DIRECT TAX REFRESHER COURSE (WIRC OF ICAI)
BUSINESS HEAD- CURRENT DEVELOPMENTS

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SUMMARY OF THE PRESENTATION

- *Kernel* & Essence of business head taxation
  - What is “business” & “profession”? Significance of head of taxation
  - Concepts of Real Income, Overriding costs/diversion of income, Taxation of gross receipts vs income, principle of netting & mere 26AS is proof of income existence ; Taxation of ‘illegal’ business income;
  - Method of accounting u/s 145, 145A (versus section 198; section 43B etc);
  - Conundrum of Capital receipt vs revenue receipt (Carbon credit, liquidated damages etc)
  - Accrual of income – Supreme Court recent ruling in P.G.& Sawoo case; TDS implications- Provisions etc

SUMMARY OF THE PRESENTATION

- Supreme Court Chennai Properties case of rental income : head?
- Service tax whether forms part of assessable receipts? Delhi & Gujarat high court decisions…
- MAT u/s 115JB vs non taxable capital receipt?
- Madras high court section 28(iv) – Waiver of loan: *taxability* – *Rev Fav decision*
- Supreme Court on agreement value- business head of taxation – Mangalore Ganesh case
- Section 36(1)(iii) – Supreme Court Hero Cycles case 379 ITR..
- Supreme Court in Taparia Tools case 372 ITR on sec. 37;
- Supreme Court in Dalmia case on consistency….

SUMMARY OF THE PRESENTATION

- Taxability of Consortium CBDT Circular when to be treated as AOP?
- Revenue neutrality argument in expense disallowance?
- Expense can be disallowed only when claimed
  - Bombay high court recent pronouncements …
  - Other court decisions (Delhi, P&H etc);

SUMMARY OF THE PRESENTATION

- Delhi high court on litigated expense allowability Aggarwal & Modi case
- Section 40A(3) Rule 6DD Whether illustrative or exhaustive etc? P&H high court, T&AP high court; Delhi & Gujarat high court decisions;
- Karnataka high court on sec. 41(1)…

SUMMARY OF THE PRESENTATION

- Section 32: Depreciation related aspects
- Section 35D related issues
- Section 40(b) conflicting decisions…Partner remuneration…partnership deed drafting?
- Section 43B actual cost…
- Mark to market loss (MTM) recent developments

SUMMARY OF THE PRESENTATION

- Section 40(a)(i), & Section 40(a)(ia) related developments
- Section 14A related aspects
- Supreme court in case of Hoogly ….
- Supreme court in case of Emico…

CONCEPT OF BUSINESS & PROFESSION

- Section 2(13) : business includes any trade, commerce, or manufacture or any adventure or concern in the nature of trade, commerce or manufacture;
- Section 2(36): profession includes vocation;
- **Section 2(47) Transfer not apply to stock in trade**
  - Ahd ITAT in Ohm Developers (8/5/2015)
  - Hyd ITAT Leo Township Developers India Pvt. Ltd (15/7/2015) (refer Hon'ble Apex Court in the cases of CIT vs. Bhurangya Coal Co. 34 ITR 802 and Alapati Venkatramiah 57 ITR 185)

CONCEPT OF BUSINESS & PROFESSION

- According to **Sampath Iyengar's Law of Income Tax (9th edition), a business** activity has four essential characteristics.
- Firstly, a business must be a continuous and systematic exercise of activity. Business is defined as an active occupation continuously carried on. Business vocation connotes some real, substantive and systematic course of activity or conduct with a set purpose.
- Secondly essential characteristic is **profit motive or capable of producing profit.** To regard an activity as business, there must be a course of dealings continued, or contemplated to be continued, normally with an object of making profit and not for support or pleasure [Bharat Development (P) Ltd. v. CIT (1982) 133 ITR 470 (Del)]
- The third essential characteristic is that a business transaction must be between two persons. Business is not as unilateral act. It is brought about by a transaction between two or more persons.
- And lastly, the business activity usually involves a twin activity. There is usually an element of reciprocity involved in a business transaction.

HON'BLE SUPREME COURT OF INDIA IN THE CASE OF **CST V. SAI PUBLICATION FUND [2002] 258 ITR 70**

- Word 'business' under section 2(5-A) of the Bombay Sales Tax Act, 1959
- *It may be stated that the question of profit motive or no-profit motive would be relevant only where a person carries on trade, commerce, manufacture or adventure in the nature of trade, commerce etc. On the facts and in the circumstances of the present case irrespective of the profit motive, it could not be said that the Trust either was "dealer" or was carrying on trade, commerce etc. The Trust is not carrying on trade, commerce etc., in the sense of occupation to be a "dealer" as its main object is to spread message of Saibaba of Shirdi as already noticed above. Having regard to all aspects of the matter, the High Court was right in answering the question referred by the Tribunal in the affirmative and in favour of the respondent-assessee. We must however add here that whether a particular person is a "dealer" and whether he carries on "business", are the mattes to be decided on facts and in the circumstances of each case."*

HON'BLE SUPREME COURT OF INDIA IN THE CASE OF **CST V. SAI PUBLICATION FUND [2002] 258 ITR 70**

- *"16. The words 'carrying on business' require something more than merely selling or buying, etc. Whether a person 'carries on a business' in a particular commodity must depend upon the volume, frequency, continuity and regularity of transactions of purchase and sale in a class of goods and the transactions must ordinarily be entered into with a profit motive (Board of Revenue v. A. M. Ansari (1976) 38 STC 577 (Supreme Court); (1976) 3 scc 512). Such profit motive may, however, be statutorily excluded from the definition of 'business' but still the person may be 'carrying on business."*

CST V. SAI PUBLICATION FUND [2002] 258 ITR 70...

- *We have stated above that the main and dominant activity of the Trust in furtherance of its object is to spread message. Hence, such activity does not amount to "business". Publication for the purpose of spreading message is incidental to the main activity which the Trust does not carry on as business. In this view, the activity of the Trust in bringing out publications and selling them at cost price to spread message of Saibaba does not make it a dealer under Section 2(11) of the Act.*

CONCEPT OF BUSINESS

- . In State of Andhra Pradesh v. H. Abdul Bakhi and Bros. (1964) 15 STC 664, the Supreme Court dealt with the expression "business" and stated that it is an expression of indefinite import. In the taxing statutes it is used in the sense of an occupation or profession which occupies time, attention or labour of a person and normally associated with the object of making profit. It was held as under:

  "4. To regard an activity as business there must be a course of dealings, either actually continued or contemplated to be continued with a profit motive, and not for sport or pleasure. But to be a dealer a person need not follow the activity of buying selling and supplying the same commodity. Mere buying for personal consumption i.e. without a profit motive will not make a person, dealer within the meaning of the Act, but a person who consumes a commodity bought by him in the course of his trade, or use in manufacturing another commodity for sale, would be regarded as a dealer.“

CIT v. Lahore Electric Supply Company Limited (1966) 60 ITR 1 (SC) held that "business", under the Act contemplates activities capable of producing profit which can be brought to tax

SUPREME COURT IN CHENNAI PROPERTIES CASE 373 ITR 673

- The facts of the case before the Hon‟ble Supreme Court were that as per the memorandum of association, the main objects of the appellant company was to acquire and hold the properties known as “Chennai House” and “Firhavin Estate” both in Chennai and to let out those properties as well as make advances upon the security of lands and buildings or other properties or any interest therein. In the return that was filed, the entire income which accrued and was assessed in the said return was from letting out of those properties. The Hon‟ble Supreme Court while relying upon its the various other decisions held that in such a case the irresistible conclusion would be that the letting of the properties was in fact the business of the assessee and the income arising therefrom was to be treated under the head “Income from Business” and that it cannot be treated as income from House Property

MUMBAI ITAT IN M/S. SHREEJI EXHIBITORS, 14.08.2015 MUMBAI BENCH "E", APPLIED CHENNAI PROPERTIES CASE

- The facts of the case of the assessee before us are on better footings. The assessee‟s objects are not in respect of letting of any particular property, but it has the main objects of acquiring, constructing, operating and maintaining of the multiplexes, business center, marriage halls etc. The very object is the commercially exploitation of the properties. Besides that the assessee is also providing hosts of amenities and facilities, as discussed above, which amounts to composite business activity.

- Thus the issue is squarely covered in favour of the assessee by the above noted decisions of the Hon‟ble Supreme Court.

- We therefore hold that the income/loss from the multiplex is liable to be assessed as „business income/loss and not as income from house property. The assessee consequently is also entitled to the claim of deductions in respect of expenditure incurred and depreciation on assets etc. in relation to such income.

CONCEPT OF BUSINESS & PROFESSION

- CBDT Circular no. 6/2016 Classification of income from sale of shares etc.
  - If assessee opts for business head- accept it
  - If assessee for LTCG treats the asset as capital asset – accept it
  - Other case : as per prevalent circulars

(objective of reducing litigation and maintaining consistency in approach on the issue of treatment of income derived from transfer of shares and securities.)

M/s. Satabdi Investments Pvt. Ltd. ITA No.605/Bang/2014 Date of Pronouncement : 11.05.2016 Bang ITAT

Held: 10. Having carefully examined the orders of lower authorities in light of rival submissions and Circulars issued by the CBDT, we are of the view that since the assessee held the shares as capital investment in its books of account, the income earned therefrom on its sale should be treated to be the 'capital gain'. The period of holding of the shares cannot be a deciding factor for the nature of receipt accrued on its transfer/sale. Therefore, we do not find ourselves in agreement with the order of the ld. CIT(Appeals) and accordingly set aside his order and direct the AO to treat the income earned by the assessee on sale of shares as 'capital gain'.

