Legal Decisions[1]

DIRECT TAXES

Income-tax Act

LD/60/59

Millennium IT Software Ltd., In re September 28, 2011 (AAR)

Section 9 read with Section 195 of the Income-tax Act, 1961 read with Section 52 of the Copyright Act, 1957 – Income – Deemed to accrue or arise in India

Without software License and Maintenance Agreement being in place, any usage of computer programme by customers would have amounted to copyright infringement; payment made under said agreement is for obtaining right to use copyright in software and, hence, taxable as royalty under clause (v) of Explanation 2 to section 9(1)(vi)

Under software License and Maintenance Agreement (SLMA) the applicant Sri Lankan company has allowed Indian company ICEL to use the software product owned by it. The Licensed Programme shall be developed and installed into the computer machines designated by ICEL. The applicant is to deploy its personnel to the designated site to train the employees of ICEL. After the installation is over and the software is given a line cutover, the applicant is required to provide at its own cost, maintenance and support services, through telephone, e-mail and facsimile number to fix or bypass programme errors. The license to use the Licensed Programme is for 4 years subject to further renewal.

The Agreement provides for payment of "License Maintenance Fee" which is a fixed amount of Rs. 50 lacs per quarter plus an additional fee based on the utilization of the Licensed Programme by ICEL, so much so that the total amount payable would not exceed Rs. 150 lacs per quarter.

The applicant submits that the 'Implementation fee' and 'Licence and Maintenance fee' are not chargeable to tax as per Income-tax Act, 1961(Act) or under DTAA with Sri Lanka. The providing of maintenance service to ICEL would not create a Permanent Establishment (PE) in India. As the payments are not liable to tax in India, ICEL is not required to withhold any tax under section 195 of the Act and would not be obliged to file a tax return in India.

The Authority for Advance Rulings held that the computer programme is "a set of instructions expressed in words, codes, schemes or *in any other form*". The use of this language signifies the legislative intent to award copyright protection to both the source code and the object code of the computer programme.

As is well understood, the term 'software' is used to describe all of the different types of computer programmes. Computer programme are basically divided into 'application programme' and 'operating system programme'. Application programme are designed to do specific tasks to be executed through the computer and the operating system programmes are used to manage the internal functions of the computer to facilitate use of application programme. These two types of programmes can be written in three levels of computer language-high level, low level and lowest level. High-level language consists of English words and symbols and are easy to learn. Lower-level language is assembly language which consists of alphanumeric labels. This language is also easily understandable by the programmer. Statements of these two languages are referred to as written in *source code*. The third, lowest-level language, is the machine language. This is a binary language using two symbols '0' and '1' called 'bits'. This is the only language which can be followed by the machine but very difficult for the programmer to utilise. Statements in machine language are referred to as written in 'object code'. It is well established that authorship of both the source code and the object code are protected by the Copyright Act as literary work.

The Courts in the USA have been awarding protection to not only the source code and the object code, but in some instances, the same has been extended to even "the overall structure" of a programme. The Trade Related Intellectual Property Rights Agreement (TRIPs) expressly provides that computer programs, whether in source code or object code, shall be protected as literary works under the Berne Convention, 1971, to which India is a party.

It has also come to our notice that during the process of registration of a copyright in a computer programme, the author also files the object code of the software with the Registrar of Copyrights. Hence, there is not an iota of doubt in our mind that both the source code and the object code of a computer programme are awarded copyright protection under the Copyright Act.

Under the SLMA, the program being licensed contains the object code which consists of 'set of instructions' in 'machine- readable medium'. Thus what has been licensed, squarely falls within the

[1] *Readers are invited to send their comments on the selection of cases and their utility at eboard@icai.org.*

definition of computer programme under section 2*(ffc)* and is a copyrightable subject matter. It is clear that the license to use computer Program means right to use the intellectual property that is the copyright in the computer program in a particular way. When intellectual property is licensed, essentially the use of the intellectual property (copyright in the present case) is passed on to another firm.

The phrase 'including the granting of a license' in the definition under section 9 of the Act is only explanatory in nature. It explains the term 'all or any rights in respect of copyright'. It is deemed that all or any rights in respect of a copyright whether under DTAA or the Act should be held to include the grant of a license.

A careful reading of section 52*(aa)* of the Copyright Act will reveal that the clause uses the term "lawful possessor". It thus, carves out an exception for lawful possessors of a computer programme as far as copies or adaptation for personal use is concerned.

The copyright in a software programme may remain with the originator of the programme, but the moment copies are made and marketed, they become 'goods', which are susceptible to sales tax. It is so stated by the Court, because Copyright Act, 1957 and Sales Tax Act are not Statutes in *Pari Materia.* In the case of *Airport Authority of India* [AAR 757-56 of 2007], this Authority has opined that Tata Consultancy decision is not applicable in such cases. The mere fact that customs law or sales tax law deems it to be goods for the purpose of those Act, does not change the inherent character of software. The World Trade Organization has itself recognised goods (GATT), Services (GATS) and intellectual property rights (TRIPS) as distinct and different classes. The purchase of software from reseller is payment for use of intellectual property and not for the purchase of goods, unless the payment falls under the exception provided by the second proviso to section 9(1)(vi) of the Act.

The scope of SLMA extends beyond installation and implementation of the Licensed Program. The maintenance service in respect of the Licensed Program is an integral part of SLMA. As per Schedule-F of SLMA, trading transactions are to be processed using the Licensed Program. After paying the implementation and customization fee, the actual use of the Licensed Program is to begin from 1-1-2010 and will last till 31-12-2014. The payment for each quarter for this period is to be determined on the basis of average trades per day in a quarter. In bifurcating the payments before and after installation and implementation, the nature of the payments remain royalty for the use of the Licensed Program and would not change its character from royalty to business income. If it was to be in the nature of business income then the SLMA would have been sale and service of Licensed Program and the fee paid would have been taxable as business income under Article 7 of the DTAA, depending on whether the applicant has a PE in India or not under Article 5 of the DTAA.

