Legal Decisions[1]

DIRECT TAXES

Income-tax Act

LD/60/70
CIT
Vs.
Asahi India Safety Glass Ltd.
October 4, 2011 (DEL)
[Assessment Years 1997-98 and 1998-99]

Section 37(1) of the Income-tax Act, 1961 – Business expenditure – Allowable as

Expenditure incurred by the assessee for installing, maintaining and updating accounting software and professional expenses was revenue expenditure

The assessee is in the business of manufacturing safety glass which is used in automobiles. Thus the main source of income of the assessee is from the said activity. The assessee entered into an agreement with Arthur Anderson & Associates (Arthur) in the financial year 1996-97 for installation of a software application for assistance in areas related to financial accounting, inventory and purchase. The said agreement between the assessee and Arthur also required the assessee to enter into a back-to-back agreement with Oracle. The reasons perhaps being that the software application supplied by the Arthur worked on oracle application. It is precisely for this reason that Arthur required the assessee to enter into a licence agreement with oracle titled Master Software Licence and Services Agreement. The assessee was thus, required to pay apart from the fee to Arthur qua its agreement with it; licence fee to Oracle. As a matter of fact Oracle also offered support and maintenance services for which a further additional fee was required to be paid to Oracle. The assessee thus admittedly in respect of the aforesaid transactions incurred an expenditure to the tune of ₹1,36,77,664 and ₹1,70,68,811 in assessment years 1997-98 and 1998-99 respectively. In the books of accounts for the assessment years 1997-98 the assessee had not written off any sum, while in the succeeding assessment year, *i.e.*, 1998-99 the assessee had written off a part of the expenditure amounting to ₹9,91,228. On these facts, could it be said that the expenditure incurred by the assessee in the aforementioned assessment years was in the nature of capital expenditure.

The Delhi High Court held that software is nothing but another word for computer programmes, *i.e.*, instructions that make the hardware work. Software is broadly of two types, *i.e.*, the systems software, which is also known as the operating system which controls the working of the computer; while the other being applications such as word processing programs, spread sheets and data base which perform the tasks for which people use computers. Besides these there are two other categories of software, these being network software and language software. The network software enables groups of computers to communicate with each other, while language software provides with tools required to write programmes.

The aforesaid would show that what the assessee acquired through Arthur was an application software which, enabled it to execute tasks in the field of accounting, purchases and inventory maintenance. The fact that the application software would have to be updated from time to time based on the requirements of the assessee in the context of the advancement of its business and/or its diversification, if any; the changes brought about due to statutory amendments by law or by professional bodies like the Institute of Chartered Accountants of India, which are given the responsibility of conceiving and formulating the accounting standards from time to time, and perhaps also, by reason of the fact that expenses may have to be incurred on account of corruption of the software due to unintended or intended ingress into the system – ought not give a colour to the expenditure incurred as one expended on capital account. On the fact that there are myriad factors which may call for expenses to be incurred in the field of software applications, it cannot be said that either the extent of the expense or the expense being incurred in close proximity, in the subsequent years, would be conclusively determinative of its nature. The assessing officer has erred precisely for these very reasons.

It was submitted by the Revenue that in the books of accounts, the assessee had not written off the expense in issue, while in the succeeding assessment year only a part of the expense had been written off and, therefore, the assessee's own understanding of the nature of the expense involved was that it was expended on capital account.

This submission is only to be stated to be rejected. The reason being that the treatment of a particular expense or, a provision in the books of accounts can never be conclusively determinative of the nature of the expense. An assessee cannot be denied a claim for deduction which is otherwise tenable in law on the ground that the assessee had treated it differently in its books. In the case of *Kedar Nath Jute Manufacturing Co. Ltd. vs CIT (1971) 82 ITR 363* the Supreme court has observed that, whether the assessee is entitled to a particular deduction or not will depend on the provision of law relating thereto and not on the view which the assessee might take of his rights nor can the existence or absence of entries in the books of accounts be decisive or conclusive in the matter. Therefore, the contention is of no avail to the revenue. Resultantly, the questions of law have to be answered in the affirmative and in favour of the assessee.

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

LD/60/71
CIT
Vs.
Amway India Enteprises
October 4, 2011(DEL)
[Assessment Years 2001-2002 and 2002-2003]

Section 37(1) of the Income-tax Act, 1961 – Business expenditure – Allowable as

Expenditures incurred by assessee in purchasing software applications and acquiring licence to use said applications, was to be allowed as revenue expenditure

Certain expenditure was incurred by the assessee on purchase of software applications. These applications are MS Office Software, Anti Virus software, Lotus Notes Software and Message Exchange applications. The assessee in respect of these applications acquired a licence to use the said applications on payment of consideration. The said expenditure has been disallowed by the Assessing Officer in each of the assessment years by treating the expenditure as one incurred on capital account.

The Delhi High Court held that the issue has been considered and decided against the revenue in a judgment delivered in *CIT Vs. M/s Asahi India Safety Glass Ltd. [ITA Nos. 1110/2006 and 1111/2006]*[2]. Following the same, expenditures incurred by the assessee was to be allowed as revenue expenditure.

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Section 37(1) of the Income-tax Act, 1961 – Business expenditure – Allowable as

Expenditure incurred on improvement of leasehold business premises would be allowable as revenue expenditure

Certain expenditure was incurred by the assessee on improvements carried out in respect of business premises held on lease. In respect of the said premises, expenses were incurred on flooring, partition, wiring, false ceiling, roofing, air-conditioning unit and duct, electric wiring, laying network for setting up computers and, on purchase of furniture. Both the Assessing Officer and CIT(A) disallowed the expenses on the ground that they were incurred on capital account. The Tribunal allowed the entire expenditure incurred on improvement of leasehold premises save and except that which was incurred on air-conditioning unit(s) and furniture.

The Delhi High Court held that in *CIT Vs. Hi Line Pens Pvt. Ltd [2008] 306 ITR 182*, had concluded that the expenditure was in the nature of revenue expenditure. In *CIT Vs. Escorts Finance Ltd [2006] 205 CTR (Delhi) 574*, the Delhi High Court held the expenses incurred on improvement of leasehold premises, were in the nature of revenue expenditure and, hence, allowed the deduction claimed under Section 37(1). In a number of cases it has been observed that in ascertaining whether an expenditure incurred is made on revenue account or otherwise one would have to bear in mind the nature of the expenditure that is, was it incurred for maintenance or preservation of an asset or was it expended otherwise. It thus concluded that if the expenditure was of the former kind it would be in the nature of revenue expenditure. In *Gulamhussein Ebrahim Matcheswalla vs. CIT (1974) 97 ITR 24 (Bom)*, the court rejected the submission that it is the amount spent on repairs which would determine the nature of the expenditure.