SHARE SALE BOMBAY HIGH COURT VIEWS

- **IHP Finvest Ltd. 21st September, 2015** INCOME TAX APPEAL NO.1754 OF 2013
- *Our attention is invited to the relevant paragraphs of the orders of the Assessing Officer as well as the CIT(A) where the assessee was held to be a trader on account of following two considerations:- (a) the respondent assessee had scrips of the same company both in investment as well as in its trading account/portfolios, (b) the respondent-assessee has full discretion to decide to show a particular scrip as an investment and a particular scrip as a stockin-trade*.
- Besides, the second test namely that it is at the sole discretion of the respondent to determine whether a particular scrip is to be treated as an investment or a scrip in which he trades, is permissible in terms of the Circular No.4/2007 dated 15 June 2007. **It is for therespondent -assessee to determine how he seeks to treat a particular scripi.e. as an investment or for trading. This intent would only be reflected in maintaining different accounts for the two.** There is no allegations of shifting of scrips from trading to investment or vice versa.

PORTFOLIO MANAGEMENT INCOME-CLASSIFICATION

- Hon'ble Karnataka High Court in the case of CIT vs. Kapur Investments (P.) Ltd. (2015) 61 taxmann.com 91 (Karnataka) Held not business

- Above decision is re-iterated in Kamall Kailash case by Karnataka high court in ITA 387/2009 (27.07.2015) Held Profits from investment in portfolio management company is not business of assessee (engaged in private co. as a professional and deriving salary)

- Delhi high court Radials International case 367 ITR Page 1 (2014) Held not business

THE ADMINISTRATOR OF THE ESTATE OF LATE SHRI E.F.DINSHAW BOMBAY HIGH COURT LAND SALE CAPITAL GAINS – CLASSIFICATION

- Referred **Janki Ram Bahadur vs. Commissioner of Income Tax** 57 ITR 21 (SC); **G. Venkataswami Naidu & Co. vs. Commissioner of IncomeTax** 35 ITR 594 (SC); **Commissioner of Income Tax vs. V.A.Trivedi BHC** (1988) 172 ITR 95; **Commissioner of Income Tax vs. Dr.Indu Bala Chhabra DHC** (2002) 258 ITR 111; **Commissioner of Income Tax vs. Sushila Devi Jain** (2003) 259 ITR 671; principles have again been succinctly summarised in the statement of law in **Kanga and Palkhivala;**
- **Principles culled out from above in lucid manner**

OTHER PRECEDENTS ON BUSINESS HEAD APPLICABILITY ISSUE

- **Lord Precedent Clyde, in Commissioners of Inland Revenue v. Livingston, (1926) 11 Tax Case 538:-** "If the vendor was one consistent simply in an isolated purchase of some article against an expected rise in price and a subsequent sale, it might be impossible to say that the vendor was in the nature of trade. The test to be applied would be whether the operations involved in the transaction are of the same kind and carried on in the same way as those, which are characteristic of ordinary trading in the line of business."

- In **Ram Narain Sons (P) Ltd. v. IT Commissioner, AIR 1961 SC 1141 it was held that in consideration whether a** transaction is or is not an adventure in the nature of trade, the problem must be approached in the light of the intention of the assessee having regard to the "legal requirements, which are associated with the concept of trade or business."

MADRAS HIGH COURT VIEWS ON CLASSIFICATION OF LAND SALE GAINS

- CIT V. Mohammed Mohideen reported in 176 ITR 393, this Court following the decision in the case of CIT Vs. Kasturi Estates (P) Ltd. reported in (1966) 62 ITR 578 (Mad), held as follows:

  "A sale of immovable property may possible be a trading or commercial transaction, but need not necessarily be so... If a land-owner developed his land, expended money on it, laid roads, converted the land into house sites and with a view to get a better price for the land, eventually sold the plots for a consideration yielding a surplus, it could hardly be said that the transaction is anything more than a realisation of a capital investment or conversion of one form of asset into another. Obviously, the surplus in such a case will not be trading or business profits because the transaction is one of realisation of assets in investment rather than one in the course of trade carried on by the assessee or an adventure in the nature of trade."

- ONKARESHWAR PROPERTIES PVT. LTD Delhi high court recent decision in ITA 287/2016 (03/05/2016) Held real estate developer can have land as capital asset

- Sakunthala Vedachalam (Mrs.) v. ACIT (2014) 369 ITR 558 /(2015) 53 taxmann.com 62(Mad.) (HC)- agricultural land sale – treatment – principles spelt

OTHER PRECEDENTS ON CLASSIFICATION

- SHANTI BANERJEE (deceased) by LRs **HIGH COURT OF DELHI ITA 299/2003 17.11.2015**
- ***Referring G. Venkataswami Naidu and Co. v. CIT [1959] 35 ITR 594Raja Bahadur Kamakhya Narain Singh v CIT [1970] 77 ITR 253. Commissioner of Income Tax v R.V. Gupta [2002]261 (Del).***
- ***Held*** Merely, because the Assessee sold two plots that fell to her share pursuant to collaboration agreement in respect of the property owned by her since 1956, it would not render the transaction as an 'adventure in the nature of trade' leading to the resultant receipt as business income in her hand.(Applied by Delhi high court in case of RAJ DULARI BHASIN **ITA 11/2004 21.12.2015**)

DELHI HIGH COURT IN VIPUL MEDCORP TPA PVT. LTD. ON CONCEPT OF PROFESSION?

- *17. The term "profession" as traditionally understood involves the idea of an occupation requiring either purely intellectual skills or if any manual skill is involved such as in painting, sculpture or surgery, **a skill controlled by the operator's intellectual skill** as distinguished from an occupation which substantially involves production or sale or arrangement for the production and sale of commodities (See Patridge vs. Mallandine (1886) 18 QBD 276)). **The word "profession" as is currently known is wider than the old definition of learned professions such as the church, medicine and law.** As per the definition clause section 2(36) of the Act, profession includes vocation.*
- ***18. According to Black's Law Dictionary, 6th Edition, profession means:-***

  *"A vocation or occupation requiring special, usually advanced education, knowledge, skill; e.g. law or medical professions. Also refers to whole body of such profession. **The labour and skill involved in a profession is predominantly mental or intellectual, rather than physical or manual.The** term originally contemplates only theology, law and medicine, but as applications of science and learning are extended to other departments of affaires, other vocations also receive the name, which implies professed attainments in special knowledge as distinguished from mere skill."*

CONCEPT OF PROFESSION

- *The word "profession" was subject matter of interpretation before the Hon'ble Rajasthan High Court in CIT v/s Bhagwan Broker Agency, [1995] 212 ITR 133 (Raj.). Their Lordships have considered various decisions as well as definition given in the dictionary and after considering all these decisions and definitions, their Lordships have arrived at a conclusion that there should be some special qualification of a person apart from skill and ability which is required in carrying on any activity which could be considered as "profession". This could be having education in a particular system either in the college or university or it may be by experience.*

BUSINESS SET UP :A CONUNDRUM..

- The *locus classicus on the question as to when a business can be said to have been set-up is the judgment of the Bombay High Court speaking through Chief Justice Chagla, in* ***Western India Vegetable Products Ltd. v. CIT : (1954) 26 ITR 151. The following pithy observations are worth quoting: -***
- "It seems to us, that the expression „setting up" means, as is defined in the Oxford English Dictionary, „to place on foot" or „to establish", and in contradiction to „commence". The distinction is this that when a business is established and ready to commence business then it can be said of that business that it is set up. But before it is ready to commence business it is not set up. But there may be an interregnum, there may be an interval between a business which is set up and a business which is commenced and all expenses incurred after the setting up of the business and before the commencement of the business, all expenses during the interregnum, would be permissible deductions under sec. 10(2)."

WHEN IS BUSINESS SET UP?

- OMNIGLOBE INFORMATION TECH INDIA PVT LTD HIGH COURT OF DELHI
  (business of voice activation and local number portability, i.e. Business Process Outsourcing (BPO) services)
- The business of the appellant had been setup as the appellant-assessee had acquired the necessary infrastructure from their sister concern, M/s Agilis, and had also started making payment of salary and wages. This training was given by professional experts under the supervision and control of the appellant-assessee. The moment the said operations were commenced, the business had been setup and the subsequent rendering of service to third parties would be at a later date when the actual services were rendered to the parent/holding company. ....

Also refer:

- ***CIT Vs. Whirlpool of India Ltd. (2009) 318 ITR 347 (Del)***
- *CIT Vs. Samsung India Electronics Limited, 356 ITR 354*
- ***Commissioner of Income Tax vs. Sauer Danfoss (P) Ltd. [2012] 22 taxmann.com251 (Delhi)***

BUSINESS SET UP- CONUNDRUM

- *CIT Vs. Dhoomketu Builders & Development Pvt. Ltd., 216 TAXMAN 76 / 34 taxmann.com 18 * 23.04.2013* & ITA 528/2012

  (development of real estates -When an assessee whose business it is to develop real estates, is in a position to perform certain acts towards the acquisition of land, that would clearly show that it is ready to commence business and, as a corollary, that it has already been set-up. The actual acquisition of land is the result of such efforts put in by the assessee; once the land is acquired the assessee may be said to have actually commenced its business which is that of development of real estate. The actual acquisition of the land may be a first step in the commencement of the business, but section 3 of the Act does not speak of commencement of the business, it speaks only of setting-up of the business..)

