset" is the period over which the property has been held by the assessee and not the nature of title over the property. The lessee of the property has rights as the owner of the property subject to the covenants of the lease deed. Accordingly, the lessee may, subject to covenants of the lease deed, transfer the leasehold rights of the property with the consent of the lessor.

High Court's decision:

The High Court, therefore, concurred with the views of the Tribunal that conversion of the rights of the lessee from leasehold to freehold is only by way of improvement of her rights over the property, which she enjoyed. It would not have any effect on the taxability of gain from such property, which is related to the period over which the property is held. Since, in this case, the period of holding is more than 36 months, the resultant capital gains would be long-term.

Set-off and carry forward of losses / Assessment of firms

17. Can the loss suffered by an erstwhile partnership firm, which was dissolved, be carried forward for set-off by the individual partner who took over the business of the firm as a sole proprietor, considering the succession as a succession by inheritance?

Pramod Mittal v. CIT (2013) 356 ITR 456 (Delhi)

Facts of the case:

In the present case, the assessee was previously a partner in a firm. As per the dissolution deed of the partnership firm, with effect from 18th September, 2004, he took

over the entire business of the partnership firm in his individual capacity including fixed assets, current assets and liabilities and the other partner was paid his dues. He then ran the business as a sole proprietor with effect from that date. The assessee, relying upon section 78(2) and the decisions of the Supreme Court in *CIT v. Madhukant M. Mehta* (2001) 247 ITR 805 (SC) and *Saroj Aggarwal v. CIT* (1985) 156 ITR 497 (SC), claimed the set-off of the losses suffered by the erstwhile partnership firm against his income earned as an individual proprietor, considering the case as inheritance of business.

However, considering that only the person who has suffered the loss is entitled to carry forward and set-off the same, the claim of the assessee was disallowed by the Assessing Officer. The Tribunal concurred with the Assessing Officer's view.

High Court's observations:

The High Court observed that upon dissolution, the partnership firm ceased to exist. Also, the partnership firm and the proprietorship concern are two separate and distinct units for the purpose of assessment. As per section 170(1), the partnership firm shall be assessed as such from 1st April of the previous year till the date of dissolution (i.e., 18th September, 2004). Thereafter, the income of the sole- proprietorship shall be taxable in the hands of the assessee as an individual. Thus, section 170(1) provides as to who will be assessable in respect of the income of the previous year from business, when there is a change in the person carrying on business by succession.

Section 78(2), however, deals with carry forward of losses in case of succession of business. It provides that only the person who has incurred the losses, and no one else, would be entitled to carry forward the same and set it off. An exception provided thereunder is in the case of succession by inheritance.

Therefore, section 170(1) providing the person in whose hands income is assessable in case of succession and section 78(2) providing for carry forward of losses in case of succession of business, deal with different situations and resultantly, there is no contradiction between these sections.

The income earned by the sole proprietor would include his share of loss as an individual but not the loss suffered by the erstwhile partnership firm in which he was a partner. The exception given in section 78(2), permitting carry forward of losses by the successor in case of inheritance, is not applicable in the present case since the partnership firm was dissolved and ceased to continue. Taking over of business by a partner cannot be considered as a case of inheritance due to death as per the law of succession. The High Court opined that the decision in *Madhukant M. Mehta's case* and *Saroj Aggarwal's case* cannot be applied since this is not a case of succession by inheritance.

High Court's decision:

Therefore, the loss suffered by the erstwhile partnership firm before dissolution of the firm cannot be carried forward by the successor sole-proprietor, since it is not a case of succession by inheritance. The assessee sole-proprietor is, therefore, not entitled to set-off the loss of the erstwhile partnership firm against his income.

Note - In *Madhukant M. Mehta's* case, the sole proprietor had expired and after his death the heirs succeeded the business as a partnership concern. Therefore, the losses suffered by the deceased proprietor was allowed to be set-off by the partnership firm since the case falls within the exception mentioned under section 78(2), i.e., a case of succession by inheritance.

Also, in *Saroj Aggarwal's* case, upon death of a partner, his legal heirs were inducted as partners in the partnership firm. The partnership firm was not dissolved on the death of the partner. The partnership firm which suffered the losses continued with induction of the legal heirs of the deceased partner. This, being a case of succession by inheritance, the benefit of carry forward of losses was given to the re-constituted partnership firm.

In the present case, however, the partnership firm was dissolved and the take over of the running business of the firm by the erstwhile partner as a sole proprietor was not a case of succession by inheritance. Hence, the carry forward of losses of the firm by the sole proprietor was not allowed in this case.

Deductions from Gross Total Income

18. Can Duty Drawback be treated as profit derived from the business of the industrial undertaking to be eligible for deduction under section 80-IB?

CIT v. Orchev Pharma P. Ltd. (2013) 354 ITR 227 (SC)

Supreme Court's Decision

On this issue, the Supreme Court, following the decision in case of *Liberty India v. CIT (2009) 317 ITR 218 (SC)* held that Duty Drawback receipts cannot be said to be profits derived from the business of industrial undertaking for the purpose of computation of deduction under section 80-IB.

