Legal Decisions[1]

Income-tax Act

LD/61/48
Shantikumar D. Majithia
Vs.
Deputy CIT, Central Circle-IV, Mumbai
October 19, 2012 (MUM-ITAT)
[Assessment Years 2006-07 & 2007-08]

Section 2(22), read with section 2(24), of the Income-tax Act, 1961 – Deemed Dividend

Where company had given its shareholders perpetual occupancy rights of flats constructed by it in lieu of which share-holder had to give interest free refundable deposit towards proportionate land cost and development cost and shareholder was entitled to transfer the occupancy rights by way of sale and transfer of block of assets and create third party rights subject to transferee deposit required amount of interest free refundable security deposit, cost of flat would be deemed dividend

The assessee was a shareholder of HPPL, which was a closely held family company. The company purchased a land at Andheri (W), constructed building and had given occupancy rights to its shareholders based on the number of shares held by them. HPPL declared the said assets as fixed assets and distributed the same amongst shareholders. Assessing Officer found that letters granting occupancy rights were given by HPPL to its shareholders on 25.3.2006 and therefore, it was covered by Assessment Year 2006-07 and Assessment Year 2007-08 and whereas assessee contended that occupancy rights were given to the shareholders for the year ending on 31.3.2002 and if the provisions of section 2(22)(a) were applied, no addition could be made as deemed dividend because HPPL did not have any accumulated profits as on 31.3.2002. However, Assessing Officer, as mentioned hereinabove, held that assessee by its letter dated 25.3.2006 had been granted occupancy rights to its shareholders and adopted market value of the property as per Stamp Duty Reckoner and added the same under Section 2(22)(a). The CIT(A) also agreed with the findings of Assessing Officer that occupancy right was given by HPPL to its shareholders in the Assessment Years 2006-07 and 2007-08.

The Tribunal held that:

The occupancy rights of the premises were given to the assessee in the Assessment Year 2006-07 as letter, dated 25.3.2006 addressed to the assessee categorically states that he had to pay interest free refundable deposit amount of ₹ 18 lakhs towards the proportionate land, construction and development cost. It was further stated therein that assessee was liable to pay municipal taxes and other outgoings in respect of flat for the occupancy right was given to the assessee every month. The municipal taxes were also to be paid by the assessee. It was also stated in the said letter that assessee was entitled to transfer the occupancy rights of the concerned flat by way of sale and transfer of block of shares and create third party rights subject to transferee depositing with HPPL the required amount of interest free security deposit and assessee shall also be entitled to give possession of the said flats to any transferee and HPPL had no objection for the same. It was evident that assessee had got the occupancy right of the premises by way of letter dated 25.3.2006. Hence, the authorities below had rightly held that said occupancy right was given to the assessee in Assessment Year 2006-07 and not in earlier assessment years.

The CIT(A) held that occupancy rights received by the assessee was benefit of perquisite under section 2(24)(iv) at ₹16,44,000 for assessment year under consideration *i.e.* Assessment Year 2006-07 and ₹17,74,000 for subsequent assessment year *i.e.* Assessment Year 2007-08.

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

The assessee had received occupancy rights in the premises on perpetual basis and in lieu of which, assessee to hold shares in HPPL and also to give interest free refundable deposit of ₹18 lakhs towards proportionate land cost and development cost. Assessee was also entitled to transfer the occupancy rights by way of sale and transfer of block of assets and create third party rights subject to transferee deposit the required amount of interest free refundable security deposit and assessee thereafter to give possession to the transferee. Therefore, the CIT(A) was not justified to hold that it was perquisite benefit given by HPPL to its shareholder and not the transfer of occupancy rights to its shareholders. Hence, the provisions of section 2(24)(iv) did not apply to grant of occupancy rights by HPPL to the shareholder, i.e. assessee herein, on the facts of the present case.

The assessee had got the occupancy right in perpetuity as assessee can transfer his occupancy rights of the premises under consideration by way of sale to a third party subject to condition that transferee was to deposit the required amount of interest free security deposit with HPPL. It was observed that the consideration to be received by the assessee on transfer of his occupancy right was not to be refunded to HPPL. It was also observed that HPPL will have no objection for creating third party rights in the occupancy right given to assessee.

Further, during the course of hearing, the assessee submitted that HPPL had given occupancy rights in the premises to the assessee perpetually and, therefore, it was to be considered release of assets by HPPL. The Revenue submitted that assessee had got in guise of occupancy rights full ownership with small amount of security deposit and, therefore, it was to be considered as deemed dividend under Section 2(22)(a). Section 2(22)(a) also provides that any distribution by a company of accumulated profits, whether capitalized or

not, if such distribution entails the release by the company to its shareholders of all or any part of the assets, it was a deemed dividend. Therefore, the value of flats received were nothing but dividend given in the form of assets by HPPL. Hence, the said occupancy right of the premises allotted by HPPL to assessee amounts to deemed dividend under Section 2(22)(a).

LD/61/49

Krishna Gopal Maheswari

Vs.