Therefore, having regard to the principles laid down in the aforementioned judgments and the nature of the expenses in issue, the revenue's appeal, on this issue, would have to be rejected.

LD/60/72
Bharati Shipyard Limited
Vs.
Dy. Commissioner of Income-tax
September 9, 2011 (ITAT-MUM-SB)
[Assessment Year 2005-2006]

Section 40(a)(ia) of the Income-tax Act, 1961 – Expenses disallowed – Interest, Commission/ Brokerage etc. paid to a resident

Amendment brought out by the Finance Act, 2010 to section 40(a)(ia) w.e.f. 01.04.2010, is not retrospective in nature; for assessment year 2005-06, even if amount of tax deducted at source was paid before filing of return of income u/s 139(1), same would be disallowed

For assessment year 2005-06, the AO noted that the assessee failed to deposit tax deducted at source within the specified time. On being show caused, it was stated that the amount of tax deducted at source was paid before the filing of return of income u/s 139(1) and hence no disallowance of expenses was called for u/s 40(a)(ia). However, the AO made additions. The question for consideration is as to whether section 40(a)(ia) amended by the Finance Act, 2010 with effect from 01.04.2010 is retrospective from 01.04.2005. Unless stated otherwise, the provisions of the Finance Act, 2010 would have applied w.e.f. 01.04.2011 *i.e.* A.Y. 2011-12. The provision in question has been specifically given retrospective effect from A.Y. 2010-11. Now the case of the assessee was that the amendment made by the Finance Act, 2010 should be given retrospective effect from 01.04.2005, being the date from which sub-clause (ia) of section 40(a) was inserted by the Finance (No. 2) Act, 2004.

The Mumbai Special Bench of Tribunal held that it has no where been expressly set out that the amendment is curative or merely declaratory of the previous law. The intention of the legislature as gathered from the Notes on clauses and the Memorandum explaining the provisions of the Finance Bill does not particularly indicate any relaxation in the provision retrospectively from A.Y. 2005-06 by providing that the expenditure on which due tax was deducted up to February, 2005 but paid before the

[2] *Reported in the Chartered Accountant Journal [LD/60/70].*

due date specified in section 139(1) of the Act would not suffer any disallowance in the A.Y. 2005-06.

Any amendment to the substantive provision is ordinarily prospective except expressly stated otherwise or it comes out so by necessary implication. Unless the amendment is made applicable with retrospective effect, such amendment to the substantive provision is to be regarded as prospective barring out cases in which it is explanatory or clarificatory on one hand or it aims at removing the unintended consequences.

Section 40(a)(ia) was inserted by the Finance (No.2) Act, 2004 with effect from 1st April, 2005 debarring deductions otherwise allowable u/s 30 to 38 in respect of the items set out in this provision if the assessee failed to deduct tax at source or after deduction, failed to pay the same during the previous year or in the subsequent year before the expiry of the time prescribed u/s 200(1). The position anterior to the insertion of sub-section (ia) of section 40(a), which is continuing today also, is that the assessees are obliged to deduct tax at source under Chapter XVII-B. The failure to deduct or pay tax as per the requisite provisions entails consequences u/s 201 and 271C etc. by which the assessee is treated as in default, becomes liable to pay interest and also suffers penalty. These provisions were also applicable prior to insertion of section 40(a)(ia). It shows that the duty of the payer to deduct tax at source was always there in the Act. With the insertion of section 40(a)(ia) by the Finance (No.2) Act, 2004 non-deduction of tax at source from the items of expenses specified or failure to pay such tax after deduction, results into one more adverse consequence in the shape of disallowance of the amount of expenditure in the year of incurring it. Simultaneous with the disallowance, proviso provides that the deduction of the expenditure shall be allowed in the subsequent year when the deducted tax is paid. To put it simply if there is no deduction of tax at source or after deduction it is paid beyond the previous year or within the time specified u/s 200(1), the income of the first year increases but at the same time the income of the subsequent year is reduced on the payment of tax. It is well-known that each year is a separate and independent unit of assessment. The potential deduction in a later year cannot be allowed to reduce the income for the earlier year and *vice versa*. Total income of an assessee for each year has to be computed as per the provisions of the Act in so far as they apply. It is neither desirable nor permissible to mix up the assessment of two years by claiming that since the deduction shall become permissible in second year, the AO should grant the deduction in the first year and ignore it in the second year. If this view point is accepted then many provisions of the Act shall become otiose. It is incumbent upon the AO to separately compute total income of each year unmindful of the possible deduction or addition in the next year. Thus it can be seen that from assessment year 2005-2006 the assessee's failure to comply with the relevant provisions has the effect of enhancing income by way of non-granting of the relevant deduction in the year of incurring such expenditure. It is an altogether different matter that in the subsequent year the assessee becomes eligible for deduction on payment of tax. Hence apart from the consequences already faced by the assessee for failure to deduct tax at source or pay late as per the prescribed time in terms of the applicability of sections 201 and 271C etc., it came to be additionally hit by section 40(a)(ia) in terms of losing deduction of expenditure in the concerned year for its failure to deduct or pay after deduction of tax at source within the prescribed time, which was otherwise available to it because of having genuinely incurred the expenditure from assessment years 2005-2006.

The sum and substance of the submission of the assessee was that the relaxation given by the Finance Act 2010 has mitigated the unintended hardship which was earlier caused to the assessee and hence it should be given retrospective effect from the date of insertion of the provision.