Note - In the case of *Liberty India v. CIT (2009) 317 ITR 218 (SC)*, the Supreme Court observed that DEPB / Duty drawback are incentives which flow from the schemes framed by the Central Government or from section 75 of the Customs Act, 1962. Section 80-IB provides for the allowing of deduction in respect of profits and gains derived from eligible business. **However, incentive profits are not profits derived from eligible business under section 80-IB. They belong to the category of ancillary profits of such undertaking.** Profits derived by way of incentives such as DEPB/Duty drawback cannot be credited against the cost of manufacture of goods debited in the profit and loss account and they do not fall within the expression "profits derived from industrial undertaking" under section 80-IB. Hence, Duty drawback receipts and DEPB benefits do not form part of the profits derived from the eligible business for the purpose of the deduction under section 80-IB.

19. Whether the process of bottling of gas into gas cylinders amounts to production of gas cylinders for the purpose of deduction under section 80-IB?

Puttur Petro Products P. Ltd. v. ACIT [2014] 361 ITR 290 (Kar.)

High Court's Decision:

Applying the rationale of the Apex Court decision in the case of *CIT v. Vinbros and Co. [2012] 349 ITR 697*, the High Court held that the process of bottling of gas into gas cylinders, which requires a very specialised process and independent plant and machinery, amounts to production of "gas cylinders" containing gas for the purpose of claiming deduction under section 80-IB.

Assessment of Various Entities

20. Would the ancestral property received by the assessee after the death of his father and was distributed among his family members be considered as HUF property or Individual property?

Commissioner of Income-tax v. D. L. Nandagopala Reddy (Individual) (2014) 360 ITR 0377 (Kar)

Facts of the case:

In the present case, Laxmaiah Reddy had no sons and therefore, he adopted the assessee vide a registered adoption deed dated June 25, 1956. The property, which is the subject matter of the suit, originally belonged to Venkateshwaraiah (assessee's grandfather). The assessee's father (Laxmaiah Reddy), took his share in the joint family property and executed a release deed in favour of the remaining members of the joint family vide a registered release deed dated November 23, 1927 and bequeathed all his properties in favour of the assessee. The assessee, in turn, distributed the property in favour of his wife and children. This was done by oral partition which was evidenced by a memorandum of partition dated August 6, 1998.

Thereafter, a transaction was entered into by the assessee with the builder for development of the property. The Assessing Officer treated the consideration received from the builder by the assessee and his wife as their individual income and assessed the same to tax in their individual hands.

Assessing Officer's contention:

The revenue contended that when assessee's father got the property under a release deed, it ceased to be the joint family property. Since that property was bequeathed in favour of the assessee, he became its owner after the death of his father. Therefore, it was a separate property and, consequently, the income derived therefrom is assessed to tax in the hands of the assessee as separate property.

High Court's observation:

The High Court observed that the property originally belonged to Hindu Undivided Family (HUF). One of the members of the family (i.e., the assessee's father) went out of the joint

family under a release deed and the remaining members continued to be the members of joint family. After the death of assessee's father and mother, the assessee, being the adopted son, became the sole surviving co-parcener. When such property came to the hands of the assessee it was not his individual property; it was the property of his Hindu Undivided Family.

High Court's Decision:

The High Court held that that when the property came to the hands of the assessee, it was not his self-acquired property; it was property belonging to his HUF. The assessee had given a portion of the property to his wife without a registered document, which is possible only if the property is a HUF property. If such property is treated as a self-acquired property, then assessee would have been able to give the portion of the property to his wife only by registered document.

Income-tax Authorities

21. **Can the Assessing Officer call for information under section 133(6), which is useful or relevant to any enquiry, where no proceeding is pending against a person, with the permission of Director or Commissioner?**

Kathiroom Service Co-operative Bank Ltd. v. CIT (CIB) (2014) 360 ITR 0243 (SC)

Facts of the case:

The Assessing Officer, with the prior approval of the Commissioner, issued notice under section 133(6) to the assessee, a co-operative society engaged in banking business, calling for general information regarding details of all persons (whether resident or non-resident) who had made (a) cash transactions of ₹ 1 lakh and above in any account, and/or (b) time deposits of ₹ 1 lakh or above, for the period of three years between April 1, 2005, and March 31, 2008, expressly stating therein that failure to furnish the information would attract penal consequences.

The assessee objected to the said notice, *inter alia*, on the ground that such notice seeking for information which is unrelated to any existing or pending proceeding against the assessee could not be issued under the provisions of the Act.

Supreme Court's Observations:

The Supreme Court observed that the Assessing Officer has been empowered to requisition information which will be useful for or relevant to **any enquiry** or proceeding under the Income-tax Act, 1961 in the case of any person. However, an income-tax authority below the rank of the Director or Commissioner can exercise this power in respect of an **enquiry** in a case where no proceeding is pending, only with the prior approval of the Director or the Commissioner.

Apex Court's Decision:

The Supreme Court held that information of general nature could be called for from banks. In this case, since notices have been issued after obtaining approval of the Commissioner, the assessing authority had not erred in issuing the notices to assessees requiring them to furnish information regarding account holders with cash transactions or deposits of more than ₹ 1 lakh. The Supreme Court, therefore, held that for such enquiry under section 133(6), the notices could be validly issued by the assessing authority.

Assessment Procedure / Appeals and Revision

22. Can an assessee, objecting to the reassessment notice issued under section 148, directly approach the High Court in the normal course contending that such reassessment proceedings are apparently unjustified and illegal?

Samsung India Electronics P. Ltd. v. DCIT (2014) 362 ITR 460 (Del.)