Additional CIT, Range-5, Firozabad

October 23, 2012 (Agra-ITAT)

[Assessment Year 2008-09]

Section 2(22) of the Income-tax Act, 1961 – Deemed Dividend

Where assessee-director failed to establish that money lending business was the substantial part of the business of the company and the loans and advances received during the course of money lending business, the assessee will not fall under the exceptional circumstances provided in section 2(22)(e)(ii) for the purpose not to include the calculation of deemed dividend.

A company in which public are not substantially interested may not declare dividends or adequate dividends and may merely give loans to shareholders and such loans, not being dividends under the general law, would not be taxable as income in the hands of shareholders. As the public would not have substantial interest in such company, those substantially interested in the company may not recover the loans or allow them to be that barred by time. The result would be that the amounts which were ostensibly received as loans or advances become the income of shareholders and yet they would not be required to pay any tax on said income under the general law. It is to avoid the evil of this nature that sub-clause (e) of section 2(22) had been enacted.

Section 2(22)(e) is applicable for any payment by a company, not being a company in which the public are substantially interested, of any sum by way of advance or loan to a shareholder, being a person who is the beneficial owner of shares holding not less than the 10% of the voting power …….. but this deemed dividend does not include any advance or loan made to shareholder by a company in the ordinary course of its business, where the lending of money is substantial part of business of the company.

The assessee had taken unsecured loan from company KBIP of ₹37,28,059. The assessee was a Director and having substantial interest in the company KBIP. The assessee was holding not less than 10% of the voting power in the said Company. The Assessing Officer sought to treat the said amount as deemed dividend as per the provisions of section 2(22)(e. Before the Assessing Officer it was submitted by the assessee that clause (3) of object clause of the Company was to carry on the business of financing enterprises and to finance whether by way of making loans or advances to or subscribing to the capital etc. The Assessing Officer after considering the assessee's submission noticed that the object clause of the company nowhere shows that the company's main business was of money lending. The Assessing Officer examined the Balance Sheet of the company and noticed that the total loans and advance were only ₹47,90,339/-, out of which loan to the

extent of ₹37,28,029/- was given to the assessee. The Assessing Officer had also examined the Profit & Loss Account of the company and noticed that interest received from the assessee of ₹62,280/- had been shown as indirect income. The company also had no license of money lending business. The Assessing Officer made addition of ₹37,28,059/- under section 2(22)(e). The Order of the Assessing Officer had been confirmed by the CIT(A).

The Tribunal held that, for doing money lending business one had to obtain necessary permission from competent authority. There was no evidence to support that the company had followed any procedure based on which it can be said that the substantial part of the business of the company was money lending. If this aspect is examined from business activities, there were accepted principles that the business activities and transaction were recorded in the books of account. In the case under consideration, the total loan and advances as on 31.03.2008 were only in respect of three parties.

Further in respect of loan and advances to one of the parties, the amount had been shown as investment in the balance sheet and not under the loans and advances. The assessee did not take interest bearing loans and advances from different parties. The auditor had also in his report clarified that the company had not granted but taken unsecured loans, interest free, from other parties covered in the register maintained under Section 301 of the Companies Act, 1956. In money lending business, the transactions are taking and giving money on finance. This is a fundamental characteristic of money lending business. The Apex Court in the case of *State of Gujarat v. Raipur Manufacturing Co. Ltd. (1967) 19 STC 1 (SC)* while defining the word business in taxing statute the Courts held that

the word "business" used in the sense of an occupation or profession are which occupies time, attention and labour of a person, normally with the object of making profit. To regard an activity as business there must be a course of dealing either only continued or contemplated to be continued with a profit motive and not for support or pleasure. Whether or not a person carries on business in a particular commodity must depend upon volume, frequency continuity and regularity of transaction of purchase and sale in a class of goods and transaction must ordinary be included into that profit motive. To carry on business ordinarily the characteristic of volume, frequency, continuity and regularity indicate and intension to continue the activity of carrying on transaction must exist.

In the light of above discussion, the assessee had failed to establish that the substantial part of business of the company was money lending and the loans and advances received to the assessee was the in the ordinary course of money lending business. Unless the assessee established that money lending business was the substantial part of the business of the company and the loans and advances received during the course of money lending business, the assessee will not fall under the exceptional circumstances provided in section 2(22)(e)(ii) for the purpose not to include the calculation of deemed dividend. Further, merely stating in the object clause that the business of the assessee company was money lending cannot be held that the case of assessee falls under exceptional circumstances not to treat the deemed dividend.

