Select Legal Decisions

1. ***CIT, Mumbai v. General Insurance Corporation (2006) 286 ITR 232(SC)***

   The issue under consideration is whether the expenditure incurred by a company on account of stamp duty and registration fees for the issue of bonus shares is allowable as revenue expenditure. The Supreme Court observed that there is no inflow of fresh funds or increase in capital employed on account of issue of bonus shares. There is merely a reallocation of company's fund on account of issue of bonus shares by capitalization of reserves. Therefore, the company has not acquired a benefit or advantage of enduring nature. The total funds available with the company will remain the same and there is no change in the capital structure of the company consequent to the bonus issue. Thus, issue of bonus shares does not result in the expansion of capital base of the company. Therefore, the expenditure incurred by the company on account of stamp duty and registration fees for the issue of bonus shares is allowable as revenue expenditure.

   Note - *While arriving at this decision, the Supreme Court has considered the effect of issue of bonus shares on the capital employed i.e. share capital plus reserves and not merely on capital alone. It may be noted that though bonus issue increases the capital of the company, the capital employed is left intact. This decision of the Apex Court has settled the long-standing dispute amongst the High Courts regarding the allowability of expenses on issue of bonus shares.*

2. ***CIT v. K.J. Ramaswamy (2006) 286 ITR 77 (Mad.) [FB]***

   The assessee was a founder of the trust of which his minor children were beneficiaries. The assessee was a partner in a firm in a representative capacity, as trustee of the trust. The issue under consideration was whether the income derived by the trustee in his representative capacity from the firm, which ultimately accrues to the beneficiaries, would be included in the income of the respective parent of the beneficiaries under the erstwhile section 64(1)(iii) read with Explanation 2A thereto.

   The High Court observed that in order to attract clubbing provisions, the income generated from transferred assets should be available for the benefit of the minor child i.e. the income must be readily available for the use of the minor. Where the income is only credited to the minor's account in the trust to remain there till he attains majority, then, such income is not for the immediate use of the minor. It was held that so long as the beneficiary – minor child receives his share income only on attaining majority, clubbing provisions are not attracted.

   Note – *Clubbing of minor's income is now covered under section 64(1A) which provides for clubbing of "all such income as arises or accrues" to a minor child. The issue in the current context is whether such income credited to a minor's account to be available for his use when he attains majority would fall outside the ambit of "all such income as arises or accrues" to a minor child under section 64(1A) also.*

3. ***Population Council, Inc., In re. (2006) 156 Taxman 125 (AAR-New Delhi)***

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The applicant, a non-resident, is a non-profit international organisation based in USA. The applicant incurs expenses in India, which include fringe benefits provided to the employees, falling under the heads traveling, conference, entertainment, hospitality etc. These expenses are met by remittances from the head office. The applicant contended that it is not liable to pay fringe benefit tax (FBT) under section 115WA since its income is not chargeable to tax in India. The question on which the applicant sought advance ruling of the Authority is whether it is liable to pay FBT under section 115WA on the fringe benefits provided to its employees working in India.

The AAR observed that section 115WA provides that FBT is in addition to income-tax and it is to be charged to tax even when no income-tax is payable by an employer on his total income computed in accordance with the provisions of the Act. Therefore, it is pointless to contend that no FBT would be payable by the employer, if its income is not chargeable to tax in India. Such an interpretation would be contrary not only to the intention of the Parliament but also to the plain language of the provision and the basic principles of interpretation. The AAR, therefore, ruled that the applicant is liable to pay fringe benefit tax.

4. ***CIT v. Aggarwal Engg. Co. (Jal.) (2006) 156 Taxman 40 (P & H)***

The assessee who was a civil contractor filed his return of income for the relevant assessment year. The assessment was made but was cancelled under section 263. Thereafter, the Assessing Officer made a best judgment assessment under section 144 applying the net profit rate on contract receipts to estimate the income from contract work. Further, he made separate addition on account of introduction of unexplained cash and unexplained payments for purchases outside the books of account. These additions were deleted by the CIT(A) and Tribunal. The High Court justified the views of the CIT(A) and Tribunal holding that once the net profit rate was applied, no further addition was called for in respect of purchases and introduction of cash.

