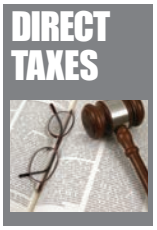
Legal Decisions[1]



Income Tax

LD/65/44

Jindal Steel and Power Ltd.

vs.

Pr. Commissioner of Income Tax

21st September, 2016

Section 220: When tax payable and when assessee deemed in default.

Order u/s 220(6) granting partial stay of demand to assessee company, modified by HC; AO is not entitled to adjust 'any refunds' arising to assessee against total demand, and adjustment can be only to the extent of the amount required for granting stay; Office Memorandum ('OM') dated February 29, 2016 issued by CBDT relied upon by HC.

The claim of deduction u/s 80IA was rejected by the Ld. A.O. during reassessment proceedings. The assessee sought stay of recovery of the total demand u/s 220(6) of ₹277 crore till the disposal of its appeal before CIT(A) subject to its paying a 15% of the total demand. The Prin. CIT granted the assessee with a stay subject to its depositing ₹41.64 crore which constituted 15% of total demand. Further, the assessee requested for adjusting a refund of ₹15.14 crore in respect of AY 2008-09 against this ₹41.64 crore, which request was accepted and so the assessee was accordingly directed to pay the balance amount of ₹26.18 crore in varying installments. The order of Prin. CIT permitted the AO to adjust any refund which may arise in favour of Assessee Company in any AY. As per the assessee's interpretation, this right to adjust the refund was limited to the amount of ₹41.64 crore directed to be deposited as a condition of stay. The authorities interpreted this order to authorise them to adjust any refund against the total tax demand of about ₹277 crore. The assessee therefore sought a clarification application of Prin. CIT's order. The Prin. CIT rejected this application seeking clarification, and relying upon the instructions dated February 02, 1993 issued by the CBDT, which stated that AO/Department may reserve the right to adjust the refund against demand.

Aggrieved, the assessee filed a writ petition before P&H HC. HC observed that instruction no. 1914 dated February 2, 1993 provided that in granting a stay, the Assessing Officer may impose such conditions as he may think fit and that he may reserve a right to adjust the refund arising, if any, against the demand. However, recent Office Memorandum dated February 29, 2016 issued by CBDT in partial modification of earlier Instruction No. 1914, entitles the Assessing Officer to reserve the right to adjust the refunds arising *"to the extent of the amount required for granting stay"*.

HC observed that the dispute was not regarding the grant of partial stay subject to paying 15% of outstanding demand, but was regarding the last sentence of order which entitled the AO *"to adjust any refund which may arise in favour of the assessee company in any assessment year"*.

HC observed that the Office Memorandum dated February 29, 2016 was issued as partial modification of the Instruction No 1914. HC held that *"Instruction No. 1914 dated 02.02.1993 as clarified by Instruction No.1914 dated 21.03.1996 must, therefore, be read together with the Office Memorandum dated 29.02.2016"*.

HC analysed the Office Memorandum dated February 29, 2016 issued by CBDT. HC held that the assessee's case would not fall under clause 4(B)(A) which gives the authority to administrative Pr CIT/CIT to decide quantum of demand to be paid for availing stay if the payment of more than 15% is warranted; and Clause 4(A) states that where the outstanding demand is disputed before the CIT(A), the AO 'shall' grant a stay of the demand on payment of 15% of the disputed demand unless the case falls in Clause 4(B).

HC observed that clause 4(E)(iii) which entitles AO to impose conditions as he thinks fit before granting stay, also entitles AO to reserve the right to adjust the refunds arising *"to the extent of amount required for stay..."* HC thus held that the right to adjust the refund is limited to the amount to be deposited by the assessee as a condition for the stay. HC thus held that the Prin. CIT's order entitling AO to adjust any refund against the entire tax demand would be contrary to the instructions of the CBDT contained in the Office Memorandum dated February 29, 2016.

[1] *Contributed by CA. Sahil Garud, Indirect Taxes Committee, CA. Mandar Telang and ICAI's Editorial Board Secretariat.*
Readers are invited to send their comments on the selection of cases and their utility at eboard@icai.in. For full judgement, write to eboard@icai.in

LD/65/45

Sunil Kumar Gupta
vs.
Asst. Commissioner of Income Tax
27th September, 2016

Section 23: Annual value how determined

Maintenance charges paid by sub-sub-licensee directly to the builder forms part of sub-licensee assessee's rent for the purpose of computing property's annual letting value u/s 23

The assessee is a sub-licensee of an apartment admeasuring 367 sq. feet in a commercial building. The assessee entered into a sub-sublicense agreement dated 03.05.2000 with one M/s RSM & Company. For AY 2002-03, the Revenue held that maintenance charges constitute rent u/s 23. As per the agreement, the sub-sub-licensee was supposed to pay to the assessee the maintenance charges.

The CIT (A) and ITAT ruled in favour of Revenue holding that maintenance charges payable by the sub-sub-licensee directly to the builder constituted rent. Aggrieved, the assessee filed an appeal before P&H HC.

HC stated that maintenance charges must form a part of the rent. As per Sections 22 and 23, the ambit of the term "rent" was wide enough to include *"any amount which is paid in consideration of the property being let"*. HC also noted that maintenance charges were payable by the sub-sub-licensee to the assessee based on the understanding between the parties and not pursuant to the agreement.

HC observed that if the maintenance charges are not included in the rent, it would enable an assessee to avoid paying tax on the true annual value of the property. Further, if maintenance-charges are not included as a part of rent, the assessee would be enabled to undervalue property's ALV for the purpose of Section 23 by the simple expedient of providing for the payment of the maintenance charges *etc.* and the rent separately.