LD/61/50
IC, In re
August 27, 2012 (AAR)

Section 9 read with Section 56 and Section 195 of the Income-tax Act, 1961 read with Article 23 of the India-US Double Taxation Avoidance Convention - Income - Deemed to accrue or arise in India

Where suits were filed against Indian company by US investors in US for manipulation and misstatement in account, and as per settlement approved by US Court, Indian company deposited settlement amount, TDS obligation of Indian company would arise as cause of action arose in India even though US investors acquired right of action as per statute in US

The shares of applicant company IC are listed in the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) in India. Its American Depository Shares (ADS) were listed in the New York Stock Exchange (NYS). The price of the shares of IC fell suddenly in the market as a result of an admission by its former Chairman from India that the accounts prepared as on 30.9.2008 contained some misstatements. Suits were filed by the US investors against IC and A and B in various jurisdictions in the US. The suits were consolidated. A consolidated Class Action Complaint was filed for alleged violation.

Under the proposed settlement IC agreed to pay $ 125 million to the Qualified Settlement Fund (QSF) to be administered by Lead counsel for distributing the compensation. The US court passed a preliminary order approving the settlement. The Reserve Bank of India

gave approval and the settlement amount was deposited by IC into an initial escrow account in USA. Subsequently, the US court passed a final order confirming the settlement arrived at. The QSF came under the control of Lead Counsel subject to control of the US court. The applications before the Authority for Advance Rulings were filed questioning as to whether on the settlement amount TDS obligation arose under section 195?

The Authority for Advance Rulings held that the Court in America took note of the several suits already filed and consolidated them and permitted them to be prosecuted as a class action in terms of the procedural laws of that country. Those suits filed were for damages or compensation. The claim was based on liability in tort. The suits were no doubt consolidated into a class action for breach of the provisions of the Securities Exchange Act of that country. But, the action had its origin in tort. The prayer was for recovery of damages for that tort. The class action complaint also avers that the action seeks to recover damages caused by the defendants 'mis-conduct'. It further says that the complaint asserts a claim under the Securities Exchange Act and the Securities Act.

The suit having been filed for damages, any settlement arrived at therein without specifically admittedly or not admitting liability for payment of compensation, cannot be considered to be compensation for forbearance to sue. The amount agreed to be paid can only be understood as damages agreed to be paid by way of settlement without going to trial and without admitting guilt or liability. Therefore, the sums of $ 125 million and $ 25.5 million agreed to be paid to Lead plaintiffs would be in the nature of damages or compensation.

A compromise is only a contract. It becomes a decree or order of court when it receives the approval of the court and it is accepted. It is a contract with the imprimatur of the court. Here, when the settlement was arrived at, it remained a mere contract for payment of damages and on the initial approval followed by the final approval, the rule of court. So, nothing turns on the procedure followed in the American court for making the settlement an enforceable one on behalf of a class of claimants.

If it is damages or compensation, then the question arises, damages or compensation for what? Here, it is compensation for the loss suffered by the class plaintiffs because of the alleged fraud perpetrated by the defendants in the suit, IC, A and B. The question then is, where did the cause of action arise? A cause of action is a bundle of facts giving rise to an action. The right to sue arose out of the misrepresentation of IC, by the alleged manipulating of the financial statements of IC with the alleged connivance of A and B, followed by the confession of the Managing Director of IC about the inaccuracy of the financial statements. All these took place in India. The suit could be filed in India. The claimants in the United States could also invoke the Securities Exchange Act and the Securities Act of U.S., but based on this cause of action. They acquired a right to sue in U.S. because of a statute providing a remedy. So, they sued in U.S. They exercised a right of action. A right of action is different from a cause of action. Even though the Lead Plaintiffs had a right of action in U.S., their cause of action arose or accrued

in India by the alleged misrepresentation, deceit or fraud practiced in India by IC, A and B. Therefore, it cannot be said that the cause of action was all in the U.S. The cause of action arose in India.

Based on a cause of action that arose in India, a class action suit was filed in US. On a settlement of the class action, the sums were agreed to be paid. The source of the compensation is the alleged tort perpetrated in India. Therefore, the right to the compensation arose in India. The source of the compensation is the alleged tort in India. The plaintiffs represented by Lead Counsel [as clarified by the order under section 245R(2)] are non-residents. In the language of section 5(2), the income by way of compensation or damages accrued or arose in India. This is because, the entitlement to receive and the receipt is based on the alleged tortuous act committed in India. The source is India.

The source should not be taken to be the class action filed in US. The action and settlement in US was only a mode of securing that compensation arising out of a cause of action that has roots in India.

Since IC has title to the funds even after depositing the amounts in the segregated account, the amount does not get credited to the QSF account. The title to the fund also does not pass. What is found on a consideration of the scheme adopted is that the fund that leaves IC reaches the QSF on the orders of Court. The adopting of the three stage procedure does not alter the fact that once the fund goes from the segregated account in India, IC loses its control over it and its right to it is solely dependent on the court not approving the settlement. On the approval of the court, the title to the fund vests in QSF with effect at least from the date it gets transferred to the initial escrow account, if not on the deposit in the segregated account itself. IC would lose its right to the fund once it goes into the segregated account on the terms of the settlement unless there is a breach of the settlement itself. Here, the transfer from the segregated account in India to the initial escrow account in US itself was based on an interim or preliminary approval by court of the settlement. That approval was subsequently confirmed by the final approval. Therefore, hold that the title to the fund passed to QSF in any event, when it got transferred from the segregate document to the initial escrow account. Thus, the settlement amount is not a capital receipt. It can be treated only as a revenue receipt.