Facts of the case

In the present case, Samsung Electronics Co. Ltd., the Korean Company was subjected to regular assessment for the assessment year 2006-07. The assessment order was passed, pursuant to the directions under section 144C(5) made by the Disputes Resolution Panel. For the same assessment year, i.e., A.Y.2006-07, assessee was issued a reassessment notice dated March 30, 2013 under section 148. Against this reassessment notice, assessee filed a writ petition before the High Court.

High Court Observations

The High Court observed the Apex court ruling in the case of *GKN Driveshafts (India) Ltd. v. ITO [2003] 259 ITR 19 (SC)*, wherein, it was laid down that **when a notice under section 148 is issued, the proper course of action for the noticee is to file a return and if he so desires, to seek reasons for issuing notices. The Assessing Officer is bound to furnish reasons within a reasonable time. On receipt of the reasons, the noticee is entitled to file objections to issuance of notice and the Assessing Officer is bound to dispose of the objections by passing a speaking order.**

The High Court noted that the assessee has not filed objections before the Assessing Officer and has directly approached the court by way of the writ petition. On this issue, the assessee contended that they were justified in approaching the High Court directly as the reassessment proceedings *ex facie* were unjustified and illegal. The assessee relied upon the decision of the Delhi High Court in *Techspan India P. Ltd. v. ITO [2006] 283 ITR 212 (Delhi)* in which reference was made to the decision of the Gujarat High Court in *Garden Finance Ltd. v. Asst. CIT [2004] 268 ITR 48 (Guj)*, wherein it was observed that the exercise of the powers under section 148 may be so arbitrary or *mala fide* that the court may entertain the petition without requiring the assessee to approach the Assessing Officer, but such a case was an exception and not a rule. In *Techspan India P. Ltd.*'s case, the High Court had given concurrent reasons and made observations when a writ court should interfere. However, there is no need to go into the said question and controversy in the present case, since it does not occasion or require a different

treatment from the procedure followed in other cases in which re-assessment proceedings were/are initiated.

High Court's Decision:

The High Court, thus, held that it will not be appropriate and proper in the facts of the present case to permit and allow the petitioner to bypass and forgo the procedure laid down by the Supreme Court in *GKN Driveshafts (India) Ltd. (supra)*, since the said procedure has been almost universally followed and has helped cut down litigation and crystallise the issues, if and when the question comes up before the Court.

Penalties

23. Can an assessee who has surrendered his income in response to the specific information sought by the Assessing Officer in the course of survey, be absolved from the penal provisions under section 271(1)(c) for concealment of income?

MAK Data P. Ltd. v. CIT (2013) 358 ITR 593 (SC)

Facts of the case:

The assessee-company filed its return of income for the A.Y. 2004-05 declaring an income of ₹ 16.17 lakh along with tax audit report. The assessee's case was selected for scrutiny and notices were issued under section 143(2) and section 142(1). During the course of assessment proceedings, it was noticed by the Assessing Officer that certain documents, namely, share application forms, bank statements, memorandum of association of companies, affidavits, copies of income-tax returns and assessment orders and blank share transfer deeds duly signed, had been found in the course of survey proceedings under section 133A conducted on December 16, 2003, in the case of a sister concern of the assessee, and the same were impounded.

The Assessing Officer issued a show cause notice dated October 26, 2006 to the assessee seeking specific information regarding the documents pertaining to share applications found in the course of survey, particularly, blank transfer deeds signed by persons who had applied for the shares.

In its reply to the show cause notice, the assessee made an offer to surrender a sum of ₹ 40.74 lakhs by way of voluntary disclosure without admitting any concealment or any intention to conceal and subject to non-initiation of penalty proceedings and prosecution. The Assessing Officer, however, completed the assessment bringing the sum of ₹ 40.74 lakhs to tax and levied penalty under section 271(1)(c) for concealment of income and not furnishing true particulars.

Assessee's contention:

The assessee contended that the penalty proceedings were not maintainable since the Assessing Officer had not recorded his satisfaction to the effect that there has been concealment of income/furnishing of inaccurate particulars of income. Further, it also

contended that the surrender of income was a conditional surrender before any investigation in the matter.

Appellate Authorities' view:

The Commissioner (Appeals) did not accept the assessee's contention. The Tribunal, however, was of the view that the amount of ₹ 40.74 lakhs was surrendered by the assessee to settle the dispute with the Department. It opined that since the assessee, for one reason or the other, agreed or surrendered certain amounts for assessment, the imposition of penalty solely on the basis of the assessee's surrender could not be sustained. The Tribunal, therefore, allowed the appeal and set aside the penalty order.

The High Court, however, accepted the plea of the Revenue that there was absolutely no explanation by the assessee for the concealed income of ₹ 40.74 lakhs. The High Court took the view that in the absence of any explanation in respect of surrendered income, the first part of *Clause (A) of Explanation 1 to section 271(1)(c)* would be attracted.

Apex Court's Observations:

The Apex Court observed that the assessee had stated that the surrender of the additional sum was with a view to avoid litigation, to buy peace and to channelize the energy and resources towards productive work and to make amicable settlement with the Income-tax Department. The Court observed that these types of defenses are, however, not recognized under the statute. It further observed that the survey was conducted and documents were impounded ten months before the assessee filed its return of income. The Court opined that had it been the intention of the assessee to make full and true disclosure of its income, it would have filed the return declaring an income inclusive of the amount which was surrendered later during the course of the assessment proceedings. It is the statutory duty of the assessee to record all its transactions in the books of account, to explain the source of payments made by it and to declare its true income in the return of income filed by it from year to year.