Under Section 23(1) for the purpose of Section 22, the annual value of the property shall be deemed to be the sum for which the property might reasonably be expected to let from year to year. The amount of rent would also be dependent upon the common facilities of a building. The better the facilities, qualitatively and/or quantitatively, the higher the rent. It can hardly be suggested that the annual value of a property which provides several common amenities such as a swimming

pool, gymnasium, security car, parking and elevators would be the same as the annual value of a property in the same area but without these facilities. The actual rent received would be much higher where the facilities are better. HC remarked that *"Where the agreement provides that the owner shall pay the amounts for the common facilities, maintenance charges, outgoings etc. it is obvious and reasonable to presume that the same is factored into the rent, fee or compensation payable by the lessee or the licensee."*

HC thus held that if the maintenance charges *etc.* are stipulated to be payable by the licensee or the lessor, it must form a part of the rent for the purpose of computing the annual value of the property.

HC thus dismissed the assessee's appeal.

LD/65/46

Jamnalal Sons Limited.
vs.
The Commissioner of Income Tax
27th September, 2016

Section 45: Capital gains

Capital contribution in the form of immovable properties, stocks and shares by assessee-company to a partnership-firm is not a taxable transfer u/s 45 for AY 1980- 81; Since computation mechanism was introduced w.e.f. AY 1988-89 (vide introduction of sub-section (3) to Section 45), capital gains earned by assessee cannot be determined in terms of Sec 48 in the relevant AY.

The assessee was a company involved in investment business. The assessee decided to commence a new business of trading in immovable properties, shares and securities, and therefore converted certain plots of land and shares held as investments into its stock-in-trade. Subsequently, the assessee entered into a new partnership firm [called as Bajaj Trading Company], with six other partners. The assessee contributed immovable property, shares and cash as part of its capital contribution. The AO held that transfer of immovable property and shares and securities into the firm resulted in long term capital gains of ₹1.19 crore.

The CIT (A) and ITAT ruled in favour of Revenue. The ITAT stated that the effect of all the transactions taken together was that the assessee was able to transfer its land to another entity i.e. partnership firm and received the market value of the same without having paid any tax. Aggrieved, assessee approached the Bombay HC.

HC placed reliance upon SC ruling in the case of *Sunil Siddharthbhai vs. CIT* and observed that this issue was not *res integra*. HC held that there arose a transfer of a capital asset when the applicant company introduced its immovable property, shares and securities as its contribution to the capital of the partnership firm.

HC observed that as per the then prevailing law, such a transfer of the capital asset by the applicant assessee by way of its capital contribution to the partnership firm did not give rise to receipt of any determinable consideration to the transferor as contemplated in Section 48 of the Act. HC observed that the SC in case of Sunil Siddharthbhai had relied on earlier ruling in the case of *CIT vs. B.C. Shrinivasa Shetty* to hold that where computation provision fails then the charging section cannot be invoked. SC had also held that the credit entry in the partners' capital account is merely a notional value and not a true value, making it intricate to deduce the share of partner at retirement/dissolution of the firm.

HC noted that sub-section (3) to Section 45 was introduced w.e.f. AY 1988-89 i.e. after the year under appeal. HC thus held that *"it cannot be said that any particular consideration is received by a partner on making contribution of a capital asset into a partnership firm. Consequently, the capital gains earned by the applicant assessee cannot be determined in terms of Section 48 of the Act."* HC noted that Section 45(3) was specifically introduced to overcome SC decision in Sunil Siddharthbhai. HC also rejected Revenue's plea that sub-section (3) of Section 45 was clarificatory and so retrospective.

HC also analysed the possibility of assessee selling the assets soon after transfer or the probability of firm having no substantial business which would require capital contribution of assessee, in order to evade tax. HC observed that the firm still existed as a fully functional firm and was duly assessed for tax, which fact defied the test of construction of firm to merely evade tax.

Referring to ruling in case of *Vodafone International vs. Union of India*, HC remarked that *"the investment made in it, cannot be a device when seen in the light of the subsequent conduct of the partnership firm of dealing in immovable properties, stocks and securities as its stock-in-trade for the subsequent years"*.

HC thus held that transfer of capital asset by way of introduction as capital in new partnership firm

did not result in capital gains and so and tax thereon. Thus, HC ruled in the assessee's favour.

LD/65/47

Shivinder Singh Brar, Karta HUF

vs.

Central Board of Direct taxes

28th September, 2016

Section 54F: Capital gain on transfer of certain capital assets not to be charged in case of investment in residential house

CBDT order rejecting grant of time-limit extension for claiming 54F deduction, upheld; Assessee could have applied for relaxation for claiming the benefit u/s 54F only within the time prescribed under that section and that too, if before making such claim, the assessee had complied with the required conditions to claim such deduction

The Assessee is a *karta* of HUF which sold 4 canals of land for a consideration of ₹2.25 crore in AY 2012-13. The assessee deposited such amount under the capital gains tax scheme, 1988 by way of a fixed deposit in the State Bank of Patiala on 28.07.2012. Further, the assessee also owned 27 *kanals* 16 *marlas* on which a residential house was intended to be constructed, but the same could not be done due to interim orders granted by the HC and SC prohibiting any construction in that area in which these lands were situated. Consequently, the assessee was precluded from constructing the residential house, within the period of three years as per Section 54F.

The assessee therefore moved an application seeking condonation of delay and simultaneous grant of extension of time beyond the stipulated three years to raise the construction. CBDT rejected the assessee's application, concluding that it failed to demonstrate compliance with the conditions stipulated u/s 119(2)(c)(ii). Aggrieved, the assessee filed a writ petition before Punjab and Haryana HC.

Before the HC, the Revenue argued that powers of the CBDT u/s 119(2)(c)(ii) could be invoked only till the time that such deduction could be claimed u/s 54F [i.e. within 3 years from transfer of capital asset] and that the assessee could not seek extension of time to claim the deduction u/s 54F in perpetuity.

HC perused provisions of Section 54F and observed that if capital gains are not utilised, fully or partly for the purchase or construction of a residential

house within 3 years from the date of transfer of the long term capital asset, then such unutilised amount ought to be charged u/s 45 as income of the previous year in which the period of three years from the date of transfer of the long term capital asset expires. Thus, the assessee could have availed benefit u/s 54F within three years of its sale i.e. up to 27/06/2014.