BUSINESS SET UP: CONUNDRUM

- CAREFOUR WC&C INDIA PRIVATE LIMITED

  HIGH COURT OF DELHI (The present assessee was engaged and incorporated for carrying on trading activities in different commodities)
- *When the business is set up, is a mixed question of law and fact and depends upon the line, nature and character of the business/professional activity. For example, for manufacturing business, purchase of new material or electricity connection may be relevant point to determine setting up but in case of a property dealer, the moment, he puts up a chair and table, or starts talking, his business is set up*. ...To set up a business, the following activities become relevant:-
- '*Preparation of a business plan; establishment of a business premises; research into the likely markets or profitability of the business; acquiring assets for use in the business; registration as an entity and under the local laws etc.'* *The said list of activities are not exhaustive and facts of each case need to be considered. Indeed purchase of goods would amount to commencement of business, but before the said act, spade work and efforts to commence have to be undertaken. **A trader before actual purchase would possibly interact and negotiate with manufacturers, landlords, conduct due diligence to identify prospective customers, spread awareness etc. These are all integral part and parcel of the business of a trader.** The said activities continue even post first sale/purchase. When first steps are taken by a trader, the business is set up, commencement of purchase and then sales is post set up.* <u>When first steps are taken by a trader, the business is set up, commencement of purchase and then sales is post set up.</u>

SIGNIFICANCE OF HEAD OF TAXATION SUPREME COURT IN D.P.SANDHU BROS. 273 ITR 1

- his Court, as early as in 1957 had, in United Commercial Bank Ltd. V. Commissioner of Income Tax Ltd., West Bengal (1957) 32 ITR 688, held that the heads of income provided for in the Sections of the Income Tax Act, 1922 are mutually exclusive and where any item of income falls specifically under one head, it has to be charged under that head and no other. In other words, income derived from different sources falling under a specific head has to be computed for the purposes of taxation in the manner provided by the appropriate Section and no other. It has been further held by this Court in East India Housing and Land Development Trust Ltd. V. Commissioner of Income Tax, West Bengal (1961) 42 ITR 49 that if the income from a source falls within a specific head, the fact that it may indirectly be covered by an another head will not make the income taxable under the latter head. (See also: Commissioner of Income Tax Vs. Chugandas and Co.(1964) 55 ITR 17).

REAL INCOME- CONCEPT IN BUSINESS HEAD OF TAXATION- DIFFERENT FACETS

SUPREME COURT IN EXCEL INDUSTRIES 358 ITR 295

- Hon'ble Supreme Court in the case of CIT Vs. Excel industries Ltd. 358 ITR 295, had laid down three tests to determine when income can be said to have accrued. : (a) **Whether the income is real or hypothetical**; (b) Whether there is a corresponding liability of the other party to pay the amount to the assessee; (c) the probability or improbability of realisation of the income by the assessee has to be considered from a realistic and practical point of view. **Thus, probability or improbability of realization of the income has to be considered from practical point of view.**

MONICA INDIA BOMBAY HIGH COURT (16TH APRIL, 2016)

- *Now, turning to the merits of the issue, it is seen that this is a case of an Assessee being charged to tax on its profits and gains of business under Section 28 of the Act. **The charge of income tax in such a case is not on the gross income / receipts but only profits and gains of business**. Section 29 of the Act provides the manner in which the profits and gains of business or profession is to be computed i.e. in accordance with Section 30 to 43D of the Act. Section 37 of the Act is a general / residury provision which allows all expenditure incurred wholly and exclusively for the purposes of the business to be deducted from income in computing profits and gains of business. The expenditure which is incurred for purchase of goods for the purpose of sale would be an expenditure allowable for the purpose of computing the profits and gains of business. One more feature which must not be lost sight of i.e. an assessee is entitled to determine its profits and gains of business either on receipt basis or on mercantile basis (Section 145 of the Act).*

TRADE LOSS CASE LAWS

- Bombay High Court in case of I.B.M. World Trade Corporation vs. CIT 186 ITR 412(Bom) has held as follows:- “As the acquisition of premises on lease would not ordinarily be in the capital field, there is no hesitation in holding that the moneys advanced by the assessee in pursuance of the agreements to the landlord for the purposes of and in connection with the acquisition of the premises on lease were for the purpose of business. Naturally, therefore when such advances are lost to the assessee the loss would be a business loss and not a capital loss.”
- Ramchandar Shivnarayan vs. CIT (1978) 111 ITR 263 (SC) the Apex Court affirming the order of the Hon’ble High Court of Madras has held that if there is a direct and proximate nexus between the business operation and the loss or it is incidental to it, then the loss is deductible, as, without the business operation and doing all that is incidental to it, no profit can be earned. It is in that sense that from a commercial standard such a loss is considered to be a trading one and becomes deductible from the total income. It is to be remembered that the direct and proximate connection and nexus must be between the business operation and the loss

TRADE LOSS CASE LAWS

- the Hon'ble Madras High Court in the case of CIT vs. Textool Co. Ltd. 135 ITR 200 (Mad) has held as follows:- "where the assessee claims a business loss, the main question to be considered is, whether the loss is incidental to the business……. The tribunal found that the assessee had to import from abroad certain component parts necessary for its manufacturing business. The assessee had to be abide by the scheme of import licences under which the assessee had to pay premiums to the Federation in advance covering the entire import entitlement. Owing to business exigencies the assessee could not fully utilize the import entitlement, resulting in a forfeiture of part of the advance deposit with the Federation. The Tribunal therefore felt no difficulty in finding that the deduction claimed by the assessee in writing off the amounts so forfeited was in the course of and incidental to the assessee's business"
- .

DELHI HIGH COURT COMMISSIONER OF INCOME TAX VS UK BOSE 212 TAXMAN 399- OVERRIDING PRINCIPLE

- *There is also the overriding principle in tax law that it is not the gross receipt that falls to be assessed but it is only the net income, after all the expenditure to earn the income is deducted, that can be assessed to tax.* ***Strictly speaking, in the present case it is not a question of any deduction being allowed from the interest receipt; it is really a question of adjusting or setting off both the interest received and the interest paid, since both have close link or nexus with each other***

DELHI ITAT IN JAGUAR ENTERPRISES DELHI ITAT LOCUS CLASSICUS VIEWS 03.07.2014 ITA NO.1815/DEL/2014

- **In order to qualify as income or expenditure, it is of paramount importance that the assessee must have earned the income or incurred the expenditure in his own right.** The expenditure should be directed towards the earning of income and the income should ordinarily be the result of incurring of expenditure. If the expenditure is incurred or income is earned not in own capacity, but as representative of some third person, then it is the expenditure or income of such third person and not that of the assessee. In such a later situation, neither the amount of expenditure incurred can be treated as the expenditure of the assessee nor the income so earned can be construed as that of the assessee. The assessee is such circumstances merely acts as representative of the third person on whose behalf he is acting. The real effect of incurring such expenditure or earning such income by the assessee is that the such incurring of expenditure is invariably coupled with the right to recover the same and earning of such income is always saddled with the liability to repay to the person on whose behalf it was earned. **Such transactions cannot be considered to have been undertaken by the assessee for his own business so as to form part of its expenditure or income.**

DELHI ITAT IN JAGUAR ENTERPRISES DELHI ITAT LOCUS CLASSICUS VIEWS 03.07.2014 ITA NO.1815/DEL/2014

- Turning back, we find it as an admitted position that the business of the assessee is of custom clearing agent. In that view of the matter, the remuneration allowed by its customers as per the terms of the contracts, is its income. Similarly, expenditure incurred by the assessee for earning such income in his own right and without any obligation or instruction from the clients, is his expenditure. These income and expenses find place on the credit and debit sides of its Profit and loss account. **These items of income and expenditure earned/incurred by the assessee in his own capacity, are either includible in the total income or qualfy for deduction as per law. On the other hand, other expenses, including customs duty, freight paid and godown rent etc. incurred for the customers can by no stretch of imagination be construed as the expenses incurred by the assessee for his business so as to make them eligible for deduction.**

DELHI U.P.GOLDEN TRANSPORT SERVICE

- ITA No. 5957 and 5958/Del/2012 *The fact that the assessee is a transport commission agent who arranges goods carriers for various parties through truck operators/drivers is not disputed by the Revenue. The parties to whom the assessee arranges trucks, make part payment to the operators/drivers as advance and the balance amount is routed through the assessee. What the assessee gets is only commission. Under these circumstances, to hold that whatever amount passes through the assessee, is its turnover, is against the facts of the case.* ***The amount is received by the assessee as a Trustee. The assessee is only a pass through entity. The amount is received on capital account and payment also is made on capital account. The assessee never had the right to receive this amount as its income. Merely because tax has been deducted at source on the amounts received by the assessee, it does not lead to an automatic conclusion that the entire amount is the income of the assessee. The amount is never claimed by the assessee as its income nor was paid by the truck owners as an expense. The amount in question is the income of the lorry owners***

- In view of the above discussion, we are of the considered view that the amount in question cannot be treated as gross receipts of the assessee on revenue account.
- ***Delhi ITAT order dated*** 31st October,2014.

M/S. RAJESHWAREE SHIPPING & LOGISTICS "D" BENCH, MUMBAI 27.05.2016

- *Therefore, as a natural corollary if there was any default in deduction of tax on such payments, made to the CFS/ICDs, the liability should be on the person claiming the payment as expenditure. The assessee having never claimed these payments as expenditure, provisions of section 40(a)(ia) are not attracted.* ***Even otherwise also, if the entire issue is looked at rationally and dispassionately it is to be noticed that during the relevant previous year, assessee has earned gross commission income of ` 83,47,952, which has been shown in the Profit & Loss account and the Assessing Officer has also not disputed the income shown by the assessee. Therefore, for earning such income of ` 83,47,952, neither the assessee can be expected to have incurred expenditure of more than ` 3 crore nor the disallowance can be made of that amount .....***

- Consequently, no disallowance under section 40(a)(ia) can be made for alleged failure of the assessee to deduct tax at source on the payment made on behalf of the importers / clients.

