Legal Decisions

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INCOME-TAX

1. *CIT v. Vallabh Leasing and Finance Co. Pvt. Ltd. (2004) 265 ITR 1 (MP)*

On the facts of the case the Assessing Officer was of the opinion that the assessee was resorting to a tax avoidance measure and wanted to apply the provisions of section 94. *The High Court applied its own earlier decision in CIT v. Sakar Lal Balabhai [1968] 69 ITR 186.* The ratio in the case was that the avoidance of tax must be exceptional, i.e. by way of exception to the normal practice of the assessee and it should not be systematic i.e. part of a regular reprehensive practice carried on by the assessee. The Court held that there had been no systematic efforts by the assessee to avoid the tax. It had been done only once. In the absence of any kind of regular transaction or recurrent transaction the provisions of sub-section (1) and (2) of section 94 were not attracted.

2. *Kerala Shipping Corporation Ltd. v. CIT (2004) 265 ITR 13 (Ker)*

In this case the assessee company owned a ship which was reported to be missing when on the high seas. The assessee claimed the insurance money. The Assessing Officer assessed the difference between the original cost and the written down value of the ship under section 41(2) [now not in the Statute book]. He held that the actual total loss presumed under section 58 of the Marine Insurance Act would amount to "destruction" as the term had been used in section 41(2) of the Act. The Tribunal held that the disappeared ship which was not recovered till date could be considered as destroyed and the provisions of section 41(2) were attracted. However, the High Court held that It could not be said that the ship was destroyed as there was no evidence for that. Missing does not mean destroyed. Section 41(2) was not therefore applicable. The provisions of section 41(2) dealing with balancing charge are no more in the Statute book. However, the case is interesting. A related issue in this context is whether the insurance moneys received would come within the scope of section 45(1A).

3. *CIT v. Rajendranathan Nair (2004) 265 ITR 35 (Ker)*

The assessee was an individual deriving income mainly from the business as a cashew exporter. He was collecting charges from other concerns for processing of their raw nuts in his factories. The assessee claim was that though the processing charges formed part of the income the same cannot be included in the total turnover while working out the deduction under section 80HHC. The Assessing Officer felt that the processing charges should be included in the turnover when the same was includible in the business profit. The CIT (Appeals) agreed. However, the Tribunal accepted the contention of the assessee. The High Court held that processing charges received from third parties do not form part of the "turnover" even under the provisions of the Kerala General Sales Tax Act for that Act is attracted only in a case where there is sales of goods. The assessee had processed raw cashew nuts belonging to third parties in his factory and had only collected the processing charges. The processing charges received by the assessee could not be included in the definition of total turnover in clause (ba) of the Explanation to section 80HHC. The provisions of clauses (iiia), (iiib) and (iiic) of section 28 did not alter the position.

4. *National Federation of Insurance Field Workers of India and Another v. Union of India and Others [2004] 265 ITR 84 (Uttar)*

The Central Board of Direct Taxes issued a notification dated September 25, 2001 stating that tax free/concessional educational facilities, leave travel concession, interest free loan/concessional loan given by an employer to its employees, free meals, club members, club expenditure etc. would be considered to be perquisites w.e.f. April 1, 2001. The rule was placed before Parliament as indicated by the Income-

tax (Twenty Second Amendment) Rules, 2001 w.e.f. April 1, 2001. Section 17(2) was introduced by the Finance Act, 2001 w.e.f. April 1, 2002. Hence it covers A.Y. 2002-03 relevant to the accounting year ending on March 31, 2002. The constitutional validity of the notification was challenged on the grounds that the notification was arbitrary and was operational retrospectively. The Court held that the notification is not vague or arbitrary. The notification is in accordance with sections 295(2)(c) and 296(1) of the Income-tax Act. It is valid.