Since, it is not capital receipt, the income arising cannot generate any capital gain. In the context of the definition of

income in the Act read with Section 56(1), the income can be held to be income from other sources. In other words, the settlement amount in the hands of QSF would be income from other sources in terms of the Act. Damages received by way of settlement or otherwise, cannot but be income in the hands of the receiver.

Since, the Lead Plaintiffs represent all the qualified claimants in the class action, the lead plaintiffs are their representatives. When the title to the funds passes to the QSF or Lead Plaintiffs the title passes to the qualified claimants. The Lead Plaintiffs on receiving the funds would be holding it for the qualified claimants in the class action.

By the settlement arrived at by the parties and the deposit of the fund in the segregated account, subject to breach of the settlement by IC or non-approval by Court, the title to the fund is lost to IC. Even if that be not the position, the title would be lost when the funds are transferred to the initial escrow account. Once it went to that account, only a disapproval of the settlement by court can revive the right of IC over the fund. Here, preliminary approval by court of the settlement was followed by the transfer into the initial escrow account after getting the permission of the Reserve Bank of India for such transfer. Since the settlement was finally approved by US court the title to the funds vested with QSF with effect from the date of it being credited to the initial escrow account, if not from the date of deposit in the segregated account itself. When a settlement is arrived at subject to the approval of Court and steps are taken thereunder, then the approval of court will be approval of each step taken as part of the settlement. That would mean that IC would lose its title to the fund from the date of deposit once the court approved the settlement subject to the terms of the settlement, like the stipulation regarding interest earned in the segregated account and the right to withdraw the taxes that may be found payable in India from the initial escrow account.

Therefore, the amount deposited by IC as part of the settlement of the class action dispute with Lead counsel is income from other sources in the hands of Lead counsel or the QSF and that income arises in India.

The QSF or Lead counsel being a resident of US is entitled to claim the benefit of the India-US Double Taxation Avoidance Convention (DTAC).

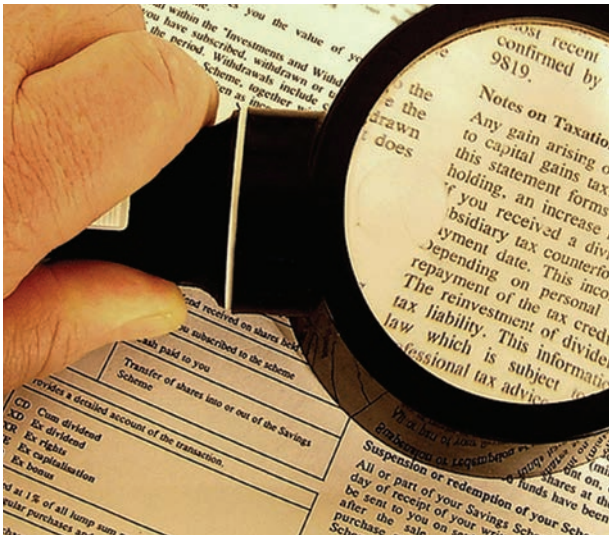
Since, the income here arises in India and since it is income from other sources arising in India, paragraph 3 of Article 23 of the DTAC has application. The income is chargeable to tax in India in terms of the DTAC. Once it is found chargeable to tax in India, IC will have the obligation to withhold tax on the amount under section 195.

LD/61/51

Dishnet Wireless Limited, In re
August 24, 2012 (AAR)

Section 9 of the Income-tax Act, 1961 read with Article 12 of the Double Taxation Avoidance Convention between India and Saudi Arabia - Income - Deemed to accrue or arise in India

Where a foreign consortium constructed and maintained submarine optic fibre telecommunication cable system which



was a facilitating and networking telecommunication infrastructure, and foreign consortium members were allocated capacity, who, in turn, transfer a part of allocated capacity to Indian company for consideration, such payment would be royalty and taxable in India

STC, a Saudi Arabian company owns and/or controls and/or operates telecommunication paths, facilities and network infrastructure in Saudi Arabia and elsewhere. A consortium, of which STC is a part, laid a fibre optic submarine cable system known as EIG, linking the Indian subcontinent and UK. The system will link the Terminal Stations in India and many Arabian and European countries. STC made an initial investment acquire 7.1265 per cent stake in the EIG cable system.

SAT under an EIG - capacity transfer agreement with the applicant for transfer a part of the capacity out of its total allocated capacity of the EIG cable system to the applicant Indian company for a consideration of $ 20 million. The applicant adopted the stand that it was the transfer of a capital asset to it by STC and that the gains of STC are not taxable in India in terms of the Double Taxation Avoidance Convention (DTAC) between India and Saudi Arabia.