HC observed that Section 119(2)(c) would apply in cases where a genuine hardship was established by the assessee. HC noted that sub-clauses (i) and (ii) of Section 119(2)(c) are cumulative. HC further observed that the assessee had also failed to comply with requirements laid down thereunder.

HC stated that instant default in not constructing the house within a period of three years was not due to circumstances beyond the assessee's control. Section 54F requires the home to be constructed within a stipulated period. It does not require the home to be constructed on the assessee's other properties, even if he has any. As per HC, an assessee may be granted an extension for a reasonable period to construct his house on his property, but that cannot be for an indefinite period of time, and there could not be an inherent right to an extension of time in such circumstances.

As per Section 119(2)(c), CBDT has power to relax any requirement contained in any of the provisions of Chapter IV or Chapter VI-A to avoid genuine hardship where the assessee has failed to comply with any requirement specified in such provision for claiming deduction thereunder because of circumstances beyond the control of the assessee and where the assessee has complied with such requirement before the completion of assessment in relation to the previous year in which such deduction is claimed.

HC noted that the assessee did not comply with Secton 119(2)(c)(ii) and that the extension can be granted only if an assessee has complied with the requirements necessary to avail the benefit under Section 54-F before completion of assessment in relation to the previous year in which such deduction is claimed.

HC observed that the assessee had not fulfilled this condition even as on the date of petition before the HC. In this regard, the assessee submitted that it would be required to comply with the provisions u/s 54F only within the stipulated period commencing from the extended date granted under Section 119 (2) (c) (ii) of the Act. HC remarked that such a submission is based on the erroneous presumption that the words *"year in which such deduction is claimed"* means the year in which the assessee seeks and is granted extension. As per the HC, the words in fact mean the year in which the assessee is eligible to tax, which is AY 12-13 in this case. If such submission of the assessee is accepted, it would entitle an assessee to postpone the payment of capital gain tax indefinitely by making the application at any time and even repeatedly.

HC thus held that the assessee could have applied for relaxation for claiming the benefit u/s 54F only within the time prescribed under that section and that too, if before making such claim, the assessee had complied with the required conditions to claim such deduction. Thus, the HC opined that CBDT had rightly rejected the application of the assessee.

LD/65/48

Commissioner of Income Tax, Gandhinagar

vs.

Gujarat Industrial Investment Corporation

29th September, 2016

Receipts on account of interest on debentures, upfront fees and interest on deposits given to other corporations by assessee-company, not chargeable to tax under erstwhile Interest Tax Act, 1974;

Issues in the instant case were whether interest on debentures and upfront fees were taxable under the Interest Tax Act, whether interest liability was to be computed on net basis or gross interest basis under the same, and whether interest on monies lent to other corporations would attract the provisions of the said act.

Section 2(7) of the Interest Tax Act defines interest to mean interest on loans and advances made in India and also provides for certain inclusions and exclusions therefrom. HC as well as ITAT had held that investment in debenture could never be equated with the advancement of loans made in India. It was further held that even the legislature recognised the distinction between the loan and deposit and thereby excluded the interest earned by assessee on the deposits made with the Financial Institutions while computing the total chargeable income of the assessee.

Aggrieved, Revenue filed an appeal before SC.

SC observed that the definition of interest given u/s 2(7) of the Interest Tax Act, 1974 would have no application in the instant case.

SC therefore dismissed Revenue's appeal.

Transfer Pricing

LD/65/49

CIT- II, Pune

vs.

PTC Software (I) P. Ltd

26th September, 2016

Comparable following different financial period was to be excluded as per unambiguous mandate of Rule 10B(4). ITAT's exclusion of comparables selected by TPO was a purely factual determination and Revenue was unable to show that ITAT's findings of fact were perverse in any manner.

The assessee is a wholly owned subsidiary of an American Company M/s. Para Metric Technology Corporation USA (holding company). The assessee is engaged in providing Information Technology (IT) services and IT enabled Services to its holding company. The assessee had adopted Transaction Net Margin Method (TNMM) for determining the ALP of the IT segment services and determined its PLI at 14.02% and computed the average profit margin of comparables as 10.70%. In respect of its IT segment, the assessee determined its PLI at 14.23% while the arithmetic mean of the PLI of comparable cases was 10.51%.

During the transfer pricing proceedings, the TPO conducted a fresh search for comparables and proposed upward adjustment of ₹10.38 crore which was confirmed by the DRP. Aggrieved, the assessee preferred an appeal before ITAT.

ITAT ruled in favour of the assessee. Aggrieved, Revenue preferred further appeal on grounds of selection of comparable companies.

1. <u>FCS Software Ltd and Compucom Software Ltd.</u>

   TPO had in his Transfer Pricing Study applied the filter of 25% in respect of related party transaction (RPT) as against the 10% adopted by the respondent assessee in its transfer pricing study. HC observed that this was a purely factual determination and the RPTs have to be considered in the context of total transactions and not by a conversion formula as adopted by the AO. The determination of percentage of RPT as adopted by ITAT was similar to the method adopted by the TPO in the earlier years. Identical method as directed in the case of M/s FCS Software Ltd. was also done in case of M/s Compucom Ltd. by the Tribunal, and that the Revenue has made no grievance in case of the impugned order to the extent of M/s. Compucom Ltd.

   Accordingly, HC held that this question was factual and did not give rise to any substantial question of law.

2. <u>KALS Information Technology Ltd. and Helios Matheson Information Technology Ltd.</u>

   These companies were functionally uncomparable to the assessee's IT segment services, since they were engaged in the business of selling of software products whereas the assessee was rendering software services to its holding company. For preceding AY 2006-07, TPO had found that KALS Ltd. and Helios & Matheson Ltd. were functionally not comparable with the assessee. In the absence of any change in the nature of activities carried out by KALS Ltd. and Helios & Matheson Ltd. in the subject AY, ITAT excluded these companies.

   HC remarked that since the findings of the Tribunal being one of the facts which had not been shown to be perverse, the question as proposed does not give rise to any substantial question of law.