Apex Court's Decision

The Apex Court was, therefore, of the view that surrender of income in this case is not voluntary, in the sense, that the offer of surrender was made in view of detection made by the Assessing Officer in the survey conducted in the sister concern of the assessee. The Apex Court, therefore, concurred with the view of the High Court that levy of penalty is correct in law.

Note: According to *Explanation 1 to section 271(1)(c)*, where in respect of any facts material to the computation of the total income of any person under this Act,-

(A) such person fails to offer an explanation or offers an explanation which is found by the Assessing Officer or the Commissioner (Appeals) or the Commissioner to be false, or
(B) such person offers an explanation which he is not able to substantiate and fails to prove that such explanation is bona fide and that all the facts relating to the same and material to the computation of his total income have been disclosed by him,

then the amount added or disallowed in computing the total income of such person as a result thereof shall, for the purposes of clause (c) of this sub-section, be deemed to represent the income in respect of which particulars have been concealed.

In this case, since the assessee has failed to offer an explanation regarding surrendered income, the amount of income surrendered is deemed to represent the income in respect of which particulars have been concealed, thereby attracting penal provisions under section 271(1)(c).

Miscellaneous Provisions

- 24. Can loan, exceeding the specified limit, advanced by a partnership firm to the sole-proprietorship concern of its partner be viewed as a violation of section 269SS to attract levy of penalty?**

CIT v. V. Sivakumar (2013) 354 ITR 9 (Mad.)

Facts of the case:

In the present case, the assessee was a partner in four firms and also had a sole-proprietary business. In the relevant previous year, the partnership firms had advanced loan to the assessee in cash exceeding the specified amount mentioned in section 269SS. The Assessing Officer initiated penalty proceedings under section 271D in view of violation of section 269SS. The Assessing Officer recorded a factual finding that the said money had been advanced by the partnership firm as a loan and were debited to the accounts of the proprietary concern; therefore, it was evident that the assessee had taken loan from the firms in cash in the capacity of the proprietor and not as a partner. Consequently, the provisions of section 269SS had been violated.

Assessee's contention:

The assessee contended that the amount is taken in the capacity of the partner and it cannot be taken as an independent transaction and therefore, there is no violation of section 269SS. Also, the assessee contended that the partnership firm has no separate legal entity and there is no separate identification between the firm and the partner.

Tribunal's view:

The Tribunal, relying upon the various court decisions, confirmed the finding of the Commissioner (Appeals) that partnership firm is not a juristic person and there is no separate identity for the firm and the partners; Being a partner, the assessee had withdrawn amounts from the firms and there were no reasons to doubt the genuineness of the transactions. Consequently, the transactions between the firm and the partner cannot be brought within the meaning of section 269SS.

High Court's decision:

The High Court, relying upon the various court decisions, upheld the decision of the Tribunal holding that there is no separate identity for the partnership firm and that the partner is entitled to use the funds of the firm. In the present case, the assessee has acted *bona fide* and that there was a reasonable cause within the meaning of section 273B. Therefore, the transaction cannot be said to be in violation of section 269SS and no penalty is attracted in this case.

Provisions for deduction and collection of tax

25. Can the transmission, wheeling and SLDC charges paid by a company engaged in distribution and supply of electricity, under a service contract, to the transmission company be treated as fees for technical services so as to attract TDS provisions under section 194J or in the alternative, under 194C?

Ajmer Vidyut Vitran Nigam Ltd., In re (2013) 353 ITR 640 (AAR)

Facts of the case:

In the present case, the applicant is a government company engaged in the business of distribution and supply of electricity to customers in various districts of Rajasthan. The activity of distribution is preceded by the production of electricity and its transmission from the point of production to the point of distribution. The production is by the generating company, which is another entity and transmission to the applicant is through the transmission system network of the transmission company. The transmission company carries the electrical energy to the applicant at the distribution system network of the applicant. The applicant then distributes the energy to the end customers.

The transmission of electricity from the point of generation to the point of distribution of the applicant is termed as “wheeling”. The applicant pays transmission and wheeling charges for this wheeling, which it contends are statutory charges. The transmission company also functions as a State Load Dispatch Centre (SLDC), which is responsible for the general co-ordination of production and transmission of electricity to ensure uniform distribution in the State. The applicant pays to the transmission company, SLDC charges, which it claims as statutory in nature, since the levy is in terms of the Electricity Act, 2003.

Applicant's contention:

The applicant contended that the above charges were not in the nature of fees for technical services to attract TDS provisions under section 194J, on the following grounds –

- (i) The transmission does not involve rendering of any technical services nor were technically qualified staff of the transmission company involved in the transmission of electrical energy;
- (ii) The SLDC charges were also mere statutory charges and does not involve rendering of technical services;
- (iii) The payment of transmission, wheeling and SLDC charges were in the nature of reimbursement of actual cost and hence, do not generate any income in the hands of the transmission company.