ONLY INCOME IS TAXABLE & NOT GROSS RECEIPT

- Delhi high court in case of Subodh Gupta (contractor case vis a vis deeming fictions of section 40A(3))
- Delhi high court In Petroleum Sports Promotion Board 362 ITR 235
- *Madras High Court The Commissioner Of Income Tax vs S.Mohammad Dhurabudeen on 11 July, 2007* (2008) 4 DTR 218 (Mad)

M/S.KANGA & CO., BOMBAY HIGH COURT – DIVERSION OF INCOME (01ST FEBRUARY, 2016)

- The appellant Revenue urges following question of law for our consideration. *"Whether on the facts and in the circumstances of the case and in law, the Tribunal was justified in holding that the sum of Rs.1,20,89,002/paid to ex partners amounted to diversion of income by overriding title and so was allowable as deduction? "* The only issue in this appeal is the exclusion from the income of the firm, the amounts relatable to the retired/deceased partner/s share by diversion on account of overriding title in favour of the expartner/ s or their heirs/ executors by virtue of the partnership deed. 4. We find that the impugned order of the Tribunal has dismissed the Revenue's appeal by inter alia recording the fact that in the order of the Commissioner of Income Tax (Appeals) (CIT(A)) had only followed the consistent view of the Tribunal in the assessee's own case for the earlier Assessment Years. In fact, the impugned order of the Tribunal has further placed reliance upon the decision of this Court in Income Tax Appeal No. 860 of 2009 dated 19/06/2009 rendered in the respondents – assessee's own case as well as decision of this Court in the case of ***CIT Vs. Mulla and Mulla and Craigie, Blunt and Caroe, (1991) 190 ITR 198*** while dismissing the Revenue's appeal. 5. In view of impugned order of the Tribunal merely following the orders of this Court, we are of the view that the appeal does not raise any substantial question of law

DELHI HIGH COURT IN CASE OF SAINIK FINANCE AND INDUSTRIES LTD 03.01.2014

- *4. This Court has considered the submissions. Both the Appellate Commissioner and the ITAT have, in the opinion of this Court, applied the correct approach. What is determinative in the proceedings under the Income Tax Act is to bring to tax amounts which are designated or deemed to be ?income? in the terms of the Act. As to whether the activity has the sanction of law or is prohibited by it, cannot generally be gone into. In the present case it is not as if the business activities are per se prohibited by any law. What is urged by the revenue is that the company could not have pursued both the commercial activities, given the provisions of section 45I(vi)(aa) of RBI Act In this regard the Court notices that the income tax authorities are not empowered to enforce the provisions powers of the RBI Act. The Reserve Bank is the sole regulator of such activities. .. In the present case apparently, the RBI did grant such licence. In these circumstances, the Assessing Officer could not have gone into the question and disallowed the amounts claimed to be losses in the cement business, as he did in the order made by him.*

CONSORTIUM AS SPV

- M/s KBL PIL Consortium **Date of Pronouncement 27/03/2015 "A", BENCH MUMBAI**
- ***The CIT(A) has relied on the decision of jurisdictional High Court in the case of M/s Ray Bel Consortium, ITA No.639 of 2009, dated 25-06-2012, which*** *is having exactly similar facts. We had gone through the decision of the Hon'ble jurisdictional High Court, wherein under the similar facts it was held that where existence of consortium is not doubted, income accrues in the hands of its members who actually execute the works. In the instant case work contracts have been executed by its two members and since contract allotted by Municipal Corporation of Brihan Mumbai was sublet to its two members, any income accrues in the hands of the two members only and not in the hands of the consortium which is special purpose vehicle for allotment of work. Similarly, the assessee has not paid any amount on account of water and sewerage charges to the Municipal Corporation but it was deducted out of its payment, therefore, the AO was not justified in disallowing the same on the plea of 40(a)(ia).* ***Respectfully following the decision of the jurisdictional High Court in case of M/s Ray Bel Consortium (supra), we do not find any infirmity in the order of CIT(A) for deleting the addition made on account of profit estimation as well as disallowance of amount deducted by municipal corporation on account of water and sewerage charges.***

- **Same order in Bombay high court in** SMC Ambika JV **INCOME TAX APPEAL NO.252 OF 2012/11th June, 2014**

RECEIPT IS TAXABLE INCOME_ REVENUE BURDEN

- The settled legal position is that all receipts do not constitute income. For a receipt sought to be taxed as income, the burden lies upon the Revenue to prove that it is within the taxing provision. Among the earlier decisions of the Supreme Court is ***Parimisetti Seetharamamma v. CIT (1965) 57 ITR 532 (SC).***
- Udhavdas Kewalram v. CIT [1967] 66 ITR 462 (SC), It is for the income-tax authorities to prove that a particular receipt is taxable

CAPITAL RECEIPT SUPREME COURT

- In *CIT v. Saurashtra Cement Ltd., 325 ITR 422 (SC), the Assessee had entered into an agreement for supply of a cement plant with a condition that in the event of delay caused in delivery of the machinery, the Assessee would be compensated at 5% of the price of the respective portion of the machinery without proof of actual loss. With the supplier failing to supply the machinery within the stipulated time, the Assessee received Rs. 8,50,000 by way of liquidated damages, whereby the ITAT held this to be a capital receipt and the High Court answered in favour of the Assessee, the Revenue went in appeal before the Supreme Court. 30.2 Affirming the decision of the High Court, the Supreme Court in CIT v. Saurashtra Cement Ltd. (supra) held the damages received by the Assessee were "directly and intimately linked with the procurement of a capital asset viz., the cement plant. The amount received by the assessee towards compensation for sterilization of the profit-earning source, not in the ordinary course of business, was a capital receipt in the hands of the assessee."*

MUMBAI ITAT IN SHRI RATAN J. BATLIBOI ITA .7313/MUM./2013 13.08.2015

- *6. After considering the submissions of the rival parties and on a perusal of the material available on record, we find merit in the submissions of the learned Counsel for the assessee. Merely because the tax has been deducted by the builder and recorded it in his books of account as revenue expenditure, the same cannot be treated as revenue receipt. The compensation received for breach of contract which relates to capital assets and, therefore, the learned CIT(A) has rightly held it to be capital in nature. Thus, we do not find any cogent reason to disturb the reasoned order passed by the learned CIT(A) and decline to interfere in the matter as such. The grounds of appeal raised by the Revenue are dismissed.*

EXPENSE CLAIM MUST FOR DISALLOWANCE

- Health India TPA Services Pvt. Ltd INCOME TAX APPEAL NO. 1797 OF 2013 **HIGH COURT OF JUDICATURE AT BOMBAY**
- ....The *Sine qua non for the application of* Section 40(a)(ia) of the Act to apply is claiming of the amount sought to be disallowed as an expenditure / deduction to determine the taxable income of the assessee. In the present case, the Revenue is not challenging the concurrent finding of the fact that the amount of Rs.4.58 crores, which is being sought to be added to the Respondent's income has not been considered i.e. deducted to arrive at its income. Thus in such a case, the stand of Revenue contrary to the clear provisions of section 40(a)(ia) of the Act is unsustainable...Date of order **30th NOVEMBER, 2015**

PHILANA BUILDERS & DEVELOPERS P. LTD DELHI BENCH: 'F' 11.02.2016

- 9.3. *Moreover, the amount paid to Vikram Electric Equipment P. Ltd. was duly reflected by the assessee in the purchases closing stock. No sales had been made during the year under consideration. It has not been shown to be otherwise. In such a scenario, in our considered opinion, no disallowance is called for*.. The provisions of section 40(a)(ia) of the Act in any case do not apply, the assessee having not claimed any deduction for any expenses on account of payment to Vikram Electric Equipment P. Ltd. either in its profit and loss account or in the computation of taxable income filed. It was only that the Assessing Officer recorded a loss of Rs. 19,700/-. This obviously, did not include any addition of either Rs. 4.02 crores or Rs. 1.24 crores.. **the grievance of the assessee is found to be correct...**

CHENNAI ITAT IN AHMAD ZAKI RESOURCES BERHAD CHENNAI PROJECT OFFICE

- For invoking the provisions of section 40(a)(ia) of the Act, it must be found that default in TDS is in respect of an amount for which deduction has been claimed by the assessee or deduction is otherwise allowable to the assessee so that the same can be disallowed ....Be it stated that section 40(a)(ia) of the Act provides for disallowance of expenditure and it does not provide for deeming an amount as income of the assessee. Thus, the Assessing Officer has clearly erred in observing that for invoking the provisions of section 40(a)(ia) of the Act the only requirement is that the assessee has made default in payment of TDS and it is immaterial whether such default is in respect of an advance for which no deduction is claimed by the assessee or the default is in respect of an expenditure for which deduction has been claimed by the assessee.
- 18-04-2013
- I.T.A.No.2240/Mds/2012