There is no force in this contention. The reason is that there is no doubt that some intended difficulty has been caused by the Finance Act, 2004 on the introduction of section 40(a)(ia). It is a hardship to the assessee from a different angle as with the insertion of this provision the expenditure otherwise deductible has become non-deductible in the year of incurring on its failure to deduct tax at source or pay such tax after deduction within the stipulated period. At the same time it is "intended" for the reason that the legislature in its wisdom has brought out this provision with a view to augment compliance of the TDS provisions. The objective sought to be achieved by bringing out section 40(a)(ia) is the augmentation of the TDS provision. If in attaining this main objective of augmentation of such provision, the assessee suffers disallowance of any amount in the year of default, which is otherwise deductible, the legislature allowed it to continue. This is the cost which the Parliament has awarded to those assesses who fail to comply with the relevant provisions by considering the overall objective of boosting TDS compliance. Apart from other consequences of failure to deduct tax at source as discussed above, one more adverse consequence has been added. The fact that this provision is still continuing in the Act, proves that the Parliament did not consider it expedient to remove section 40(a)(ia) projecting so called hardship, which is only the side effect in the attainment of the larger goal of augmentation of compliance of TDS provision. The Finance Act, 2008 brought out certain amendments by relaxing the rigor of the provision by making two categories of defaults causing disallowance on the basis of the period of the previous year in which tax was deductible. It is important to note that the amendment by the Finance Act, 2008 was made with retrospective effect from 01.04.2005. Thus it can be seen that from the

assessment year 2005-2006 up to assessment year 2009-2010, post the retrospective amendment carried out by the Finance Act, 2008, the first category of disallowances included the cases in which tax was deductible and was so deducted during the last month of the previous year but there was failure on the part of the assessee to pay such tax on or before the due date specified in sub-section (1) of section 139; and the second category included cases in which tax was deductible and was so deducted during the first eleven months of the previous year but there was failure to pay it before the last day of the previous year. The Finance Act, 2010 has made partial change in the specified time for payment of tax only in the above referred second category by extending it from the last day of the previous year to the time specified u/s 139(1) of the Act, in parity with the specified time of the first category. Except for that there is no change in the overall structure of the provision. Non-deduction of tax at source from the specified payments still warrants disallowance u/s 40(a)(ia) as was there under the Finance (No. 2) Act, 2004 and the Finance Act, 2008. Further the disallowance per se has also been maintained in the provision in its current form, where the assessee, after deduction of tax at source, fails to pay it within the specified time. Still further, the prescription of the proviso providing for the remedial relief in the subsequent year in which tax has been paid, also exists.

None can appreciate the contention raised on behalf of the assessee that the undue hardship caused to the assessee has been relaxed by the legislature with the amendment carried out by the Finance Act, 2010. The so called hardship as caused with the insertion of section 40(a)(ia) with effect from 1st April, 2005 is still continuing as such. The effect of amendment by the Finance Act, 2010 is limited only to extending the time available for deposit of tax in the second category of cases from the last day of the previous year to the time specified u/s 139(1) of the Act. Thus it is vivid that the amendment by the Finance Act, 2010 is not aimed at removing any unintended hardship to the assessee, but to relax the intended hardship to some extent by increasing the time available for deposit of tax in one category of cases. When the amendment does not remove the unintended hardship or is not explanatory, the same cannot be held to be retrospective unless it is specifically provided.

It is abundantly clear that the time limit to deposit of tax deducted at source for one category of cases has now been extended by the Finance Act, 2010 to the due date u/s 139(1) of the Act. Such a benefit was earlier specifically excluded as it was available only in respect of the other category of cases. As such, it can not be inferred that the later extension of time is indicative of the intention of the legislature to have made it available even in the earlier years.

In view of the fact that section 40(a)(ia) has been amended by the Finance Act, 2010 with retrospective effect from 01.04.2010, the Court should refuse to declare it as having retrospective effect from the date of insertion of the provision *i.e.* 01.04.2005.

The legislature has employed the words 'such sum' in the language of the proviso and not 'any sum'. These words in the proviso talk of the sum referred to in the main provision of sub-clause (ia) of section 40(a). The words 'such sum' have tightly tied the proviso with the main provision. It is imperative to note the proviso to sub-clause (ia) always contained the words 'such sum' whether it is the insertion of section 40(a)(ia) by the Finance (No. 2) Act, 2004 or amendment by the Finance Act, 2008 or by the Finance Act, 2010. One needs to consider the non-obstante clause in the beginning of section 40 which provides that : "Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head 'Profits and gains of business or profession'". To put it simply, in order to fall within the trap of sub-clause (ia) of section 40(a) causing disallowance, it is sine qua non that the expenditure should be otherwise deductible in the year as per sections 30 to 38. Proviso obtains its scope from the main provision of sub-clause (ia) which, in turn, refers to the amounts otherwise

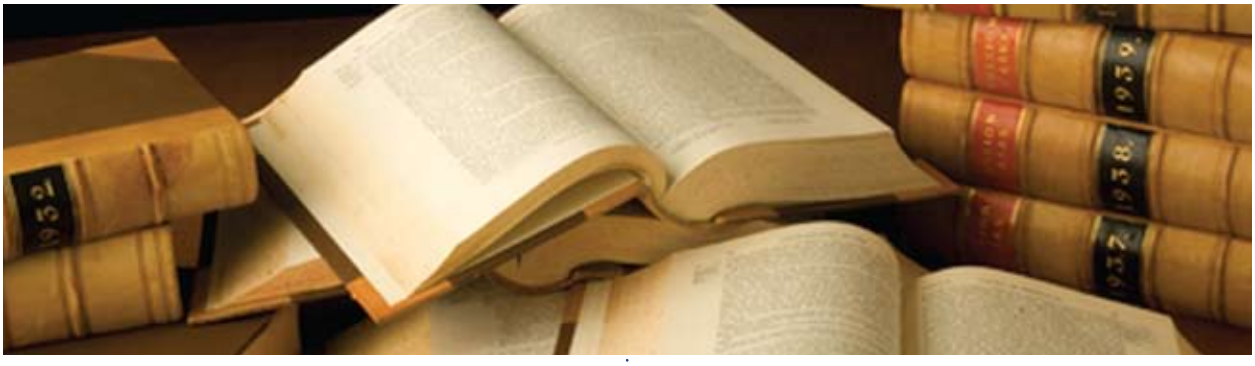
deductible in the year of incurring such expenditure under the head 'Profits and gains of business or profession'. Only when the assessee is otherwise eligible for deduction in respect of interest, commission, brokerage etc. in the year of its incurring, that the question of making disallowance u/s 40(a)(ia) arises. Thus the proviso is controlled by the main provision of sub-clause (ia) of section 40(a) and cannot be looked upon as *de hors* the main provision. Following the meaning of the words 'such sum' in the proviso, it becomes manifest that the sum deductible as expenditure in the year of payment of tax is the one which was not allowed as deduction due to disabling provision of section 40(a) in the year of incurring such expenditure. It cannot refer to the expenditure neither claimed nor disallowed as per the main provision in the earlier year. The proviso allows deduction of the amount of such expenditure in computing the income of the subsequent year, when tax is paid. To put it simply, the proviso is only an enabling provision in the subsequent year, of the disabling provision of the main part of the section 40(a)(ia) in an earlier year of incurring such expenditure. When a particular amount of expenditure is disallowed in the first year for failure to deduct tax at source or to pay tax thereon after such deduction as per the main provision of sub-clause (ia), then such amount of expenditure wins deduction on the payment of tax in the later year.