5. CIT v. C.P. Lonappan & Sons (2004) 265 ITR 101 (Ker)

The assessee's land was acquired by the State Government for widening the National Highways pursuant to a declaration made on October, 11, 1991. On August 30, 1991, the assessee got a sum of Rs.27,08,000 as advance towards compensation payable for the acquisition of the land. Later, the Land Acquisition Officer passed the award on December 18, 1992. Under the award, the assessee became entitled to get a total sum of Rs.38,11,604 by way of compensation. After adjusting the advance payment, the balance amount was paid to the assessee on January 11, 1993. The Assessing Officer took the view that the entire compensation received by the assessee should be subjected to capital gains tax in the assessment year 1992-93. However, according to the Tribunal, by virtue of the provisions of section 45(5)(a) of the Act, the advance payment of Rs.27,08,000 had to be assessed in the year of receipt, that is in the assessment year 1992-93, and the balance consideration under the award had to be assessed in the assessment year 1993-94, since the same was received on January 11, 1993. The High Court held that it was clear that it was the transfer of the capital asset, which attracted liability to capital gains under section 45. For understanding when transfer takes place in the case of compulsory acquisition we have to look to the provisions of the Land Acquisition Act, 1894, itself. From a reading of sections 11 and 12 of the Land Acquisition Act, it is clear that the transfer is effective only on the passing of the award and on surrendering the documents of title and on getting the award amount. It held that the entire award amount (Rs.27,08,000 and Rs.9,23,219) had to be assessed only during the assessment year 1993-94. However, though the Tribunal had held that the advance payment of Rs.27,08,000 had to be assessed in the year of receipt, the assessee had not come up in appeal. In the above circumstances, the finding of the Tribunal that the sum of Rs.27,08,000 must be assessed in the assessment for the year 1992-93 was not to be disturbed.

6. CIT v. Hotel Control Pvt. Ltd. [2004] 265 ITR 109 (Uttar)

The assessee was running a hotel in Mussoorie. It claimed Rs.6,32,718 as revenue expenditure incurred on repairs and maintenance of the building, compound, furniture and maintenance of the hotel. However, the Assessing Officer granted deduction 1,01,718 and he capitalized the balance of Rs.5,31,000 as capital expenditure. The High Court held that the assessee had shown that it was required to incur the expenditure at regular intervals due to weather conditions prevailing in Mussoorie. Hence, the expenditure was in the nature of "current expenditure". It was deductible.

7. Kotak Mahindra Finance Ltd. v. Dy. Commissioner of Income-tax [2004] 265 ITR 114 (Bom)

Entry III of Appendix I to the Income-tax Rules, 1962, *inter alia*, contains the items "motor buses, moor lorries and motor taxies used in a business of running them on hire. Depreciation is available at higher rate if such vehicles are run on hire. The issue was whether the assessee was hiring the vehicles or leasing the vehicles. In the cited case, the assessee was a leasing and financing company. Its income was from lease rent, bill discounting and service charges. Therefore, merely because the assessee let out motor buses, motor trucks and motor vans to its customers, it could not be stated that the assessee was using the said vehicles in the business of running them on hire. Just because higher depreciation was granted by the Department for the earlier years, the Department was not bound to grant higher depreciation for the assessment year 1989-90. Under the Income-tax Act, each year is a separate event of assessment. The principle of re judicata was not available.

8. CIT v. Kotak Mahendra Finance Ltd. (2004) 265 ITR 119 (Bom)

There was a shortfall in payment of advance tax in the

context of computation of income under section 115J (now 115JB). The issue was whether interest could be levied under section 234B and 234C. The High Court held that once it is found that the total income computed under the Act is less than 30 per cent of the book profit and consequent upon this there is non payment or short payment of advance tax then, the provisions of sections 234B and 234C are automatically attracted.

9. CIT v. Catholic Syrian Bank Ltd. (2004) 265 ITR 177 (Ker)

Whether the penal interest paid by banks to the Reserve Bank of India for non-maintenance of cash reserve is interest or penalty? It was held that if the payment is made by the assessee-bank under sub-section (4) or under sub-section (5)(a) of section 42 of the Reserve Bank of India Act in respect of the first default in complying with the requirement imposed under the main part of the section it cannot be treated as a penal provision. However, if the payment relates to the second default or subsequent default such payment has to be treated as penalty for infraction of law.

10. Commissioner of Income-tax v. P. Soman [2004] 265 ITR 197 (Ker)

There was a search in the business premises of the assessee. Consequently, a redemption fine and penalty were levied. The assessee claimed the sums as deductible expenditure because they were compensatory in nature. The Assessing Officer rejected the claim holding that the payment was effected for infraction of law. However, the High Court held that whenever any statutory impost paid by an assessee by way of damages or penalty or interest was claimed as an allowable expenditure under section 37(1), the Assessing authority was required to examine the scheme of the provisions of the relevant statutes providing for payment of such impost notwithstanding the nomenclature of the impost as given by the statute to find out whether it was compensatory or penal in nature.