Since without the SLMA being in place, any usage of the computer programme by the customers would have amounted to copyright infringement, the payment made under the SLMA was for obtaining the right to use the copyright in the software and taxable as royalty under the DTAA and the IT Act.

Therefore, Fees paid by ICEL to the applicant is taxable as royalty under clause (v) of *Explanation* 2 to section 9(1)(vi) of the Act. As the fees payable by ICEL to the applicant arise in India, it is taxable under Article 12.2 of the DTAA in India. The applicant does not have a PE in terms of Article 5 of the DTAA. The applicant is taxable on the fees paid by ICEL. The provision of withholding tax under section 195 would apply. As the applicant is liable to tax in India, it is required to file a return of income under the provision of the Act.

LD/60/60

Director of Income-tax, International Taxation, Bangalore

Vs.

Mrs. Jennifer Bhide

September 26, 2011 (KAR)

[Assessment Year 2007-08]

Section 54 read with section 54EC of the Income-tax Act, 1961 – Capital Gains – Profit on sale of residential property

To attract section 54 and section 54EC, what is material is the investment of sale consideration in acquiring residential premises or constructing a residential premises or investing amounts in bonds set out in section 54EC; once the sale consideration is invested in any of these manner the assessee would be entitled to benefit of these provisions; there is no express provision contained in these sections that investment should be in name of assessee only, and not in name of any other person

The assessee has derived income from house property, income from long term capital gains on sale of property for ₹2,21,00,000 and had invested an amount of ₹49,09,804 on purchase of residential property in her name and her husband's name and claimed exemption u/s 54. Similar investment was made for ₹50 lakhs in Rural Electrification Corporation Ltd. bonds in the names of both and exemption for the

entire amount of ₹50 lakhs u/s 54EC was claimed. As part of investment was in the name of the husband, the Assessing Officer disallowed 50% of the investment.

The High Court of Karnataka held that provisions of section 54 as well as section 54EC makes it clear that when capital gains arise from the transfer of long term capital asset to an assessee and the assessee has within the period of one year before or two years after the date on which the transfer took place purchase or has within the period of three years after the date of construction of residential house then instead of capital gain being charged to Income-tax as income of the previous year in which the transfer took place, it shall be dealt with in accordance with the provision made under the section which grants exemption from payment of capital gains as set out thereunder. Therefore, in the entire section 54, the purchase to be made or the construction to be put up by the assessee, should be there in the name of the assessee, in not expressly stated. Similarly even in respect of section 54EC, the assessee has at any time within a period of six months after the date of such transfer invested the whole or any part of the capital gains in the long term specified asset then she would be entitled to the benefit mentioned in the said section. There also it is not expressly stated that the investment should be in the name of the assessee. Therefore, to attract section 54 and section 54EC, what is material is the investment of the sale consideration in acquiring the residential premises or constructing a residential premises or investing the amounts in bonds set out in section 54EC. Once the sale consideration is invested in any of these manners the assessee would be entitled to the benefit conferred under this provisions. In the absence of an express provision contained in these sections that the investment should be in the name of the assessee only any such interpretation were to be placed, it amounts to Court introducing the said word in the provision which is not there. It amounts Court legislating when the Parliament has deliberately not used those words in the said Section.

In the instant case the assessee has purchased the property jointly with her husband. She has invested the money in rural bonds jointly with her husband. It is nobody's case that her husband contributed any portion of the consideration for acquisition of the property as well as bonds. The source for acquisition of the property and the bonds is the sale consideration. It is not in dispute. Once the sale consideration is utilized for the purpose mentioned under sections 54 and 54EC, the assessee is entitled to the benefit of those provisions. As the entire consideration has flown from the assessee and no consideration has flown from her husband, merely because either in the sale deed or in the bond her husband's name is also mentioned, in law he would not have any right. In that view of the matter, the assessee cannot be denied the benefit of deduction of the aforesaid amount.

LD/60/61
CIT
Vs.
Kinetic Capital Finance Ltd.
September 2, 2011 (DEL)
[Assessment Year 1998-99]

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

When an unexplained credit is found in books of account of an assessee initial onus is placed on assessee to disclose identify of creditors; assessee is not required to prove genuineness of transactions as between its creditors and creditors' source of income, viz., sub-creditors

During the course of scrutiny the Assessing Officer discovered that the assessee had received deposits from eighty six persons. The assessee was asked to explain the credits found qua these deposits in its books of accounts. The Assessing Officer during the course of scrutiny also issued summons to these persons. Out of these eighty six persons, sixteen persons acknowledged the receipt of summons and admitted to the fact that they had deposited money with the assessee. The Assessing Officer, however, was not satisfied qua the remaining seventy depositors and concluded that the assessee had not been able to discharge its onus that the amounts in issue did not belong to the assessee.

The Delhi High Court held that it has to be borne in mind that while making an addition under section 68, the Assessing Officer has to advert to each and every entry and not pick up a couple of entries, as in the present case, and label the entire set of deposits made during the assessment year as undisclosed income of the assessee.

The Tribunal has correctly appreciated the position in law which is that when an unexplained credit is found in the books of account of an assessee the initial onus is placed on the assessee. The assessee is required to discharge this initial onus. Once that onus is discharged, it is for the revenue to prove that the credit found in the books of accounts of the assessee is the undis closed income of the assessee. In the circumstances obtaining in the present case, the assessee had discharged that initial onus. The assessee was not required thereafter to prove the genuineness of the transactions as between its creditors and that of the creditors' source of income, *i.e.*, the sub-creditors.

The Tribunal is the final fact finding authority. The Tribunal appeared to have been satisfied with the quality of the evidence placed before it. There was no perversity in the findings, notwithstanding the stray sentence in its order pertaining to service of depositors. In these circumstances, the findings returned by the Tribunal could not be upset.

