

Section 45 of the Income-tax Act, 1961 Capital gains

Chargeability of Enhanced compensation and interest thereon under Land Acquisition Act are taxable in year of receipt

Commissioner of Income-tax, Faridabad vs. Ghanshyam (HUF), (SC)

The assessee received enhanced compensation on its lands being acquired by Haryana Urban Development Authority (HUDA) as also interest thereon during the previous year relevant to assessment year 1999-2000. In its return of income, he did not offer the amount of enhanced compensation and the interest received thereon during the relevant previous year for taxation, on the plea that the amount of enhanced compensation received had not accrued to the assessee during the year of receipt as the entire amount was in dispute in appeal before the High Court which appeal stood filed by the State against the order of the Reference Court granting enhanced compensation. The amount was received by the assessee in terms of the interim order of the High Court against the assessee's furnishing security to the satisfaction of the executing court. The interest received on enhanced compensation during the previous year was also, according to the assessee, not chargeable to tax on the same plea.

The question before this Court was: whether additional amount under Section 23(1A), solatium under Section 23(2), interest paid on excess compensation under Section 28 and interest under Section 34 of the 1894 Act, could be treated as part of the compensation under Section 45(5) of the 1961 Act?

The Supreme Court held that from Section 45 it is clear that capital gains are not income accruing from day to day. It is deemed income which arises at a fixed point of time, viz, date of transfer. Section 45(5), newly inserted by the Finance Act, 1987, w.e.f. 1.4.88 has two aspects. Firstly, Section 45(5) deals with transfer(s) by way of compulsory acquisition and not by way of transfers by way of sales etc. covered by Section 45(1). Secondly, Section 45(5) talks about enhanced compensation or consideration which in terms of Land Acquisition Act, 1894 results in payment of additional compensation. The scheme of Section 45(5) was inserted w.e.f. 1.4.88 as an overriding provision. Compensation under the L.A. Act, 1894, arises and is payable in multiple stages which does not happen in cases of transfers by sale etc. Hence, the legislature had to step in and say that as and when the assessee/claimant is in receipt of enhanced compensation it shall be treated as "deemed income" and taxed on receipt basis. This understanding is supported by insertion of clause (c) in Section 45(5) w.e.f. 1.4.04 and Section 155(16) which refers to a situation of a subsequent reduction by the Court, Tribunal or other authority and recomputation/amendment of the assessment order. Section 45(5) read as a whole [including clause (c)] not only deals with re- working as urged on behalf of the assessee but also with the change in the full value of the consideration (computation) and since the enhanced compensation/consideration (including interest under Section 28 of the 1894 Act) becomes payable/paid under 1894 Act at different stages, the receipt of such enhanced compensation/consideration is to be taxed in the year of receipt subject to adjustment, if any, under Section 155(16), later on. Hence, the year in which enhanced compensation is received is the year of taxability. Consequently, even in cases where pending appeal, the Court/Tribunal/ Authority before which appeal is pending, permits the claimant to withdraw against security or otherwise the enhanced compensation (which is in dispute), the same is liable to be taxed under Section 45(5). This is the scheme of Section 45(5) and Section 155(16). Even before the insertion of Section 45(5)(c) and Section 155(16) w.e.f. 1.4.2004, the receipt of enhanced compensation under Section 45(5)(b) was taxable in the year of receipt which is only reinforced by insertion of clause (c) because the right to receive payment under the 1894 Act is not in doubt. It is important to note that compensation, including enhanced compensation/ consideration under the 1894 Act, is based on the full value of property as on date of notification under Section 4 of that Act. When the Court/Tribunal directs payment of enhanced compensation under Section 23(1A), or Section 23(2) or under Section 28 of the 1894 Act it is on the basis that award of Collector or the Court, under reference, has not compensated the owner for the full value of the property as on date of notification.

Accordingly, appeal of the Department was allowed.

Section 32 of the Income-tax Act, 1961 – Depreciation

Benefit of depreciation given to the assessee by the AO cannot be withdrawn by the Department

Mcorp Global Private Limited vs. Commissioner of Income Tax, Ghaziabad (Supreme Court)**1st Transaction:**

The assessee carried on the business of trading in lamination machines & binding and punching machines. The assessee had bought 5,46,000 soft drink bottles from M/s Glass & Ceramic Decorators. The bottles were directly supplied to M/s Coolade Beverages Pvt. Ltd. in terms of Lease. The AO found that M/s Coolade had received only 42,000 bottles out of total 5,46,000 bottles receivable by them from the assessee and that the remaining bottles received after 31.3.1991. The AO restricted the depreciation only to 42,000 bottles and consequently disallowed the depreciation of Rs. 18,04,572. In Appeal, the CIT(A) remanded the matter to the AO who on remand held that all 5,46,000 bottles stood paid for and dispatched before 31.3.1991 and, therefore, the assessee was entitled to 100% depreciation. Till date the findings of the

AO (on remand) has not been challenged. When the Appeal (s) came before the Tribunal, it was held that since the lease was not renewed and since the bottles were not returned on expiry, the transaction in question was only a financial arrangement and not a lease, hence, ITAT disallowed the depreciation claim of the assessee.

2nd Transaction:

A lease was executed between the assessee as lessor and 'A' as lessee on 15-03-1991 whereas there was a sub-lease between 'A' and 'U' dated 8-03-1991. An amount of Rs. 30,17,122/- was claimed as depreciation by the assessee. The AO held that since the transaction was not proved by the assessee it was not entitled to depreciation. This finding has been accepted by the Tribunal and the High Court.

1st Transaction:

The Supreme Court observed that the AO has granted depreciation in respect of 42,000 bottles out of 5,46,000 bottles. That benefit is sought to be taken away by the Department, which is not permissible in law. This is the infirmity in the impugned judgment of the High Court and the Tribunal. Hence, the benefit of depreciation given to the assessee by the AO in respect of 42,000 bottles cannot be withdrawn by the Department. Further, on remand the Assessing Officer came to the conclusion that all 5,46,000 bottles stood sold before 31-03-1991 and this finding of the fact has become final as it has not been challenged. Hence, the Department has erred in disallowing depreciation.

However AO was right in coming to the conclusion that transaction dated 15-03-1991 was not proved and the assessee was not entitled to claim depreciation of Rs.30,17,122 in respect of the second transaction.

2nd Transaction:

In the instant case, the tell-tale circumstance against the assessee was that sub-lease dated 8-03-1991 between 'A' (lessee) and 'U' (sub-lessee). This sub-lease precedes the lease dated 15-03-1991 between the assessee (lessor) and 'A' (lessee). As rightly questioned by the AO as to how 'A' (lessee) could have entered into a sub-lease in favour of 'U' bottlers on 8-03-1991 when it had not acquired leasehold rights till 15.03.1991 from the assessee as the lessor. Moreover, there is nothing in the alleged lease deed dated 15.03.1991 indicating commencement of the lease from a prior date. The sub-lease between 'A' (lessee) and 'U' (sub-lessee) it is stated that 'A' is the absolute owner of the bottles and the lessee 'A' shall have no right, title or interest to create a sub-lease without the permission of the lessor. No such permission has been produced. For the aforesaid reasons, it could be held that the transaction dated 15.03.1991 was not proved. Therefore, the AO was right in disallowing depreciation amounting to Rs. 30,17,122/-.

The appeal was partly allowed.

Section 28 read with Sections 22 and 56 of the Income-tax Act, 1961 Business income

Where letting/leasing out of property was part of business object of a concern/person, rental income would be treated as 'business income'

Commissioner of Income Tax, New Delhi vs. D. S. Promoters and st Developers Private Limited, (Delhi).

The assessee received rental income from J&K Bank Limited in respect of its property at Lajpat Nagar, New Delhi and from Total Care (India) Pvt. Ltd. as well as Shivalik Tyres Ltd. in respect of the building in South Extension, New Delhi. The Lajpat Nagar property was directly owned by the Assessee, whereas the South Extension property has been leased out to the Assessee. Both the Commissioner (Appeals) and the Tribunal found that same to be business income. The case of the Revenue was that the income derived by the Assessee from the two properties was taxable as 'Income from other sources'.

The Delhi High Court held that: The fact that the prominent object of the assessee was "to purchase develop, take in exchange or on lease or otherwise acquire lands, houses, farm house, buildings, sheds industrial or otherwise and other fixtures on land and buildings and to let them out on lease, rent, contract or any other agreements as might be deemed fit, or to, construct improve, sell, exchange mortgage lands, houses, flats, sheds, factories sheds and buildings apartments to any person on terms and conditions as might be deemed fit, or to hold, maintain sell, allot, houses apartments, sheds or buildings thereof to the shareholders or to any other person". Even after scrutiny carried out for Assessment Year 1997-1998 to 2000-2001 the receipts were accepted as business income, which was indubitably a plausible view. Since no fresh facts had been brought to light, the consistency rules had been applied. There was no error in this conclusion that the amount received by the assessee from J&K Bank was 'Business income'.