11. Dhanji R. Zalte v. Assistant CIT (2004) 265 ITR 204 (Bom)

The Assessee was an advocate who claimed to have specialized in land acquisition cases under the Land Acquisition Act, 1894. Search operations were carried out at his residential and other premises during which various incriminating documents and records were seized. A block assessment order was passed. In the said order the Assistant Commissioner had noted that the assessee was guilty of violating the provisions of sections 269SS and 269T of the Act inasmuch as loans as well as deposits in excess of Rs.20,000 were accepted and repaid in cash. Penalty was imposed under section 271E. The High Court upheld the penalty.

12 Indian Shavings Products Ltd. v. CIT (2004) 265 ITR 250 (Raj)

The assessee did not have its own funds sufficient even to run its business and was running in huge losses in the assessment years 1989-90 and 1990-91 but during these years the assessee had borrowed huge amounts from financial institutions and given advances free of interest to its four subsidiaries. For this purpose, it paid interest of Rs.75,83,860 in the assessment year 1989-90 and Rs.73,27,616 in the assessment year 1990-91 and claimed deduction of this interest on the ground that the assessee wanted to have control over another company after purchasing its shares through the subsidiaries. The Tribunal found that it was not the business of the assessee to purchase and sell shares and that it failed to establish that this advance amount had any nexus with the amount it had obtained from the U.K. company free of interest. The High Court held that the order of the Tribunal could not be interfered with.

13. CIT v. Dynavision Ltd. (2004) 265 ITR 289 (Mad)

The assessee company formed a trust and it was the settler. All the dealers of the television sets manufactured by the assessee were the beneficiaries of the trust. The object of the trust were wide and some of the objects were to render financial help to the dealers in case of financial difficulties interest free or at concessional rate of interest, to arrange holiday trips and tours for the recreation of the dealers, to take up publicity campaigns for promoting the sales of dealers, to present gifts in cash or in kind at marriages, birthday functions etc. of dealers and their dependent family members, to benefit dealers and stockists on account of indigence, ill-health or other emergent circumstances,

to take up any work which would help the dealers or stockists achieve common goals like promotion of sales, making their products more competitive, reducing their overheads and making them more useful for the company. A sum of Rs.50 lakhs was paid by the assessee company to the trust. It claimed the same as deductible business expenditure. However, the High Court did not allow it. This case raises interesting issues. By forming a trust the assessee company is trying to get deduction in respect of various disbursements some capital in nature, some revenue in nature and some not at all related to the business. All these categories of disbursements are attempted to be claimed under the cloak of contribution to a trust created for the benefit of the assessee's own dealers. A good tax planning attempt.

14. Tamilnadu Bricks and Tile Manufacturers Industrial Service Cooperative Society Ltd. v. CIT [2004] 265 ITR 332 (Mad.)

In this case the issue was whether purchase bonus payable to the members of the above mentioned cooperative societies Ltd. could be deductible as business expenditure. The Court held that the purchase bonus was really a deferred discount that was paid to the members after determination of the net profits of the cooperative society. Therefore, this expenditure was paid for the business of the assessee and was a business expenditure and was allowable as a business deduction. The Central Board of Direct Taxes in consultation with the Department of Community Development and Cooperation has issued a circular to the effect that rebate or bonus would be in the nature of deferred discount passed on by the consumer cooperative stores to their members and this is an allowable deduction in the computation of income of the cooperative society. Though the circular was issued in the case of consumer cooperative stores, there are no reasons to take a different view that it would not be a deferred discount in the case of other cooperative societies where bonus is paid to the members of the cooperative societies on the value of the purchases made by them during the year

15. CIT v. Saptarshi Services Ltd. [2004] 265 ITR 379 (Guj.)

The controversy as to whether income from a business center should be treated as business or property income was resolved in the above case. It was found after review of the case law on the subject, that the income of a sub-lessee developing the property as a business center and providing various services like provision of lift, services as those of receptionist besides secretarial services, data processing, conference room, etc. with many facilities, has necessarily to be assessed as business income. Special leave against this decision has also since been refused by the Supreme Court [2003] 264 ITR (St.) 36.