3. <u>Transwork Information Services Ltd.</u>

   The financial period of this comparable was from 1st July, 2006 to 30th June, 2007 whereas assessee's financial period was from 1st April, 2006 to 31st March, 2007. As per provisions of Rule 10B(4), the analysis for comparison shall be on the data relating to the financial year in which the international transaction has been entered into. ITAT therefore had excluded this comparable. HC held that the provisions of Section 10B(4) of the Rules are clear in as much as it obliges that the data to be used for comparability analysis should be of the same financial year in which the international transactions were entered into by the tested party. HC rejected Revenue's submission that mandate of Rule 10B of the Rules can be ignored as the difference is only of three months, stating that no such liberty is granted in terms of Rule 10B(4) of the Rules. HC thus dismissed this question.

4. <u>Vishal Information Technologies Pvt. Ltd [VITPL].</u>

   This company was functionally different as it was engaged in IT enabled services and

also in providing agency services by way of outsourcing services to third party vendors. ITAT had held that the functional profile of Vishal was different from that of the assessee, and also that Vishal had entered into RPT at 86% i.e. far in excess of 25% filter. Revenue argued before HC that VITPL was excluded on the basis of RPT filter without considering the fact that the notes to the account were incomplete. HC however observed such argument was not made before ITAT and also that Revenue had made no such submission with regard to percentage of RPT undergoing a change if the notes to accounts are considered in their entirety.

HC thus held that this question did not give rise to any substantial question of law.

5. Vishesh Infotechnics Ltd.

HC observed that ITAT order rendered a finding of fact that the services rendered by M/s. Vishesh Infotechnics were inherently different from the nature of services being rendered by the assessee. HC therefore held that this question did not give rise to any substantial question of law.

6. Galaxy Commercial Ltd.

This company was accepted as comparable on account of being functionally similar. Galaxy Commercial had earned income from transportation business, but it was merely 7% while the income earned from BPO operations was 87%. Since ITAT had ruled in favour of assessee on facts, HC held that this question did not give rise to any substantial question of law.

Accordingly, HC dismissed Revenue's appeal on grounds as dealt above.

Service tax

LD/65/50

Commissioner of Central Excise and Service Tax, vs. Jaikumar Fulchand Ajmera

09th March, 2016

Individual truck-owner transporting goods for public distribution are excluded from purview of tax u/s 65(105)(zzp) r/w Section 65(50b) of Finance Act, viz. "goods transport agency.

The assessee had been retained by District Supply Office ('DSO'), Osmanabad to move food grains and other goods in the operation of public distribution system ('PDS') and received a sum of ₹11.97 crore between January 2005-August 2009 on which tax of ₹34.82 lakh was confirmed as due as provider of 'goods transport agency' service.

The Commissioner (Appeals) held that individual truck owners were not providers of 'GTA service' and relying on ruling in *Commissioner of Central Excise & Customs, Guntur vs. Kanaka Durga Oil Products Pvt. Ltd.* [2009(15) STTR 399 (Tri- Bangalore)] set aside the demand. Aggrieved, the Revenue filed appeal before CESTAT. Revenue contended that said relied-upon decision was challenged before SC. It also contended that tax was leviable u/s 65(105)(zzp) of Finance Act for providing GTA service as defined in Section 65(50b) and that the recipient not being one of the entities listed in Rule 2(1)(d)(v) of Service Tax Rules, the service provider was liable to pay tax.

CESTAT perused the definition of GTA in Section 65(50b) and observed that the essential characteristic of service provider is the issuance of consignment note. Perusing the definition provided u/s 65(50b), CESTAT found that the essential characteristic of service provider is the issuance of consignment note. CESTAT remarked that *"Revenue had resorted to a circular logic by claiming that Rule 4B of Service Tax Rules requires GTA to issue consignment note. This according to us, is a specious line of reasoning as the provider of GTA being determined by issuance of consignment note under the statute, it is not within the ambit of subordinate legislation to create a class of taxable persons by imposing condition that would, perforce, bring such persons within the tax net. The intent and purpose of Rule 4B had been misinterpreted by the Reviewing Authority".*

CESTAT further held that decision in *Kanaka Durga Oil Products Ltd.* still prevailed, which excluded individual truck owner from the purview of tax in Section 65(105)(zzp).

CESTAT stated that goods transported by District Supply Officer (DSO) were for public service which involved a distribution chain. The distributors were mere designated outlets for PDS and till the transfer of title of goods to the intended beneficiaries of the system the goods were in possession of the DSO. Consequently, during the transportation stage, assessee does not acquire any lien on the goods which is implicit in the issue of consignment note. CESTAT therefore held that, by no stretch of imagination could the document issued by DSO conveying the goods transported be construed as consignment note to render assessee to be a GTA.

Accordingly, CESTAT rejected Revenue appeal for lack of merits.

LD/65/51

Union of India and Ors,
vs.
Mega Cabs P. Ltd.
26th September, 2016

Revenue's SLP is admitted by SC. Operation of Delhi HC judgment in case of Mega Cabs Pvt. Ltd. that struck down Rule 5A(2) of Service Tax Rules (as amended by December 2014 Notification) to the extent it empowered Service Tax Dept. officers, audit party deputed by Commissioner or CAG to seek production of Cost Audit / Income Tax Audit Reports on demand, is stayed;

In the case of the assessee, the Delhi HC had held that Rule 5A(2) exceeds the scope of the provisions under the Finance Act. This is the result whether Rule 5A(2) is tested *vis-a-vis* Section 72A of the Finance Act which pertains to special audit or Section 72 which pertains to assessment or Section 73 which pertains to adjudication or even Section 82 which relates to searches. HC had further held *"... under the garb of the rule making power, the Central Government cannot arrogate to itself powers which were not contemplated to be given it by the Parliament when it enacted the FA. This is an instance of the Executive using the rule making power to give itself powers which are far in excess of what was delegated to it by the Parliament"*. HC had further held that verification of the records can take place by the officers of the Department provided such officers are authorised to undertake an assessment of a return or of adjudication for the purposes of Section 73 of the Finance Act and it is not any and every officer of the Department who could be entrusted with the power to demand production of records of an Assessee.