MUMBAI ITAT ON DISALLOWANCE WHEN EXPENSE CLAIMED

- *IN THE INCOME TAX APPELLATE TRIBUNAL "C" Bench, Mumbai ITA No.2188/Mum/2013 (Assessment year: 2009-10) Paramount Health Services (TPA) Pvt. Ltd. Date of Pronouncement : 25/07/2014 (Similar order in Seminis Vegetable Seeds (I) Pvt Ltd (Now Merged with Monsanto Holdings P Ltd), in ITA 365/Mum/2012 16-09-2015)- Para 7)*
- Though the assessee is under the obligation to deduct tax at source under section 194J however, the consequential liability is only under section 201 and 201(1A) and the disallowance under section 40(a)(ia) cannot be automatic when the assessee has not claimed this payment as expenditure against the income. The assessee has shown the income, only the service charges receivable from insurance companies for rendering services as 3rd party administrator and not having any margin or profit element in the payment received from the insurers for the purpose of remitting to the hospitals to settle medical claim of the insured. *Therefore, when the said payment has not been claimed as expenditure incurred for earning the income by the assessee then the provisions of section 40(a)(ia) is not attracted for non deduction of tax at source in respect of the said payment. Following the decisions of the Tribunal as relied upon by the assessee and discussion above we hold that no disallowance can be made under section 40(a)(ia) in respect of the payment in question. Accordingly the ground raised in assessee's appeal is allowed and ground raised in the revenue's appeal is dismissed.*

DISALLOWANCE- SINE QUA NON EXPENSE CLAIMED

- Similar citations
  - *Delhi high court in Noble & Hewiit 305 ITR 324*
  - *P&H high court in CIT Vs. Mark Auto Industries Limited reported in (2013) 358 ITR 43 (P&H)* observed that no expenditure could be disallowed u/s.40(a)(i) of the Act if such expenditure was capitalized and not claimed as a revenue expenditure. Applied in Pune ITAT in Gera Development case in ITA 598/PN/2013 (31/12/2014)
  - *Bombay high court F.A.C.E Entertainment Pvt. Ltd**/ INCOME TAX APPEAL NO. 1419 OF 201307TH MAY, 2015 (Service tax not routed through P&L a/c)***

DELHI ITAT ON SEC. 40(A)(IA) AO'S DUTY

- M/s LDS Engineers Pvt. Ltd. **12.9.2014**
- The AO cannot pick up any item of expense debited to the Trading or Profit and loss account and disallow the same by invoking section 40(a)(ia) of the Act generally without first showing as to how there existed an obligation on the assessee to deduct tax at source from such payment under a particular section. It assumes more significance because such sections requiring deduction of tax at source have varying rates for deduction of tax at source

BOMBAY HIGH COURT SUNIL VISHWAMBHARNATH TIWARI,

- After hearing the respective counsel, we find that the fact that TDS was not effected by the respondent assessee, is not in dispute. In view of the scheme of Section 40 of the Act, as TDS is not effected, payment to contractors cannot be deducted, as those expenditure become inadmissible. The expenditures therefore are added back to the income, which is nothing but, eligible income. This income which is eligible for deduction in terms of Section 80IB(10) of the Act, therefore, only increases by said figure of disallowed expenditure.
- **INCOME TAX APPEAL NO. 2/2011.** 11.09.2015

BOMBAY STOCK EXCHANGE LTD BOMBAY HIGH COURT

- **WRIT PETITION NO.2468 OF 2011 Pronounced on : 12th June, 2014.**
- We also find force in the submission of Mr Dastoor that section 40(a) will not apply to the Petitioner at all as it is not carrying on any business. It is a charitable institution whose income is exempt under section 11 of the Act. Section 11 falls under Chapter III with the heading *"INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME". On the other hand,* Section 40(a) falls under Chapter IV with the heading *"COMPUTATION OF TOTAL INCOME"....* It is clear that section 40 applies to deductions claimed in computing the income chargeable under the head *"profit and gains of business and profession". In the present case, admittedly, the income of the Petitioner is* exempted under section 11 of the Act.

MUNJAL SHOWA LIMITED DELHI HIGH COURT- MTM HELD CBDT INSTRUCTION CANNOT OVERRIDE COURT RULINGS

- The Assessee has been following AS- 11 and AS-30 issued by the ICAI, in terms of which the loss/gains on outstanding derivatives contracts are to be recognized on mark to market basis. ***The Assessee is right in contending that CBDT Instruction No. 3 of 2010 cannot possibly override the existing decisions of the Supreme Court/ High Court on similar issues***. The legal position in this regard has been explained in Ratan Melting (supra) and has been reiterated in CIT v. Nagesh Knitwears (P.) Ltd. [2012] 345 ITR 135 (Delhi) and CIT v. Indian Oil Co. Ltd., (2012) 254 CTR 113 (Bom).

CBDT CIRCULAR CANNOT CROSS COURT RULINGS

- IN THE HIGH COURT OF DELHI AT NEW DELHI 1. + ITA 45/2016
- MITSUBISHI CORPORATION INDIA PVT. LTD. ..... Respondent
- % 10.02.2016
- 4. The next issue that has been urged is regarding the disallowance under Section 14A of the Act with reference to the expenditure incurred for earning exempt income. On this issue learned counsel for the Revenue submits that the decision of this Court in **CIT v. Holcim India (P) Ltd. [2014] 272 CTR 282** (Del) may require reconsideration by a larger Bench particularly in light of Circular No. 5/2014 of the Central Board of Direct Taxes dated 11th February 2014. 5. Having heard learned counsel for the Revenue and considering the fact that the judgment in CIT v. Holcim India (P) Ltd. (supra) was delivered on 5 th September 2014, the Court is not persuaded to accept the above plea of the learned counsel for the Revenue. **In any event, the circular of CBDT cannot possibly override a binding decision of the Court. Consequently,** the Court declines to frame any question as far as the above issue is concerned

DELHI HIGH COURT IN TATA TELESERVICES LIMITED ON RESTRICTIVE SCOPE OF SEC.119- CBDT CLARIFICAITONS

- *17. The idea of vesting the CBDT with the above power is to ensure that there is an ease of administration of the Act and that ambiguities in the practice and procedure may get clarified. At the same time it has to be ensured that such instructions or orders do not add to the difficulties of the tax payers. Circulars, orders and instructions issued by the CBDT under Section 119 of the Act, to the extent they are beneficial to the Assessees are binding on the Department. If they are prejudicial to the tax payer, then they cannot prevail over the statute, which does not envisage such harsher measure.*

SERVICE TAX WHETHER PART OF GROSS RECEIPT ASSESSABLE

- Delhi high court in MITCHELL DRILLING INTERNATIONAL PVT LTD. **ITA 403/2013** *The Court accordingly holds that for the purposes of computing the 'presumptive income' of the assessee for the purposes of Section 44 BB of the Act, the service tax collected by the Assessee on the amount paid t it for rendering services is not to be included in the gross receipts in terms of Section 44 BB (2) read with Section 44 BB (1). The service tax is not an amount paid or payable, or received or deemed to be received by the Assessee for the services rendered by it. The Assessee is only collecting the service tax for passing it on to the government*.
- CBDT Circular No. 1/2014 no TDS on service tax element (noted in above order)

KANTI AUTO FABRICATION PVT LTD. HIGH COURT OF GUJARAT 02/02/2016

- *We would focus only on the question of income of the assessee chargeable to tax having escaped assessment. In this context, we may recall that the reason recorded by the Assessing Officer for issuing the impugned notice states that the assessee had leased out a property for monthly rent of Rs.3 lacs, which was exclusive of the service tax. He had collected service tax of Rs.8.23 lacs and showed it under the head of administrative and other expenses. According to the Assessing Officer, instead, the assessee should have shown gross income of Rs.44.23 lacs of rental income and thereafter should have claimed Rs.8.23 lacs of service tax as expense. In our opinion, whichever way it is shown, in the eventual tax computation, it would not make any difference*. Whether the assessee showed net income of Rs.36 lacs by way of rental income or showed the gross income of Rs.44.23 lacs inclusive of the service tax and claimed Rs.8.23 lacs of service tax separately as expense, in the ultimate analysis, it was this sum of Rs.36 lacs which was chargeable to tax. **In other words, the service tax component of Rs.8.23 is not only as per the CBDT circular noted above, even as per the Assessing Officer himself, as indicated in the reasons recorded, was not chargeable to tax.** That being the position, mere accounting entry or even if there was some defect in indicating such amount in the accounts presented by the assessee, as long as income chargeable to tax had not escaped assessment, reopening of the assessment would not be permissible.

GURUKRIPA SOFTWARE SOLUTIONS (P) LTD“C” BENCH: KOLKATA24/10/2014

- We have heard both the Id. Counsel and perused the record. Upon careful consideration, we note that the AO has made addition as regards the difference between the sum credited in the P & L account on account of commission received from M/s. PCPL and as per confirmation received from M/s. PCPL. Before the Id.CIT(A) the assessee has submitted that the difference was on account of service tax. In this regard, copy of service tax return and tax payment challan was also filed by the assessee before the Id.CIT(A). We have also seen the concerned bill in proper page no.27. The bill clearly shows that the amount of bill was Rs. 1,08,36,000/- and service tax component was Rs. 13,39,330/- and the total of the bill thus comes to Rs.1,21,75,330/-. This bill was also before the AO. Hence, AO clearly failed to appreciate the reason of the difference noted by him. That the difference was on account of service tax is also supported by the service tax return and tax payment challan accepted by the Id.CIT(A). Hence, we do no find any infirmity in the order of the Id.CIT(A) on this issue. Hence, we uphold the same.(Service tax component of Rs.13,39,330/- was not routed through assessee’s profit & loss account but through separate service tax account.)