16. Jubilant Organosys v. CIT [2004] 265 ITR 420 (All.)

Bad debt is allowed on its being "written off as irrecoverable in the accounts of the assessee" vide section 36(1)(vii) of the Act. Obviously the intention of the Explanation was that where the account of the debtors is squared up in the books, it is tantamount only to a provision. In this case the High Court held that in the light of the amendment, the Commissioner was justified in taking action under section 263 for disallowing the bad debt, which was not squared up. The High Court found that though the assessee had debited it in the profit and loss account, it has not credited the debtor's account. Obviously, it was credited to the provision for doubtful debts. This could not be right in the light of the Explanation.

17 M/s Lalsons Enterprises v. DCIT, New Delhi

A special bench of the Income Tax Appellate Tribunal has decided the three controversies on the issue of computation of deduction under Section 80HHC as under :

1. For the purpose of computing the deduction allowable under the proviso to sub-section (3) of Section 80HHC in respect of the export incentives mentioned in Section 28(iiia), (iiib) and (iiic), the loss, if any,suffered by the assessee under any of the clauses (a), (b) or (c) of the sub-section shall be ignored and the deduction shall be allowed in respect of the amount computed under the said proviso.

2. For the purpose of applying Explanation (baa) below sub-section (4B) of Section 80HHC and

while reducing 90% of the receipt by way of interest from the profits of the business, it is only the 90% of the net interest remaining after allowing a set off of interest paid, which has a nexus with the interest received, that can be reduced and not 90% of the gross interest.

3. For purposes of clause(c) of sub-section (3) of Section 80HHC, the loss arising in either the export of manufactured goods or trading goods shall be set off or adjusted against the profits arising in the other business. In other words, the results of the business of export of manufactured goods and the business of the export of trading goods shall be adjusted against each other.

In view of the above judgement, the controversies before the Tribunal stand settled and the assessee shall be entitled to set off interest expenditure against interest income in case there is nexus between the two. Secondly, for deduction under Section 80HHC, if the profit of the business is negative, the same has to be ignored and the assessee shall be entitled to claim benefit of 90 per cent of export incentive in the ratio of export turnover to total turnover.

Indirect Taxes (Contributed by Ms. Smita Pandey, Executive Officer)

E-Returns

The Central Board of Direct Taxes has issued a press note informing all corporate deductors to file their TDS return in electronic format only. It has been clarified that those companies which have filed their TDS return in paper format after 1st June, 2003, are required to file the TDS return again in the electronic format. The return is to be filed in the revised form No.24, 26 or 27 as the case may be.

18. Commissioner of Customs, Calcutta vs. Indian Oil Corporation Ltd. 2004(165) E.L.T. 257(S.C.)

Whether demurrage charges payable on account of delay in discharging goods from a vessel includible in assessable value?

Indian Oil Corporation Ltd. imported various petroleum products and crude oil into India. It cleared the imported goods by paying customs duty. Demurrage charges were being paid by it on account of delay in discharging goods from the vessel. The company claimed that demurrage charges were not includible in the assessable value based on a Circular issued by the Department. The Supreme Court held that although a circular was not binding on a Court or an assesee, it was not open to the Revenue to raise the contention that was contrary to a binding circular by the Board. When a circular remains in operation, the Revenue is bound by it and cannot be allowed to plead that it is not valid nor that it is contrary to the terms of the statute.

19. Collector of Central Excise vs. Technowled Industries 2003 (155) E.L.T. 209 (S.C.)

Whether the process of drawing wires from wire rods would amount to manufacture if the two of them fall under separate entries of Central Excise Tariff Act, 1985?

The assessee purchased duty paid wire rods and drew the wire into a thinner gauge. The issue for consideration is that since the two items fall under different tariff headings whether the process involved is manufacture thereby attracting excise duty on thinner wires. The Apex Court held that the initial product was a wire rod, the ultimate product is also a wire. All that is done is that the guage of the rod is made thinner and the product is finished a little better. There is no manufacture of a new product. Merely because there are two separate entries does not mean that the product becomes excisable. The product becomes excisable only if there is manufacture. The verdict confirmed the earlier decisions given by the Tribunal on the identical issue in various other cases.