HC had quashed CBEC Circular No. 995/2/2015-CX prescribing detailed norms to be followed by Audit Commissioners, stating that the Circular did not have any statutory backing under Finance Act and cannot be relied to legally justify audit undertaken by Service Tax Department Officers. HC had further noted that Circular or Manual could not travel beyond scope of the statute itself and struck down Circular No. 181/7/2014-ST which stated that legal backing for Service Tax Department Officers to conduct audit was available in terms of Section 92(4)(k).

Thus, HC had declared that Rule 5A(2) as amended in terms of Notification No. 23/2014-Service Tax dated 5th December 2014 of the Central Government, to the extent that it authorised the officers of the Service Tax Department, the audit party deputed by a Commissioner or the CAG to seek production of the documents mentioned therein on demand was *ultra vires* the FA and, therefore, struck it down to that extent.

Now, the SC has admitted Revenue SLP and stayed the operation of above Delhi HC judgment which struck down Rule 5A(2) of Service Tax Rules (as amended by Dec. 2014 notification) to the extent it empowered Service Tax Department officers, audit party deputed by Commissioner or CAG to seek production of cost audit/income tax audit reports on demand.

Note: The summary of Delhi HC ruling was reported at LD/65/12 in the August edition of the ICAI Journal.

LD/65/52

Concept Hydro Pneumatic (P.) Ltd.
vs.
Commissioner of Central Excise, Bangalore Commissionerate (Karnataka HC)
24th August, 2016

Delay in filing an appeal as a result of financial difficulty to make mandatory pre-deposit is condonable as it shows that assessee was prevented by sufficient reasons in not preferring the appeal.

Tribunal dismissed the appeal as time barred by not condoning the delay. Before the High Court, the appellant contended that, on account of financial constraints, it could not make payment of 10% of pre-deposit in time, which is pre-requisite for filing an appeal, and therefore, there had been a delay of 117 days in preferring the appeal. On merits, appellant contended that, it had an arguable case. The department resisted the aspects of condonation of delay on the ground when there was delay or-lapse on the part of the appellant in not putting the case before the Board of Directors and even after the knowledge, the appeal was not filed.

The Hon'ble Karnataka High Court held that ground of financial inability to pay mandatory pre-deposit, which is a pre-requisite for filing an appeal, can be considered as one of the valid grounds for accepting the contention that the appellant was prevented by sufficient reasons in not preferring the appeal. It further held that, in a given case, Court may decline to exercise discretion for condoning the

delay, if, during the period of delay, the rights of the parties are substantially altered and/or irreversible situation is created, but no such circumstances exists in the present case. Having said so, the Court considered the aspect that declining the exercise of discretion for condonation of delay may result into grave injustice to the appellant and appellant would be deprived of the case to be considered on merits, more particularly, when no prejudice is going to be caused to the respondent-Department, since on the demand, the interest if ultimately is maintained, it is to follow. Under these circumstances, the High Court allowed the Appeal and directed restoration of appeal before the Tribunal on payment of nominal cost of ₹10,000.

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LD/65/53

Pr. Commissioner of Service Tax, Delhi
vs.
T. T. Ltd.
(Delhi HC)
30th August, 2016

For the purpose of export incentives, when new services are added to parent notification by subsequent notifications issued on different dates, refund/exemption in respect of such new services has prospective effect i.e. only from date of subsequent notification.

Adjudicating authority has the primary jurisdiction to examine eligibility of refund claim even when the matter is remanded to him only for verification of refund claim vis-à-vis documents.

The *Notification No. 40/2007-ST*, dealing with refund to exporters in respect of certain input services, was issued on 17.09.2007 and it listed down 4 services. It was superseded by *Notification No. 41/2007-ST dated 06.10.2007* leading to inclusion of 12 services in base notification. Subsequently new services were further added to this list *vide Notification No. 3/2008 dated 19.02.2008, Notification No. 17/2008-ST dated 01.04.2008* and *Notification No. 33/2008-ST dated 07.12.2008*. Respondent, an exporter of manufactured cotton yarn, sought refund in terms of Notification No. 41/2007-ST as amended by later notifications issued in 2008. At the first instance, adjudicating authority rejected refund claim. On appeal, the First Appellate Authority remitted the matter to adjudicating authority, who then granted part refund. When respondent again preferred an appeal, the Commissioner in his order-in-Appeal dated 02.09.2011 held that substantial exports by respondent were eligible for service tax refund. However, the matter was remitted to adjudicating authority with specific direction to examine the relevant documents and co-relate them to check as to whether the assessee could claim the amount.

The Adjudicating authority in his order-in-original dated 06.11.2012 held that substantial portion of refund claim pertained to services which were not part of '2007 notifications' but that of '2008 notifications' and hence, respondent was not entitled to claim refund. Aggrieved by the order of adjudicating authority, respondent preferred appeal before the Tribunal. The Hon'ble Tribunal set aside the order of adjudicating authority by holding that adjudicating authority could not adjudicate upon the refund claim afresh and further, directed him to sanction the refund claim by verifying documents in terms of order of the commissioner dated 02.09.2011. The Hon'ble Tribunal also examined the correctness of reasons given by the Adjudicating authority on merits and held that, even otherwise since the base notification i.e. 41/2007 was amended and various services in respect of which refund was claimed by the assessee were in fact included, there was nothing expressly stated to prohibit their application for the periods in question.

Department challenged correctness of the Tribunal's order before the Hon'ble High Court. Before the Court respondent, the assessee contended that in the absence of any express stipulation in 2008 notifications stating that inclusion of new services should have prospective application covering future exports only, such amendment would take effect from date of base notification, and that inclusion of particular service in exemption notification is relevant and not the date of its inclusion. Respondent also urged that in rejecting the refund claim on new ground, adjudicating authority exceeded the scope of the remand given by order of Commissioner dated 02.09.2011 and thereby violated the law and hence, pleaded for sustaining order of the Tribunal.