Since the Assessee was not an owner of the South Extension property, it could obviously not have been taxed under the head of 'Income from house property' and, therefore, would have to be assessed under the head 'Income from other sources'. The CIT(A) had also discussed various clauses in the Franchise Agreement in great depth and detail, and had held that the income/commission received by the Assessee from Total Care (India) Pvt. Ltd. was business income. He observed that the premises were chosen by Total Care (India) Pvt. Ltd. firstly because of the location and secondly

because of the large number of walk-ins since a restaurant, as well as a Bar, was being run within the same building; the businesses were complimentary to each other; the appellant had covenanted not to open a competing business; Total Care (India) Pvt. Ltd. relied on the expertise of the assessee with respect to display of goods; the appellant exercised control over the opening and closing of the showroom by Total Care (India) Pvt. Ltd.; since Total Care (India) Pvt. Ltd. could not achieve desirable levels of sales, the Agreement had been terminated. In its place a restaurant by the name of Gourmet Gallery had been opened. The Tribunal had also made an in-depth study of the agreements as also the user to which the entire building in South Extension had been put. It noted that the business of the Assessee, apart from dealing in properties, was also the running of restaurants; that the assessee's purpose was to commercially exploit the business asset, that is, building in South Extension in respect of which it had invested a sum of approximately Rupees 1.3 crores for renovations; that the premises have been earlier utilised to run a store selling garments under the trade name Golden Arch. The thinking of the Tribunal was largely influenced by the manner in which the entire building had been utilised. There was no reason to dislodge the concurrent findings of fact, as there was no perversity in the conclusion arrived at. Accordingly, the amount received by the assessee from Total Care was 'Business income'. So far as another income was concerned, the Assessee had also been in the restaurant business. All throughout the Assessee was also running its own Bar and had even offered the use of its Bar Licence to Shivalik Tyres Ltd., in the event that the latter had failed to obtain its own.

Shivalik Tyres Ltd. was already engaged in the business of restaurant in the name of Orlando at Noida, whilst the Assessee was running Gourmet Gallery. The Assessee had taken a decision to exploit its business assets by entering into an arrangement with Shivalik Tyres Ltd. related to the restaurant business. The fact that the minimum guarantee amount was stipulated in the agreement to ensure the minimum returns of the investment made by the Assessee could as well be a business decision as it could be a lease agreement. Nothing turns on it. These concurrent findings of fact were not perverse and to the contrary, these were relevant. Therefore, the amount received from Shivalik Tyres was business income. The Revenue's appeal was dismissed.

Section 37 of the Income-tax Act, 1961 - Business expenditure - Allowability of
Where standard warranty was required to be given during sell and assessee made provision for warranty which exceeded actual expenditure and excess amount was reversed, claim for deduction under section 37 of said excess amount could not be denied

Rotork Controls India (P.) Ltd. vs. Commissioner of Income Tax (SC)

A provision is a liability which can be measured only by using a substantial degree of estimation. A provision is recognized when: (a) an enterprise has a present obligation as a result of a past event; (b) it is probable that an outflow of re-sources will be required to settle the obligation; and (c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision can be recognized. Liability is defined as a present obligation arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

A past event that leads to a present obligation is called as an obligating event. The obligating event is an event that creates an obligation which results in an outflow of resources. It is only those obligations arising from past events existing independently of the future conduct of the business of the enterprise that is recognized as provision. For a liability to qualify for recognition there must be not only present obligation but also the probability of an outflow of re-sources to settle that obligation. Where there are a number of obligations (e.g. product warranties or similar contracts) the probability that an outflow will be required in settlement, is determined by considering the said obligations as a whole. In this connection, it may be noted that in the case of a manufacture and sale of one single item the provision for warranty could constitute a contingent liability not entitled to deduction under Section 37. However, when there is manufacture and sale of an army of items running into thousands of units of sophisticated goods, the past event of defects being detected in some of such items leads to a present obligation which results in an enterprise having no alternative to settling that obligation.

The assessee-company had been manufacturing and selling Valve Actuators. At the time of sale the assessee provided a Standard Warranty for a period and undertook to rectify or replace the defective part free of charge. This warranty is given under certain conditions stipulated in the warranty clause. The assessee made a provision for warranty at the rate of 1.5% of the turnover. This provision was made by the assessee on account of warranty claims likely to arise on the sales effected by the appellant and to cover up that expenditure. During the assessment year 1991-92, since the provision made was for Rs.10,18,800/- which exceeded the actual expenditure, the assessee reversed Rs.5,00,246 as Reversal of Excess Provision. Consequently, the assessee claimed deduction in respect of the net provision of Rs.5,18,554/- which was disallowed by the revenue on the ground that the liability was merely a contingent liability not allowable as a deduction under Section 37.

The Supreme Court held that Valve Actuators are sophisticated goods. Over the years appellant had been manufacturing Valve Actuators in large numbers. The statistical data indicated that every year some of these manufactured Actuators were found to be defective. The statistical data over the years also indicated that being sophisticated item no customer was prepared to buy Valve Actuator without a warranty. Therefore, warranty became integral part of the sale price of the Valve Actuator(s). In other words, warranty stood attached to the sale price of the product. These aspects were important.

Obligations arising from past events have to be recognized as provisions. These past events are known as obligating events. In the instant case, therefore, warranty provision needed to be recognized because the appellant was an enterprise having a present obligation as a result of past events resulting in an outflow of resources. Lastly, a reliable estimate could be made of the amount of the obligation. In short, all conditions for recognition of a provision were satisfied in this case.

When Valve Actuators were sold and the warranty costs were an integral part of that sale price then the appellant had to provide for such warranty costs in its account for the relevant year, otherwise the matching concept would fail. In such a case the option of making a provision for warranty only when the customer would make a claim was also inappropriate. Under the circumstances, the option of providing for warranty at 2% of turnover of the company based on past experience (historical trend) was most appropriate because it fulfilled accrual concept as well as the matching concept.

For determining an appropriate historical trend, it is important that the company has a proper accounting system for capturing relationship between the nature of the sales, the warranty provisions made and the actual expenses incurred against it subsequently. Thus, the decision on the warranty provision should be based on past experience of the company. A detailed assessment of the warranty provisioning policy is required particularly if the experience suggests that warranty provisions are generally reversed if they remained unutilized at the end of the period prescribed in the warranty. Therefore, one should scrutinize the historical trend of warranty provisions made and the actual expenses incurred against it. On this basis a sensible estimate should be made. The warranty provision for the products should be based on the estimate at year end of future warranty expenses. Such estimates need reassessment every year. As one reaches close to the end of the warranty period, the probability that the warranty expenses will be incurred is considerably reduced and that should be reflected in the estimation amount. Whether this should be done through a pro rata reversal or otherwise would require assessment of historical trend. If warranty provisions are based on experience and historical trend(s) and if the working is robust then the question of reversal in the subsequent years, may not arise in a significant way.

On the facts and circumstances of this case, provision for warranty was rightly made by the appellant enterprise because it had incurred a present obligation as a result of past events. There was also an outflow of resources. A reliable estimate of the obligation was also possible. The appellant had incurred a liability, during the relevant assessment year which was entitled to deduction under Section 37. Therefore, all conditions for recognizing a liability for the purposes of provisioning stood satisfied in this case. It is important to note that there are four important aspects of provisioning. They are - provisioning which relates to present obligation, it arises out of obligating events, it involves outflow of resources and lastly it involves reliable estimation of obligation.

The present value of the contingent liability like the warranty expense, if properly ascertained and discounted on accrued basis, could be an item of deduction under Section 37. The principle of estimation of the contingent liability is not the normal rule. It would depend on the nature of business, the nature of sales, the nature of the product manufactured and sold and the scientific method of accounting being adopted by the assessee. It will also depend upon the historical trend. It would also depend upon the number of articles produced. If it is a case of single item being produced then the principle of estimation of contingent liability on pro rata basis may not apply. However, in the instant case, it was not so. In the instant case large number of items being produced. They were sophisticated goods. They were supported by the historical trend, namely, defects being detected in some of the items. The data also indicated that the warranty cost(s) was embedded in the sale price. The data also indicated that the warranty was attached to the sale price. A liability is a present obligation arising from past events, the settlement of which is expected to result in an outflow of resources and in respect of which a reliable estimate is possible of the amount of obligation.

If the historical trend indicates that large number of sophisticated goods were being manufactured in the past and in the past if the facts established show that defects existed in some of the items manufactured and sold, then the provision made for warranty in respect of the array of such sophisticated goods would be entitled to deduction from the gross receipts under section 37. It would all depend on the data systematically maintained by the assessee. In view of the above, the assessee succeeded.