Revenue's contention:

The Revenue, on the other hand, was of the view that the transmission of electrical energy from the point of generation to the point of distribution of the applicant involves rendering of technical services and consequently, the applicant was bound to withhold tax. The Revenue supported its view on the basis of the following contentions –

- (i) Transmission of electrical energy is a technical service and requires constant involvement of a technical system consisting of sophisticated instruments, constant

monitoring and supervision by persons with a technical ability and knowledge to operate and manage the system so as to ensure regular and consistent supply of electricity at the grid voltage at the distribution point of the applicant.

- (ii) As regards SLDC charges, the services rendered require the technical support and services of technically qualified staff and therefore they were technical services within the meaning of section 194J.
- (iii) The fact that the contract between both the parties is backed by a statutory obligation cannot alter the nature of services rendered.

AAR's observations:

The AAR did not agree with the applicant's contention regarding transmission and wheeling charges not constituting fees for technical services on the ground that no rendering of technical services was involved for maintaining proper and regular transmission of electrical energy. It was also not in agreement with the applicant's argument that the services of technical personnel were not needed for ensuring due and proper transmission of electrical energy from the generation point to the distribution point. The AAR concurred with the Revenue's view that the personnel of the transmission company had to ensure regular and consistent transmission of electrical energy at the grid voltage at the distribution point of the applicant.

AAR's decision:

The AAR, considering the definition of fees for technical services under section 9(1)(vii) and the process involved in proper transmission of electrical energy, held that transmission and wheeling charges paid by the applicant to the transmission company are in the nature of fees for technical services, in respect of which the applicant has to withhold tax thereon under section 194J.

As regards SLDC charges, the AAR opined that the main duty of the SLDC is to ensure integrated operation of the power system in the State for optimum scheduling and dispatch of electricity within the State. The SLDC charges paid appeared to be more of a supervisory charge with a duty to ensure just and proper generation and distribution in the State as a whole. Therefore, such services were not in the nature of technical service to the applicant; Resultantly, it does not attract TDS provisions under section 194J or under section 194C.

26. Can discount given on supply of SIM cards and pre-paid cards by a telecom company to its franchisee be treated as commission to attract the TDS provisions under section 194H?

Bharti Cellular Ltd. v. ACIT (2013) 354 ITR 507 (Cal.)

High Court's observations:

On this issue, the Calcutta High Court observed the Supreme Court ruling in *Bhopal Sugar Mills' case (1977) 40 STC 42*, wherein it was held that the true relationship

between the parties has to be gathered from the nature of the contract, its terms and conditions. The terminology used by the parties is not decisive of the said relationship.

The High Court, on perusal of the agreement between the assessee-telecom company and the franchisees, observed that –

- (1) the property in the start-up pack and pre-paid coupons, even after transfer and delivery to the franchisee, remained with the assessee-telecom company;
- (2) the franchisee really acted as a facilitator and/or instrument of providing services by the assessee-telecom company to the ultimate subscriber;
- (3) the franchisee had no free choice to sell the pre-paid coupons and sim cards and everything including the selling price was regulated by the assessee-telecom company;
- (4) the rate at which the franchisee sells to the retailers is also regulated and fixed by the assessee-telecom company.

In the real sense, the franchisee acted on behalf of the assessee-telecom company for selling start-up pack, prepaid recharge coupons to the customer. Therefore, the relationship between the assessee and the franchisee is essentially that of principal and agent, though the nomenclature used is “franchisee”. The franchisees were, thus, agents of the assessee, getting a fixed percentage of commission, in the form of discount.

High Court’s decision:

Considering the above, the High Court held that there is an indirect payment of commission, in the form of discount, by the assessee-telecom company to the franchisee. Therefore, the assessee is liable to deduct tax at source on such commission as per the provisions of section 194H.

Note - Similar ruling was pronounced by the Kerala High Court in *Vodafone Essar Cellular Ltd. v. ACIT (TDS) (2011) 332 ITR 255*, wherein it was held that there was no sale of goods involved as claimed by the assessee-telecom company 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 consequently, the discount given to him was within the meaning of commission on which tax was deductible under section 194H.

27. **Would commission payment remitted outside India to a non-resident (who is not liable to pay tax in India) for procuring export orders outside India attract disallowance under section 40(a)(i) for non-deduction of tax at source under section 195?**

CIT v. Model Exims (2013) 358 ITR 72 (Allahabad)

Facts of the case:

The assessee is a partnership firm engaged in manufacture and export of finished leather, shoe-uppers and leather products. For the assessment year 2007-08, the assessee made a payment to overseas entities, in respect of the services of procurement of export orders outside India, without deduction of tax at source under section 195, on the understanding that these payments were covered by Circular Nos. 23/1969, 163/1975 and 786/2000² and were hence, not taxable under the scheme of the Act.

The Assessing Officer, however, disallowed the commission payment under section 40(a)(i) for non-deduction of tax at source, on the basis of the provisions contained under section 195 and section 9.

Revenue's contention:

The Revenue contended that the liability to deduct tax arises out of section 195; therefore, the liability has to be determined in accordance with the provisions of law and not of the circulars. Even if earlier circulars did not make it obligatory on the part of assessee to deduct TDS, the assessee would be liable to deduct tax at source as –

- (i) the Circulars did not create any vested right and were only clarificatory in nature;
- (ii) the Circulars were withdrawn by virtue of Circular No.7/2009 dated 22.10.2009, and the withdrawal would be retrospective in nature; and
- (iii) the assessment is to be made after withdrawal of the circulars, in accordance with law.