LD/60/62

Tiong Woon Project & Contracting Pte. Ltd., In re
September 19, 2011 (AAR)

Section 90 of the Income-tax Act, 1961 – Double taxation agreement – Existence of

Where Applicant Singapore company secured four work orders and all four projects are independent projects and there is no interconnection and interdependence amongst them, none of them appears to be an extension of another, aggregation of periods of contracts cannot be made for these four contracts and consequently, applicant cannot be said to have a PE in terms Indo-Singapore DTAA

Applicant is a company formed in Singapore. It has secured four work orders. According to the applicant these four projects are independent of each other and secured through independent work orders. Applicant is of the view that as these are installation projects, these can be considered to have a Permanent Establishment only if each of these four installation projects continues for a period of more than 183 days individually in any previous year in terms of Article 5.3 of the Double Taxation Avoidance Agreement with Singapore (DTAA). As the income from the execution of these projects is in the nature of business profits, it would be taxable in India as per Article 7.1 of the DTAA only if it has a Permanent Establishment in India.

The Authority for Advance Rulings held that all these are independent projects and there is no interconnection and interdependence amongst them. None of them appears to be an extension of another. Therefore the duration test for installation and assembly projects provided under article 5.3 of the DTAA cannot be construed to be read for all the projects that do not pass the test of cohesiveness, interconnection and interdependence. Therefore, in the given facts of the case, aggregation of the periods of the contracts cannot be made for these four contracts and consequently the applicant cannot be said to have a PE in terms of article 5.3 of the DTAA. In view of the above, the income earned by the applicant from its activities of execution of four installation projects referred above is not liable to tax in India.

LD/60/63

Dinesh B. Parikh
Vs.
CIT
August 2, 2011 (CAL)
[Assessment Years 1987-88 to 1997-98]

Section 158B of the Income-tax Act, 1961 – Tax on profits and gains of life insurance business

Where sufficient evidence had not been produced by appellant to rebut statement made at time of search that 'he had invested money in different names but shares actually belonged to him', addition made in block assessment would be justified

A search was conducted by the Income-tax Department at the place of the business and residential premises of the appellant. The appellant's case was that initially he had disclosed shares in the company called JCL of ₹11 lac. The shares amounting to ₹8 lac in JCL were purchased in different names which the appellant admitted as belonging to him. Subsequently, he wrote letter and submitted that from record, he found that the shares of amount of ₹8 lac were actually held by group companies. The Assessing Officer took note of the letter subsequently written by the assessee by which he sought to retract from his statement earlier made. By the said letter, he explained that the investment was made out of the fund in form of capital/loan/advance amount with the firm JMS where he was a partner, FAL and JML which he was a director and apart from the above sources, the investments in shares were made through the accumulated savings lying in the Savings Bank A/C in a span of over four decades. The assessee further explained that his group companies were also holding shares in JCL. The assessee gave xerox copies of the balance sheets of group companies FAL and UKL to show that those two companies held shares worth ₹9,35,000. The Assessing Officer discarded the said reply on the ground that his two earlier replies did not match such statement. In his statement, the assessee clearly stated that apart from ₹11 lakh disclosed share investment, he had invested ₹8 lakh in different names but the shares actually belonged to him and he never mentioned the names of FAL and UKL at that time. Before the CIT (Appeals), without filing any application for admission of additional documents, he relied upon affidavits of the broker confirming that the list did not represent the shares purchased on behalf of the assessee but represents the list of quotation made by him with various brokers. It appeared that the CIT (Appeals) did not take into consideration such affidavit but deleted the amount of ₹7,82,000 in view of balance sheets of the two companies wherein the investment in shares of JCL had been shown.

The Calcutta High Court held that the Tribunal was quite justified in setting aside such a perverse finding made by CIT (Appeals) in deleting the said sum of money. It was rightly pointed out by the Assessing Officer that the explanation offered subsequently was not sufficient to rebut the earlier statement and the subsequent explanation was not matching with the earlier statements. There was no substance in the contention of the assessee that the Tribunal committed substantial error of law in not considering the affidavit of the broker.

An additional evidence can be adduced before the CIT (Appeals) on compliance of the statutory provisions for acceptance of the same and formal application must be filed and at the same time, specific order must be recorded by the CIT (Appeals) allowing such prayer and specifying the point on which such additional evidence should be taken. If such application is allowed, the other side must be given opportunity to adduce evidence of rebuttal. The CIT (Appeals) did neither accept the affidavit by passing any order nor did it rely upon such affidavit annexed to the written note of argument but allowed the appeal on a different ground which was not tenable in the eye of law. The assessee did not even pray before the Tribunal for allowing the acceptance of the affidavit of the broker and even before the High Court; no application had been filed for acceptance of such affidavit as additional evidence.

Thus, no duty was cast upon the Tribunal to look into such affidavit annexed to the written note of argument filed before the CIT (Appeals). From the materials on record it was clear that no sufficient evidence had been produced by the appellant to rebut the statement made at the time search that he had invested ₹8 lakh in different names but the shares actually belonged to him and the Tribunal below had rightly set aside the order of the CIT (Appeals) which was not based on any cogent reason.

LD/60/64
General Electric Company
Vs.
Dy. DIT
August 12, 2011 (DEL)

Section 163 read with Section 9 of the Income-tax Act, 1961 – Non-resident – Agent of

In respect of transfer of shares held by a foreign company in Indian subsidiary company to another non-resident outside India, Indian subsidiary could not be taxed as representative assessee, when it had no role in said transfer; merely because shares related to Indian subsidiary, that would not make Indian subsidiary an

agent qua deemed capital gain purportedly earned by foreign company

The first petitioner is a US company. It had been assessed to tax in India over the last several years in respect of its income taxable in India, as a non-resident. The second petitioner was a Mauritius group company. It had a wholly owned subsidiary in India viz., respondent no. 4 which was engaged in BPO business. The petitioner transferred its shares in the respondent no. 4 company to another non-resident. Notice was issued under section 163 to respondent no. 4 by which respondent No.4 was sought to be taxed as representative assessee holding respondent No.4 as agent qua deemed capital gain purportedly earned by the petitioner.