Section 32 of the Income-tax Act 1961 – Depreciation

Higher rate of depreciation is also admissible when the motor lorry is used by the assessee in his own business of transportation of goods on hire.

Commissioner of Income Tax, Thane vs. S.C. Thakur and Brothers, Raigad (MUM)

Issue before the High Court was whether the assessee, who was only a civil contractor and was not engaged in the business of trucks/ dumpers transportation, would be entitled to depreciation @ 50 per cent and @ 40 per cent for the Assessment Years 1991-91 and 1996-97 on the value of trucks/dumpers owned by him.

The High Court observed that according to circular No. 652 dated 14-06-1997, under sub-item 2(ii) of item No.3 of Appendix 1 to Income Tax Rules, 1962, Higher rate of depreciation is admissible on motor buses, motor lorries and motor taxis used in a business of running them on hire. The higher rate of depreciation is also admissible when the motor lorry is used by the assessee in his own business of transportation of goods on hire. The appeal was dismissed.

Section 37(1) of the Income-tax Act, 1961 – Business Expenditure – Whether allowable

An expenditure can be treated as revenue expenditure, if the expenditure is in respect of an ongoing business of the assessee and there is no enduring benefit.

Commissioner of Income Tax , Mumbai vs. Geoffrey Manners and Company Limited, Mumbai (BOM)

The Respondent assessee has incurred expenditure on film production by way of advertisement for the marketing of products manufactured by them and claimed as revenue expenditure which was disallowed by the Assessing Officer. On appeal, the Tribunal held that the assessee to keep mass interest in its products has to continuously strive to keep on advertising its products in ever increasingly novel ways and methods, through the media and as such the expenditure incurred on the production of the advertisement film was in the nature of revenue expenditure.

The High Court held that if the expenditure is in respect of an ongoing business of the assessee and there is no enduring benefit it can be treated as revenue expenditure. If , however, it is in respect of business which is yet to commence, then the same cannot be treated as revenue expenditure , as the expenditure is on a product yet to be marketed.

The appeals were dismissed.

Section 37(1) of the Income –tax Act, 1961 – Business Expenditure – Whether allowable

Corporate membership fee is eligible for deduction under section 37(1)

Commissioner of Income Tax vs. Samtel Color Limited (DEL)

Corporate membership fee paid by the assessee was disallowed by the revenue. The Tribunal allowed the claim by the holding that there was no reason to disallow the expenditure either wholly or in part, as the expenses were for business purposes since membership allowed the employees to interact with its customers.

The High Court observed that the true test for qualification of expenditure under section 37 is that it should be incurred wholly or exclusively for the purposes of business and the expenditure should not be towards capital account. In the instant case the admission fee paid towards corporate membership is an expenditure incurred wholly and exclusively for the purposes of business and not towards capital account as it only facilitates smooth and efficient running of a business enterprise and does not add to the profit earning apparatus of a business enterprise.

The appeal was dismissed.

Section 80P of the Income-tax Act, 1961 Deduction in respect of income of Co-operative Societies

Where a co-operative acted as an agent of the Government in distributing State controlled commodities and received "commission", and it was held not entitled to deduction under section 80P(2)(e)

Udaipur Sahkari Upphokta Thok Bhandar Ltd. vs. Commissioner of Income-tax (SC)

The appellant-society was a cooperative society registered under Rajasthan Co-operative Societies Act, 1965. It was running a consumer cooperative store at Udaipur since 1963. The appellant was doing the work of distribution of controlled commodities such as wheat, sugar, rice and cloth on behalf of the Government under the Public Distribution Scheme (PDS) for which it was getting commission. The price, quantity and the person from whom the delivery was to be taken was fixed by the State Government under the relevant State Order. After taking the delivery, appellant stores these goods in its godowns, both owned and rented.

The quantity, price and the FPS to whom the delivery was to be given was fixed by the State Government. According to the appellant, the above modus operandi indicates that the State Government exercises total control over the stock of controlled commodities stored in the godowns of the appellant-society. In its returns for assessment year 1989-90, the appellant claimed deduction under Section 80P(2)(e) on the income of commission received by it from the Government for storage of controlled commodities. The A.O. disallowed the claim on the ground that the appellant-society was a wholesaler of foodgrains and it was not a mere stockist as claimed.

The issue which arose for determination was as to whether, "commission" received by the appellant from the State Government was really in the nature of payment for the letting of the godowns maintained by the appellant for storage. The Supreme Court held: Under section 80P(2)(e), an assessee is entitled to claim special deduction from its gross total income to arrive at total taxable income. The assessee has to establish that exemption is available in respect of income derived from the letting of godowns or warehouses, only where the purpose of letting is storage, processing or facilitating

the marketing of commodities. If the godown is let out (including user) for any purpose besides storing, processing or facilitating the marketing of commodities, then the assessee is not entitled to such exemption.

On the distinction between contract of sale and contract of agency there is no straight-jacket formula. However, some important circumstances do bring out the effect of the transaction. The income derived by the cooperative society for the purpose of exemption under clause (e) must be relatable to the letting out or the use of its godowns for any of the three purposes mentioned in clause (e). Any income derived by the society unconnected with such letting or use of the godowns would not fall under clause (e). The High Court was right in coming to the conclusion that the assessee was storing the commodities in question in its godowns as part of its own trading stock and, hence it was not entitled to claim deduction for such margin under section 80P(2)(e).

In every case of this nature one has to examine the contract between the parties. One has also to examine the conduct of the parties. The instant case was concerned with Rajasthan Foodgrains & Other Essential Articles (Regulation of Distribution) Order, 1976. The instant case was concerned with statutory or compulsory sales. Each contract has to be interpreted on its own terms. In the case there are two sales. The first sale was between the Government (through FCI) and the appellant-society, and the second sale was between the appellant-society and Fair Price Shop. The former was the condition precedent to the latter. The issue price was set-off against the sale price which clearly indicates that the netting/difference between the two prices constituted receipt on a commercial basis or net profit. Lastly netting/difference also indicated that the appellant had treated the stock as its own trading stock. Consequently, the appellant was not entitled to exemption/special deduction under Section 80P(2)(e).

Thus, appeal filed by the assessee was dismissed.

Section 41 of the Income-tax Act, 1961

Profits chargeable to tax Taxability of balancing charge of items costed less than Rs. 5,000 prior to and after amendment by Finance Act (No. 2) Act, 1995 with effect from 1-4-1995

Nectar Beverages Pvt. Ltd. vs. Deputy Commissioner of Income Tax (SC)

The assessee who is the manufacturer of soft drinks, purchased bottles and crates, each item of which costed less than Rs. 5,000. During relevant assessment years 1990-91 to 1998-99, the Department sought to tax the sale proceeds of the 100% depreciated written off assets as the business income of the assessee under Section 41(1).

The Supreme Court held that section 41 falls under Chapter IV which deals with computation of business income. Section 41(1) has remained unchanged, both, before 1.4.1988 and even after 1.4.1998. Section 41(2), however, stood deleted between assessment years 1988-89 and 1998-99 for about ten years. Under Section 41(1), where any allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee, and subsequently during any previous year the assessee had obtained, such loss or expenditure in respect of such trading liability by way of remission or cessation thereof, the amount obtained by him, shall be deemed to be income of that previous year in which the recoupment takes place. Prior to 1.4.1988, Section 41(1) and Section 41(2), both, existed on the statute book. Section 41(2) specifically brought to tax the balancing charge as a deemed income under the 1961 Act. It stated that where any plant owned by the assessee and used for business purposes was sold, discarded or destroyed and the moneys payable in respect of such plant exceeded the written down value, then, so much of the surplus which did not exceed the difference between the actual and the written down value was made chargeable to tax as business income of the previous year in which moneys payable for the plant became due. In other words, section 41(2) made the balancing charge taxable as business income. If the argument of the Department of reading the balancing charge under Section 41(2) into Section 41(1) was to be accepted then it was not necessary for Parliament to enact Section 41(2) in the first instance. In that event, Section 41(1) alone would have sufficed. Section 41(1), Section 41(2), Section 41(3) and Section 41(4) operated in different spheres. One more aspect needs to be highlighted. Each of the sub-sections to Section 41 deals with different and distinct circumstances. For example, Section 41(1) deal with recoupment of trading liability. Section 41(2) dealt with the balancing charge. Section 41(3) specifically deals with balancing charge in respect of assets relating to scientific research whereas Section 41(4) deals with recovery of bad debts earlier allowed. Therefore, each of the subsections deal with different and distinct topics and one cannot read recoupment under one sub-section into another.