High Court's observations:

The High Court observed that the earlier Circulars did not oblige the assessee to deduct tax at source. The assessment in question for the assessment year 2007-08 would be governed by the said circulars, which were operative at the relevant time. The assessee was not entitled to deduct tax at source as per the said circulars. Circular No. 7/2009 dated 22.10.2009, withdrawing the earlier circulars became operative only from that date and not earlier. The circulars in force in the relevant year were binding upon the Department; the Assessing Officer did not have any right to ignore the circulars and to disallow the expenditure under section 40(a)(i) for non-deduction of tax at source under section 195.

High Court's decision:

The High Court further observed that there was no obligation to deduct tax at source under section 195 on commission paid to a non-resident, who was not liable to pay tax in India. The payment of commission to foreign agents also did not entitle such foreign agents to pay tax in India. Thus, there was no obligation to deduct tax at source under section 195 on the commission paid to a non-resident recipient, who was not liable to pay tax in India.

² These circulars were later withdrawn by Circular No. 7 dated 22.10.2009

Further, there was also nothing on record to demonstrate that the non-resident agents had been appointed as selling agents, designers or technical advisers³.

Note – Even after withdrawal of Circular Nos. 23/1969, 163/1975 and 786/2000 by Circular No.7/2009 dated 22.10.2009, commission payment to a foreign agent, not having a permanent establishment in India, for booking orders outside India is not subject to tax deduction at source. A foreign agent of an Indian exporter operates in his own country and no part of his income accrues or arises in India. His commission is usually remitted directly to him and is, therefore, not received by him or on his behalf in India. The commission paid to the non-resident agent for services rendered outside India is, thus, not chargeable to tax in India.

Since commission income for booking orders by non-resident who remains outside India is not subject to tax in India, consequently, disallowance under section 40(a)(i) is not attracted in respect of payment of commission to such non-resident outside India even though tax has not been deducted at source.

- 28. Where the assessee fails to deduct tax at source under section 194B in respect of the winnings, which are wholly in kind, can he be deemed as an assessee-in-default under section 201?**

CIT v. Hindustan Lever Ltd. (2014) 361 ITR 0001 (Kar.)

Facts of the case:

In the present case, the assessee is a company engaged in the business of manufacture and sale of various consumer goods/products. During the previous years relevant to A.Y.2001-02 and A.Y.2002-03, it had conducted certain sales promotion schemes. The assessee advertised the schemes wherein coupons were inserted in packs/containers of their products. Some of those coupons indicated that on purchase of the packs/containers, they would get prizes, as indicated in coupons. The prizes that were offered were Santro car, Maruti car, gold chains, gold coins, gold tablas, silver coins, emblems, etc. The total amount of prizes distributed valued ₹ 6,51,238 for the A.Y.2001-02 and ₹ 54,73,643 for the A.Y.2002-03.

The Assessing Officer, having received the information about the schemes, sought clarification and also conducted survey of the assessee's business premises under section 133A. The Assessing Officer, thereafter, passed an order dated 3.1.2002, under sections 201(1) and 201(1A) for the A.Y.2001-02 and treated the assessee as an assessee-in-default of its obligation in terms of section 194B. Similar order was passed for the A.Y.2002-03. According to the Assessing Officer, the assessee was obliged to ensure that the tax in respect of the winnings, wholly in kind, was remitted before the winnings were released. Having failed to do so, the proceedings under section 201(1)

³ In case the payments were in the nature of fees for technical services, the same would have necessitated deduction of tax at source on account of "deemed accrual" of such income as per *Explanation* below section 9(2), if such services were utilized in India.

were initiated. The Assessing Officer held that although the customers did not pay anything extra to receive the prize, nevertheless, they had participated in the scheme by purchasing the products advertised to take a chance at winning the prize. It was further held that what has been paid as prize-in-kind in various schemes conducted by the assessee is a lottery on which the tax was deductible under section 194B. As the assessee neither deducted the tax nor ensured payment thereof before the winnings were released, he treated the assessee as an assessee-in-default. He passed similar order dated 28.3.2002 for the A.Y.2002-03.

Appellate Tribunal's view:

The Tribunal held that the schemes conducted by the assessee were not a lottery, as the said expression was understood up to the A.Y.2001-02. The Tribunal observed that the customers did not pay any excess amount for getting coupons indicating winnings in the packs/containers of products they purchased, and, therefore, nothing was paid by them for participating in the scheme. Accordingly, the Tribunal concluded that although there was an element of chance but as no consideration or payment was made by the customers for the purpose of participation in the lottery with the object of winning the prizes, the schemes conducted by the assessee would not fall within the ambit of section 194B.

The Tribunal further held that having regard to the insertion of *Explanation* below section 2(24)(ix), the scheme conducted by the assessee would be a lottery for the A.Y.2002-03 but nevertheless they accepted the alternate contention that having regard to *Circular No. 390, dated August 8, 1984 [See (1984) 149 ITR (St.) 5]*, there was no obligation on the respondent to deduct tax at source in respect of prizes paid in kind and in the absence of any such obligation, no proceedings under section 201 could be taken against the respondent.