It is the complete provision of section 40(a)(ia) together with its proviso as prevailing in a particular year which governs the non-deductibility of expenditure in one year and then its deductibility in the later year. Because of the thread of 'such sum' in the language of proviso, it becomes impermissible to look at the main provision as amended by the Finance Act, 2008 for making disallowance of expenditure and then at the proviso as amended by the Finance Act, 2010 for allowing expenditure in the subsequent year of payment. The situation would have been otherwise, if the expression 'any sum' had been used in the language of the proviso instead of 'such sum'. In that case any amount of expenditure, on which tax deducted had been paid in a particular year, irrespective of the year of incurring expenditure, would have got deduction in such year of payment of tax. It is only in that case that payment of tax made in July 2009 would have suffered complete disallowance both in the A.Y.s 2009-10 and 2010-11. But fortunately, position is not so as the deduction will be permissible to the assessee in A.Y. 2010-11 going by the provision as amended by the Finance Act, 2008.

It can be seen that the Finance Act, 2010 has not repealed the provision of sec. 40(a)(ia) that it could be claimed that the hardships enumerated above which were caused by the Finance (No. 2) Act, 2004 have been done away with. The latest amendment has simply extended the time limit for deposit of tax deducted at source in certain cases. The other consequences of section 40(a)(ia) are still present in the provision. That apart, it is simple and plain that if the expenditure is not genuine or not incurred for the purpose of business, it would not at all qualify for deduction at the very threshold and the resultant application of section 40(a)(ia) would be automatically ruled out. None can be convinced with the contention of substantial compliance of the provisions on late deposit of tax deducted at source. There can be either compliance or non-compliance of a particular provision. Given the time limit for the deposit of tax deducted at source, if it is deposited by the time prescribed it is a case of compliance of the provision and if it is late deposit even by a single day, it is non-compliance. It cannot be said that by depositing such tax belatedly, the assessee substantially complied with the provisions of section 40(a)(ia).

The Finance Act, 2010 has extended the time limit for depositing tax deducted at source by the due date u/s 139(1) of the Act from the earlier lesser time available for compliance. If the tax is deposited by the due date, it would mean escape from the clutches of section 40(a)(ia) for assessment year 2010-2011, but if it is deposited even the next day beyond the due date, natural consequences would follow and it would call for disallowance u/s 40(a)(ia) in the year of incurring the expenditure. In the like manner, in the year under appeal, if the tax deducted at source up to February, 2005 had been deposited up to 31st March, it would have amounted to compliance of the provision, but the late deposit even on 1st April, 2005 would amount to noncompliance warranting interference by section 40(a)(ia) entailing disallowance of expenditure in the Assessment year 2005-06. However the fact that the assessee deposited it beyond the prescribed period, would amount to compliance of the prescription of the proviso, entitling the assessee to deduction in the A.Y. 2006-07.

Further if one proceeds with the hypothesis of substantial compliance even on late deposit not causing any disallowance u/s 40(a)(ia) in the year of incurring the expenditure, it will make the proviso redundant. When one considers the mandate of section 40(a)(ia) in entirety, it becomes apparent that it has two ingredients, viz., first, the disallowance of expenditure due to non-deduction or non-deposit of tax deducted at source in time and second, the allowing of expenditure in the later year in which the amount of tax deducted at source is deposited. It is one composite provision. Both these limbs, that is, the disallowance of expenditure in the year of incurring expenditure and allowing it in the year of payment are integral part of the provision. As per the proviso, the assessee gets deduction of expenditure in the year of payment of tax deduced at source. But if the Court allows deduction of the expenditure in the year of its incurring on some equitable ground or on the theory of substantial compliance despite the fact the tax was deposited beyond the prescribed time, then it would



mean the obliteration the proviso from the provision, which is obviously impossible.

In view of the foregoing reasons, the amendment carried out by the Finance Act, 2010 with retrospective effect from assessment year 2010- 2011 cannot be held to be retrospective from assessment year 2005-2006. The question posted before the Special Bench is, therefore, answered in negative, in favour of the Revenue and against the assessee by holding that the amendment brought out by the Finance Act, 2010 to section 40(a)(ia) w.e.f. 01.04.2010, is not remedial and curative in nature.

LD/60/73
CIT
Vs.
Lawrence D'Souza
September 14, 2011 (KAR)
[Assessment Year 1996-97]

Section 48 of the Income-tax Act, 1961 – Capital gains – Computation of

Where hotel business was stopped but assessee had to pay rent and interest and renovation expenses so that business could be sold as going concern, these expenses were to allowed as deduction in computing capital gains

The assessee was carrying on hotel business. Due to labour problem he stopped the business and wanted to sell it as a going concern. Even though he had stopped his business, the liability to pay rent and interest continued. It was not a personal liability of the assessee. Interest was payable on the amount borrowed for carrying on the business and rent was payable for the business premises. Therefore, the assessee claimed deduction of these amount while computing capital gains.

The Karnataka High Court held that in so far as renovation expenses was concerned, it was the specific case of the assessee that after the business was stopped, in order to get a good price, when he intended to sell the business as a going concern, he renovated the hotel premises. That was how these expenses were incurred after the closure of the premises. These expenses were incurred in connection with the business, though the business was stopped in the year 1994. Therefore, the authorities were justified in granting the said deduction.

LD/60/74
CIT
Vs.
Gaur Brahmin Vidya Pracharini Sabha
October 10, 2011 (P&H)

Section 80G read with Section 10(23C) of the Income-tax Act, 1961 read with Rule 11A of the Income-tax Rules, 1962 – Deductions – Donations to certain funds, charitable institutions, etc.