The Delhi High Court held that a conjoint reading of sections 160 to 163 would show that under the given circumstances, certain persons can be treated as representative assessee on behalf of non- resident specified in sub-section(1) of Section 9. This would include an agent of non-resident and also who is treated as an agent under Section 163. Section 163 deals with special cases where a person can be regarded as an agent. These are:

(i) who is employed by or on behalf of the non-resident: or
(ii) who has any business connection with the non-resident; or
(iii) from or through whom the non-resident is in receipt of any income, whether directly or indirectly; or
(iv) who is the trustee of the non-resident; or
(v) any other person, a resident or even a non-resident, who has acquired a capital asset in India by means of transfer.

Once a person comes within the net of any of the aforesaid Clauses, such a person would be the 'agent' of the non-resident for the purposes of the Act. However, merely because a person is an agent or is to be treated as an agent, it would lead to an automatic conclusion that he becomes liable to pay taxes on behalf of the non-resident. That would only mean that he would be treated as representative assessee. However, liability of such a representative assessee only if the eventualities stipulated in section 161 are satisfied. Section 161 makes a representative assessee liable only "as regards the income in respect of which he is a representative assessee".

Of course, once a representative assessee is held liable, then he will be liable in the same manner as a non- resident and tax shall be levied and recovered from him in the same manner it could be recovered from the person represented by him. Since tax is recovered from such a representative assessee treating him as agent of other person, Section 162 gives representative assessee right to recover the sum paid by him from the person on whose behalf it is paid. This Section even makes a provision allowing representative assessee to retain out of any moneys that may be in his possession or may come to him in his representative capacity, an amount equal to the sum so paid. In the event, the principal question is right to retain such an amount, the representative assessee or person may secure from the (Assessing) Officer a certificate stating the amount to be so retained pending final settlement or the liability, and the certificate so obtained shall be his warrant for retaining that amount. Issuance of such certificate even secures the representative assessee as at the time of final settlement, the amount recoverable form such representative assessee or person at the time of final settlement shall not exceed the amount specified in such certificate. The only exception is that when such representative assessee or person may at such time may have in his hands additional assets of the principal, as in that even, even if excess amount stipulated in certificate is recoverable from the representative assessee, he is secured by having additional assets of the principal in his hands from where the representative assessee can always recompense.

A harmonious reading of Sections 160, 161, 162 and 163 would show that:

(i) In order to become liable as a representative assessee, a person must be situated such as to fall within the definition of a representative assessee;
(ii) The income must be such as is taxable under section 9;
(iii) The income must be such in respect of which such a person can be treated as a representative assessee;
(iv) The representative assessee has a statutory right to withhold sums towards a potential tax liability;
(v) Since the liability of a representative assessee is limited to the profit representative assessee, there can be multiple representative assessees in respect of a single non-resident entity – each being taxed on the profits or gain relateable to such representative assessee.

There was a business connection between the petitioner and the respondent No.4. But that by itself would not be sufficient for the Revenue to sail through. Even if business connection is proved, it would at the most make the respondent No.4 an agent of the petitioners and in that eventuality, the Income Tax Department can treat the respondent No.4 as representative assessee of the first petitioner. However, in order to assess a particular income, it

has to be further established by the Department that the respondent No.4 had some connection with the income earned by the first petitioner which is sought to be taxed at the hands of the respondent No.4. There was no live link of income earned by the first petitioner and the respondent No.4 in respect of the transaction which is sought to be taxed. Section 163 has to be read in conjunction with section 161 which provides that the specified person can be treated as assessed ".....as regards the income in respect of which he is a representative-assessee....." Therefore, an agent can only be a representative-assessee as regards the income in respect of which the alleged agent has business connection and/or from or through directly and/or indirectly the income was received.

The ingredients of Section 161 are not satisfied as the petitioner as assessee could be taxed only as regards the income and in respect of which he is a representative assessee. No case was made out by the Department that in respect of transaction in question, viz., transfer of share to third party, that too, outside India. Respondent No.4 was sought to be taxed as representative assessee when he had no role in the said transfer. Merely because those shares relate to the respondent No.4-company, that would not make respondent No.4 as agent qua deemed capital gain purportedly earned by the petitioner.

LD/60/65
Raju Bhojwani
v.
CCIT
September 9, 2011 (DEL)
[Assessment Year 2002-03]

Section 234B and 234C read with Section 80HHC of the Income-tax Act, 1961 – Interest on Advance tax

Where after initiation of reassessment, due to retrospective amendment to section 80HHC (5th proviso), assessee rather stood benefited as assessee became entitled for deduction of ₹1,27,292 instead of Nil deduction before said amendment, interest would be accordingly calculated

The petitioner-assessee filed a return of income declaring total income to ₹6,76,660. The Assessing Officer held that the assessee had suffered loss in export business and, therefore, not entitled to deduction under section 80HHC. Deduction under section 80HHC was also denied on the ground of interest received and rental income had been included for computing the said deduction. The total income was assessed at ₹13,72,974. Interest under section 234B was directed to be levied as per law.

The Commissioner (Appeals) noticed that Section 80HHC had been retrospectively amended by the Taxation Laws (Amendment) Act, 2005 and the assessee was entitled to benefit of the proviso added with retrospective effect from 1st April 1998 on account of profits from sale of export incentives. The Commissioner (Appeals) also directed to treat 90 per cent of interest income as income qualifying for deduction under section 80HHC. Direction of the Assessing Officer to charge interest under section 234B was not interfered with.

The Revenue and the assessee both approached the Tribunal but without success.

The petitioner thereafter filed an application under section 234B and 234C for waiver of interest before the Commissioner of Income-Tax, which has been rejected. The Commissioner of Income-Tax has held that the request for waiver of interest is not covered either under CBDT Circulars dated 23rd May, 1996, 30th January, 1997 or under the Circular No. 2/2006 dated 17th January 2006.