The Authority for Advance Ruling held that allocated capacity cannot be understood as conferring on STC an absolute title to a segment of the system. It would be proper to understand it, as a right to exclusive user or exploitation of a segment of the system with a right in it to share the user with another. The agreement between STC and the applicant also suggests that it is only the right to participate in the use of the EIG System that is given to the applicant. It is discernible from the agreements that a transferee like the applicant is only permitted to operate and use the capacity and permitted to activate it at the relevant terminal point. The restraint placed on the applicant from transferring the capacity to any third party and the reverting back of the rights of the applicant to STC on the termination of its agreement with STC negates the theory of a part of the ownership having passed to the applicant.

A transfer of a capital asset is different from the transfer of a right to use exclusively a part or segment of the system. What is involved is not the transfer of a Capital Asset that generates capital gains.

On a true construction of the two agreements, one between STC and its consortium and another between STC and the applicant, it may be found that it is not the transfer of a capital asset, but it is only the right of user that is granted to the applicant.

The payment made by the applicant cannot be considered to be a payment made to the consortium on behalf of STC. The obligation of STC to the consortium is independent of the obligation of the applicant to STC. The payment is to STC and that payment is for the right to use and the use of equipment or capacity. The applicant cannot be said to be reimbursing the costs of the STC. STC had farmed out the right of user over a pari of the segment, the exploitation of which is allotted to it under the EIG C&MA, for a consideration. The concept of reimbursement does not arise. Even if the applicant does not pay STC, the obligation of STC to pay the consortium will

remain. The applicant also did not have an obligation to pay the consortium. It had entered into no agreement with the consortium. What is to be seen is the character of the payment based on the payer and what he pays for. So viewed, what the applicant had paid STC is for the right to use the system with a right to access it and exploit it.

What is the right to use in this case? That is the right to access the particular segment of a larger system to use the capacity of the system powered by the equipments of the whole system. The consideration paid for this right to access and the right to use and exploit the system, is royalty according to the Revenue. It is pointed out that *Explanations* 5 and 6 to Section 9(1)(vi) introduced by the Finance Act 2012 with retrospective effect, makes it clear that the consideration being paid by the applicant to STC is royalty under the Act. Even otherwise, it was a right to use a process and a right to use equipment coming within *Explanation* 2 to Section 9(1)(vi).

Under paragraph 3 of Article 12 of the DTAC, consideration paid, for use of or the right to use a design or model plan, commercial or scientific equipment would be royalty. Under paragraph 2, if the consideration is royalty it is taxable in the country of the prayer according to the laws of the State of the payer. Here, that would be according to the laws of India. Especially in view of the clarificatory amendment of Section 9(1)(vi), there cannot be much doubt that what is paid by the applicant is for a right to use a process and/or a right to use a commercial or scientific equipment.

Therefore, the payment made by the applicant to STC under the EIG Capacity Transfer Agreement towards acquisition of EIG capacity is chargeable to tax in India as royalty in terms of paragraph 2 of Article 12 of the DTAC between India and Saudi Arabia.

LD/61/52

CIT

Vs.

Valibhai Khanbhai Mankad

October 1, 2012 (GUJ)

[Assessment Year 2006-07]

Section 40(a)(ia) read with Section 194C of the Income-tax Act, 1961 - Expenses disallowed – Interest, commission or brokerage etc. payable to a resident

Where sub-contractors provided Form 15-I and thus, TDS was not deducted, for subsequent failure of assessee to furnish Form 15J to Department as required under Rule 29D of IT Rules, no disallowance could be made under section 40(a)(ia)

The respondent-assessee was engaged in the transport business. He had not deducted tax at source for payment of ₹7,91,02,011 made to the transporter on the ground that from the transporters, Form No. 15-I was obtained and, therefore, no TDS was required to be deducted. The Assessing Officer disallowed such expenditure under section 40(a)(ia) of the Income Tax on the ground that the assessee had not furnished Form No.15-J before 30th June 2006 as required under Rule 29D of the Income Tax Rules, 1962. The Commissioner (Appeals) did not accept the assessee's appeal. The Tribunal reversed the view of the Revenue

authorities and held that disallowance under section 40(a)(ia) was not justified. The Tribunal was of the view that the requirement of furnishing Form No.15-J was not related to the liability to deduct tax at source.

The Gujarat High Court held that under section 40(a)(ia), payments made towards interest, commission or brokerage etc. would be excluded for deduction in computing the income chargeable under the head 'profits and gains of business or profession', where though tax was required to be deducted at source, is not deducted or where after such deduction, the same has not been paid on or before the due date. Thus for application of section 40(a)(ia), the foremost requirement would be of tax deduction at source.

Section 194C makes provision where for certain payments, liability of the payee to deduct tax at source arises. Therefore, if there is any breach of such requirement, question of applicability of section 40(a)(ia) would arise. Despite such circumstances existing, sub-section (3) makes exclusion in cases where such liability would not arise. The instant case was concerned with the further proviso to sub-section (3), which provides that no deduction under sub-section (2) shall be made from the amount of any sum credited or paid or likely to be credited or paid to the sub-contractor during the course of business of plying, hiring or leasing goods carriages, on production of a declaration to the person concerned paying or crediting such sum in the prescribed form and verified it in the prescribed manner within the time as may be prescribed, if such sub-contractor is an individual who has not owned more than two goods carriages at any time during the previous year.