High Court's view:

From a bare perusal of section 194B, it is clear that the person responsible for paying to any person any income by way of winnings from any lottery in an amount exceeding ten thousand rupees shall, at the time of payment thereof, deduct income-tax thereon at the rates in force. A combined reading of sections 194B and 201 shows that if any such person fails to "deduct" the whole or any part of the tax or after deducting, fails to pay the tax as required by or under the Act, then such person shall, without prejudice to any other consequences which he may incur, be deemed to be an assessee in default in respect of such tax. **The provisions contained in these sections do not cast any duty to deduct tax at source where the winnings are wholly in kind. If the winnings are wholly in kind, as a matter of fact, there cannot be any deduction of tax at source. The word "deduction" employed in this provision postulates a reduction or subtraction of an amount from a gross sum to be paid and payment of the net amount thereafter.** Where the winnings are wholly in kind the question of deduction of any sum therefrom does not arise and in that eventuality, the only responsibility, as cast under section 194B, is to ensure that tax is paid by the winner of the prize before the prize or winnings is or are released in his favour.

High Court's decision:

The High Court observed that if the assessee fails to ensure that tax is paid before the winnings are released in favour of the winner, then, section 271C empowers the Joint Commissioner to levy penalty equivalent to the amount of tax not paid, and under section 276B, such non-payment of tax is an offence attracting rigorous imprisonment for a term which shall not be less than three months but which may extend to seven years and with fine. However, the High Court held that proceedings under section 201 cannot be initiated against the assessee.

- 29. Are TDS provisions under section 194H attracted in a case where an assessee, a dairy, makes an outright sale of milk to its concessionaires at a certain price (which is lower than the MRP fixed by the assessee-dairy) and the concessionaires make full payment for the purchases on delivery and bear all the risks of loss, damage, pilferage and wastage?**

C IT v. Mother Dairy India Ltd. (2013) 358 ITR 218 (Delhi)

Facts of the case:

The assessee-dairy undertook activities in connection with procurement, processing, storage and marketing including retail sale of milk and other products. The Dairy was called upon to explain why orders should not be passed under section 201(1)/(1A) treating it as an assessee in default, for failure on its part to deduct tax at source on the difference between the payments made by concessionaires to the assessee-dairy and the MRP at which the concessionaires had to sell the milk to the ultimate consumer, by the treating such difference as "commission" within the meaning of *Explanation (i)* to section 194H.

Assessee's contention:

In reply to the show cause notice, the assessee-dairy explained that it had sold the products to the concessionaires on a principal to principal basis, and the same can be evidenced from the following facts:

- the concessionaires bought the products at a given price after making full payment for the purchases on delivery;
- the milk and other products once sold to the concessionaires became their property and could not be taken back; and
- any loss on account of damage, pilferage and wastage was to the account of the concessionaires.

Owing to these facts, the assessee contended that the difference between payment made by the concessionaires and the MRP could not be treated as "commission" for services rendered and consequently, there was no liability on the part of the assessee to deduct tax at source.

Assessing Officer's view:

The Assessing Officer, however, contended that the relationship existing between the assessee-dairy and the concessionaires was not that of principal to principal but it was a relationship of a principal and an agent, due to the following reasons –

- (i) The booths from which the concessionaires sold milk and other products of the assessee, were owned by the Dairy; and
- (ii) Even after sale to the concessionaires, the assessee-dairy had a right to inspect the booths and check the milk and other products stored in the booth at any time.

Accordingly, he treated the difference between the bill value and the MRP fixed by the assessee-dairy as commission paid to the concessionaires on which the assessee-dairy ought to have deducted tax at source under section 194H.

Appellate Authorities' view:

The Commissioner (Appeals) concurred with the opinion of the Assessing Officer and passed an order affirming the Assessing Officer's view.

The Tribunal, however, on a perusal of the agreement entered into between the assessee-dairy and the concessionaires as well as the other relevant facts of the case, observed that there was an actual sale of milk by the assessee to the concessionaires on delivery and that the assessee was not under any obligation to take back any portion of the unsold milk in any condition whatsoever. The Tribunal was of the view that the other conditions imposed on the concessionaires by the assessee such as the right to inspect the booths at any time, right to check the registers and ensure the proper usage of the equipment, furniture, machinery by the concessionaires did not affect the relationship of principal to principal between the assessee and the concessionaires. The Tribunal opined that such terms were included in the agreement only for the purpose of safeguarding the booths, the equipment, furniture etc. which were owned by the assessee. The Tribunal concluded that since the real test was whether the property in the milk and the products passed to the concessionaires at the time of delivery, and this test was satisfied, the difference between the price at which the assessee sold the milk and the other products to the concessionaires and the MRP at which the concessionaires were to sell them to the consumers was not liable to be treated as commission within the meaning of section 194H.

High Court's Observations:

The High Court concurred with the Tribunal's ruling holding that the terms of the agreement clearly indicated that the relationship between the assessee and the concessionaire was on a principal to principal basis. The Dairy having given space, machinery and equipment to the concessionaire would naturally like to incorporate clauses in the agreement to ensure that its property is properly maintained by the concessionaire, especially because milk and other products are consumed in large quantities by the general public and any unattended defect in the storage facilities can cause serious health hazards. These terms are included in the agreement only to

ensure the smooth operation of the system. Therefore, merely due to the existence of these clauses, it cannot be inferred that the relationship between the assessee and the concessionaire is that of principal and an agent.