The High Court of Delhi held that the assessee had income from sale of export incentives. 90 per cent of the said amount was computed at ₹9,06,433 and deduction under section 80HHC was calculated at 70 per cent of the said amount, i.e., ₹6,34,503 and was claimed as a deduction in the original return. This claim was reiterated in the return filed on 5th July, 2004 pursuant to the notice under Section 147. This second return was after the decision of the Supreme Court in IPCA *Laboratory Limited vs. Deputy Commissioner of Income Tax,* [2004] 266 ITR 521 (SC), wherein it has been held that deduction under Section 80HHC is to be arrived at and claimed on profits earned from both export of self-manufactured goods and trading goods and profit and loss of both trades have to be taken into consideration. If after the adjustment there is positive profit, then only deduction under Section 80HHC can be claimed. If there is loss, there cannot be any entitlement. As per the computation made in Form No. 10CCAC, the petitioner had business loss of ₹7,16,188, after excluding the income from the export incentives. In these circumstances, it is not possible to accept the contention of the petitioner that the retrospective amendment by Taxation Law (Amendment) Act, 2005 was detrimental and had reduced the claim for deduction made by him under Section 80HHC as originally claimed. In fact, this aspect has been dealt with and explained vide response given by the Revenue to the application for waiver of interest filed by the petitioner. In the said response, it had been stated that with retrospective amendment to section 80HHC (5th proviso) the assessee rather stood benefited as the

assessee became entitled for deduction of ₹1,27,292 instead of Nil deduction before the said amendment.

Hence, the assessee's contention that interest under section 234B and 234C became chargeable due to unforeseen retrospective amendments to section 80HHC was not acceptable. Further, there was no issue of profits on sale of Duty Entitlement Pass Book credits or Duty Free Replenishment Certificate in the instant case to which the Circular No. 2/2006 refers.

The aforesaid factual position was not disputed. It was clear that as a result of the insertion of the proviso, the petitioner became entitled to deduction under Section 80HHC of ₹1,27,292. The proviso did not act as a detriment or negate or reduce the claim of deduction. In view of the aforesaid, there was no merit in the writ petition and the same was accordingly dismissed.

INDIRECT TAXES

Delhi Value Added Tax Act

LD/60/66

Dharam Pal Satya Pal Ltd.
Vs.
The Commissioner, Value Added Tax
September 2, 2011 (DEL-FB)
[Assessment Year 2004-05]

Section 74A read with Section 106 of the Delhi Value Added Tax Act, 2004 read with Section 46 of the Delhi Sales Tax Act, 1975 - Revision

Commissioner under Delhi Value Added Tax Act, 2004 (DVAT Act) can exercise suo motu power of revision under Section 74A of DVAT Act in respect of assessments that have been completed under Delhi Sales Tax Act, 1975

The petitioner-company has called in question the legality and validity of the initiation of the revisional proceedings against the petitioner by issuance of notice dated 08.04.2010 under Section 74A read with Section 106 of the DVAT Act by the Commissioner, Trade Taxes, purporting to revise the orders of the Additional Commissioner dated 14.01.2008 and 25.11.2008 and to restore the order passed by the assessing authority on 30.03.2006. It is pleaded that the orders of the assessing authority as well as that of the first appellate authority relate to the assessment year 2004-05 to which the DST Act is applicable and not the provisions of the DVAT Act which came into force with effect from 01.04.2005. It is contended that the initiation of the revisional proceedings against the petitioner is wholly without jurisdiction and without proper authority of law inasmuch as the power of revision engrafted in Section 74A of the DVAT Act cannot be pressed into service in respect of orders passed under the provisions of the DST Act. That apart, the provision of Section 74A of the DVAT Act has no application at all to the year 2004-05 during which the said provision had not come into force. It is urged that the proceedings being fundamentally unsustainable are *ab initio* void and, hence, deserve to be lanceted in exercise of the inherent and equitable jurisdiction of this Court.

The High Court of Delhi held that the following principles can safely be culled out:

(i) The concept of liability "accrued" or "incurred therein" and "obligation" have different connotations. (ii) The meaning of "right accrued" and "vested right" will depend upon the language of the statute and the intention expressed by the Legislature. (iii) The intention of the Legislature must be absolutely clear whether it intends to destroy the old liabilities and it would depend upon the entire scheme of the Act. (iv) An order of assessment is final subject to the provisions relating to appeal, revision, reassessment and rectification. (v) A statute is not to be interpreted to be retrospective or retroactive to touch the existing final orders. (vi) Even if no action is taken under the repealed Act, the civil as well as the criminal liability that had incurred under the repealed statute are not obliterated and are kept alive if there is a saving provision. (vii) A legal proceeding which could have been initiated under the repealed Act continues to subsist if the savings and repeal provision so stipulates subject to the law of limitation. To elaborate, the right to initiate a legal proceeding can only be obliterated or effaced or meet its legal death if the period of limitation thereon has expired.

The basic facet of Section 106 of the DVAT Act has to be interpreted on the touchstone of the above culled out principles. Sub-section (1) of Section 106 of the DVAT Act, as it clearly reveals, is a simple repeal of the DST Act. Sub-section (2) saves the right, title, entitlement, obligation or liability already acquired, accrued or incurred under the repealed Act. Sub-section (3) postulates that anything done under the DST Act shall be deemed to be done or taken in exercise of the power conferred by or under the DVAT Act. Thus, three situations, namely, (i) assessment completed and already revised; (ii) assessment completed and revisional power invoked but the process not completed; and (iii) assessment completed, but no revisional power invoked, do contextually emanate.