The Hon'ble High Court held that the amendment in '2007 notification' i.e. base notification by subsequent '2008 notification' was expressly prospective as the wordings of '2008 notifications' clearly stated that they would come into force on the dates of their publication in the official gazette. The Hon'ble HC further held that a notification can be said to be clarificatory when base/original notification enunciates something leading to requirement of clarification. The Hon'ble HC distinguished the decision in cases of *WNS Global Services (P.) Ltd. vs. CCE [2008] 13 STT 37 (Mum.-CESTAT) and Commissioner of Central Excise vs. Sesa Goa Ltd. 2015 (321) ELT A66 (SC)*, which were

relied upon by the respondent, by observing that facts of the present case are entirely different. It observed that the base notification included within its purview only certain specified services and not all and that inclusion of other services by way of three separate notifications on which were effective from different dates gives clear indication that subsequent notifications are not merely clarificatory, but seeks to expand the scope of base notification and thereby cannot be said to be effective from date of original notification.

As regards respondent's contention of adjudicating authority going beyond scope of remand, the Hon'ble HC noted that the fact that commissioner remitted the matter to adjudicating authority twice for verification shows that the scope of remand was widened, that since the exemption and refund applications are to be construed strictly and narrowly as affirmed by the Hon'ble Apex court in case of *CCE vs. Hari Chand Shri Gopal 201*0 (260) ELT 3 (SC), in present case the adjudicating authority cannot be said to lack primary jurisdiction merely because of a circumscribed demand. Accordingly the matter was decided in favour of revenue by setting aside the Tribunal's order.

LD/65/54

M/s Marudhan Motors

vs.

Commissioner of Central Excise and Service Tax, Jaipur

29th July 2016

Prior to 01.04.2011, 'exempt service' as defined in Rule 2(e) of CCR, 2004 did not include 'trading activities' and therefore rule 6(3) of CCR, 2004 has no application in respect of credit of common input services used for providing taxable services as well as trading activities.

Appellant, apart from providing taxable services namely authorised service station, business auxiliary service and tour operator services, was also undertaking trading activities during the period 2005-2006 to 2009-2010. When appellant took cenvat credit of common input services used for providing both taxable services and trading activities, department disallowed such cenvat credit under Rule 14 of CCR, 2004, on the ground that trading activity would constitute 'exempted service' in terms of Rule 2(e) of CCR, 2004 and as such, in terms of Rule 6(3)(A) of CCR, 2004, appellant is required to maintain separate accounts or pay the amount towards provision of service of undertaking trading activity.

The Hon'ble Tribunal noted that Rule 2(e) of CCR, 2004 defines the term 'exempted service' to mean taxable services which are exempted from whole of service tax leviable thereon, and include services on which no service tax is leviable under Section 66 of the Finance Act, 1994. By an amendment to said definition of 'exempted service' *vide* Notification No. 3/2011-CE (N.T.) dated 01.03.2011, an explanation was added to the said rule, clarifying that exempted service includes trading. The Hon'ble Tribunal held that perusal of both i.e. amended and unamended provisions of exempted service reveal that activity of trading was not included within the ambit of definition prior to 01.04.2011, and since the amended definition of exempted service would not apply in present case, Rule 6(3) of CCR, 2004 should not have any application for taking cenvat credit of common input services used for providing taxable services and trading activity. Accordingly, order denying credit of common inputs was set aside.

LD/65/55

Federation of Hotels and Restaurants Association of India

vs.

Union of India

12th August 2016

High Court upholds the constitutional validity of Section 65 (105)(zzzzv) read with Section 66E (i), Section 65 (22) of the Finance Act 1994 as well as Rule 2C of the Service Tax (Determination of Value) Rules, 2006, but strikes down Section 65 (105) (zzzzw) of the Finance Act 1994 pertaining to levy of service tax on the provision of short-term accommodation and the corresponding instructions/circulars seeking to operationalise the levy as unconstitutional and invalid

In this Writ Petition, the petitioners challenged three things namely (i) the constitutional validity of Section 65 (105) (zzzzv) of the Finance Act 1994 (FA) whereby the provision to any person by a restaurant, by having the facility of air-conditioning in any part of its establishment serving food or beverage, including alcoholic beverages or both, in its premises has been made amenable to service tax. (ii) the constitutional validity of Section 65 (105) (zzzzw) of the FA whereby the provision by a hotel, inn, guest house, club or camp-site by whatever name called to any provision, accommodation for a continuous period of less than three months has been made amenable to service tax.(iii) constitutional validity of Section 66E(i) of the Finance Act 1994(from 01.07.2012)

to the extent it seeks to constitute a service portion in an activity of supply of food or other articles as 'declared service' and consequently validity of Rule 2C of the Service Tax (Determination of Value) Rules, 2006.

The High Court first noted the legislative history of 46th Constitutional Amendment and observed that, Parliament inserted Article 366 (29 A) (f) by the 46th Amendment to the Constitution to overcome the decisions in *State of Himachal Pradesh vs. Associated Hotels of India* 2002-TIOL-65-SC-CT-CB and *Northern India Caterers (India) Ltd. vs. Lt. Governor* (1978) 4 SCC 36 & (1980) 2 SCC 16 and various other decisions. It further noted that, in para 13 of the Statement of Reasons for the 46th Amendment to the Constitution, it was observed that the *"proposed amendments would help in the augmentation of the State revenues to a considerable extent."* The High Court therefore expressed a view that, the focus of the said amendment was on ensuring that State sales tax was leviable on the portion of supply of food and drinks even where it was as a part of a composite catering contract. The focus at that stage was not on capturing any portion of that composite contract for the purpose of levy of service tax. This was 1982 and service tax was not thought of till a decade later. Therefore, the High Court expressed a view that, it is difficult to imagine that Parliament had in 1982 at the time of the 46th Amendment consciously decided that no portion of the composite contract of a catering contract would be amenable to levy of Union Service Tax.