ACCRUAL OF INCOME- RECENT DEVELOPMENT

- Supreme Court In Excel Industries 358 ITR 295 (*including revenue neutrality aspect)*
  - *P&H High court recent order in* Vee Gee Industrial Enterprises **28.7.2015 (Income Tax Appeal No. 187 of 2014)**
  - ***Commissioner of Income-Tax, Delhi, Ajmer, Rajasthan and Madhya Bharat v. Nagri Mills Co. Ltd. (1958) ITR 681,***
  - Delhi High Court in ***Commissioner of income-Tax and Another v. Dinesh Kumar Goel (2011) 333 ITR 10 (Delhi).***
  - Hon'ble Delhi High Court in the case of CIT vs Vishnu Industrial Gases (ITR No. 229/1988)

ACCRUAL OF INCOME- RECENT DEVELOPMENT

- **M/S P.G.& W.SAWOO PVT.LTD.& ANR. ...APPELLANT(S) APRIL 19, 2016 Supreme Court**

- The income in question being income from house property is liable to be computed in accordance with the provision of Sections 22 and 23 of the Act. The premises belonging to the appellant was let out on rent to the Government of India. The rent was enhanced from Rs.4.00 to Rs.8.11 per sq.ft. per month effective from 01.09.1987. The said enhancement of rent was made by a letter dated 29.03.1994 of the Estate Manager of the Government of India. The said letter makes it clear that the enhancement was subject to conditions including execution of a fresh lease agreement and communication of acceptance of the conditions incorporated therein. Such acceptance was communicated by the appellant by letter dated 30.03.1994

ACCRUAL OF INCOME- RECENT DEVELOPMENT

- M/S P.G.& W.SAWOO PVT.LTD.& ANR. ...APPELLANT(S) APRIL 19, 2016 Supreme Court
- .. The contention of the assessee before us is that having regard to the provisions of Section 5, 22 and 23 of the Act and the decision of this Court in 'E.D. Sassoon & Company Ltd. And Others vs. Commissioner of Income-Tax', (1954) 26 ITR 27, no income accrued or arose and no annual value which is taxable under Sections 22 and 23 of the Act was received or receivable by the assessee at any point of time during the previous year corresponding to the assessment year 1989-1990. Hence, the impugned notice seeking to reopen the assessment in question is without jurisdiction or authority of law.
- This Court in E.D. Sassoon 26 ITR 27 (supra) has held in categorical terms that income can be said to have accrued or arisen only when a right to receive the amount in question is vested in the appellant-assessee.
- Viewed from the aforesaid perspective, it is clear that no such right to receive the rent accrued to the assessee at any point of time during the assessment year in question, inasmuch as such enhancement though with retrospective effect, was made only in the year 1994. The contention of the Revenue that the enhancement was with retrospective effect, in our considered view, does not alter the situation as retrospectivity is with regard to the right to receive rent with effect from an anterior date. The right, however, came to be vested only in the year 1994.

BOMBAY HIGH COURT
M/S. NEON SOLUTIONS PVT. LTD. ACCRUAL PRINCIPES 5TH APRIL, 2016

- *On further appeal, the Tribunal by the impugned order takes into account the fact that even in mercantile system of accounting an item would be regarded as accrued income only if there is certainty of receiving it and not when it has been waived.* The Tribunal has in the impugned order very succinctly set out the principles to be applied while recovering income in following the mercantile system of accounting:-
  "(A) that merely because assessee was following mercantile system of accounting, it could not be held that income had accrued to it.
  (B) earning of the income, whether actual or notional, has to be seen from the viewpoint of a prudent assessee. If in given facts and circumstances the assessee decides not to charge interest in order to safeguard the principal amount and ensure its recovery, it cannot be said that he has acted in a manner in which no reasonable person can act.
  (C) The guidance note on accrual of income on accounting issued by the ICAI lays down that where the ultimate collection with reasonable certainty is lacking, the revenue recognition is to be postponed to the extent of uncertainty involved. In terms of the guidance note, it is appropriate to recognize revenue in such cases only when it becomes reasonably certain that ultimate collection will be made. ...

BOMBAY HIGH COURT
M/S. NEON SOLUTIONS PVT. LTD. ACCRUAL PRINCIPES 5TH APRIL, 2016

- *(D) Non-recognition of income on the ground that the income had not really accrued as the realisability of the principal outstanding itself was doubtful, is legally correct under the mercantile system of accounting, when the same is in accordance with AS-I notified by the Government.*
  (E) It is one of the fundamental principles of accounting that, as a measure of prudence and following the principle of conservatism, the incomes are not taken into account till the point of time that there is a reasonable degree of certainty of its realization, while all anticipated losses are taken into account as soon as there is a possibility, howsoever uncertain, of such losses being incurred.
  *(F) The provisions of Section 145(1) are subject to, inter alia, mandate of AS-I which also prescribes that 'Accounting policies adopted by an assessee should be such so as to represent a true and fair view of the state of affairs of the business, profession or vocation in the financial statements prepared and presented on the basis of such accounting policies.' **In the name of compliance with Section 145(1), it cannot be open to anyone to force adoption of accounting policies which result in a distorted view of the affairs of the business. Therefore, even under the mercantile method of accounting, and, on peculiar facts of instant case, the assessee was justified in following the policy of not recognizing these interest revenues till the point of time when the uncertainty to realize the revenues vanished."***

SAVITRIDEVI RINGSHIA BOMBAY HIGH COURT]

29TH JUNE, 2015

- Held:
- 8 In view of the settled position of law by the decisions of this Court and Apex Court, it follows that the amount received under an interim order which is still subject to further final adjudication of the dispute cannot be considered to be an accrued income of the respondentassessee. The amount received under the interim order is not granted on resolution of the dispute but pending the final decision on the dispute. Thus, no income has accrued to the assessee on the amounts received under the interim order. In the above view, we find no substantial question arises for our consideration.

- (Bombay high court in *C.I.T. v/s Saksaria Biswan Sugar Factory Pvt. Ltd., reported in 195 ITR 778 &* Supreme Court in the case of *C.I.T. v/s Hindustan Housing & Land Development Trust Ltd.,* reported in *161 ITR 524 (SC))*

- *IOT Infrastructure & Energy Services Ltd – Bombay high court – Percentage complétion basis & mercantile basis- milestone basis – income recognition not entire amount recd. (18/04/2016)*

HIGH COURT OF KARNATAKA : *KARNATAKA POWER TRANSMISSION CORPORATION LTD. VS. DCIT (2016) 383 ITR* 59(KARN)

- *"We have examined the applicability of section 194A of the Act to the present case. Section 194A of the Act mandates the tax deductor to deduct "income-tax" on "any income by way of interest other than income by way of interest on securities". **The phrase "any income" and "income-tax thereon" if read harmoniously, it would indicate that the interest which finally partakes the character of income, alone is liable for deduction of be income-tax on that income by wav of interest. If the said interest is not finally considered to be an income of the deductee, as per reversal entries of the provision in the present case, section 194A(1) of the Act would not be made applicable. In other words, if no income is attributable to the payee, there is no liability to deduct tax at source in the hands of the tax deductor.** In view of the admitted fact that interest being not paid to the payees (suppliers) being reversed in the books of account, we are of the considered opinion that there would be no liability to deduct tax as no income accrued to the payees (suppliers). It is true that in the case of Ericsson Communication Limited (supra), the Delhi High Court was dealing with the case of section 195 of the Act wherein obligation of a person to deduct tax at source would be applicable to the "income chargeable under the Act". Absence of such words "chargeable to tax" under the provisions of section 194A of the Act would not empower the authorities to invoke the provisions of section 201(1) and 201(1A) of the Act ignoring the words 'any income by way of interest. "*

BANG BENCH: NO TDS ON MERE PROVISIONS WHERE NO ACCRUAL OF INCOME

- **Hon'ble Tribunal in the case of M/s.Bosch Ltd. vs. ITO in ITA No.1583/Bang/2014/ 01/03/2016,**
- *The short point that arises for our consideration is whether the liability for deduction of tax at source has arisen the moment the amount is credited in the books of accounts. Having regard in the scheme of tax deducted at source, under Chapter-XVIIB of the IT Act, we are of the considered opinion that the liability to deduct tax at source arises only when there is accrual of income in the hands of the payee. (CIT Vs M/s Shoorji Vallabhdas & Co. 46 ITR 144 & GE Technology 327 ITR 456 referred)*
- **M/s.TE Connectivity India Pvt. Ltd ITA No.3/Bang/2015 (Assessment year: 2012-13 Date of pronouncement : 25/05/2016**

  (The issue in appeal relates to the liability of the assessee-company to deduct tax at source on provisions made as at the end of the accounting year. The undisputed fact is that the provisions, made at the end of the accounting year are reversed in the beginning of the next year. No payees are identified. The exact amount of liability also cannot be quantified. The provisions are made merely on for Management Information System. In our considered opinion, liability to deduct tax at source does not arise.)
- *Industrial Development Bank of....vs. ITO (107 ITD* 45)(ITAT, Mumbai); *Pfizer Ltd. vs. ITO (TDS)(OSD) (28 Taxmann.com* 17(ITAT, Mumbai); **M/s. Rediff.com India Ltd ITA NOs.4661,4662,4663/Mum/2013 13/04/2016 (para 11.7) ;** Aditya Birla Nuvo Ltd 17 September, 2014 Income Tax Appellate Tribunal - Mumbai