Thus, it is quite clear that Section 106(2) of the DVAT Act not only saves the right, title and entitlement but also saves the obligations and the liability. The term "obligation" includes every duty enforceable by law. It is an expression which includes not only duty

but something more. The expression "liability incurred thereunder" has a larger canvas and makes one remain liable under law subject to statutory boundaries. The term "finality" has to be understood in its truest denotation and an order of assessment by itself does not earn the status of being final unless it is totally barred by law to be touched. Section 106(3) of the DVAT Act clearly lays a postulate that an order passed under Section 46 of the DST Act and the process of assessment leading to it is deemed to have been done in exercise of the power conferred under the DVAT Act. What is provided under Section 106(2) is that the repeal shall not affect the previous operation of the DST Act or any right, title, entitlement, obligation or liability already acquired, accrued or incurred thereunder. On a seemly scanning of the provision engrafted under Section 46 of the DST Act, a suo motu revision could be initiated and concluded within five years of the order of assessment. In sub-section (2)(b) of Section 74A of the DVAT Act, a rigor has been attached that no order under this section shall be passed after the expiry of four years from the end of the year in which the order passed by the subordinate officer has been served on the dealer. Section 74A (2)(c) carves out a period of five years under certain other circumstances. The right to a dealer would have attained finality and become a vested or ripened right after the expiry of the period of limitation under the DST Act and if the proceedings are initiated within the period of limitation, the exercise of the suo motu power of revision cannot be treated as illegal. In other words, if the time to exercise the revisionary power had not expired before coming into force of the DVAT Act, the said power could be exercised in respect of an order under the DST Act in terms of Section 74A of the DVAT Act read with Section 106 of that Act.

Turning to three categories of cases, in the first category of cases, wherein assessment has been completed and already revised, by virtue of the language employed in Section 106(3) of the DVAT Act, the order passed has to be considered as an order passed under the DVAT Act. In the second category of cases, wherein assessment has been completed and revisional power has been invoked though the process is not completed, the assessee has incurred the liability of the order of the Assessing Officer being scrutinized by the Commissioner which includes the revisional power and sub-section (3) gets attracted. In the third category of cases, where the assessments are completed but no revisional power is invoked, here again sub-section

(3) of Section 106 would be attracted as if the same is deemed to be an order passed under the DVAT Act. If the order of assessment could not have been revised under the DST Act as on 1.4.2005, the power of revision conferred under the DVAT Act cannot be exercised if the time span has expired. To elaborate, if an order of assessment has attained finality in toto and a right has vested in the assessee, no suo motu power can be exercised as the right fully accrues in favour of the assessee without having any obligation and further having no liability.

Further it may be noted that the legislature made Section 74A retrospective from the date the DVAT Act came into existence to reaffirm its intendment that it never intended not to confer the power of revision on the revisionary authority. The interpretation placed by us on the language employed under Section 106(2) and 106(3), analysis made hereinbefore on the impact of insertion of Section 74A initially from 16.11.2005 and thereafter to make the provision retrospective from 1.4.2005, clearly conveys that the legislature at all point of time intended to protect the interest of the revenue.

In view of the aforesaid premised reasons, the conclusions may be recorded in seriatim:

(a) On incorporation of Section 74A in the DVAT Act on 16.11.2005, the suo motu revisional proceeding could be initiated at the commencement of the DVAT Act, i.e., 1.4.2005. It could not be said that on the date the Act came into force the provision pertaining to exercise of suo motu revisionary power did not exist in respect of the proceedings under the DST Act as the assessment had attained finality and were closed.

(b) The order of assessment framed under the DST Act is deemed to be an order framed under the DVAT Act and on reading of Sections 106(2) and 106(3) in a conjoint manner, it is not correct to state that once the order of assessment has been passed, the transaction is closed and, therefore, the assessment/order is not revisable under Section 74A of the DVAT Act.

(c) The liability incurred or accrued under the DST Act has a larger expanse and a broader canvas and it would in view of Section 106(2) of DVAT Act include initiation of any legal proceeding which is permissible within the period of limitation and till then no final or vested right accrues in favour of the assessee.

(d) The amendment brought by the legislature retrospectively incorporating Section 74A with effect from 1.4.2005 has been done to further elucidate the legislative intention and has to be given full effect to. The said amendment has been brought in the statue book by ex *abundanti cautela* and in essence, removes the anomaly and is only curative in nature.

(e) The proceeding initiated under the DST Act is saved by the DVAT Act and further the proceedings could be initiated under Section 74A during the period of limitation as stipulated under Section 74A subject to the conditions precedent stipulated therein.

Arbitration Act

LD/60/67

Cauvery Coffee Traders Vs. Hornor Resources (Intern.) Co. Ltd.

September 13, 2011 (SC)

Section 11 of the Arbitration and Conciliation Act, 1996 – Appointment of Arbitrator

In case, final settlement has been reached amicably between parties even by making certain adjustments and without any misrepresentation or fraud or coercion, then, acceptance of money as full and final settlement/ issuance of receipt or vouchers etc. would conclude the controversy and it will not be open to either of the parties to lay any claim/demand against the other party

A Purchase Contract was entered between the applicants and the respondents to purchase Iron Ore. The agreement provided that the iron content should not be less than 63 per cent; otherwise the buyer would have a right to reject the cargo.

The Purchase Agreement also contains a clause providing for price adjustment in case the supplied ore did not meet the requirement of specification provided for iron ore. In case of any dispute between the parties, the agreement provided for arbitration in any third country.

The applicants shipped a total consignment from Port, India to the port of discharge, China. The delivery of the same was taken by the respondents and on chemical analysis, according to them, the iron content was found to be 62.74 per cent. The respondents vide email dated 7.10.2008informed the applicants that US$ 1.5 million could be the amount for the final settlement in respect of the shipment in question, in spite of the fact that the agreed amount had been US$ 18,91,204.00. By the said email, applicants were asked by the respondents to inform through their banker in case of their acceptance to the said proposal.

Under these peculiar facts and circumstances, as the goods had already reached China and applicants

were in dire need of money, they informed through their banker that they agreed to receive payment under the Letter of Credit in a sum of total claim of US$ 18,91,204.00. By email dated 7.10.2008 the respondents stated that the applicants should accept US$ 1.5 million in full and final settlement. Accordingly, an amount of US$ 1.5 million had been received by them.

The arbitration applications under Section 11(5) & (9) of the Arbitration and Conciliation Act, 1996, had been filed for appointment of Arbitrator in an international arbitration dispute to adjudicate the disputes/differences which had arisen between the parties.

The Supreme Court held that the Purchase Agreement contained a clause providing for price adjustment in case the supplied ore did not meet the requirement of specification provided for iron ore. In case of any dispute between the parties, the agreement provided for arbitration in any third country.