The entire controversy would stand resolved if one understands the meaning of "balancing charge". Where any allowance or deduction had earlier been made in respect of any loss, expenditure or trading liability and subsequently the assessee has obtained or realized any amount towards such loss, expenditure or trading liability, Section 41(1) deems such realisation/recoupment as assessee's income for the year in which it is realised. Section 41(2) as it stood at the material time stated that if in respect of any plant and machinery, any depreciation had been allowed and subsequently such plant

and machinery was sold, discarded or destroyed, the assessee might get some value either as a result of sale or insurance or from salvage or compensation thereabout. The necessity to keep Section 41(2) as a provision in addition to Section 41(1) arose from the fact that, in its very nature, depreciation is neither a loss, nor an expenditure, nor a trading liability, referred to in Section 41(1). The depreciation recovered on sale of the capital asset was includible in the total income as balancing charge only under Section 41(2). That concept was foreign to the scheme of Section 41(1). The balancing charge under Section 41(2) arose only where any depreciable asset (building, machinery, plant or furniture) was sold. In fact, when the concept of "block of assets" stood introduced w.e.f. 1.4.1988, Section 41(2) stood deleted. However, even after 1.4.1988, the proviso to Section 32(1)(ii) continued till 1.4.1996 when by the Finance (No. 2) Act, 1995 the bottles and crates even below Rs. 5,000 came within the "block of assets" as defined under Section 2(11).

By the above Finance (No. 2) Act, 1995, the first proviso to Section 32(1)(ii) stood deleted w.e.f. 1.4.1996. Consequently, bottles, crates and cylinders whose individual cost did not exceed Rs. 5,000 also came to be included in the block of assets. In *M/s. Cron Bottling Company Pvt. Ltd. vs. ACIT* [Civil Appeal Nos. 356-357 of 2006], the sale proceeds relating to bottles and crates purchased after 1.4.1995 were taken into consideration for the purpose of computation of short term capital gains under Section 50 whereas the sale proceeds relating to bottles and crates purchased prior to 31.3.1995 was not offered for short term capital gains on the ground that the assets stood depreciated at 100% under the proviso to Section 32(1)(ii) and hence did not form part of the block of assets.

It was, thus, clear that, bottles and crates purchased prior to 31.3.1995 did not form part of the block of assets and, hence, profits on sale of such assets were not taxable as a balancing charge, neither under Section 41(1) nor under Section 50. In respect of bottles and crates purchased after 1.4.1995, on account of deletion of proviso to Section 31(1)(ii) (vide Finance Act, 1995) such bottles and crates formed part of block of assets and, consequently, such assets purchased after 1.4.1995, in this case, became exigible to capital gains tax under Section 50.

Thus, the assessee succeeded.

Section 68 read with Section 143 of the Income –tax Act, 1961- Cash Credits

Revenue can make addition under Section 68 only if the assessee is unable to explain the credits appearing in its books of accounts.

Commissioner of Income Tax vs. Gangour Investment Limited (DEL).

The assessee filed its income tax return declaring a loss. The Assessing Officer enquired in respect of shareholders as he had noticed that there was an increase in share capital of the assessee to the extent of Rs 1 crore. Out of the said Rs 1 crore, Rs 71 lakhs was invested by 'T' accordingly made an addition. This addition was deleted by the Commissioner (Appeals) and that was affirmed by the Tribunal.

The High Court on facts held that the assessment order did not disclose as to how the Assessing Officer had come to the conclusion that funds invested by 'T' were nothing but assessee's own funds which had been routed through the investor expect the bald statement to that effect.

The High Court further held that the Revenue can make addition under Section 68 only if the assessee is unable to explain the credits appearing in its books of accounts. In the instant case the assessee had filed the subscription form of each of the investors in particular 'T'. The said subscription form contained details, which set out not only the identity of the subscribers, but also gave information, with respect to their address, as well as, PAN numbers. Hence, the assessee has been able to discharge its onus in respect of the veracity of the transactions.

The appeal was dismissed.

Section 143 read with Section 147 of the Income-tax Act, 1961- Assessment

Stay of demand during pendency of the appeal

Sinhgad Technical Education Society, Pune vs. P.L Pathade, Pune and others (BOM)

The Petitioner is a trust registered under Section 12A and accordingly its income was exempted. Its registration was cancelled on the basis of seizure of Rs. 1.20 crores as well as some documents from the premises of principal trustee. The registration was restored by the Tribunal on appeal. In the meantime, by assessment orders all dated 7-8-2008, the Assessing Officer made reassessment / assessment for the Assessment Year 1999-2000 to 2006-2007. On appeal, the Commissioner (App-eals) has disposed of the stay applications by directing the petitioners to pay 10% of the demands raised for the Assessment Year 2005-06 and 2006-07 by 30-1-2009 and further directed the petitioner to pay a sum of Rs. 50 lakhs by 27th of every month till the appeals are heard and disposed of.

On writ petition, the High Court held that in the instant case on the basis of the seized documents the findings recorded is that the admissions were granted subject to donation and the donation received has been diverted to the principal trustee and further whether donations were actually received by the petitioner and whether they were recorded in the books or the additions were made by recasting the accounts is the question to be considered by appellate authority at the final hearing of appeals.

The High Court further held that the interest of justice would be met by modifying the order of the Commissioner (Appeals) to the extent that the stay of recovery of tax payable in respect of Assessment Year 2005-06 and 2006-07 to be subject to the petitioner furnishing within a period of four weeks, a bank guarantee in the sum of Rs. 1.50 crore valid till the disposal of the appeals.

The petition disposed of.

Section 148 read with Section 147 and 149 of the Income-tax Act, 1961 read with Section 27 of the General Clauses Act, 1897- Service of Notice

Principal incorporated in Section 27 of the General Clause Act, 1897 can profitably be imported in a case where the sender has dispatched the notice by post with the correct address on it

Mayawati vs. Commissioner of Income Tax, Delhi (Central-I) and Others (DEL)

The Assessing Officer issued notice under Section 147 on ground that he had reason to believe that income of petitioner had escaped assessment. The Respondent issued notice under Section 147/148 on 25-03-2008 which was end-eavoured to serve on petitioner on 29-03-2008 wherein serving officer was informed that petitioner had shifted her residence to Lucknow where it should be delivered. Thereafter notice sent by speed post on 29-03-2008 to Lucknow address and incidentally petitioner had dispatched a letter dated 25-03-2008 to Revenue of her change of address from that of Delhi to Lucknow which was received in office on 31-03-2008. The issue before the Supreme Court was whether notices had been duly issued in name of petitioner.

The High Court held that notice contemplated by Section 147 relates to the furnishing of a return and not to the decision to initiate proceedings under Section 147. Secondly, the period of thirty days (as omitted by Finance Act, 1996) is with regard to the furnishing of the return.

The Court further held that where a statute postulates the issuance of a notice and not its service, a fortiori the presumption of fiction of service must be drawn on the lines indicated in section 27 of the General Clause Act, 1897. The Supreme Court in the case of *V.Raja Kumari -vs- P. Subbarama Naidu AIR 2005 SC 109* held that the principle incorporated in Section 27 can profitably be imported in a case where the sender has dispatched the notice by post with the correct address written on it; then it can be deemed to have been served on the sender unless he proves that it is not really served and that he was responsible for such non-service.

Therefore, the petitioner must be deemed to have been served in New Delhi on 29-03-2008 itself since those were the premises allotted to her by the Government of India in her status as a Member of Parliament.

The petitioner was dismissed.

Section 132 of the Income-tax Act, 1961 Search and seizure

It is not mandate of section 132 or any other provision in Act that reasonable belief recorded by designated authority before issuing warrant of authorisation must be disclosed to assessee

Genom Biotech Private Limited, Mumbai vs. Director of Income Tax, Mumbai (Bom.)

Where revenue had produced before Court the confidential information received by the designated authority as well as the satisfaction note recorded by the designated authority before issuing the warrant of authorization, but had earlier declined to furnish a copy of the satisfaction note to the assessee on the ground that the said note contained the name of the informer and disclosing the name of the informer would seriously prejudice the investigation, it was to be held that it is not the mandate of section 132 or any other provision in the Act that the reasonable belief recorded by the designated authority before issuing the warrant of authorisation must be disclosed to the assessee, and, therefore, the fact that a copy of the information received or the satisfaction note recorded had not been furnished to the assessee could not be a ground to hold that the search and seizure was bad in law.

Section 132 of the Income-tax Act, 1961 Search and seizure

Where information received was that investments made out of funds brought to India represented undisclosed income of petitioner No. 2 and, therefore, designated authority was justified in forming a belief that conditions set out in clause (c) of section 132(1) were satisfied

Genom Biotech Private Limited, Mumbai vs. Director of Income Tax, Mumbai (Bom.)