The exclusion provided in sub-section (3) of section 194C from the liability to deduct tax at source under sub-section (2) would thus be complete the moment the requirements contained therein are satisfied. Such requirements, principally, are that the sub-contractor, recipient of the payment produces a necessary declaration in the prescribed format and further that such sub-contractor does not own more than two goods carriages during the entire previous year. The moment, such requirements are fulfilled, the liability of the assessee to deduct tax on the payments made or to be made to such sub-contractors would cease. In fact he would have no authority to make any such deduction.

The later portion of sub-section (3) which follow the further *proviso* is a requirement which would arise at a much later point of time. Such requirement is that the person responsible for paying such sum to the sub-contractor has to furnish such

particulars as prescribed. Under Rule 29D of the Rules, such declaration has to be made by the end of June of the next accounting year in question.

Therefore, once the conditions of further *proviso* of section 194C(3) are satisfied, the liability of the payee to deduct tax at source would cease. The requirement of such payee to furnish details to the income tax authority in the prescribed form within prescribed time would arise later and any infraction in such a requirement would not make the requirement of deduction at source applicable under sub-section (2) of section 194C. Therefore, the Tribunal was perfectly justified in taking the view in the impugned judgment. It may be that failure to comply such requirement by the payee may result into some other adverse consequences if so provided under the Act. However, fulfillment of such requirement cannot be linked to the declaration of tax at source. Any such failure, therefore, cannot be visualized by adverse consequences provided under section 40(a)(ia).

When on the basis of the record it is not disputed that the requirements of further proviso were fulfilled, the assessee was not required to make any deduction at source on the payments made to the sub-contractors. If that be the conclusion, application of section 40(a)(ia) would not arise since section 40(a)(ia) would apply when there is a requirement of deduction of tax at source and such requirement is either not fulfilled or having deducted tax at source is not deposited within prescribed time.

LD/61/53

Assistant CIT, Business Circle- IV, Chennai
Vs.
Shri C. Ramabrahmam
October 31, 2012 (Chennai-ITAT)
[Assessment Year 2007-08]

Section 48, read with section 24 of the Income-tax Act, 1961 - Capital gains - Computation of

Claim of deduction under section 24(b) of interest on housing loan is no bar to its deduction under section 48 while computing capital gains on sale of said house

The assessee had availed the loan for purchasing the property in question. Since the assessee had shown the income under the head 'house property', he preferred to raise the claim of deduction under section 24(b). The assessee's claim of deduction was allowed. After the property was sold, he also chose to include the interest amount while computing capital gains under section 48.

The Tribunal held that deduction under section 24(b) and computation of capital gains under section 48 are altogether covered by different heads of income *i.e.*, income from 'house property' and 'capital gains'. Further, a perusal of both the provisions makes it unambiguous that none of them excludes operative of the other. In other words, a deduction under section 24(b) is claimed when concerned assessee declares income from 'house property', whereas, the cost of the same asset is taken into consideration when it is sold and capital gains are computed under section 48. The interest in question is indeed an

expenditure in acquiring the asset. Since both provisions are altogether different, the assessee in the instant case is certainly entitled to include the interest amount at the time of computing capital gains under section 48.

LD/61/54
CIT, Muzaffarnagar
Vs.
Muzaffarnagar District Co-Operative Bank Ltd.
November 8, 2012 (ALL)

Section 80P of the Income-tax Act, 1961 - Deductions - Cooperative societies, income of

Interest earned by a Co-operative Bank on the deposits of its non-statutory liquidity ratio (non-SLR) funds is income from Banking Business and, consequently, exempt under section 80-P(2)(a)(i)

The Supreme Court in Court in *Bihar State Co-operative Bank Ltd. v. CIT, (1960) 39 ITR 114 (SC)* had explained that the interest earned out of deposits of surplus fund had to be treated as interest earned in the banking business.

It cannot be said that the interest earned out of deposits of non-statutory liquidity ratio (non-SLR) funds, cannot be treated as profits and gains of business attributable to the activity of carrying on business of banking, or providing credit facilities to its members under Section 80P(2)(a)(i).

The question as to whether the income is derived from or attributable to SLR or non-SLR funds would not make any difference for the purposes of qualifying the interest earned by the cooperative bank under Section 80P(2)(a)(i) as the deposits of surplus idle money available from working capital, including reserves, excess collection of interest tax and other incomes are all attributable to the business of banking. The interest from such deposits cannot be said to be beyond the legitimate business activities of the bank.

Therefore, the cooperative bank will qualify for exemption under Section 80P(2)(a)(i).