Stand of the respondents throughout had been that the Price Adjustment under the Purchase Contract in respect of the iron ore, the buyers had a right to reject the whole consignment Negotiations started as is evident from the email messages and it was in pursuance of these negotiations that the applicants had instructed their banker to accept the proposal made by the respondents and it was in pursuance of their instructions, the banker vide email dated 8.10.2009 accepted the proposal and agreed to receive a sum of US $500,000.00 as full and final settlement for the consignment in issue. The payment made was accepted by the applicants and it was after 3 months thereafter that they served a legal notice dated 14.11.2008 for making a reference to the Arbitrator. The applicants in the present application do not dispute the negotiations or giving instructions to their banker or in respect of the email by their banker to the respondents or receiving the money in lieu thereof.

In case, final settlement had been reached amicably between the parties even by making certain adjustments and without any misrepresentation or fraud or coercion, then, acceptance of money as full and final settlement/issuance of receipt or vouchers etc. would conclude the controversy and it is not open to either of the parties to lay any claim/demand against the other party.

The applicants had not pleaded that there had been any kind of misrepresentation or fraud or coercion on the part of the respondents. Nor it was their case that payment was sent by the respondents without any settlement/agreement with the applicants, and was a unilateral act on their part. The applicants reached the final settlement with their eyes open and instructed their banker to accept the money as proposed by the respondents. Proposal itself was on the basis of the Purchase Contract which provided for Price Adjustment. For a period of three months after acceptance of the money under the full and final settlement, applicants did not raise any dispute in respect of the agreement of price adjustment. In such a fact-situation, the plea that instructions were given by the applicants to the banker erroneously, being, afterthought is not worth acceptance.

The transaction stood concluded between the parties, not on account of any unintentional error, but after extensive and exhaustive bilateral deliberations with a clear intention to bring about a quietus to the dispute. These negotiations, therefore, are self explanatory steps of the intent and conduct of the parties to end the dispute and not to carry it further. Thus, the applicants could not take a complete somersault and agitate the issue that the offer made by the respondents had erroneously been accepted.

Therefore, the arbitration applications under Section 11(5) & (9) for appointment of Arbitrator in an international arbitration dispute to adjudicate the disputes/differences which had arisen between the parties, were to be dismissed.

Competition Act

LD/60/68
Arun Kumar Tyagi
Vs.
Software Engineering Institute
September 30, 2011 (CCI)

Section 3, read with sections 4 and 19, of the Competition Act, 2002 – Anti-Competitive Agreements

Where High Court is floater of tender for digitizing old records, Indian computer technologies company is a bidder for the tender and foreign company is agency which accredited 'CMM1 Level 5' to Indian company and it is amply clear that these three opposite parties are not engaged in similar trade or business, mere agreement between foreign company and Indian company in this case would not amount to cartelization

The information in this matter has been filed against the OP1 Software Engineering Institute, USA, the OP2 High Court of Uttarakhand and the OP3 HCL Technologies Ltd. with the allegation that the opposite parties have acted in concert in the tendering process for procurement of computer software by OP2 for digitizing its old records with a view to kill free and fair competition and to eliminate other competitors from the bidding process.

It is stated in the information that in order to monopolize the aforesaid bidding process for procurement of computer software, the OP1 and OP3 have formed a cartel and persuaded OP2 to stipulate certain minimum eligibility technical pre-conditions in the tender notice which are exclusively met by OP3.

The Competition Commission of India held that in order to attract the provisions of section 3(3) of the Act, the enterprises must be engaged in similar trade or business. In the present case, OP2 is the floater of the tender, OP3 is a bidder for the tender and OP1 is the agency which accredited 'CMM1 Level 5' to OP3. Thus, from the facts and allegations set out in the information it is amply clear that OP1, OP2 and OP3 are not engaged in similar trade or business. The agreement between OP1 and OP3 in this case does not amount to cartelization in terms of section 3(3) of the Act as OP 1 is not engaged in similar trade or business as OP3, rather it has merely accredited 'CMM1 Level 5' to OP3. Therefore, there is no *prima facie* violation of section 3 of the Act in the present matter.

RBI

LD/60/69

Gupta & Gupta Chartered Accountants
Vs.
Reserve Bank of India
October 10, 2011 (DEL)

Section 30 of the Banking Regulation Act, 1949 - Audit

Where RBI failed to afford Chartered Accountants an opportunity of defending itself against Nationalised Bank's allegations and also, neither RBI nor Bank had communicated to Chartered Accountants decision to discontinue it as an Statutory Central Auditor for extended review period, it was violative of principles of natural justice and was, therefore, illegal

The procedure for the appointment of a firm of auditors as Statutory Central Auditor (SCA) for a public sector bank envisages a primary role for the RBI, which acts as such in exercise of its powers under Section 30 (1A) of Banking Regulation Act, 1949 ['the BR Act']. In terms of Section 10 (1) of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 ['1970 Act'] and the corresponding provision in the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 ['1980 Act'], the RBI has to mandatorily grant prior approval to the appointment of SCAs of twenty-six public sector banks. The RBI has issued circulars specifying the norms for appointment of SCAs in public sector banks. Where the total liabilities and assets of the public sector bank is up to ₹50,000 crore the prescribed number of SCAs is four; where it is between ₹50,000 crore and up to ₹1 lakh crore, the number of SCAs is five and above ₹1 lakh crore, the number of SCAs is six. The SCAs appointed during 2006-07 and thereafter would have a tenure of four years after which they were to be rested for two years. Further, the Office of Comptroller & Auditor General of India ('CAG') is entrusted with the responsibility of calling for applications from auditors/ audit firms desirous of being appointed as SCAs in public sector banks every year. After subjecting the applications to scrutiny in terms of the prescribed norms, the CAG prepares a list of eligible auditors/ audit firms. That list is then forwarded by the CAG to the RBI. Finally, the selection of auditors/audit firms by the RBI is made from amongst the auditors/audit firms found eligible by CAG.