Merely because an educational institution is making a profit it would not render itself ineligible for registration under the provisions of section 10(23C)(vi), nor this would be a ground to deny registration under section 80G(5)(vi)

The Commissioner rejected the application filed by the respondent society under section 80G(5)(vi) of the Income Tax Act, 1961 on the ground that the respondent society was running five educational institutions, and it was charging fee in the range of 36,000/- to 1 lac and, therefore, it was not a charitable purpose. The Commissioner has relied upon the table wherein percentage of profit was reflected from 20.44% to 28.49% and came to the conclusion that the respondent was enhancing the earning capacity of the institutions through acquisition of the buildings and fixed assets and not fulfilling any noble objects.

The Tribunal noticed that the society was spreading education without any distinction of caste and creed by establishing educational institutions. The assessee was entitled for registration under Section 12AA of the Act with effect from 29.9.1980 and has been running educational institutions since then. Though the assessee derived income yet such income was held not liable to inclusion in total income as per Sections 11 and 12 of the Act. Reference had also been made to Section 2(15) of the Act to hold that the education is *per se* charitable purpose irrespective of the fact that for imparting education, the assessee charges fee and there is no condition to hold that to become eligible for charitable

purposes in respect of imparting education, the same should be imparted freely or without charging any fee.

The Punjab and Haryana High Court held that in *Sonepat Hindu Educational Charitable Society v. CIT (2005) 278 ITR 262 (P&H)*, it was held that where the petitioner society has been regularly allowed exemption under Section 80G and especially where it is registered under section 12A for charitable purposes then the position has to be sustained and not changed in subsequent years without any sufficient proof that the institution is not carrying its activities in furtherance of its object.

Mere making of profit would be ground to deny registration once the objects of the society were for charitable purpose and especially where five educational institutions were being run by the respondent which was registered since 29.9.1980 under the Societies Registration Act, 1860, and solely because the respondent was charging fees and was getting surplus, would not be a reason to deny registration.

It was held that, if an institution is making a profit, it would not render itself ineligible for registration under the provisions of section 10(23C)(vi). Merely, because there are some surplus with a charitable institution, this should not be a ground to deny the registration under section 80G(5)(vi). Even otherwise Proviso to section 2(15) of the Act also mentions that assessee should not carry activities in the name of trade, commerce and business.

Where, as a matter of fact, the Tribunal had found that the conditions laid down in Rule 11AA of the Income Tax Rules, 1962 had also been complied and held that the Trust was eligible for registration under section 80G(5)(vi), no substantial question of law as contended arose.

LD/60/75
CIT
Vs.
Ms. Jagriti Aggarwal
October 10, 2011 (P&H)
[Assessment Year 2006-07]

Section 139 read with Section 54 of the Income-tax Act, 1961 – Return of income

Due date for furnishing return of income as per section 139(1) is subject to extended period provided under sub-section (4) of section 139

Sub-Section (4) of section 139 of the Act is, in fact, a *proviso* to sub-section (1) of section 139 of the Act fixes the different dates for filing the returns for different assesses. In the case of assessee who is an individual, it is 31st day of July of the assessment year in terms of clause (c) of the *Explanation* 2 to sub-section 1 of section 139 of the Act, whereas sub-section (4) of Section 139 provides for extension in period of due date in certain circumstances.

A reading of the sub-section (4) would show that if a person has not furnished the return of the previous year within the time allowed under sub-section (1) *i.e.* before 31st day of July of the assessment year, the assessee can file return before the expiry of one year from the end of the relevant assessment year. Thus, sub-section (4) of section 139 provides extended period of limitation as an exception to sub-section (1) of section 139. Sub-section (4) is in relation to the time allowed to an assessee under sub-section (1) to file return. Therefore, such provision is not an independent provision, but relates to time contemplated under Sub-Section (1) of section 139. Therefore, such sub-section (4) has to be read along with sub-section (1).

The due date for furnishing the return of income as per section 139(1) of the Act is subject to the extended period provided under sub-section (4) of section 139. Where the sale of the asset took place on 13-1-2006, falling in the previous year 2006-2007, the return could be filed before the end of relevant assessment year 2007-2008, *i.e.*, on 31.3.2007.

LD/60/76
Alok Todi
Vs.
CIT
July 13, 2011 (CAL)
[Block Period 1987-88 to 1996-97]

Section 260A read with Section 144 of the Income-tax Act, 1961 – High Court – Appeal to

Where in spite of service, neither any return was submitted nor any cause shown pursuant to notice, best judgment assessment of Assessing Officer cannot be said to be vitiated by any error of law

The new plea sought by the assessee before the High Court was that the Assessing Officer should have furnished necessary documents and intimates the date of personal hearing. However, no such plea was taken either before the Assessing Officer or the Tribunal. In spite of service of notice, nobody even submitted return or had shown cause as required.

The Calcutta High Court held that raising new questions which were essentially questions of fact could not be permitted to be raised for the first time in appeal before High Court under section 260A and the Revenue in terms of sub-section 4 of section 260A would be entitled to raise the question that the ground formulated were not involved within the scope of this appeal. When no material had been produced dislodging the finding of the Assessing Officer that in spite of service neither any return was submitted nor any cause shown pursuant to the notice, the best judgment assessment of the Assessing Officer cannot be said to be vitiated by any error of law.

Finance (No. 2) Act, 1998

LD/60/77

Union of India[3]

Vs.

Nitdip Textile Processors Pvt. Ltd.

November 3, 2011 (SC)

Section 87 of the Finance (No. 2) Act, 1998 – Kar Vivad Samadhan Scheme

Section 87(m)(ii) (b) of Finance (No.2) Act, 1998 is not violative of Article 14 of the Constitution of India even though it seeks to deny the benefit of the 'Kar Vivad Samadhana Scheme, 1998 to those who were in arrears of duties etc., as on 31.03.1998 but to whom the notices were issued after 31.03.1998