RETENTION MONEY- GUJARAT HIGH COURT AMARSHIV CONSTRUCTION PVT. LTD 19TH MARCH 2014

- Mere fact that the amount was received by the assessee would not mean that income had accrued. Whether income did accrue or not would depend on the fact whether the right to receive said amount had accrued or not. ***The fact that tax was deducted at source on said amount also would be of no consequence. Tax was deducted by SSNNL. The assessee had no control over such deduction. Merely whether tax was deductible or not would not decide the taxability of certain receipts.*** The manner in which the assessee accounted for such receipt in its books of account can also not determine its tax liability, as held by the Supreme Court in case of ***Kedarnath Jute Mfg. Company Limited v. Commissioner of IncomeTax [Central], Calcutta reported in 82 ITR 363.(Also SC in Taparia case*** 372 ITR 605).. **The expenditure incurred by the assessee could not be proportionately divided into that covering the assessee's ninety *per cent of the bill amount and relatable* to the rest ten percent.**
- Held the Assessing Officer is directed to tax the said as per the terms of the contracts *ie., after* the defect liability is over and after the EngineerinCharge certifies that no liability attaches to the appellantretention money

LOK HOUSING & CONSTRUCTIONS BOMBAY HIGH COURT DECISION (CANCELLED TRANSACTION & REVISED RETURN U/S 139(5)

- INCOME TAX APPEAL NO.877 OF 2013; APRIL 13, 2015
- *In the present case, the argument was, that this income which was declared could not have been thereafter termed as such. It not being realised as the Sale Agreements have been cancelled. 11. In that regard, we find that the Tribunal was informed by the Revenue that there is a doubt about the cancellation of the relevant Agreements. That cancellation is not genuine and bona fide. The other argument was that these are Agreements with sister concerns and therefore in the first place, there was some deliberate exercise and with a view to avoid paying the legitimate taxes. In any event, the Agreements being subsequently cancelled supports the Revenue's version as above.*

- *The correct legal principles were applied and a finding of fa is arrived at in para 48, that no income could be said to have really accrued to the assessee as a result of the five transactions in the immovable properties and which income was chargeable to tax in the year under consideration. Once income had not accrued to the assessee in the real sense, then the original return represents wrong statement which was corrected by the assessee by filing a revised return. **Therefore, no hypothetical income of the assessee could have been brought to tax***

MRS. HEMAL RAJU SHETE – ACCRUAL OF INCOME- APPLIES TO CAPITAL GAINS ALSO BOMBAY HIGH COURT (29TH MARCH, 2016)_

- Further the formula presc ribed in the agreement itself makes it clear that the deferred consideration to be received by the respondent-assessee in the four years would be dependent upon the profits made by M/s. Unisol in each of the years. Thus in case M/s. Unisol does not make net profit in terms of the formula for the year under consideration for payment of deferred consideration then no amount would be payable to the respondent-assessee as deferred consideration. *The consideration of Rs.20 crores is not an assured consideration to be received by the Shete family. It is only the maximum that could be received. Therefore it is not a case where any consideration out of Rs.20 crores or part thereof (after reducing Rs.2.70 crores) has been received or has accrued to the respondentassessee*
- *Apex Court in **Morvi Industries Ltd. vs. CIT (1971) 82 ITR 835***
- *Supreme Court in **E.D. Sassoon & Co. Ltd. Vs. CIT (1954) 26 ITR 27***
- *the Apex Court in **Commissioner of Income-Tax vs. M/s. Shoorji Vallabdas and Co. (1962) 46 ITR 144***
- *Apex Court in the case of **K.P. Varghese vs. Income-Tax Officer, Ernakulam & Anr***

Also refer Bombay high court in Skyline Great Hills,case order dated 16/2/2016 in ITA 2299/2013 – SECURITY DEPOSIT- BUSINESS INCOME – YEAR OF TAXABILITY WHEN POSSESSION & LICENSE GIVEN

CIT VS. CHEMOSYN LTD (BOMBAY HIGH COURT)

- *i) In **Chaturbhuj Dwarkadas Kapadia**, the issue was to determine the year in which the property was transferred for the purpose of capital gains. In this case the issue is what is the consideration received for the transfer of an asset. No income is accrued or received of the value of 18000 sq.feet of constructed area under the development agreement because the said agreement was not acted upon as it came to be uperseded/modified by the Tripartite agreement. This was the position when the return of income was filed. On the application of the real income theory, there would be neither accrual nor receipt of income to warrant bringing to tax to the constructed area of 18,000 sq.ft which has not been received by the assessee (**CIT vs. Shoorji Vallabhdas** 46 ITR 144 (SC) followed);*

“C” BENCH, MUMBAI -M/S PHE CONSULTANTS, 10.7.2015

- The assessee firm is engaged in the business of undertaking contract works and offering consultancy services. The assessee has received a sum of Rs.153.26 lakhs from Municipal Office, as advance amount for providing certain Consultancy work. The Municipal Office deducted tax at source of Rs.17,36,471/- from the above said payment. During the year under consideration the assessee offered a sum of Rs.5,41,295/- only, out of the above said amount of Rs.153.26 lakhs and the balance amount of Rs.148.27 lakhs was shown as liability in the balance sheet. However, it appears that the assessee had claimed the entire TDS amount of Rs.17,36,471/- against the tax payable and accordingly claimed refund also.
- The AO noticed that the provisions sec. 198 states that the TDS amount deducted shall be deemed to an income received by the assessee. Accordingly, the AO took the view that the assessee should have offered the TDS amount of Rs.17,36,471/- as its income during the instant year. However, during the year under consideration, the assessee had declared gross receipt of Rs.5,41,295/- only and the corresponding TDS amount thereon worked out Rs.61,329/-. Accordingly the AO took the view that the balance amount of TDS amount Rs.16,75,142/- (Rs.17,36,471/- (-) Rs.61,329/-) was to be assessed as income of the assessee under section 198 of the Act and accordingly added the same to the total income

"C" BENCH, MUMBAI -M/S PHE CONSULTANTS, 10.7.2015

- *"198. All sums deducted in accordance with the foregoing provisions of this Chapter shall, for the purposes of computing the income of an assessee, be deemed to be income received." careful perusal of the above said provisions would show that (a) It is a deeming provision, i.e., it deems that the TDS amount is an income received by the assessee. (b) It is for the purposes of computing the income of an assessee*
- *It is pertinent to note that the provisions of sec. 198, though states that the Tax deducted at source shall be deemed to be income received, yet it does not specify the year in which the said deeming provisions applies. However, sec. 198 states that the same is deemed to be income received "**for the purpose of computing the income of an assessee." The provisions of sec. 145 of the Act state that the income of an assessee chargeable under the head "Profits and gains of business** or profession" or "Income from other sources" **shall be computed in** accordance with either cash or mercantile system of accounting regularly employed by the assessee. Hence a combined reading of provisions of sec. 198 and sec. 145 of the Act, in our view, makes it clear that the income deemed to have been received u/s 198 has to be computed in accordance with the provisions of sec. 145 of the Act, meaning thereby, the TDS amount, per se, cannot be considered as income of the assessee by disregarding the method of accounting followed by the assessee. Hence it is provided in Rule 37BA of the Income tax Rules that TDS credit is to be given to the assessee in the assessment year in which such income is assessable, meaning thereby, the TDS amount shall also be given proportionate credit.*

SECTION 145A PUNE ITAT IN MUNAF IBRAHIM MEMON, 30.10.2015

- In respect of first aspect of the issue that whether the assessee is correct in not recognizing the VAT relatable to its sales as part of the sale consideration in view of the Maharashtra Value Added Tax Act, 2002, we are of the view that the Centre by way of Finance (No.2) Act, 1998 had proposed the introduction of a new section 145A of the Act. Under the said provision, it is provided that valuation of purchase, sale and inventory shall be made in accordance with method of accounting regularly employed by the assessee and such valuation shall further be increased to include the amount of any tax, duties, cess or fees, by whatever name called, actually paid or incurred by the assessee, in the valuation of the goods. In view of the provisions of the Act i.e. section 145A of the Act, we find no merit in the plea of the assessee in not recognizing the VAT attributable to its sales as part of the sale consideration of the goods while computing its Profit & Loss Account.

SECTIO N 145A PUNE ITAT IN MUNAF IBRAHIM MEMON, 30.10.2015

- *The mandatory provisions of Central Act i.e. section 145A of the Act supersedes the provisions of any State Act i.e. Maharashtra Value Added Tax Act, 2002. Once the assessee recognized the VAT amount as part of the sale consideration, it tantamount to the said entry being routed through the Profit & Loss Account, especially in the cases where the assessee is following mercantile system of accounting. Admittedly, in the facts of the present case, the assessee was following mercantile system of accounting*. Now, coming to second aspect of the issue that, where the assessee had not recognized the amount of VAT payable / paid in its Profit & Los s Account and had only made entries in the Balance Sheet, are the provisions of section 43B of the Act attracted in the case? *In view of the cumulative provisions of sections 145A and 43B of the Act, the assessee is entitled to claim the deduction on account of such tax, duties, cess or fees, by whatever name called and the same is to be allowed only on payments and once the payment has not been made in the year to which the said liability relates, then the said amount is to be added back as income of the assessee for the relevant year. **Accordingly, we direct the Assessing Officer to verify whether the assessee has deposited the said amount before the due date of filing the return of income under section 139(1) of the Act and allow the claim in accordance with law***