5. ***Mahanagar Telephone Nigam Ltd. In re (2006) 286 ITR 211 (AAR)***

MTNL, a notified resident-applicant, entered into an agreement with one ITI for purchase of plant and machinery. The agreement provided that MTNL would be entitled to liquidated damages in case of failure by ITI to deliver the equipment within the stipulated time. The amount recovered by MTNL towards liquidated damages was adjusted against the cost of the assets in some years and shown as income in some years. ITI sent representations to MTNL for waiver of liquidated damages stating that the delay was due to reasons beyond its control. Thereafter, MTNL received a direction from the Telecom Commission to waive the liquidated damages. Accordingly, the Board of Directors of MTNL decided to waive the liquidated damages and refunded certain amounts to ITI during the relevant assessment year. The issue under consideration is whether the amount refunded by the applicant on account of waiver of liquidated damages would be allowable as deduction from business income.

The AAR observed that MTNL had reluctantly agreed to refund a part of the charges only to comply with the directions of the Telecom Commission and not voluntarily for business purpose. Since the

equipments supplied by ITI were capital assets, damages recovered on account of supply of capital assets were capital in nature and were not allowable as revenue expenditure. Such expenditure was outside the purview of both section 37(1) and 57(iii).

Note – *The question as to whether refund of liquidated damages can be allowed as deduction would also depend on the method of accounting followed by the assessee in respect of accounting for liquidated damages. If the liquidated damages were treated as a revenue receipt and credited to the profit and loss account, then it is possible to treat refund of the same as revenue expenditure, if such refund was wholly and exclusively for the purpose of its business.*

6. CIT v. Raghav Behl (2006) 286 ITR 134 (Delhi)

The assessee had purchased shares through two share brokers. The assessee could not make payment for the shares on time due to shortage of funds. Therefore, he had to pay interest till the date when he made payment and took delivery of shares. He claimed such interest as a deduction. The High Court held that charge of interest for delayed payment was customary in the trade of share transactions, and therefore, interest paid to brokers was allowable business expenditure.

7. CIT v. Abhishek Industries Ltd. (2006) 286 ITR 1 (P & H)

Under section 36(1)(iii), deduction is allowed for interest on loan raised for business purposes. Where the assessee claims such deduction, the onus lies on him to satisfy the Assessing Officer that such loan has been used for the purposes of business. Where in the process of examining the genuineness of the claim, it comes to light that the assessee had made interest-free loans or advances to its sister concerns, the onus would be on the assessee to justify such payment for non-business purposes in spite of pending interest-bearing term loans and working capital loans.

The assessee contended that such interest-free advances to its sister concerns for non-business purposes were made out of its own funds i.e. capital introduced in the business. This contention was not acceptable since the assessee's plea at the time of raising loan was that the capital was introduced by it as a margin for loans being raised. Subsequently, the assessee diverted substantial amounts to sister concerns for non-business purposes without interest and took the plea that the amount was advanced out of its capital. Such a plea might have been acceptable if the assessee had not raised any loan at the time of diversion of funds. This was not so in the instant case.

The High Court held that where the assessee had borrowed certain funds on which there was a liability to pay interest and had diverted amounts to its sister concern for non-business purposes without interest, then the interest to the extent of such interest-free advance made cannot be allowed as deduction under section 36(1)(iii).

8. CIT v. Chandra Charitable Trust (2006) 156 Taxman 19 (Guj)

There are two issues in this case, namely,

(i) Is Jainism not only a simple philosophy or a life-style, but a religion in itself?

(ii) Is exemption under section 11 available to a trust promoting Jainism in addition to other charitable goals?

The High Court placed reliance on the judgement of the Apex Court in *Bal Patil v. Union of India AIR 2005 SC 3172* in contending that Jainism is not a simple philosophy or a life-style but is in fact a religion in itself. Therefore, if a trust is formed only to promote Jainism, section 13(1)(b) would be attracted and the assessee would not be entitled to exemption under section 11.