The Gujarat High Court, *vide* its impugned judgment and order dated 25.07.2005, has declared that Section 87(m)(ii) (b) of Finance (No.2) Act, 1998 (the Act) is violative of Article 14 of the Constitution of India insofar as it seeks to deny the benefit of the 'Kar Vivad Samadhana Scheme, 1998 to those who were in arrears of duties etc., as on 31.03.1998 but to whom the notices were issued after 31.03.1998 and further, has struck down the expression "on or before the 31st day of March 1998" under Section 87(m)(ii)(b) of the Act as *ultra vires* of the Constitution of India and in particular, Article 14 of the Constitution on the ground that the said expression prescribes a cut-off date which arbitrarily excludes certain category of persons from availing the benefits under the Scheme. The High Court has further held that as per the definition of the 'tax arrears' in Section 87(m) (ii)(a) of the Act, the benefit of the Scheme was intended to be given to all persons against whom the amount of duties, cess, interest, fine or penalty were due and payable as on 31.3.1998. Therefore, this cut-off date in Section 87(m)(ii) (b) arbitrarily denies the benefit of the Scheme to those who were in arrears of tax as on 31.03.1998 but to whom notices were issued after 31.3.1998. This would result in unreasonable and arbitrary classification between the assessees merely on the basis of date of issuance of Demand Notices or Show Cause Notices which has no nexus with the purpose and object of the Scheme. In other words, the persons who were in arrears of tax on or before 31.03.1998 were classified as those, to whom Demand Notices or Show Cause Notices have been issued on or before 31.03.1998 and, those to whom such notices were issued after 31.3.1998. The High Court observed that this classification has no relation with the purpose of the Scheme to provide a quick and voluntary settlement of tax dues. The High Court further observed that this artificial classification becomes more profound in view of the fact that the Scheme came into operation with effect from 1.9.1998 which contemplates filing of declaration by all persons on or after 1.9.1998 but on or before 31.1.1999. The High Court further held that all persons who are in arrears of direct as well as indirect tax as on 31.3.1998 constitute one class, and any further classification among them on the basis of the date of issuance of Demand Notice or Show Cause Notice would be artificial and discriminatory. The High Court concluded by directing the Revenue to consider the claims of the respondents for grant of benefit under the Scheme, afresh, in terms of the Scheme.

The Supreme Court held that the Scheme was introduced by Finance (No.2) Act and is contained in Chapter IV of the Act. The Scheme is known as Kar Vivad Samadhana Scheme, 1998. It was in force between 1.9.1998 and 31.1.1999. Briefly, the Scheme permits the settlement of "tax arrears" as defined in Section 87(m) of the Act. The object and purpose of the Scheme is to minimize the litigation and to realize the arrears of tax by way of Settlement in an expeditious manner.

The Scheme defines the meaning of the expression 'Tax Arrears', in relation to indirect tax enactments. It would mean the determined amount of duties, as due and payable which would include drawback of duty, credit of duty or any amount representing duty, cesses, interest, fine or penalty determined. The legislation, by using its prerogative power, has restricted the dues of duties quantified and payable as on 31st day of March, 1998 and remaining unpaid till a particular event has taken place, as envisaged under the Scheme. The date has relevance. The definition is inclusive definition. It also envisages instances where a Demand Notice or Show Cause Notice issued under indirect tax enactment on or before 31st day of March, 1998 but not complied with the demand made to be treated as tax arrears by legal fiction. Thus, legislation has carved out two categories of assessees viz. where tax arrears are quantified but not paid, and where Demand Notice or Show Cause Notice issued but not paid. In both the circumstances, legislature has taken cut off date as on 31st day of March 1998. It cannot be disputed that the legislation has the power to classify but the only question that requires to be considered is whether such classification is proper. It is now well settled by catena of decisions of this Court that a particular classification is proper if it is based on reason and not purely arbitrary, caprice or vindictive. On the other hand, while there must be a reason for the classification, the reason need not be good one, and it is immaterial that the Statute is unjust. The test is not wisdom but good faith in the classification. It is too late in the day to contend otherwise. It is time and again observed by this Court that the Legislature has a broad discretion in the matter of classification. In taxation, 'there is a broader power of classification than in some other exercises of legislation'. When the wisdom of the legislation while making classification is questioned, the role of the Courts is very much limited. It is not reviewable by the Courts unless palpably arbitrary. It is not the concern of the Courts whether the classification is the wisest or the best that could be made. However,

[3] *Decision of the Gujarat High Court in Special Civil Application No. 735 of 1999 dated 25.07.2005 was set aside.*

a discriminatory tax cannot be sustained if the classification is wholly illusory.

Kar Vivad Samadhan Scheme is a step towards the settlement of outstanding disputed tax liability. The Scheme is a complete Code in itself and exhaustive of matter dealt with therein. Therefore, the courts must construe the provisions of the Scheme with reference to the language used therein and ascertain what their true scope is by applying the normal rule of construction. Keeping this principle in view, the reasoning of the High Court is to be considered.

The tests adopted to determine whether a classification is reasonable or not are, that the classification must be founded on an intelligible differentia which distinguishes person or things that are grouped together from others left out of the groups and that the differentia must have a rational relation to the object sought to be achieved by Statute in question. The Legislature in relation to 'tax arrears' has classified two groups of assessees. The first one being those assessees in whose cases duty is quantified and not paid as on the 31st day of March, 1998 and those assessees who are served with Demand or Show Cause Notice issued on or before the 31st day of March, 1998. The Scheme is not made applicable to such of those assessees whose duty dues are quantified but Demand Notice is not issued as on 31st day of March, 1998 intimating the assessee's dues payable. The same is the case of the assessees who are not issued with the Demand or Show Cause Notice as on 31.03.1998. The grievance of the assessee is that the date fixed is arbitrary and deprives the benefit for those assessees who are issued Demand Notice or Show Cause Notice after the cut off date namely 31st day of March, 1998. The Legislature, in its wisdom, has thought it fit to extend the benefit of the scheme to such of those assessees whose tax arrears are outstanding as on 31.03.1998, or who are issued with the Demand or Show Cause Notice on or before 31st day of March, 1998, though the time to file declaration for claiming the benefit is extended till 31.01.1999. The classification made by the legislature appears to be reasonable for the reason that the legislature has grouped two categories of assessees namely, the assessees whose dues are quantified but not paid and the assessees who are issued with the Demand and Show Cause Notice on or before a particular date, month and year. The Legislature has not extended this benefit to those persons who do not fall under this category or group. This position is made clear by Section 88 of the Scheme which provides for settlement or tax payable under the Scheme by filing declaration after 1st day of September, 1998 but on or before the 31st day of December, 1998 in accordance with Section 89 of the Scheme, which date was extended upto 31.01.1999. The distinction so made cannot be said to be arbitrary or illogical which has no nexus with the purpose of legislation. In determining whether classification is reasonable, regard must be had to the purpose for which legislation is designed. While understanding the Scheme of the legislation, the legislation is based on a reasonable basis which is firstly, the amount of duties, cesses, interest, fine or penalty must have been determined as on 31.03.1998 but not paid as on the date of declaration and secondly, the date of issuance of Demand or Show Cause Notice on or before 31.03.1998, which is not disputed but the duties remain unpaid on the date of filing of declaration. Therefore, the Scheme 1998 does not violate the equal protection clause where there is an essential difference and a real basis for the classification which is made. The mere fact that the line dividing the classes is placed at one point rather than another will not impair the validity of the classification.