LD/61/55
CIT, Delhi-IV
Vs.
Usha International Ltd.
November 5, 2012 (DEL)
[Assessment Year 1983-84]

Section 271(1)(c), read with section 35CCA of the Income-tax Act, 1961 - Penalty – For concealment of income

Where a huge loan of ₹10 lakhs was purportedly given as a donation to donee-trust in order to claim relief under Section 35CCA which would reduce taxable income of assessee and after survey revised return withdrawing claim for deduction under Section 35CCA was filed, it would not follow, as a matter of law, that in all such cases penalty could not be imposed

There were searches and investigations which resulted in the income tax authorities unearthing a concerted design to enable the reduction of the taxable income of income tax assessees by making use of the provisions of Section 35(2A), Section 35(1)(ii) and Section 35CCA. The assessee made a donation of ₹10 lacs to a rural development Trust by cheque and subsequently got the cheque encashed through a bogus account opened in the bank for the said purpose. On inquiries by the department it was revealed that the account was opened in

the bank only to take away the amount of ₹10 lakhs purportedly given as a donation to the donee-trust in order to claim the relief under section 35CCA which would reduce the taxable income of the assessee. The amount never left the coffers of the assessee; it also did not reach the donee-trust. It was brought back to the assessee.

Though the assessee contended that it was a victim of a fraud played by several persons acting in concert, it was found that for convenience, the special crossing in the cheque was converted or altered into an ordinary crossing by the assessee's Account Manager and Senior Advisor who had also affixed their signatures. No proceedings, civil or criminal have been taken against them. No proceedings have also been taken against the person who falsely representing that he was connected to the trust. Moreover, P, a director of the assessee company was also involved in opening the bank account in the name another company which in turn helped the trust to open an account in the same bank.

The cash book did not contain the name of the donee, though an entry had been made regarding the donation. Even in the donation account appearing in the assessee's ledger the name of the donee had not been entered when the survey was conducted in the assessee's premises.

Subsequent to survey, the revised return withdrawing the claim for deduction under Section 35CCA was filed after two months.

The Delhi High Court held that the survey itself was a result or as a follow up action to the searches and other inquiries conducted earlier. The cash book of the assessee was impounded during the survey. The proceeds of the donation cheque had already been taken out of the bank account. That account itself had been closed immediately thereafter. In the light of these facts, the contention that the revised return was filed voluntarily is untenable. It was provoked by the evidence collected by the revenue and the survey conducted in the assessee's premises. In other words the revised return was filed by the assessee only when it was cornered and the income tax authorities had collected material on the basis of which it could be said that the claim for deduction was false or bogus. The filing of the revised return is thus an act of despair and the assessee can gain nothing from it.

There was enough material gathered by the revenue authorities to show that the assessee had made a false or bogus claims of deduction under Section 35CCA in the first return, and had also impounded the cash book of the assessee where the entry for the donation had been made, though without the name of the donee being mentioned therein or in the donation account in the ledger. The materials referred to in the penalty order, *prima facie* show the guilt of the assessee; the revised return filed after the survey cannot, therefore, be considered to be voluntary.

The question whether a revised return filed by the assessee withdrawing a claim or offering additional income was voluntary or not is essentially a question of fact to be decided in the light of the entire material brought on record and the facts and circumstances of each case and particularly having regard to the fact whether the revised return was filed by the assessee when cornered by the evidence or material collected by the revenue authorities

or before that stage. However, as noted by the Madras High Court in *CIT v. Ramdas Pharmacy, (1970) 77 ITR 276*, the filing of a revised return "will not expatiate the contumacious conduct if any, on the part of the assessee in not having disclosed the true income in the original return"; and it was observed at the same time that the Court was "not willing to accept the contention put forward on behalf of the revenue that the filing of the second return is of no consequence at all", while considering the penal liability of the assessee for concealment. The Madras High Court proceeded to observe that it is not possible to construe the original return alone in isolation without reference to the conduct of the assessee subsequent to the filing of the original return and that all the facts and circumstances commencing with the filing of the original return and ending with the assessment may be taken as relevant for considering the liability of the assessee for penalty.

The question of concealment and the relevance of filing a revised return withdrawing the claim for deduction are all fact-dependent, and merely because in one case it was held that there was no concealment, it does not follow, as a matter of law, that in all such cases penalty cannot be imposed. At best, those earlier cases could only have a persuasive value. Therefore, the penalties could not be concealed without assigning any valid reason and without examining the facts.