The information was received that during the period from Financial Year 2001-02 to 2007-08 the petitioner No. 1 had evaded tax by claiming deduction of business expenditure amounting to Rs. 170 crores on the ground that the said amounts had been paid to Cyprus / UK based companies towards marketing and advertisement expenses, but in fact the said amount had been credited by the said Cyprus & U.K. based companies in the private bank account of petitioner No.2 in Cyprus. It was informed that the petitioner No.1 had not paid the tax on the said amount of Rs.170 crores. However, the said amounts had been received by the petitioner No.2 from the Cyprus & U.K. based companies represented the undisclosed income of the petitioner No.2. On discreet enquiry, it was found that the informer as well as the assessee was available at the place mentioned in the written complaint received by the designated authority. On the basis of the preliminary investigation, the designated authority formed a reasonable belief that any delay in taking action might result in removal or destruction of the evidence and accordingly after recording reasons on 13/5/2008 for initiating search and seizure action, issued the warrant of authorisation on 14/15-5-2008.

The High Court held that the prima facie belief formed by the designated authority that the tax evasion can be unearthed by initiating search and seizure action would be in consonance with the provisions of section 132(1).

Where the information was that the tax due to the revenue had been evaded by furnishing fake or exaggerated bills, it would be reasonable to believe that the assessee would not disclose the actual modus operandi adopted for such tax evasion. Similarly, if the information received was that the assessee had received undisclosed income, then it would be reasonable to believe that the assessee would not disclose details of the undisclosed income received. In the instant case, the information received was that the assessee had been manufacturing fake exaggerated invoices and, therefore, the designated authority was justified in forming a belief that conditions set out in clause (b) of Section 132(1) was satisfied. Similarly, the information received was that the investments made out of the funds brought to India represented the undisclosed income of the petitioner No. 2 and, therefore, the designated authority was justified in forming a belief that conditions set out in clause (c) of Section 132(1) were satisfied.

Section 281B of the Income-tax Act, 1961 Provisional attachment to protect revenue

When seized documents showed that director of company was mastermind in siphoning off funds of company to his personal bank account in foreign countries through foreign companies with which he was closely associated, fact that notice under Section 153A as well as order of provisional attachment under Section 281B had been issued on same date would not affect validity of order of such attachment

Genom Biotech Private Limited, Mumbai vs. Director of Income Tax, Mumbai (Bom.)

The incriminating documents seized during the course of search and seizure operation revealed that the payments made by the petitioner No.1 company to Cyprus / UK based companies towards marketing and advertisement expenses were further liable to be paid over to Ukrainian advertising agencies who were in fact supposed to have advertised the product of the petitioner No.1 company in Ukraine. However, the documents revealed that the said Cyprus/UK based companies credited the amounts received from the petitioner No.1 in the private bank account of the petitioner No.2, Director of the petitioner No. 1 company in Cyprus. Moreover, during the course of search, incomplete and / or unsigned invoices of the foreign companies along with their seals / stamps were recovered from the office of the petitioner No.1. These incriminating documents prima facie established that large scale tax fraud had been committed. The petitioner No. 2, director promised that he would explain the entire seized materials but he left for UK and till date the petitioner No. 2, director had failed to furnish requisite information.

The High Court held that invoking Section 281B to protect the interest of revenue could not be faulted. The fact that the notice under Section 153A as well as the order under Section 281B had been issued on the same date would not affect the validity of the provisional attachment, because, under Section 132 it is not mandatory that the proceedings must be pending on the date of invoking Section 281B. Provisional attachment can be levied even in cases where the proceedings are yet to be initiated. Therefore, issuing 153A notice and invoking Section 281B on the same day would not affect the validity of the order passed under Section 281B.

On facts, it could not be said that invoking Section 281B was unreasonable or uncalled for, especially when the seized documents showed that the petitioner No. 2, director was the mastermind in siphoning off the funds of the petitioner No. 1

to his personal bank account in the foreign countries through the Cyprus/UK based companies with which he was closely associated. Whether the petitioner No.2 continued to be closely associated with those companies was yet to be investigated. In these circumstances, attachment of the shares held by the petitioner No. 2, director in his demat account out of the funds brought from the foreign companies could not be faulted.

Section 148 of the Income-tax Act, 1961 - Issue of notice where income has escaped assessment

Where there was no new material in hands of Revenue leading to view that there was reason to believe that income had escaped assessment, instead, case was a classic instance of a change of opinion, notice under Section 148 was to be quashed.

Jal Hotels Company Limited vs. Assistant Dir. of Income Tax (Delhi)

A decision may be right or wrong but that was none of the concern of the subsequent officers. So long as the Assessing Officer has consciously considered the facts, the decision cannot be reopened. It is necessary for new material to come to light in order to justify the issuance of notice under section 148.

In Calcutta Discount Co. Ltd. vs. ITO [1961] 41 ITR 191 (SC) the Constitution Bench opined that if from primary facts more inferences than one could be drawn, it would not be possible to say that the assessee should have drawn any particular inference and communicated it to the assessing authority. An assessee could not be charged with failure to communicate an inference, which he might or might not have drawn. In CIT, Calcutta vs. Burlop Dealers Ltd., 1971 (1) SCC 462 it was held that if the assessee had disclosed his books of account and evidence, from which material facts could be discovered; it was under no obligation to inform the Income-tax Officer about the possible inferences which may be raised against him. It was for the Income-tax Officer to raise such an inference and if he did not do so, the income which has escaped assessment cannot be brought to lay under Section 34(1)(a).

Once the basic or primary facts have been disclosed, the burden to prove that amounts represent undisclosed income of the assessee is on the Revenue. One of the tests prescribed to investigate whether any new material had come to the notice of the officer concerned which material would constitute "reason to believe". This new material was wholly missing in the case in hand.

Where there was no new material in the hands of the Revenue leading to the view that there was reason to believe that income had escaped assessment, instead, the case is a classic instance of a change of opinion, and the impugned notice under Section 148 was to be quashed.

Section 143 of the Income-tax Act, 1961 - Assessment

Assessing Officer should pass an independent order of assessment and Commissioner or other higher authority may have supervisory jurisdiction, but they cannot interfere with functions of Assessing Officer

CIT vs. Greenworld Corporationm (SC)

The Assessing Officer conducted survey and accepted the income returned by the assessee. In the assessment order, the Assessing Officer recorded a noting that he visited the CIT, Simla who glanced through all documents, queries and replies, and the CIT, Simla in presence of Addl. CIT, Solan directed that once the replies were satisfactory, no more information were required. He also noted that as per direction of the CIT, Simla needful was done and approval was received from Addl. CIT, Solan.

The principal question which arose for consideration was as to whether the order of assessment was passed at the instance of the Higher Authority. A question with regard to the propriety on the part of the Commissioner of Income-tax to interfere with the functions of the Assessing Officer was raised, stating that the said order was passed at the dictate of the higher authorities.

The Supreme Court held that the noting of the Assessing Officer was specific. It was stated so in the proceedings sheet at the instance of the higher authorities itself. No doubt in terms of the circular letter issued by CBDT, the Commissioner or for that matter any other higher authority may have supervisory jurisdiction but it is difficult to conceive that even the merit of the decision shall be discussed and the same shall be rendered at the instance of the higher authority who, as noticed hereinbefore, is a supervisory authority. It is one thing to say that while making the orders of assessment the Assessing Officer shall be bound by the statutory circulars issued by CBDT but it is another thing to say that the assessing authority exercising quasi judicial function keeping in view the scheme contained in the Act, would lose its independence to pass an independent order of assessment.

When a statute provides for different hierarchies providing for forums in relation to passing of an order as also appellate or original order; by no stretch of imagination a higher authority can interfere with the independence which is the basic feature of any statutory scheme involving adjudicatory process.

In the instant case, one would be constrained to think that the Assessing Officer had passed an order at the instance of the higher authority which was illegal.

Section 50C read with Section 48 of the Income –tax Act, 1961 – Capital gain – Full value of consideration
Section 50 C has application only to the extent of determining sale consideration for computation of capital gain and it cannot be applied for determining the income under other heads.

Inderlok Hotels Private Limited vs. Income Tax Officer, Mumbai (ITAT-MUM)

Assessee company undertook construction of the residential building .During Assessment Year 2005-06 the assessee sold two flats and shown profit on sale of flats as business income which was accepted by the AO. But in respect of the sale of the two flats, the AO was of the opinion that as the valuation made for the purpose of the stamp duty was more than the sale consideration shown in the sale deeds, hence, in view of the provisions of section 50C, the valuation adopted for the purpose of the stamp duty should be treated as the sale consideration. Accordingly addition was made.

The Tribunal held that basic intention to insert section 50C is for the purpose of determining full value sale consideration for the purpose of computation of capital gains under section 48 of the Act. Section 50C has application only to the extent of determining sale consideration for computation of capital gain under chapter IV-E of the Act and it cannot be applied for determining the income under other heads. Sale of the flats is treated as the business income and not as a capital gain; hence, the provision of the section 50C is not applicable.