In view of the above discussion, the findings and the conclusion reached by the High Court could not be upheld.

OTHER ACTS

Companies Act

LD/60/78

Podar Finance (P.) Ltd.

Vs.

Official Liquidator

October 10, 2011 (RAJ)

Section 536, read with section 428, of the Companies Act, 1956 – Avoidance of transfers, etc., after commencement of winding up

Court has absolute discretion to validate the transaction of transfer of shares after commencement of winding up only if it is found that the transaction was for the benefit of and in the interest of the company or for keeping the company going or keeping things going generally

Shakti Mills was a holding company while Jaipur Spinning Mills was its subsidiary company. Shri G.N. Poddar is Director in Shakti Mills and also in Jaipur Spinning Mills and his son Ajay Poddar is also Director in Jaipur Spinning Mills and the applicant Poddar Finance and his another son Pawan Poddar is Director of applicant-Poddar Finance. A petition for winding up of company Shakti Mills was filed on 25-4-1978 and the High Court ordered winding up of Shakti Mills on 21-1-1981. The applicant-Podar Finance purchased certain shares of Jaipur Spinning Mills from Shakti Mills and those shares were transferred on 10-5-1979. The applicant-Podar Finance filed an application and it was prayed that applicant-Poddar Finance be held to be a contributory of Jaipur Spinning Mills in liquidation. The Official Liquidator contested theapplication stating that in view of section 536(2), the transfer of shares after presentation of winding up petition of Shakti Mills was void as shares held by Shakti Mills could not have been legally transferred after presentation of winding up petition. The Company Judge also held that the applicant could not be held to be contributory. The Company Judge has assigned the following reasons while recording the finding that applicant-Poddar Finance cannot be treated to be a contributory of Jaipur Spinning Mills in liquidation:-

(i) That transfer of shares in question in the same management by one company to another was made on the under-valued price and therefore, transfer of shares could not be said to be in the interest of creditors, which was of paramount consideration and should not be defeated.

(ii) That the Court has not validated the transaction, as such, the applicant-Poddar Finance could not be treated to be a contributory of Jaipur Spinning Mills in liquidation.

(iii) That applicant-Poddar Finance cannot be held to be a contributory merely because it holds fully paid-up shares of Jaipur Spinning Mills in liquidation and the transfer of shares in question is hit by the provisions of section 536(2) of the Act.

The Rajasthan High Court held that the applicant-Poddar Finance had not claimed any investment in Jaipur Spinning Mills as was evident from the balance sheets and thus, cloud was cast over the genuineness of the transaction in question. The Official Liquidator of Shakti Mills had also objected to the transfer of shares in question *vide* letter dated 2.8.2011.

As per Section 428, "contributory" includes holder of any shares which are fully paid-up. It includes any person alleged to be a contributory. Section 536(2) provides that in the case of a winding up by the Court, any transfer of shares in the company or alteration of the status of its members, made after the commencement of the winding up, shall, unless the Court otherwise orders, be void.

There is power given to the court to validate the transfer which has taken place after the commencement of the proceedings for winding up of the company. As per provisions of section 441(2), winding up order relates back to the date of presentation of the petition for winding up. In the instant case, winding up of Shakti Mills had been ordered and since the transfer of shares in question was made after commencement of the winding up proceedings, the same was void under section 536(2) unless otherwise ordered by the Court. It was not the case of the applicant-Poddar Finance that any court had otherwise ordered. Thus, the expression "unless otherwise ordered by the Court, any transfer made after the commencement of the winding up proceedings is void" has to be given full effect. The Court is given power to validate the transaction. Thus, any disposition would not be *ab initio void*. The word 'void' is not conclusive as Court has been given power to order otherwise. However, the fact remains that in the instant case, the Court has not so far ordered otherwise.

Under section 536 (2) transaction of transfer of share or other disposition is not required to be annulled by court. It is void unless court orders otherwise. An order "to the otherwise" is required to be made in order to validate transfer of share/other disposition. It was at option of the applicant to avoid it but he has not chosen that recourse. The submission to the contrary raised could not be accepted that it was for official liquidator to get transfer of shares declared void or court to make such declaration. It was for Poddar Finance to get transfer of shares validated. Whatever it may be, in the absence of validation, statutory expression as to voidity of transaction mandated in section 536(2) of the Act has to be given full effect.

Under section 443, the Court may dismiss the petition or make an order of winding up. Under sub-section (2) of Section 443, the Court may refuse to make order of

winding up. Before appointing a provisional liquidator, the Court has to give notice to the company and reasonable opportunity to make representation. As per Section 449 of the Act, on a winding up order being made in respect of a company, the official liquidator becomes the liquidator of the company. In the instant case, the order of winding up of Shakti Mills had been passed and official liquidator had been appointed by Bombay High Court with respect to Shakti Mills and thus, transaction in question had to be treated as void unless the court otherwise ordered and the court had not ordered otherwise. Consequently, the transaction was void, the applicant- Poddar Finance could not be said to be a contributory.

In *Tulsidas Jasraj Parekh v. Industrial Bank of Western India, AIR 1931 Bom. 2*, it has been laid down by the Bombay High Court that any *bona fide* transaction carried out and completed in the ordinary course of current business will be sanctioned by the Court under section 227(2) of Companies Act, 1913. On the other hand, it will not allow the assets to be disposed of at the mere pleasure of the company and thus, cause the fundamental principles of equity amongst creditors to be violated.

The Court has absolute discretion to validate the transaction. However, discretion is to be controlled and exercised judicially. If it is found that the transaction was for the benefit of and in the interest of the company or for keeping the company going or keeping things going generally, it ought to be confirmed.

The Bombay High Court in the case of *Sarigam Containers (P.) Ltd. V. Magatul Industries Ltd. [2009] 90 SCL 321 (Bom)* held that it is also to be shown as to what were the compelling circumstances necessitating the company in liquidation to enter into such transaction during the pendency of winding up action. In absence of such pleadings that transaction was for the benefit and in the interest of company or for keeping the company going or for keeping things going generally, the question of validating such transaction by the court does not arise. No improper transaction which is covered by section 536(2) of the Act can be validated by the Court.