While deciding the constitutional validity of "restaurant service" u/s 65(105)(zzzzv), the High court felt that, to examine the challenge, it is essential, to determine whether the composite catering contract is capable of being segregated into the portion pertaining to supply of goods and the portion pertaining to the service provided. After examining provision contained in Art.366(29A)(f) the Court held that, the subject matter of "transfer, delivery or supply" are the 'goods', which in this case would be food or any other article fit for consumption whether or not intoxicated. The key expression is not just 'supply' but 'supply of goods'. Explaining the "dominant intention test" emphasised in BSNL's case (2006) 3 SCC 1 and subsequently considered in L&T's case (2014) 1 SCC 708, the High Court expressed a view that, even if some part of the composite transaction involves the rendering of service, there should be no difficulty in recognising the power of the Union to bring to tax that portion. It also noted that, Section 66F(i) defines declared service to be only a 'service portion' in composite activity. As regards the decision of the Hon'ble Supreme Court in the case of *K. Damodarasamy Naidu vs. State of Tamil Nadu (2000) 1 SCC 521*, the Court held that, the said decision did not engage with the question whether the service element involved in the supply of food and drink would be amenable to service tax. The only question was whether the entire transaction was exigible to sales tax even where the supply of food and drink was in the course of providing a service and that question that was answered in the affirmative. Therefore the said decision is not an authority for proposition that in a catering contract, which is admittedly a composite contract, the service portion thereof cannot be made exigible to service tax levied by a Union legislation. The High Court, on the other hand relied upon decision in the case of *Tamil Nadu Kalyana Mandapam Association vs. Union of India AIR 2004 SC 3757*, to hold that, there is possibility of splitting up of the composite transaction into the provision of service element and the supply of food. Challenged to constitutional validity of Section 65(105)(zzzzv) was thus not accepted by the Court.

The Court further held that, as regards Section 66F(i), the legislative carving out of the service portion of the composite contract of supply of food and drinks has sound constitutional basis, and consequently the constitutional validity of Section 66F(i) was upheld.

As regards Rule 2C, the court held that, the said rule only enables the assessing authority to put a definite value to the service portion of the composite contract of supply of goods and services in an air-conditioned restaurant. Hence, the said ready reckoner formula is useful where an assessee does not maintain accounts in a manner that will enable the assessing authority to clearly discern the value of the service portion of the composite contract. However, when during the course of assessment proceedings an assessee is able to demonstrate, on the basis of the accounts and records maintained by it for that purpose, that the value of the service component is different from that obtained by applying Rule 2C the assessing authority would be obliged to consider such submission and give a decision thereon. The Court accordingly upheld the constitutional validity of Rule 2C.

While deciding the constitutional validity of "short term accommodation service" contained

in Section 65(105)(zzzzw) the Court noted that, main contention of the Petitioners is that levy of tax on luxuries as contemplated under Article 246 read with Entry 62 of List II (State List) of the Constitution entirely covers the field and therefore, Parliament lacks the legislative competence to levy such service tax. The Hon'ble Court referred to the provisions of Delhi Tax Luxuries Act, 1996 and held that, the very same taxable event of providing service by way of accommodation in a hotel *etc.* is the subject matter of both levies viz., luxury tax under the Delhi Tax Luxuries Act and service tax under the Finance Act. The High Court relied upon the decision in the case of *International Tourist Corporation vs. State of Haryana*, in which it was held that, before exclusive legislative competence can be claimed for Parliament by resort to the residuary power, the legislative incompetence of the State legislative must be clearly established. The Court held that, the Delhi Tax Luxuries Act, 1996 which provides for levy of luxury tax on provision of the service of accommodation in a hotel *etc.* is traceable to Entry 62 of List II and the State is therefore competent to levy and collect luxury tax on such taxable event. The High court also noted decision in the case of *Godfrey Phillips India Ltd. vs. State of U.P., (2005) 2 SCC 515*. The High Court further observed that, levy also fails due to lack of machinery provision for levy and collection of tax on accommodation holding that there is no corresponding provision for determining the value of the service in the case of Section 65 (105) (zzzzw) of the Finance Act. The High Court accordingly, struck down Section 65 (105) (zzzzw) of the Finance Act 1994 pertaining to levy of service tax on the provision of short-term accommodation and the corresponding instructions/circulars seeking to operationalise the levy as unconstitutional and invalid

Excise

LD/65/56

Commissioner of Central Excise vs. Castings (India) Inc. 22nd August, 2016

Section 2(f): Definition of 'manufacture'.

De-coiling, straightening and cutting of TMT coils into TMT bars/rods does not amount to manufacture u/s 2(f) of Central Excise Act; Value addition in end product is also irrelevant since the same is due to various factors such as labour, customer satisfaction and demand in market, and so is conclusive factor for 'manufacture'. Mere applicability of different tariff rates does not mean that two products are essentially different.

The assessee, Castings India Ltd. [CIL] is a conversion/external processing agent of Tata Steel Limited [TSL] and performs the activities of processing TMT coils into TMT bars/rods after de-coiling, straightening and cutting into sizes for TSL, for a processing charge. Revenue issued Show Cause Notices (SCN) to assessees demanding payment of differential duty on account of substantial value addition to TMT bars considering the process undertaken by the assessee amounted to manufacture. The notice alleged that converting TMT coils into TMT bars results into an altogether different item falling within Sub-Heading 7213.90 of Central Excise Tariff Act, 1985 (CETA) and that TMT bars and TMT rods had been cleared from the factory of assessee without payment of central excise duty. Thus the Revenue alleged contravention of the provision of Section 4 and 6 of the Central Excise Act, 1944 and violation of Rules 4,6,8,9,10,11 and 12 of the Central Excise Rules, 2002 and since there was evasion of central excise duty for the different periods, the aforesaid show-cause notices were issued and they were held liable for payment of excise duty as well as the interest and penalty etc.

CESTAT allowed assessees' appeals aggrieved by which the Revenue approached the HC.

HC perused the definition of 'manufacture' u/s 2(f) of the Excise Act 1944 and observed that if no different and distinct article emerges having a distinct name, character and use, after the process applied upon the original product, there is no manufacturing at all. Commercially new and distinct articles ought to emerge out of the process applied.