Section 56 read with Section 4 and 14 of the Income-tax Act, 1961- Income from other Sources
Interest earned on funds primarily brought for infusion in the business could not have been classified as income from other sources

Indian Oil Panipat Power Consortium Limited vs. Income Tax Officer (DEL)

Issue which arose for consideration of the authorities below was as to the treatment which was to be accorded to the interest earned on monies received as share capital by the assessee which were temporarily put in a fixed deposit awaiting acquisition of land which had run into legal entanglements on account of title. The Assessing Officer had treated the interest as 'income from other sources' whereas the Commissioner (Appeals) had accepted the stand of the assessee that the interest was in the nature of capital receipt which was liable to be set off against pre-operative expenses. On appeal, the Tribunal reserved the decision of the Commissioner (Appeals).

The test which permeates through the judgment of the supreme of the Supreme Court in *Tuticorin Alkali Chemicals and Fertilizers Ltd vs. Cit (1997) 227 ITR 172* is that if funds have been borrowed for setting up of a plant and if the funds are 'surplus and then by virtue of that circumstances they are invested in fixed deposits the income earned in the form of interest will be taxable under the head "Income from other sources". On the other hand the ratio of the Supreme Court judgment in *CIT vs. Bokaro Steel Ltd. (1999) 236 ITR 315* is that if income is earned , whether by way of interest or in any other manner on funds which are otherwise 'inextricably linked' to the setting up of the plant, such income is required to be capitalized to be set off against pre-operative expenses.

On facts, once it is held that the assessee's income is an income connected with business, which would be so in the present case , in view of the findings of fact by the CIT(A) that the monies which were inducted into the joint venture company by the joint venture partners were primarily infused to purchase land and to develop infrastructure – then it cannot be held that the income derived by parking the funds temporarily with Bank, will result in the characters of the funds being changed, in as much as, the interest earned from the bank would have a hue different that that of business and be brought to tax under the head 'income from other sources'.

It is well-settled that an income received by the assessee can be taxed under the head "income from other sources" only if it does not fall under any other head of income as provided in section 14. It is clear upon a perusal of the facts as found by the authorities below that the funds in the form of share capital were infused for a specific purpose of acquiring land and the development of infrastructure, therefore, the interest earned on funds primarily brought for infusion in the business could not have been classified as income from other sources.

The appeals were allowed.

Section 194C of the Income-tax Act, 1961- Deduction of tax at source – Payment to contractors and sub-contractors

Various services rendered by a hotel to its customers would be outside the purview of Section 194C

East India Hotels Limited, Calcutta vs. Central Board of Director Taxes, New Delhi (MUM)

The petitioner No. 1 company operates a number of Five Star Deluxe Hotels all over India. The services rendered by the petitioners apart from boarding and lodging are, providing highly trained / experienced multi-lingual staff, 24-hour service for reception, information and telephones, house-keeping of the highest standard, select restaurants, bank counter, beauty saloon, barber shop, car rental, shopping center, laundry/valet, health club, business center service etc. The issue is whether these services would constitute 'carrying out any work' under Section 194C.

The High Court observed that the word 'carrying out any work' in Section 194C is limited to any work which on being carried out culminates into a product or result. As services rendered by a hotel to its customers do not involve carrying out any work which results into production of the desired object and, therefore, it would be outside the purview of Section 194C.

The petition was allowed.

Section 199 of the Income- tax Act, 1961- Deduction of Tax at source- Credit for tax deducted

Apportionment of tax deducted at source, is to be in the same proportion, as the income earned by the parties (sharing the fruits of the common investment)

Commissioner of Income Tax, Patiala vs. Punjab Financial Corporation (P& H)

In terms of agreement between the respondent and the state of Punjab amounts deposited by the State of Punjab with the respondent are invested by the Punjab Financial Corporation Limited and the income is shared between them in the ratio of 2:1. Whatever income is derived on account of equity dividend, by the aforesaid two sharing parties, is also liable to deduction of tax at source. The afore-stated benefit of deduction on account of tax deducted at source is liable to be in the same ratio in which the parties share the income.

On facts the Court held that there can be no doubt that the credit for tax deduction at source should be available to the Punjab Financial Corporation Limited as also the State of Punjab in the same proportion as their income. Thus apportionment of tax deducted at source, is to be in the same proportion, as the income earned by the parties (sharing the fruits of the common investment). Hence, the Punjab Financial Corporation could claim credit on account of the tax deduction at source in the same proportion as it shares the income from dividend income/ income from preference shares with the State of Punjab.

Section 150 of the Income-tax Act, 1961 – Provision for cases where assessment is in pursuance of an order on appeal, etc.

If there is no proceeding before appropriate authority or if assessment year in question is also not a matter, which would fall for consideration before higher authority, section 150 of the Act will have no application

CIT vs. Greenworld Corporationm (SC)

The provision of Section 150 although appears to be of a very wide amplitude, but would not mean that recourse to reopening of the proceedings in terms of Sections 147 and 148 can be initiated at any point of time whatsoever. Such a proceeding can be initiated only within the period of limitation prescribed therefor as contained in Section 149.

Section 150(1) is an exception to the aforementioned provision. It brings within its ambit only such cases where reopening of the proceedings may be necessary to comply with an order of the higher authority. For the said purpose, the records of the proceedings must be before the appropriate authority. It must examine the records of the proceedings. If there is no proceeding before it or if the Assessment year in question is also not a matter which would fall for consideration before the higher authority, Section 150 will have no application.

Section 32 of the Income-tax Act, 1961- Depreciation**Once spares are considered as emergency spares, assessee can seek capitalization and depreciation****Commissioner of Income Tax-IV, New Delhi vs. Insilco Limited (DEL)**

The question for consideration is whether Tribunal was correct in law in allowing depreciation to the assessee on spare parts?

The High Court observed that expression 'used for the purposes of business' appearing in s. 32 of Income tax Act, 1961 also takes into account emergency spares which even though ready for use are not as a matter of fact consumed or used during the relevant period, as these are spares specific to a fixed asset and will in all probability be useless once the asset is discarded, thus, the concept of passive user which is applied to standby machinery will be applicable to emergency / insurance spares. Once spares are considered as emergency spares required for plant and machinery as found by the Tribunal, the assessee was entitled to seek capitalization of the entire cost of spares amounting to Rs. 1,41,64,495/- and claim depreciation thereon. Assessee was right as found by the Tribunal in claiming depreciation on the entire capitalized cost of spares.

The appeals were dismissed.

Section 32 read with Section 37(1) of the Income-tax Act, 1961- Depreciation [Assessment Year 2000-01]**Allowability of depreciation to certain expenditure relatable to the plant and machinery. Allowability of Corporate Membership paid by the assessee****ACIT, Aayakar Bhavan, Mumbai vs. Indexport Limited, Hindustan Lever House (ITAT-Mum)**

The assessee is carrying on the business of sea food culturing and processing. The issues were whether expenditure incurred by assessee for relocating its machinery in view of the fact that the lease deed of the old premises had come to an end, is capital in nature and whether the claim of the assessee on account of Corporate Membership Fee paid on account of Membership Fee availed by the personnel of the assessee company is to be allowed.

The Tribunal held that in case certain expenditure relatable to the plant and machinery has been capitalized in the hands of the assessee, depreciation is to be allowed on such expenditure as per law.

The claim of the assessee with regard to the Corporate Membership paid on account of Membership availed by the personnel of the assessee company is to be allowed.

Section 37(1) of the Income-tax Act, 1961- Business expenditure**Provision for a liability is amenable to a deduction if there is an element of certainty****Commissioner of Income-Tax-IV, New Delhi vs. Insilco Limited (DEL)**

The question for consideration is whether Tribunal was justified in rejecting appeal of Revenue on the issue of allowance of provision for "Long Service Award" payable by the assessee to its employees. Revenue contended that liability under the 'long service award' scheme of the assessee is contingent as the payment under the same scheme is dependent on the discretion of the management.

Held, if a liability arises within the accounting period, the accounting period, the deduction should be allowed though it may be quantified and discharged at a future date, therefore, the provision for a liability is amenable to a deduction if there is an element of certainty that it shall be incurred and it is possible to estimate the liability with reasonable certainty even though the actual quantification may not be possible as such a liability is not of a contingent nature- Provision was estimated based on actuarial calculations, therefore, deduction claimed by the assessee had to be allowed.

The appeals were dismissed.

Section 263 of the Income-tax Act, 1961 - Revision of orders prejudicial to revenue

An order of Assessing Officer can be interfered suo motu by Commissioner not only when an order passed by Assessing Officer is erroneous but also when it is prejudicial to interests of Revenue; Both conditions precedent for exercising jurisdiction under section 263 are conjunctive and not disjunctive

CIT vs. Greenworld Corporationm (SC)

An Income Tax Officer while passing an order of assessment performs judicial function. An appeal lies against his order before Appellate Authority. A Revision Application would also lie before Commissioner of Income Tax. It is trite that jurisdiction exercised by Revisional Authority pertains to his Appellate jurisdiction.