20. Union of India vs. Ahmedabad Electricity Co. Ltd. & Ors. 2003 (111) ECR 274 (SC)

Whether 'cinder', the unburnt or half burnt portion of coal left out in boilers is liable to excise duty?

The assessee used coal as fuel for producing steam to run the machines used for manufacturing the end

product. Coal was burnt in boilers and furnaces to produce steam. Normally coal is reduced to ash when it is burnt in boilers. Some part of it does not get fully burnt because of its low combustible quality. This unburnt or half burnt portion left out in the boiler is called cinder. Department demanded excise duty on such cinder produced by the assessee on the grounds that cinder was an excisable good as it finds a place in Serial no. 26.21 of Chapter 26 of the First Schedule of The Central Excise Tariff Act, 1985. Serial no.26.21 covers "other slag and ash, including seaweed ash (kelp). Further, cinder is exigible to excise duty as it is manufactured as a by-product of coal that emerges in the course of manufacture of the end product. Also, it is marketable as the same is sold by the assessee.

The apex court observed that simply because goods find mention in one of the entries of the First Schedule does not mean that they are liable for payment of excise duty. Goods have to satisfy the test of being produced or manufactured in India. Further, it held that cinder is not ash – it is something between coal and coal ash. On the issue regarding manufacture Supreme Court held that excise duty is an incidence of manufacture and, therefore it is essential that the product sought to excise duty should have gone through the process of manufacture i.e. the raw material should have gone through the process of transformation into a new product by skillful manipulation. In producing cinder there is no manufacturing process involved. Coal is simply burnt as fuel to produce steam. Coal is not tampered with, manipulated or transformed into the end product. Burning of coal for purpose of producing stream cannot be said to be manufacturing activity. From burning coal no new product emerges except cinder or ash that is nothing but the inferior quality of coal itself.

Moreover, coal which leads to production of cinder is not used as a raw material for the end product. It is being used only for ancillary purpose that is as a fuel. Therefore, irrespective of the fact whether any manufacture is involved in production of cinder it should be held to be out of tax net for the reason that it is not a raw material for the end product. As regards the marketability aspect the Court held that since cinder fails the test of being manufactured in India, even if it is saleable, it does not make any difference.

21. J.J. Foam Pvt. Ltd. vs. Commissioner of Central Excise, Ghaziabad 2004 (165) E.L.T. 309 (Tri.-Delhi)

Whether PU Foam sheets cut to size of mattresses with industrial tape affixed on edges classifiable under Heading 94.04 of Central Excise Tariff as mattresses?

The sides of the PU Foam sheets for mattresses were taped with cotton tape as packing to protect the edges from damage. The assessee intended to claim such sheets under heading no. 39.01 meant for foam sheets etc. Department objected to such classification and classified the product under heading no. 94.04 meant for mattresses.

The Tribunal observed that sheets as such were not usable as mattresses as they were liable to be dispersed, disheveled or bulged out or wither out. Sheets were not usable as mattresses unless they were further worked, reinforced or supported on the edges. By the process of reinforcing and support of the edges the sheets had assumed the shape of mattresses. The Tribunal further observed that when the sheets and mattresses are separately described in the tariff, it is the form in which the goods are cleared which is relevant for classification. Therefore, the Tribunal held that the goods in question should be classified under Heading 94.04 as mattresses.

22. ***Surat Bevereages Pvt. Ltd. vs. Commissioner of Central Excise, Surat-I 2004 (165) E.L.T. 313 (Tri.- Mumbai)***

Is an inkjet printer, used to print the date of manufacture, on the products a capital good eligible to Cenvat credit?

The asset in the question was an ink-jet printer used for printing dates of manufacture and sale price on the bottles containing beverages, manufactured and cleared by the assessee. The assessee claimed it to be a capital asset used in the manufacture of the final product and availed Cenvat credit on it. The Tribunal observed that the law required a manufacturer of beverage to print the sale price on the bottles containing them; even the sale of the beverage not bearing the sale price on the container would have been contrary to law. Therefore, it was held by the Tribunal that the printing of price on the bottle of the beverage was a process of manufacture and the ink-jet printer would be considered as capital goods. ■