The discontinuance of an SCA, selected through such a rigorous process, is likely to have adverse consequences for its reputation and goodwill if such discontinuance is as a result of a complaint about its competence or integrity. For a firm of auditors the appointment as SCA of a public sector bank is bound to be seen to be a prestigious one. As a corollary the discontinuance of a firm of auditors as SCA, unless for circumstances unconnected with integrity or competence, is bound to be viewed negatively. Further, since the number of SCAs of a public sector bank is unlikely to be more than six, the appointment and discontinuance of an SCA is likely to be known immediately to all chartered accountants.

An SCA of a public sector bank discharges statutory responsibilities traceable to Section 224 (2) of the Companies Act, 1956, the BR Act, the 1970 Act and the 1980 Act. In the context of the circulars issued by the RBI on the charging of interest by public sector banks, the Supreme Court in *Central Bank of India v. Ravindra* [2001] 107 Comp. Cas. 416 explained that the power conferred on the RBI under Sections 21 and 35A of the BR Act is coupled with the duty to act fairly and reasonably. The RBI's circulars were held to be binding on "those who fall within the net of such directives." By analogy the RBI's circulars as regards the appointment and continuance of SCAs must be viewed as binding on public sector banks including the PNB. RBI discharges a statutory duty when it selects a firm of auditors to act as an SCA of a public sector bank. It is a reflection of both the competence as well as integrity of the firm of auditors. It acknowledges that the answerability of the public sector bank is as much as to the law as to the public in general whose monies it is the custodian of. On their part the SCAs are expected to discharge their professional duties in the context of the above statutory obligations and their answerability to both the RBI and the public in

general. The relationship of an SCA with the public sector bank whose audit they are engaged to undertake transcends the usual client-auditor relationship. The involvement of the RBI in the appointment and discontinuance of an SCA is meant to ensure a degree of protection to the SCA which is expected to discharge its professional duty fearlessly and independently. The discontinuance of an SCA cannot be brought about by the public sector bank acting by itself. Just as there can be no appointment of an SCA without the intervention of the RBI, there can be no discontinuance of an SCA without the RBI taking a decision in that regard. The greater the power to appoint and remove an SCA, the higher the responsibility on the RBI as the holder of such power to exercise it in a fair and reasonable manner after following a just procedure which comports with the principles of natural justice.

Where a complaint is made against an SCA by a public sector bank, it would be the duty of the RBI to examine such complaint carefully. In the audit of large public sector banks, there are bound to be queries raised by the SCAs about the accounts of the large account holders of the bank. If there are complaints by the bank, like in the present case, that the audit is getting delayed on account of the bank having to answer such queries, the RBI will have to examine the tenability of such claim after seeking an explanation from the SCA.

The Petitioner, a firm of chartered accountants, is aggrieved by a decision of Reserve Bank of India ('RBI'), communicated to Punjab National Bank ('PNB'), advising that the PNB may carry out the quarterly review for the quarter ending 30th June 2009 with the five existing statutory central auditors ('SCAs'), excluding the Petitioner firm in view of the circumstances mentioned in the PNB's letter dated 27th May 2009 addressed to the RBI.

The High Court of Delhi held that the PNB first wrote to the RBI on 24th April 2009 blaming the Petitioner for the delay in the finalization of the accounts. The Petitioner's comments on the said letter were sought by the RBI. The Petitioner then submitted a reply dated 7th May 2009 explaining that there was no delay on its part. This reply was furnished to the PNB by the RBI for its response. In response thereto, on 27th May 2009 the PNB made several allegations questioning the Petitioner's professional competence and integrity. In other words, the tenor of the allegations by PNB against the Petitioner in the letter dated 27th May 2009 was not confined to the issue of delay. Specifically, PNB alleged that the intention of the Petitioner was "to malign the reputation and image of the bank"; that the Petitioner was "abrasive ab initio and uncooperative in their approach right from the first audit and are lacking in professionalism."; that they have been "putting the entire system to undue stress and holding the bank to ransom"; "their objective has been to embarrass the bank and harass its officers. The behaviour and attitude is indicative of cynicism and sadism." Then came the impugned decision of the RBI communicated in its letter dated 24th June 2009 permitting PNB to discontinue the Petitioner as SCA for the limited extended review for the quarter ending 30th June 2009.

It is not as if the letter dated 24th June 2009 simply states that the Petitioner will be discontinued. It refers to the PNB's letter dated 27th May 2009 and states that the Petitioner could be discontinued as SCA "in view of the circumstances cited in the above letter." It is therefore not possible to view the said discontinuance as being innocuous and routine and not casting a stigma on the Petitioner. The RBI could not have arrived at the decision without some kind of an inquiry. The RBI was performing an important and sensitive task. Allegations concerning the competence and integrity of an SCA, selected by the RBI through a fairly rigorous process, cannot be permitted to be made lightly and equally accepted on face value without some probe by the RBI. Otherwise it might be easy for a bank to have an inconvenient SCA discontinued. Considering that the accounts of public sector banks are to be audited by employing the best possible standards, the RBI was under a statutory obligation to ensure that the discontinuance of the Petitioner, on a complaint about its professional competence, was preceded by a proper procedure comporting with the principles of natural justice. Admittedly, even a copy of PNB's letter dated 27th May 2009 was not sent to the Petitioner for its comments although it contained serious allegations about the Petitioner's conduct and professional competence. Thereby RBI failed to afford the Petitioner an opportunity of defending itself against PNB's allegations. Also, neither the RBI nor PNB communicated to the Petitioner the decision to discontinue it as an SCA for the extended review period.

Therefore, the impugned decision of the RBI, as communicated in its letter dated 24th June 2009 to the PNB, to discontinue the Petitioner as an SCA, even for the limited extended period ending 30th June 2009, was violative of the principles of natural justice and was, therefore, illegal. However, since the period in question is over no consequential relief can be granted except to clarify that the said decision of the RBI, will not come in the way of the Petitioner being hereafter appointed as an SCA in accordance with the norms devised by the RBI. ■