However, in this case, from the covenants of the Trust Deed, it was evident that there were other charitable objects in addition to promoting Jainism. In such a case, the Trust would become a Charitable and Religious Trust and section 13(1)(b) would not be applicable. This was observed by the High Court in *CIT v. Barkate Saifiyah Society (1995) 213 ITR 492,* where it was held that in such cases, the assessee would be entitled to exemption under section 11.

9. ***Excise Commissioner v. Mysore Sales International Ltd. (2006) 286 ITR 136 (Karn.)***

The appellants were State Government undertakings engaged in manufacturing arrack. They conducted public auctions for granting leasehold rights upon contractors/buyers for retail vending of arrack in different areas in the State. The winning bidders in whose favour contracts were awarded were entitled to purchase arrack from the manufacturers and bottling units for sale in retail trade at the rate fixed by the State Government. The appellants submitted that they were not required to collect tax at source as the Excise Commissioner had issued a circular stating that they were not required to collect tax at source from contractors. The High Court held that collection of tax at source from contractors in respect of purchases of liquor was mandatory and the Excise Commissioner was not the competent authority for issuing such circulars. However, relief can be given to the extent tax has been paid by the contractors directly to the Government.

10. ***CIT, Lucknow v. Raza Buland Sugar Co. (2006) 156 Taxman 69 (All.)***

In this case, the High Court held that the excess amount realised by the sugar mill as sale price of sugar over and above the levy price fixed by the Government did not form part of the trading receipt.

11. *JCIT v. M/s. Usha Martine Industries Ltd. (I.T.A. No.1304/Cal./2000)*

The issue under consideration was whether the provision made for doubtful debts, advances and investments fall within the purview of adjustment mentioned in clause (b) of the Explanation to the erstwhile section 115JA and whether the Assessing Officer was justified to make adjustment of the same in computing the book profits. On this issue, the Tribunal observed that the Assessing Officer had nowhere stated that the provision made by the assessee for bad and doubtful debt is excessive or unreasonable considering the purpose for which the provision is made. The Revenue had also not proved that the provision made for bad and doubtful debts is excessive or unreasonable. The Tribunal, therefore, held that the Revenue's claim that the provision for bad and doubtful debts would fall within clause (b) of the Explanation to section 115JA is not acceptable. Accordingly, the addition made by the Assessing Officer in respect of provision for bad and doubtful debt was deleted.

INDIRECT TAXES

1. *Indian Oil Corporation Ltd. v. Collector of CEx., Baroda 2006 (202) ELT 37 (SC)*

Notification No. 75/84-CE read with the clarificatory Circular exempts Low Sulphur Heavy Stock (LSHS) or Reduced Crude Oil (RCO) consumed captively in a refinery for generation of electricity which, in turn is used in the process of manufacture of petroleum products. The Supreme Court has held that the exemption would not be denied if LSHS/RCO is consumed in a thermal power plant located within the refinery area. However, the exemption would not be available if RCO/LSHS is used in the generation of electricity which is not used in the manufacture of petroleum products within the refinery area.

In the instant case, the Apex Court elaborated upon one more point regarding the finality of orders due to non-filing of appeal. It has been held that the department is not entitled to raise same point in other cases when no appeal has been preferred against the order (involving that point) passed by the appellate authority, as the same becomes final. The Supreme Court held that the Revenue having accepted the principle laid down in an identical case could not be permitted to take a different stand in another appeal.

Note: *This case highlights that finality of orders due to non-filing of appeal affects other cases too.*

2. *CCEx. Bangalore-II v. Karnataka State Agro Corn Products Ltd. 2006 (202) ELT 47 (Kar.)*

The Karnataka State Agro Corn Products Limited (assessee) manufactured food products and was fully owned by the State Government. The food products were supplied to various Government departments on payment of excise duty. However, subsequently, it was noticed that the assessee was not liable to pay excise duty and thus, a refund claim was filed. The department rejected the refund claim on the ground of unjust enrichment i.e., the State being different from State Undertakings; the duty burden had been passed on.

The High Court observed that the State Government controlled the Government undertakings in the matter of management, finance, administration etc. State Government had an effective control over these Undertakings as the policies or programmes of these Undertakings were

also, to a certain extent, evolved by the State Government. The High Court held that unless the department was able to show that the Government undertakings were totally different from all angles, it would not be possible to accept the argument of unjust enrichment on the part of the State undertakings. A refund granted to the State Undertaking would ultimately go to the State's exchequer.