In *Administrator, MCC Finance Ltd. V. Ramesh Gandhi, [2009] 63 SCL 326 (Mad)*, the Madras High Court has considered the provisions of section 536(2) of the Act and has observed that the object of section 536 seems to be to prevent improper disposition or dissipation of the property or transfer of shares of the company otherwise available for distribution among the creditors of the company in liquidation. If the transfer is not *bona fide*, in terms of section 536(2), the transaction would be void. Once winding up has been ordered, the provisions of section 536(2) are attracted.

In the present case, considering of aspect that interest of creditors is of paramount consideration, the Official Liquidator had rightly opined that transaction in question was grossly under-valued. The Official Liquidator of Shakti Mills had also preferred an application in the Bombay High Court alleging under-value of the transaction by more than ₹17 lakhs. 1,65,010 equity shares of ₹10/- each and 12,478/- preference shares of ₹100/- each of Jaipur Spinning Mills were transferred by Shakti Mills in favour of applicant-Poddar Finance for a paltry consideration of ₹22,854. The transaction could not in any manner be said to be for the benefit and interest of the company or for keeping the company going or keeping things going generally. It had not been shown as to what were the compelling circumstances necessitating Shakti Mills to transfer the shares in question of Jaipur Spinning Mills in favour of applicant-Poddar Finance after commencement of proceedings of winding up. Considering the surrounding circumstances and *inter-se* relationship of the Directors of all the three managements, the transaction in question could not be said to be *bona fide* and it was to be treated as void in view of section 536(2) of the Act. The court had not ordered otherwise under section 536(2) and even no application has been filed by the applicant for validation in court so as to order otherwise. The applicant had failed to satisfy as to *bona fide* nature of the transaction in question. Thus, the transfer in question was to be treated as void in term of section 536(2) of the Act. On the basis of such transaction, applicant could not claim to be contributory.

No application for validation of transaction in question has been filed by the applicant-Poddar Finance for the last 30 years. When winding up of Shakti Mills had been ordered, obviously transaction was void as per statutory mandate of section 536(2) which could not be ignored by us while adjudging the question whether the applicant Poddar Finance was contributory or not. The surrounding circumstances showed that transaction was not to benefit creditors or to keep company going, it appeared to be under-valued also. Unless and until transaction was legal and validated, the applicant-Poddar

Finance could not claim itself to be a contributory and the Company Court and Official Liquidator had rightly opined so. The applicant had as per agreement availed recourse of settlement of its claim as contributory with the Official Liquidator under the provisions of the Act and the Rules. Thereafter, finding had been recorded by the Official Liquidator that applicant could not be treated to be a contributory and report was submitted to the Company Court and the Company Court had also expressed the same opinion that applicant could not be held to be a contributory, which was in accordance with the law. Since the transfer of shares in question was void in view of section 536(2) of the Act, the applicant-Poddar Finance could not be treated to be a contributory.

The intendment of section 537 is to prevent fraudulent preference, transactions which are not in good faith or are not effected in ordinary course of business and even attachment, distress or execution are avoided unless permitted by court. In the instant case, provisions of section 536(2) of the Act were attracted and the applicant-Poddar Finance Private Limited could not be held to be a contributory of company Jaipur Spinning Mills in liquidation.

SEBI

LD/60/79
Pawan Goyal
Vs.
Securities and Exchange Board of India
September 16, 2011 (DEL)

Section 27 read with Section 24 of the Securities and Exchange Board of India Act, 1992 read with Regulations 26 and 27 of the Securities and Exchange Board of India (Collective Investment Schemes) Regulations, 1999 – Offences by Companies

Where in the complaint it has been averred that directors were the persons in charge of and responsible for conduct of business of accused company and, thus, were liable for the violations committed by accused company, as provided by section 27 of the Act, petitions by directors seeking relief from liability should be dismissed

A complaint was filed on behalf of the Securities and Exchange Board of India and taking cognisance of the same the accused, *i.e.*, the company and persons stated to be its directors and in day to day control of the affairs of the company were summoned to face trial by the Metropolitan Magistrate. It is alleged that as per Regulation 68 of the Securities and Exchange Board of India (Collective Investment Schemes) Regulations, 1999 persons operating Collective Investment Schemes had to register the scheme before the Board and as per regulation 73 in the failure to do so, the scheme would be wound up with information to the investors and the board and simultaneously the investments would be returned to the investors. It was alleged in the complaint that the last date by which the Collective Investment Schemes had to be got registered was March 31, 2000. Alleging that accused company had neither got registered the Collective Investment Scheme(s) floated by it nor refunded the amounts to the investors; thus, an offence punishable under section 24 of the Act was committed. The petitioners who were stated to be the directors of the company and were impleaded as accused have filed the petitions stating that all of them have resigned as directors of accused company in the years 1994 and 1996 and thus were not liable for default of the company.

The High Court of Delhi held that it is not the grievance in the petitions that the averments made in the complaint do not make out any case against the petitioners assuming that the petitioners are directors of the company. On the plea that the petitioners had resigned, suffice would it be to state that along with the petitions, certified copies of Form No. 32, prescribed under the Companies Act, 1956, have not been filed, and thus it would be a matter of trial whether the petitioners ceased to be directors of the company in the year in which they allege to have resigned as directors of the company.

It was a continuing offence if money was not returned to the depositors upon the Collective Investment Scheme not being registered with the SEBI latest by March 31, 2000 and in the complaint in question there is an averment that since the company did not register the scheme by March 31, 2000, on December 7, 2000, the SEBI directed the company to refund the money collected under the scheme to the investors within one month and report compliance, and despite repeated directions, compliance has not been made. In other words, the wrong continues till the amounts collected are not returned to the depositors.

The offence is upon not getting the scheme registered retaining the amount received from the depositors and not refunding the same to them within the time prescribed. The offence is not to have got registered the Collective Investment Scheme. The offence is to continue with the scheme post March 31, 2000, in spite of the scheme not being registered and the deposits not returned to the investors.

Since no argument has been advanced with respect to the deficiency or otherwise in the complaint pertaining to the vicarious liability of the alleged directors, the issue was not dealt with. It is simply highlight that in the complaint it has been averred that as directors were the persons in charge of and responsible for the conduct of the business of accused Company and thus were liable for the violations committed by accused company, as provided by section 27 of the SEBI Act, 1992. Therefore, the petitions were liable to be dismissed. ■