Section 263 provides for a revisional power. It has its own limitations. An order of the Assessing Officer can be interfered suo motu by the Commissioner not only when an order passed by the Assessing Officer is erroneous but also when it is prejudicial to the interests of the Revenue. Both the conditions precedent for exercising the jurisdiction under Section 263 are conjunctive and not disjunctive. An order of assessment passed by an Income-tax Officer, therefore, should not be interfered with only because another view is possible. The scope of provisions of Section 263 is no longer res integra. The power to exercise of suo motu of revision in terms of Section 263(1) is in the nature of supervisory jurisdiction and same can be exercised only if the circumstances specified therein, viz., (1) the order is erroneous; (2) by virtue of the order being erroneous prejudice has been caused to the interest of the revenue, exist.

Section 43B of the Income-tax Act, 1961- Certain deductions to be only on actual payments

Bottling fees chargeable from assessee under Rules framed under Rajasthan Excise Act, 1950 and interest chargeable on late payment of bottling fees, would not amount to tax, duty, cess or fees and such fees are not covered by section 43B

Commissioner of Income-tax vs. Mcdowell & Co. Ltd., (SC)

Bottling fees chargeable from the assessee producer of IMFL under the Rules framed under the Rajasthan Excise Act, 1950 and interest chargeable on late payment of bottling fees, would not amount to tax, duty, cess or fees within the meaning of Section 43B, so as to attract the said provisions while considering allowability of deduction of such expenses.

The Assessing Officer as well as the Commissioner (Appeals) took stand that the assessee was not entitled to deductions in terms of Section 43B. The amount in question related to payability of excise duty on wastages. The assessee took the stand that the provision for excise duty made on wastage of IMFL in transit which was debited to the customers account and credited to this account did not bring in application of Section 43B. The Income Tax Officer as well as the Commissioner held that the assessee's stand was not acceptable. However, the Tribunal and the High Court decided the issues in favour of the assessee.

The Supreme Court held that section 43B after amendment w.e.f. 1.4.1989 refers to any sum payable by assessee by way of tax, duty or fee by whatever name called under any law for the time being in force. The basic requirement, therefore, is that the amount payable must be by way of tax, duty and cess under any law for the time being in force. The bottling fees for acquiring a right of bottling of IMFL which is determined under the Excise Act and Rule 69 of the Rajasthan Excise Rules, 1962 is payable by the assessee as consideration for acquiring the exclusive privilege. It is neither fee nor tax but the consideration for grant of approval by the Government as terms of contract in exercise of its rights to enter a contract in respect of the exclusive right to deal in bottling liquor in all its manifestations. It would be pertinent to note that the expression now used in Section 43B(i)(a) is "Tax, Duty, Cess or fee or by whatever name called". It denotes that items enumerated constitute species of the same genus and the expression 'by whatever name called' which follows preceding words 'Tax', 'Duty', 'Cess' or 'fee' has been used ejusdem generis to confine the application of the provisions not on the basis of mere nomenclatures, but notwithstanding name, they must fall within the genus 'taxation' to which expression 'Tax', 'Duty', 'Cess' or 'Fee' as a group of its specie belong viz. compulsory exaction in the exercise of State's power of taxation where levy and collection is duly authorised by law as distinct from amount chargeable on principle as consideration payable under contract.

The 'Tax', 'Duty', 'Cess' or 'fee' constituting a class denotes to various kinds of imposts by State in its sovereign power of taxation to raise revenue for the State. Within the expression of each specie each expression denotes different kind of impost depending on the purpose for which they are levied. This power can be exercised in any of its manifestation only under any law authorising levy and collection of tax as envisaged under Article 265 of the Constitution which uses only expression that no 'tax' shall be levied and collected except authorized by law.

It in its elementary meaning conveys that to support a tax, legislative action is essential, it cannot be levied and collected in the absence of any legislative sanction by exercise of executive power of State under Article 73 of the Constitution by the Union or Article 162 of the Constitution by the State. Under Article 366 (28) of the Constitution, "Taxation" has been

defined to include the imposition of any tax or impost whether general or local or special and tax shall be construed accordingly. "Impost" means compulsory levy. The well known and well settled characteristic of 'Tax' in its wider sense includes all imposts. Imposts in the context have following characteristics:

- (i) The power to tax is an incident of sovereignty.
- (ii) 'Law' in the context of Article 265 means an Act of legislature and cannot comprise an executive order or rule without express statutory authority.
- (iii) The term 'Tax' under Article 265 read with Article 366(28) includes imposts of every kind viz., tax, duty, cess or fees.
- (iv) As an incident of sovereignty and in the nature of compulsory exaction, a liability founded on principle of contract cannot be a "tax" in its technical sense as an impost, general, local or special.

The Supreme Court has in the light of decisions starting from State of Bombay v. F.N. Balsara (AIR 1951 SC 318) held that the expression "fee" is not used in the State excise laws or rules in the technical sense of the expression. By 'licence fee' or 'fixed fee' under excise laws relating to potable liquors/ intoxicant means the price or consideration which the Government charges to the licences for parting with its exclusive privilege and granting them to the licencees. There is no fundamental right to do trade or business in intoxicants. The State under its regulatory powers has the right to prohibit absolutely every form of activity in relation to intoxicants, its manufacture, storage, export, import, sale and possession in all their manifestations these rights are vested in the State. It is the duty of revenue authorities to ascertain whether the deduction which is to be tested on the touch stone of section 43B(a) in the amount payable is by way of tax or duty or fees or cess. The amount in the instant case did not fall within the purview of section 43B

Section 43B of the Income-tax Act, 1961 – Certain deductions to be only on actual payments.

Furnishing of bank-guarantee is not same as making actual payment as required under section 43B

Commissioner of Income-tax vs. Mcdowell & Co. Ltd., (SC)

The question arose as to whether unpaid amount of bottling fee, on furnishing of bank guarantee, is to be treated as actual payment and previous section 43B would be applicable.

The Supreme Court held that the requirement of Section 43B is the actual payment and not deemed payment as condition precedent for making the claim for deduction in respect of any of the expenditure incurred by the assessee during the relevant previous year specified in Section 43B. The furnishing of bank guarantee cannot be equated with actual payment which requires that money must flow from the assessee to the public exchequer as required under Section 43B. By no stretch of imagination it can be said that furnishing of bank guarantee is actual payment of tax or duty in cash. The bank guarantee is nothing but a guarantee for payment on some happening and that cannot be actual payment as required under Section 43B for allowance as deduction in the computation of profits

Section 2(ea) of the wealth-tax Act, 1957 read with section 40 of the Finance Act, 1983 – assets

If the asset is not used but given on lease, then the asset would be considered for computing net wealth

Anand Estate Private Limited vs. Deputy Commissioner of Income Tax (MUM)

The assessee is in the business of warehousing. The Tribunal held that the godowns in question were given on rent for both assessment years under appeal as such occupied by the lessee for their business and were not occupied by the appellants for their business. Hence the value of the godowns is to be included in the net wealth of the assessee. The issue is whether merely because the rental income derived therefrom was shown under the head "Income from House Property", it becomes the asset of the appellant.

The High Court observed that it is only the building or land appurtenant thereto other than building or part thereof used by the assessee for the purpose of his building or as residential accommodation for his employees and the like which would be excluded. If the asset is not used but given on lease, then the asset would be considered for computing net wealth. As the business of the assessee is of running a warehouse, the building would not fall within the expression "asset" for the purpose of computing net wealth. Once there be a specific provision in so far as closely held company is concerned which deals with the expression "asset" then the general definition would be excluded. In this case admittedly the assessee is closely held company and as such for the purpose of computing net wealth it will be the provisions of sections 40(3) of the Finance Act, 1983 which are relevant

The appeals were dismissed.

International Taxation***IKEA Trading (Hong Kong) Ltd A.A.R. No. 771 of 2008 (2008 TIOL 23)***

The applicant, Ikea Trading (Hong Kong) Limited (ITHKL), a non-resident under the Income-Tax Act, 1961, is a company incorporated in Hong Kong. ITHKL is part of the Ikea Group ('Ikea'), which is a multinational retailer of furniture and home furnishing products doing business under the brand name IKEA. Ikea purchases its products from suppliers worldwide including India. For purchase from India, right has been granted to ITHKL.

ITHKL has setup a Liaison Office (LO) in New Delhi for the purpose of undertaking liaison activities in connection with purchase of goods from India. The LO does not buy or sell the goods itself, it only facilitates the purchase of goods by the applicant at Hong Kong from the Indian suppliers. Orders are placed by ITHKL on Indian suppliers, who supply the goods directly to Ikea Group distribution outlets at Belgium and other countries. Payment for the purchases is made by the centralized payment facility of the Ikea Group in Switzerland.