HC observed that the test to ascertain whether a process amounts to manufacturing or not is to check whether change brought by the process causes the commodity to reach a point where commercially it can no longer be regarded as the original commodity, but, instead is recognised as a new and distinct article and that mere cutting or slitting of steel sheets does not amount to manufacture because the identity of the product remains unchanged as the steel folded in coil remains steel even after cutting and merely because of change in tariff item, the resultant product cannot be different and distinct commodity.

HC observed that there would be no manufacturing even though the process involves unwinding, cutting/slitting and packing, if the

characteristics of the raw material and final product remain the same.

With respect to the process employed by the assessee of decoiling, straightening and cutting of TMT coils into TMT bars and rods, HC noted that for cutting TMT coils into bars and rods, de-coiling and straightening are must and therefore, the major question was whether cutting of TMT coil would result in manufacturing or not. HC observed that in various decisions, it has been held that cutting *per se* does not amount to manufacturing. Reliance was placed upon SC ruling in *Aman Marble Industries Pvt. Ltd. vs. Collector of Central Excise, Jaipur* [2003 (157) ELT 393 (SC)], wherein it was held that cutting and polishing stones into slabs did not result in any manufacture of new commodity and that the end product remains the same. Thus, HC observed that original identity of TMT coils also remains as it is even after being converted into TMT bars and rods.

HC rejected Revenue contention that there is value addition in the end product after the said conversion of TMT coils into bars and rods and hence, the same would be manufacture. HC observed that the value addition is on account of the labour put in the said process and not because of any change in the characteristic of the resulting commodity. HC placed reliance upon SC decision in *Satnam Overseas Ltd. vs. Commissioner of Central Excise* [2015 (318) ELT 538 (SC)], wherein it was observed that mere addition in value and ultimately even the market price after original product has undergone certain process would not bring it within 'manufacture' definition unless original identity also undergoes transformation and becomes distinctive and new product. HC also rejected Revenue's contention that since TMT coils and TMT bars/rods fall under different entries as per Schedule to Excise Act, the said process amounts to manufacture.

HC stated that merely because there is change in the tariff item for the end product, it does not become excisable as the product must be 'manufactured' and become marketable. HC relied on ruling in case of *Prabhat Sound Studios vs. Additional Collector of Central Excise* [1996 (88) ELT 635 (SC)] wherein it was held that although after recording the sound of magnetic cassettes, *etc*, the end product may be covered by another tariff entry, but, the process of recording of sound of such tapes does not amount to manufacturing and observed that only because raw material and final product fall under different headings, does not mean that it automatically amounts to manufacturing.

HC observed that the Revenue in the present case, had failed in discharging the burden of proving that the process employed by assessee amounted to manufacturing.

Accordingly, HC ruled in favour of assessees and dismissed Revenue appeals.

LD/65/57

M/s SRF limited

vs.

Commissioner of Central Excise, Chennai

30th August, 2016

Section 35G makes it clear that an appeal to High Court shall lie, provided it not being an order relating to the determination of any question having a relation to the rate of duty of excise or to the value of goods for the purpose of assessment; Madras HC refuses to entertain assessee's appeal.

Assessee is engaged in the manufacture of Nylon Filament Yarn, falling under Chapter 54 of the Central Excise Tariff Act, 1985. During the relevant period, the assessee, claimed exemption, under Central Excise Notification No.08/1996 dated 23/07/1996. The notification allowed exemption to Nylon Filament Yarn of 210 denier with ±4% variance. The test reports indicated that denier range of the yarn was above the permissible limit, under Notification No.08/96. Notice was issued by the Revenue demanding differential duty. The said duty was confirmed by Original Authority and Adjudicating Authority. Further the appeal filed by the assessee was rejected by the CESTAT. Being aggrieved the assessee has filed an appeal before the HC.

Revenue challenged the maintainability of petition before the HC in view of Section 35G of Central Excise Act 1944. Therefore, the issue before Madras HC was whether the appeal filed by the assessee under Section 35G of the Central Excise Act 1944 (Act) is maintainable when the same relates to the rate of duty of excise, as raised in the substantial question of law by the assessee. Revenue contended that mere perusal of the substantial questions of law would clearly show that the assessee has raised questions of law pertaining to the claim of exemption, under the Exemption Notification.

The Assessee contended that the test reports of the samples taken for one particular batch, cannot

be applied for the yarn of the next batch, as the process parameters may vary for each batch. The Assessee also contended that the Revenue rejected the benefit of export, on the ground that the assessee was not able to prove that the twine exported is made out of the quantity of yarn produced during the relevant period. The Assessee further argued that rejection of the appellant's plea by the CESTAT, without considering the FIFO method was incorrect, as per the principles laid down, by the Hon'ble Supreme Court, in the case of *TELCO vs. Municipal Commissioner, [(1993) Suppl. (1) SCC 361]*.

Revenue submitted that the test reports cannot be questioned since tests were repeated at the request of the assessee by getting the same tested at CRCL, New Delhi and similarly, at the request of the assessee samples were again tested at the National Test House, with regard to its tenacity and denier. Further, admittedly, the assessee had not intimated any process change to the department, whereby such reduction of denierage was recorded; especially when it is the case of the assessee that denierage is based on various factors, including the inputs used by them.

HC perused Section 35G and stated that as per the said section an appeal to HC shall lie, provided it not being an order relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for the purpose of assessment. In the instant case, the issue was related to the claim for exemption under the exemption notification, and whether it was applicable to the assessee or not. HC noted that the conditions in the exemption notification for the tolerance limit of nylon yarn were not fulfilled by the assessee. Therefore, any dispute relating to rate of duty could not be decided under Section 35G of the Act.

The Assessee had also submitted that appeal was pending for a period of 10 years, and therefore the same need not be dismissed now, for want of jurisdiction. HC stated that if the Court proceeds with the merits of the case, having no jurisdiction to entertain an appeal, then the judgment passed by the Court, would amount to nullity.

HC thus held that the substantial questions of law raised by the assessee relate to the rate of duty and hence stated that the appeal was not maintainable under Section 35G of the Act. ■

Don't wait. The time will never be just right. - Napoleon Hill