Central Excise

INDIRECT TAXES

LD/61/56
CCE, Bangalore-II
Vs.
Osnar Chemical Pvt. Ltd.
January 13, 2012 (SC)

Section 2(f) of the Central Excise Act, 1944 - Manufature

Addition and mixing of polymers and additives to base bitumen does not result in manufacture of a new marketable commodity and as such not exigible to Excise duty; Polymer Modified Bitumen (PMB) and Crumbled Rubber Modified Bitumen (CRMB) cannot be treated as bituminous mixtures falling under CSH 27150090 and shall continue to be classified under CSH 271320.00 pertaining to tariff for petroleum bitumen

The expression 'manufacture' defined in Section 2(f), *inter alia* includes any process which is specified in relation to any

goods in the Section or Chapter Notes of First Schedule to the Tariff Act. It is manifest that in order to bring a process in relation to any goods within the ambit of Section 2(f), the same is required to be recognised by the legislature as manufacture in relation to such goods in the Section notes or Chapter notes of the First Schedule to the Tariff Act. Therefore, in order to bring petroleum bitumen, falling under CSH 271320.00, within the extended or deemed meaning of the expression 'manufacture', so as to fall under CSH 271500900, the process of its treatment with polymers or additives or with any other compound is required to be recognised by the legislature as manufacture under the Chapter notes or Section notes to Chapter 27.

No such process or processes of manufacture have been specified in the Section notes or Chapter notes in respect of petroleum bitumen falling under Tariff Item 271320.00 or even in respect of bituminous mixtures falling under Tariff Item 27150090 to indicate that the said process amounts to manufacture. Thus, it is evident that the said process of adding polymers and additives to the heated bitumen to get a better quality bitumen, viz. PMB or CRMB, cannot be given an extended meaning under the expression manufacture in terms of Section 2(f) (ii).

It is trite to state that "manufacture" can be said to have taken place only when there is transformation of raw materials into a new and different article having a different identity, characteristic and use. It is well settled that mere improvement in quality does not amount to manufacture. It is only when the change or a series of changes take the commodity to a point where commercially it can no longer be regarded as the original commodity but is instead recognized as a new and distinct article that manufacture can be said to have taken place.

The process of mixing polymers and additives with bitumen does not amount to manufacture. Bitumen remained bitumen. There was no change in the characteristics or identity of bitumen and only its grade or quality was improved. The said process did not result in transformation of bitumen into a new product having a different identity, characteristic and use. The end use also remained the same, namely for mixing of aggregates for constructing the roads.

Therefore, the Polymer Modified Bitumen (PM B) and crumbled Rubber Modified Bitumen (CRMB) cannot be treated as bituminous mixtures falling under CSH 27150090 and shall continue to be classified under CSH 271320.00 pertaining to tariff for petroleum bitumen.

Companies Act

LD/61/57

Leela Mercantile Private Limited
Vs.
Eastman Fab Limited
December 9, 2011 (P&H)

Section 433 of the companies Act, 1961 - Circumstances in which company may be wound up by Court

Where respondent did not dispute receipt of goods and issuance of declaration in

Form 'C' and also entry in balance sheet, defence taken that goods had only been retained due to personal relationship could not be said to be bonafide defence; and winding up petition was to be admitted

The respondent company placed an order on the petitioner-company for packing material for sweets and candies. The petitioner supplied the packaging material and had also issued invoice dated 25.4.2007 for a sum of ₹4,08,815. The said material sent by the petitioner had been duly received and consumed by the respondent-company. The respondent-company had also issued Form 'C' to the petitioner- company being the Form of declaration to avail sales tax concession. The petitioner had also obtained balance sheet of the respondent- Company as on 31st March 2009 which showed that the respondent company had admitted that an amount of ₹4,08,815 was due and payable to the petitioner. The name of the petitioner appears in the detail of sundry creditors of the respondent-company. No payment being made by the respondent company, the petitioner sent a legal notice under sections 433 and 434 and later on filed the present petition for winding up.

The primary ground of contest was that the petitioner had closed its manufacturing unit and had requested the respondent to keep the packing material with it with the condition that the payment would be subject to the sale of the material and therefore, no amount as claimed by the petitioner was due.

The respondent further submitted that even according to the case of the petitioner, the goods were allegedly supplied on 25.4.2007 and therefore, the suit became time barred on 25.4.2010 whereas the present petition having been filed on 28.4.2010 was clearly barred by time.

The Punjab and Haryana High Court held that the respondent had not disputed that the material had been received by it. It was not

established by the respondent that either the material had been returned to the petitioner or the value of the same had been paid to it. In the facts and circumstances of the present case, the plea taken by the respondent that the articles had been received to be kept by it did not stand to logic and reasoning. The respondent was unable to justify as to why entry with regard to liability in the balance sheet and also certificates regarding payment of sales tax had been issued if the ownership of the goods was not transferred to the respondent by the petitioner.

The contention of the respondent that the debt was time barred also did not carry any substance as the same had been depicted in the balance sheets for the year ending on 31.3.2008 and 31.3.2009 and would be governed by section 19 of the Limitation Act. Furthermore, even period of three weeks prescribed under section 434 for issuance of prior notice comes to the rescue of the petitioner.

The respondent did not dispute the receipt of the goods and the issuance of the declaration in Form 'C' and also entry in the balance sheet. In such circumstances, the defence taken that the goods had only been retained due to personal relationship cannot be said to be bonafide defence. Once it was concluded that the defence was not justified, the irresistible conclusion was that the case would fall within the ambit of Section 433(e) and the winding up petition was liable to be admitted. ■