The main issue before the AAR was "whether any income can be deemed to accrue or arise in India to the LO / ITHKL in view of clause (b) to Explanation 1 to Section 9(1)(i) of the Act under which no income shall be deemed to accrue or arise in India to a non-resident through or from operations confined to the purchase of goods for the purpose of export".

The AAR following its earlier decision in the case of Mushtaq Ahmed (307 ITR 401), held that ITHKL, the applicant, does not earn any income in India because its activities are confined to the purchase of goods which are exported by Indian vendors to the applicant or its nominees. Since the applicant does not effect any sales in India no income accrues or arises in India. No income can be attributed to the purchase operations in India by resorting to the deeming fiction under Section 9(1)(i) because the Explanation thereto excludes such attribution. Clause (b) of Explanation 1 acts as an embargo against attributing any income to the purchase operations carried out in India, if such purchases are for the purpose of export.

Section 5 read with Section 9 of the Income-tax Act, 1961- Total income- Accrual of Where applicant does not earn any income in India because its activities are confined to the purchase of goods, which are exported by the Indian vendors to the applicant or its nominees**Ikea Trading (Hong Kong) Ltd., Hong Kong, In Re (AAR)**

Applicant is a company incorporated under the laws of Hong Kong and is a tax resident of Hong Kong. Applicant has established a liaison office in New Delhi for the purpose of undertaking liaisoning activities in connection with purchase of goods from India. The questions for consideration are (i) whether any income would accrue or arise or deemed to accrue or arise in India in terms of section 5(2)(b) of income-tax Act, 1961; (ii) Whether various activities carried out by liaison office of applicant in India is covered under the phrase 'through or from operations which are confined to the purchase of goods in India for the purpose of export's as used in part (b) of explanation 1 to Section 9(1)(i); and (iii) Whether the whole or any part of applicant's income (if so what part) is liable to be taxed in India.

While arriving at the deemed income accruing or arising directly or indirectly through a business connection in India, no part of the income shall be attributed to the operations limited to the purchase of goods for the purpose of export. It was held that there was no material to hold that the applicant received service fee or commission from its sister concerns and that no sale price was received by the applicant. The applicant does not earn any income in India because its activities are confined to the purchase of goods, which are exported by the Indian vendors to the applicant or its nominees. Admittedly, the applicant does not effect any sales in India. Thus, no income accrues or arises in India.

The next point is, no income can be attributed to the purchase operations in India by restoring to deeming fiction under Section 9(1)(i) because the Explanation thereto excludes such attribution. While arriving at the deemed income accruing or arising directly or indirectly through a business connection in India, no part of the income shall be attributed to the operations limited to the purchase of goods for the purpose of export. In the instant case, the activities set out by the applicant are all in relation to and integrally connected with purchases and hence fall within clause (b) of Explanation 1. The fact that actual export is done by the Indian seller does not detract from the position that the goods purchased by the applicant through the aegis of its liaison office were meant to be exported. The intimate and perhaps inextricable link between purchase and export is an undeniable fact. The result is, if the applicant's case falls under the substantive part of the charging provision contained in Section 9(1)(i), Explanation 1 (b) comes to the rescue of the applicant. It is then not possible to attribute or apportion any income on account of purchase operations. Thus, either from the standpoint of Section 5(2) or Section 9(1)(i) read with Explanation 1(b), it cannot be said that the applicant can be brought within the net of taxation under the Income-tax Act, 1961.

JDIT vs. Krupp Uhde GmbH [2009] 28 SOT 254 (Bom.)

The assessee, Krupp Udhe GmbH, Germany (Krupp), is a company incorporated in Germany. It is engaged in providing (i) technical know-how/licence, (ii) basic engineering services and (iii) supervisory activities in connection with construction or installation of specified machineries/assembly provisions. During the A. Y. 1998-99 & 1999-00, it earned income from various projects and supervisory activities. Apart from this it also received interest from the Income-Tax Department. It offered the income to tax @ 10% as per Article 12 and Article 11, respectively, of the IndiaGermany DTAA (DTAA).

Appeals had been filed by Krupp as well as the Income-Tax Department. The order of the ITAT covers appeal filed by both. The Tribunal answered the various questions raised before it as under:

1. Whether the overall period for rendering supervisory activities should be clubbed together while determining the existence of a Permanent Establishment (PE) or each contract should be considered separately?

Held Various projects/sites which are independent of each other and have no interconnection whatsoever should not be considered together while computing the minimum period of six months as prescribed in Article 5(2)(i) of the Tax Treaty. In case, the activities of one project are dependent on certain other projects, then the minimum period may be computed from the date the first activity commenced. However, where different projects are not interdependent on each other, then the period of six months would be counted in respect of each activity separately.

2. Date from which period for determining existence of PE would commence from the date when the supervisory activity commenced or from the date when the site/construction commenced?

Held Where initially only supervisory activity is being carried out under a separate and independent contract, the minimum period of six months would commence only when such activity itself had commenced and not from the date of the commencement of the project.

3. Whether only the actual days of stay of the technicians, excluding the intervening period, would be considered while counting the period of six months?

Held Once an activity commenced it continued till its completion and any intervening period cannot be excluded while computing the threshold limit. The tax payer should have offered to tax the amount received by it from an Indian company in respect of deputing its two technicians for inspection of equipments supplied by it as the same amounted to FTS. Further, it was held that as reimbursement of expenses does not result in any income per se, therefore, the same could not be taxed under Article 12 of the Tax Treaty.

4. Whether period under Article 5 should be calculated with reference to each financial year?

Held The threshold time limit for a project should be computed from the date the first activity commenced and ending on the completion of the contract and any intervening period cannot be excluded there from. Further, such period has to be counted activity-wise irrespective of the financial years involved therein.

5. Whether tax is payable in respect of fees for technical services where there is no PE in India?

Held The fees received by the assessee from an Indian company in respect of deputing its two technicians for inspection of equipments supplied by it amounted to FTS and the same should have been offered to tax by it. However, it was held that as reimbursement of expenses did not result in any income per se to the assessee, the same could not be taxed under Article 12 of the Tax Treaty.

Section 245R read with Section 9 of the Income-tax Act, 1961-Advance ruling – Procedure on receipt of application***Microsoft Operations Pte. Ltd., In Re (AAR) 27th February 2009***

Applicant is a company incorporation in Singapore. The question for considerations are (i) Whether payments received by MOL Corporation (MOLC) from applicant for functions performed in Singapore under license agreement granting manufacturing and distribution rights to applicant are in nature of 'royalty income' sourced and arising in India and taxable in India under provision of section 9(1)(vi) of Income-tax Act, 1961 and/or provisions of DTAA between India and USA from which tax is required to be withheld by applicant?, (ii) Whether under arrangement payments made by independent Indian distributors to Microsoft Regional Sales Corporation ('MRSC') should be regarded as licensing revenues accruing to

MOLC which are taxable as 'royalty income under provisions of section 9(1)(vi) of Act and/or provisions of DTAA between India and USA , from which tax is required to be withheld by applicant?

It was held that tax withholding issue can only be determined by recording a finding on liability of MOLC to pay income tax in India in respect of income derived by it under relevant agreements to which applicant is also a party. The obligation of applicant to withhold tax at source cannot be decided de hors issues raised concerning liability of MOLC. The findings of appellate authority in Gracemac's appeals and outcome of further appeal to Tribunal will have inevitable bearing on question raised in present application.

It was further held that definition of 'advance ruling' is given in clause (a) of Section 245-N, definition of 'applicant' is in clause(b). The manner of making application is set out in Section 245Q. Section 245-R lays down "procedure on receipt of application". The eligibility criteria for being an applicant and scope and parameters of advance ruling are set out in definition clause. Unless advance ruling sought conforms to said provisions in definition clause, Authority cannot proceed to consider application. Then comes sub-section (2) of section 245R. The language clearly admits of an element of discretion to this statutory body while passing an order u/s 245R(2). Going by clear language, discretion is implicit in provision. Each one of clauses in Proviso operates as a legal bar to entertainment of application and hearing same on merits. Authority is precluded from 'allowing' application if application is hit by any of embargoes laid down in proviso. It is not open to Authority to ignore legal bar created by proviso notwithstanding discretion conferred on Authority in apparently wide terms under main provision i.e, sub-section (2). However, it does not follow that application is bound to be admitted and heard on merits once factors set out in proviso do not come in way of admission. The proviso Section 245-R(2) does not have effect of taking away discretion to reject application on other unspecified grounds.

It was held that on basis of facts, it is not possible to draw an inference on a prima facie consideration that question raised in application "arises out of a transaction designed prima facie for avoidance of income tax". The resultant effect of transaction by itself is not determinative of applicant's design to avoid tax. Moreover, when department itself did not set up such a case in assessments made against Gracemac and MRSC, Court cannot say on basis of material available, that there was no real commercial purpose behind post-1998 transactions/ arrangements. Hence objection of Revenue on this aspect is over-ruled.

The application is rejected.

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