3. ***New Shorrock Mills v. CCEx. and Cus., Vadodara 2006 (202) ELT 192 (Tri.-LB)***

The Large Bench of the Tribunal held that doubling or multifolding of duty paid single yarn would not amount to manufacture. The Large Bench of the Tribunal relied upon the decision of the Apex Court in case of Banswara Syntex Ltd. 1996 (88)ELT 645 wherein it was held that a single ply yarn was first manufactured and thereafter it was doubled or multifolded, depending upon the type of fabric to be woven. The liability to pay excise duty arose on the manufacture of the single ply yarn and not after the same had been doubled or multifolded. The stage of levy of excise duty in such cases was the single yarn stage.

As regards the fact that doubled or multifolded yarn were completely exempt from payment of duty vide an exemption notification, the Large Bench of the Tribunal held that mere mention of an item in the notification was not determinative of its excisability.

4. ***Ispat Industries Ltd. v. CCus., Mumbai 2006 (202) ELT 561 (SC)***

The mother vessel anchored at Bombay Floating Light (BFL). After obtaining the out of charge order, the cargo was discharged at BFL from the mother vessel to the barges which then ferried the cargo to the Dharamtar jetty, the place approved under section 8(a) of the Customs Act, 1962. The cargo could not be discharged directly from the mother vessel to the Dharamtar jetty due to lack of draft. In the bills of entry, the assessable value of the cargo was arrived at by including freight from the place of export to the port of discharge viz., Mumbai/JNPT/Dharamtar. However, the Assistant Commissioner of Customs included the freight incurred on barges in transporting the cargo from BFL to the Dharamtar jetty in the assessable value of the cargo by virtue of Rule 9(2)(a) of the Customs (Valuation) Rules, 1988.

The Supreme Court observed that since the cost of transportation (from BFL to Dharamtar jetty) was already included in the price paid to the seller under CIF contract, a further addition to transport charges under Rule 9(2)(a) of the Customs Valuation Rules, 1988 was not permissible.

Section 14(1) states that the value of the imported goods shall be the *deemed* price at which such or like goods are *ordinarily* sold or offered for sale, for delivery at the time and place of importation in the course of international trade. The Apex Court asserted that section 14 creates a deeming fiction, therefore the prevailing price in the market has to be seen and not the actual price mentioned in the contract between the supplier and the importer. The Supreme Court observed that if Rule 9(2)(a) is read independently without considering it along with section 14, then the submission of the department could have been sustained. However, Rule 9(2) has to be read along with section 14 and it could not be read independently. Since, section 14 creates a legal fiction, the *ordinary value of the imported goods in the*

course of international trade at the place and time of import should be considered. Therefore, specific cases for determining value of imported goods should be ignored.

The Apex Court asserted that Rule 9(2)(a) is subservient to section 14 of the Customs Act, 1962, and hence should be interpreted in such a way so as to make it in accordance with the main object of section 14. The object of section 14 is 'primary' whereas conditions in Rule 9(2) are 'accessories'.

Note: *It may be noted that Circular No. 29/2004–Cus., dated 13.04.2004 issued by CBE&C has clarified that barging/lighterage charges borne by the importer in bringing the goods from the outer anchorage to the landmass have to be included in the assessable value as "extended cost of transportation" under Rule 9(2)(a) of Customs Valuation (Determination of Price of Imported Goods) Rules, 1988.*

A reading of the judgment and the above-mentioned circular may lead to the conclusion that where the price paid is limited to delivery at the outer anchorage by the specific terms of the CIF contract and the goods are subsequently transported and ultimately delivered at another place to make them as part of the landmass, the transportation changes thereof would be includible in the assessable value.