High Court's decision:

The High Court opined that the issue had to be decided on the basis of the fact as to when and what point of time the property in the goods passed to the concessionaire. In this case, the concessionaire became the owner of the milk and products on taking delivery of the same from the assessee-dairy. Therefore the relationship between the assessee and the concessionaire is a Principal to Principal relationship. The High Court, therefore, held that the difference between the purchase price (price paid to the Dairy) and the MRP is the concessionaire's income from business and cannot be categorized as commission to attract the provisions of section 194H.

30. Are the provisions of section 234D levying interest on excess refund attracted in a case where the refund granted to the assessee in pursuance of the order of Commissioner (Appeals) was reversed on account of setting aside of such order by the Tribunal?

DIT (International Taxation) v. Delta Air Lines Inc. (2013) 358 ITR 0367 (Bom.)

Facts of the case:

In the present case, the Assessing Officer disallowed the benefit of article 8 of the Double Taxation Avoidance Agreement between India and the U.S.A. (DTAA) to the assessee. The Commissioner (Appeals), on the other hand, held that the assessee was entitled to the benefit of article 8 of the DTAA. The Tribunal, however, set aside the order of the Commissioner (Appeals) and restored the order passed by the Assessing Officer. While giving effect to the order of the Tribunal, the Assessing Officer apart from levying interest under sections 234A and 234B, also levied interest under section 234D on the refund granted to the assessee pursuant to the order of Commissioner (Appeals).

Appellate Authorities' contention:

The assessee challenged the order of the Assessing Officer levying interest under section 234D by filing an appeal before the Commissioner (Appeals). The Commissioner (Appeals) opined that since the refund was not granted under section 143(1), section 234D was not attracted. The Tribunal concurred with the view of the Commissioner (Appeals).

High Court's decision:

The High Court observed that interest under section 234D is chargeable only where the refund has been granted to the assessee while processing the return of income under section 143(1) and thereafter, such refund is found to be excessive under the regular assessment.

In the present case, the refund was not granted under section 143(1). The refund was not granted even by way of an assessment order passed under section 143(3) read with section 147. The same was granted pursuant to the order passed by the Commissioner (Appeals). Consequently, the High Court concurred with the Tribunal's view that the provisions of section 234D were not attracted in this case.

Note: Section 234D(1) provides that where any refund is granted to the assessee under section 143(1) and -

- (a) no refund is due on regular assessment; or
- (b) the amount refunded under section 143(1) exceeds the amount refundable on regular assessment,

the assessee shall be liable to pay simple interest @1½% on the whole or the excess amount refunded, for every month or part of a month comprised in the period from the date of grant of refund to the date of such regular assessment.

Explanation 1 to section 234D provides that where, in relation to an assessment year, the assessment is made for the first time under section 147 or section 153A, the assessment so made shall be regarded as regular assessment for the purpose of this section.

Therefore, the above provisions of section 234D(1) read with Explanation 1 thereto makes it clear that interest thereunder is attracted only in a case where refund is granted to the assessee under section 143(1), which becomes refundable on account of the order passed under section 143(3) or section 147 or section 153A.

31. **Can refund of tax due to the assessee for a particular assessment year be adjusted, against sums due from the assessee in respect of another assessment year, under section 245, without giving prior intimation to the assessee of the proposed adjustment?**

Jeans Knit P. Ltd. v. DCIT (2013) 358 ITR 0505 (Kar.)

Facts of the case:

In the present case, the company is an export oriented unit. A certain deduction was disallowed for A.Y.2007-08 by the Assessing Officer, but subsequently, on appeal by the assessee, the same was allowed by the Commissioner (Appeals). Consequent to the order of Commissioner (Appeals), the assessee became entitled to a refund of ₹ 14.25 crores. While giving effect to the order of Commissioner (Appeals), the Assessing Officer adjusted the refund towards the tax demand for the A.Y. 2008-09.

High Court's Observations:

On the issue of whether refund can be adjusted against demand for the subsequent year without prior intimation, the Karnataka High Court referred to the following High Court rulings—

- (i) The Karnataka High Court's ruling in *Fosroc Chemicals (India) Ltd. v. CIT (2001) 248 ITR 607*, wherein it was observed that for the purpose of any adjustment of the

amount due to the assessee by way of refund against an outstanding demand due from the assessee to the Revenue, an intimation in writing is required to be given to the concerned person of the action proposed. Proposed action would mean a notice before making the adjustments and not an intimation of making the adjustment. An order passed purporting to adjust the refund due to the assessee without prior intimation would be against the express provisions of law and is hence, bad in law. The provisions of section 245 are mandatory in nature.

- (ii) The Delhi High Court's ruling in *Vijay Kumar Bhati v. CIT* (1994) 205 ITR 110, wherein it was held that any order of set-off of refund purporting to be made without prior intimation is neither fair, nor just, nor reasonable and has to be ignored.
- (iii) The Calcutta High Court's ruling in *J.K. Industries Ltd. v. CIT* (1999) 238 ITR 820, wherein it was held that the Revenue has no jurisdiction to make an adjustment of a refund without following the provisions section 245 and without giving prior intimation to the assessee as required by that section.

High Court's Decision:

In view of the above rulings, the Karnataka High Court, in this case, held that the communication informing the adjustment of refund, without prior intimation to the assessee, is illegal and contrary to law. Therefore, the High Court set aside the order in so far as it relates to adjustment of refund against tax due.