5. ***Baraka Overseas Traders v. Director General of Foreign Trade 2006 (202) ELT 3 (SC)***

All duty free advance licenses would be transferable whether they are in the "norms category" or "no norms category". The grant of licence creates certain rights in the favour of the licensee, and if the Licensing Authority is of the opinion that license is obtained by misrepresentation, then a show because notice should be given to the licensee as well as an opportunity of hearing. The Supreme Court held that DGFT had wrongly refused the appellant's request for endorsement of transferability of licence on ground that description of export items wrongly shown in "no norms category". Neither an opportunity of hearing was given to the appellant nor the licence was cancelled. Thus, DGFT was directed by the Apex Court to endorse transferability of licence in question.

6. ***Secretary, Council of Science & Tech., UP v. CCus. (Port) 2006 (202) ELT 241(Cal.)***

An ex-bond bill of entry in respect of certain warehoused goods was filed by the appellants. The duty was assessed at the applicable rate and was paid accordingly by the appellants. However, the goods were not cleared or removed from the warehouse. In the meanwhile, (when the goods were still in the warehouse) an exemption notification exempting the said goods was issued. The appellants contended that they were eligible for refund of the duty being paid by them on the said goods as the notification came in to effect when the goods were still in the custody and control of the proper officer in the warehouse. On the other hand, department contested the refund claim on the ground that the appellants had applied for warehousing in terms of section 49 of the Customs Act.

The High Court observed that section 15 of the Customs Act, 1962 *inter alia* lays down that in the case of the imported goods cleared from a warehouse the relevant date for determination of rate of duty and tariff valuation is the date on which the said goods are actually removed form the warehouse. The High Court stated that inspite of the payment of duty; the customs

authorities did not permit the clearance of the goods. The goods were in custody and control of the proper officer in the warehouse. Further, the department was unable to bring on record the application of the appellant seeking warehousing of goods under section 49. The High Court held that as the goods were cleared from the warehouse after the exemption notification came into force, the appellants were entitled to its benefit and were thus, eligible for the refund of duty.

Note: *Section 49 provides for storage of imported goods in the warehouse pending clearance. If the imported goods (both dutiable and non-dutiable) entered for home consumption cannot be cleared within a reasonable time, such goods may, pending clearance, be permitted to be stored in a public warehouse or in a private warehouse if facilities for deposit in a public warehouse are not available. Such a deposit will be permissible only when the importer applies for the same to the satisfaction of the Assistant/Deputy Commissioner of Customs. However, such goods are not deemed as warehoused goods for the purposes of the Customs Act and accordingly the provisions of Chapter IX do not apply to such goods.*

7. Surat Municipal Corpn. v. CCEx., Surat 2006 (4) STR 44 (Tri.-Del.)

Activity of letting out halls and stadiums for consideration for various social and official functions, such as sports, garbas, and educational programmes, cultural and religious programmes would be liable to service tax under the category of manadp keeper's services. In this case, the halls and stadiums were built by the Surat Municipal Corporation. It was held that there could not be any malafide intention of evading tax in case of a statutory government body.

Note: *The Bangalore Tribunal in the case of Secy., Town Hall Committee, Mysore City Corpn. v. CCEx., Mysore 2006 (4) STR 78 has held that a town hall built by Mysore City Corporation for holding public functions including cultural and political functions could not be considered as a mandap liable to service tax under mandap keeper's services.*

8. Bharat Matrimony.com Pvt. Ltd. v. CST, Chennai 2006 (4) STR 27 (Tri.-Chennai)

Matrimonial service provided from the portals/websites would be liable to service tax. They would be charged to service tax under the category of on-line information and database access or retrieval services.

"Note: This has reference to the Supreme Court ruling in *Amin Chand Payarelal v. Inspecting Assistant Commissioner, Income-tax (2006) 155 Taxman 633* reported in the November 2006 issue of the journal. It may be noted that now, penalty is attracted under section 271F for failure to furnish return of income as required under section 139(1) before the end of the relevant assessment year. The time allowed for filing a belated return is up to one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier. If the belated return is filed before the end of the relevant assessment year, penalty under section 271F is not attracted. However, if the same is filed after the end of the relevant assessment year, penalty under section 271F is attracted".

Further, in *Headstart Business Solutions (P.) Ltd., In re. (2006) 155 Taxman 639 (AAR – New Delhi),* please read "Authority for Advance Rulings" in the place of "High Court" at both places where reference is made to "High Court".