MAT SEC. 115JB- WHETHER CAPITAL RECEIPT (NON TAXABLE FORMS PART OF IT?) RECENT VIEWS

- Mumbai ITAT in **Shivalik Venture Pvt. Ltd** August 19, 2015
- The assessee held a parcel of land admeasuring about 61,506 sq.mtr as its capital asset. The said land was attached with development rights/FSI. The assessee transferred development rights/FSI of 55,464.04 sq.mtr which was available on a portion of above said land to its wholly owned Indian subsidiary company. The said transfer generated Long Term Capital Gain (LTCG) of 300.68 crores. The assessee disclosed the same as "Extra Ordinary Income" in the profit and loss account. The said LTCG was not chargeable to tax u/s 47(iv) of the Act as it arose from the transfer of a capital asset by a company to its wholly owned Indian subsidiary. For purposes of computation of book profits u/s 115JB, the assessee inserted a note in the accounts stating that the said amount credited to the P&L A/c did not have the character of "income" and was not chargeable as "book profits". The AO & CIT(A) relied on the judgement of the Special Bench in Rain Commodities Ltd v/s DCIT (2010) (40 SOT 265; 131 TTJ 514) where it was held that if an amount, though not chargeable as capital gains u/s 47(iv), is credited to the P&L A/c, the same cannot be excluded from the book profits u/s 115JB. Refer: 325 ITR 565 & 52 SOT 381
- **S. 115JB: (i) Even if an amount is credited to the P&L A/c, the assessee can seek exclusion of that amount for purposes of "book profits" if a note to that effect is inserted in the A/cs (ii) The exemption conferred by S. 115JB to sums exempt u/s 10 should be extended to all sums which are not chargeable to tax....***If the said logic is extended further, an item of receipt which does not fall under the definition of "income" at all and hence falls outside the purview of the computation provisions of Income tax Act, cannot also be included in "book profit" u/s 115JB of the Act.*

CHENNAI ITAT M/S A.V. THOMAS LEATHER & ALLIED PRODUCTS PRIVATE LIMITED : 05.02.2016

- *Now coming to the assessee's appeal, the only contention of the assessee is while computing book profit under Section 115JB of the Act, the agricultural income cannot form part of book profit. The Ld. representative for the assessee placed his reliance on the decision of Cochin Bench in Harrisons Malayalam Ltd. (supra) and contended that the amount of income to which the provisions of Section 10 of the Act applies, such amount, if credited to the Profit & Loss account, shall be reduced from the book profit for the purpose of Section 115JB of the Act. The Ld. representative further found that in computing the total income of previous year of any person, agricultural income shall not be included therein. In this case also, it is an admitted fact that the land in question is an agricultural land and the assessee was carrying on agricultural operation. Therefore, as discussed earlier, the profit on sale of the land has to be treated as agricultural income. Therefore, if any such income is credited to the Profit & Loss account, the same has to be reduced from the book profit while computing income under Section 115JB of the Act. Therefore, this Tribunal is unable to uphold the order of the CIT(Appeals) on this issue. By following the order of Cochin Bench of this Tribunal in Harrisons Malayalam Ltd. (supra), the orders of the lower authorities are set aside. The Assessing Officer is directed to reduce the profit on sale of agricultural land from the book profit for the purpose of computing income under Section 115JB of the Act.*

M/S L.H. SUGAR FACTORY LTD LUCKNOW BENCH "B", LUCKNOW 09/02/2016

- By respectfully following these Tribunal's orders, we hold that in the present case also, the receipt on account of transfer of carbon credit which is held to be a capital receipt needs to be excluded from profit as per P&L account for the present year while computing the book profit u/s 115JB of the Act.
- ACIT Vs. M/s Shree Cement Ltd. in ITA Nos. 614, 615 & 635/JP/2010 dated 09.09.2011:we hold that capital receipt in the form of Sales Tax incentive needs to be excluded from profit as per P&L Account for the year in computing Book profit u/s 115JB of the Act.

KARNATAKA HIGH COURT ON MAT/115JB:

- In case of Hariram Hotels Pvt Limited in ITA 53/2009 (order dated 16/12/2015) Held in context of question of law that " Whether on the facts and the circumstances of the case , the tribunal is justified in holding that the income from capital gain should be included for the purpose of computing book profit u/s 115JB of the Act? Answered in appellants favor by observing that " In the light of the judgment of Apollo Tyres (supra) we are of the opinion that AO has no power to compute book profit and has to rely upon the authentic statements of the accounts of the company, the accounts being scrutinized and certified by statutory auditors though with a qualification, approved by the company in general body meeting and thereafter filed before the ROC, who has a statutory obligation to examine and be satisfied that the accounts of the company are maintained in accordance with the requirements of the Companies Act"

M/S. APOLLO FINVEST (I) LTD. .. BOMBAY HIGH COURT 8/2/2016 BOMBAY HIGH COURT

- *he respondent assessee had claimed 100% depreciation on Energy Measuring Devices purchased from Haryana State Electricity Board (the HSEB). After purchase, the same was leased back to HSEB under Lease Agreement dated 29th September, 1995. During the course of the assessment proceedings, the Assessing Officer held that the Lease Agreement styled as purchase and lease back transaction was infact and in substance a finance lease agreement. The Assessing Officer in his order dated 21st March, 2002 placed reliance upon Circular No.2 of 2001 issued by the CBDT, which states that "where assets are factually non-existent created by havala transaction, the question of allowing depreciation does not arise". On the aforesaid ground, the Assessing Officer disallowed the depreciation amounting to Rs.1.99 crores claimed by the respondent assessee and added the same to its income*

- *Being aggrieved, the Revenue carried the issue in appeal to the Tribunal. The Tribunal by the impugned order dismissed the Revenue's appeal. This by placing reliance upon the decisions of Apex Court in I.C.D.S. Ltd. Vs. Commissioner of Income Tax & Anr. (2013) 350 ITR 527 SC and of the Tribunal in Development Credit Bank Ltd. Vs. DCIT, (ITA No. 3006/M/01, 4892/M/03 and 3620/M/01). The impugned order also makes a reference to the decision of the Tribunal in West Coast Paper Mills Ltd.(Supra) to conclude that the claim of depreciation on the sale and lease back of assets is allowable.*

M/S. APOLLO FINVEST (I) LTD. .. BOMBAY HIGH COURT 8/2/2016

- 7. We find that the decision of the Apex Court in ICDS (Supra) would apply to the present facts. The distinction drawn by Mr. Pintois that the case ICDS (Supra) was a case of hire purchase and not so in this case, is no distinction for the reason that the Supreme Court in ICDS (Supra) held that the Assessee was in the business of leasing of vehicles and not hire purchase. The Apex Court in ICDS (Supra) has held that for claim of depreciation to be allowed, the con dition precedent are ownership of the assets and

  user for purposes of business
  i.e. not usage of the assets by the Assessee itself but for purposes of its business of leasing. Both in ICDS (Supra) and this case, the

  respondent is in the business of leasing.

  Thus, claim of depreciation is allowable.

M/S RANA POLYCOT LIMITED
HIGH COURT OF PUNJAB AND HARYANA
DATE OF DECISION: 10.8.2015

- *The primary issue that arises for consideration in the present appeal relates to allowance of depreciation under Section 32(1) of the Act @ 15% on ` 10,00,000/- paid by the assessee as fees to the Registrar of Companies for the expansion of capital base and capitalized towards plant and machinery. The amount of fees paid to Registrar of Companies for augmenting the aforesaid share capital for expansion of the business had been capitalized by the assessee against plant and machinery as according to the assessee, the same was paid to generate funds for the expansion of the existing business. In such circumstances, the claim of the assessee cannot be held to be unjustified whereas neither the Assessing Officer nor the Tribunal have recorded any cogent and convincing reasons for holding it otherwise. Once it is held that the amount of fees paid to Registrar of Companies for increasing the authorized share capital is capitalized against plant and machinery as a necessary corollary, the assessee is entitled to depreciation at the rate of 15% on ` 10 lacs amounting to ` 1,50,000/-. The CIT(A) had rightly accepted the claim of the assessee. Examining the alternative plea of the assessee, it may be noted that in case, it is held that the fees paid to Registrar of Companies is a*

M/S RANA POLYCOT LIMITED
HIGH COURT OF PUNJAB AND HARYANA
DATE OF DECISION: 10.8.2015

.....capital expenditure not attributable to any capital asset and the assessee is not entitled to claim any depreciation, then in that eventuality, the assessee would be entitled to claim an amount equal to one fifth i.e. 20% of such expenditure for each of the five successive previous years as amortization of preliminary expenses under Section 35D(2)(c)(iv) of the Act . Similarly, in ***CIT vs. Mahindra Ugine and Steel Co. Limited,****(2001) 250 ITR 84 (Bom.),* ***Autolite India Limited vs. CIT,*** *(2003) 264 ITR 117 (Raj.), and* ***CIT vs. Ashok Leyland Limited****, (2012) 349 ITR 663 (Mad.), expenses incurred on issue of shares or public issue for expansion of existing unit were allowed to be amortized under Section 35D(2) (c) (iv) of the Act Viewed from any angle, it is concluded that the claim of the assessee cannot be declined. Since the fees paid to Registrar of Companies for enhancing the authorized share capital for expansion of the business had been capitalized against plant and machinery, the assessee would be entitled to depreciation at the rate of 15% on ` 10,00,000/- and the benefit of Section 35D(2)(c)(iv) of the Act would not be available to the assessee. Upshot of the above is that the substantial question of law is answered accordingly and the appeal is disposed of by holding that the assessee shall be entitled to depreciation of ` 1,50,000/- @ 15% on ` 10,00,000/- under section 32(1) of the Act on the amount capitalized towards plant and machinery by including the fees paid to Registrar of Companies by the assessee*

SUPREME COURT HERO CYCLES SEC. 36(1)(III) – 379 ITR / (2015) 281 CTR 481

- Further appeal of the Revenue before the High Court filed under Section 260A of the Income Tax Act, however, has been allowed by the High Court vide impugned judgment dated 06.12.2006. Challenging that judgment, special leave petition was filed in which leave was granted and that is how the present appeal comes up for hearing. A perusal of the order passed by the High Court would reveal that the High Court has not at all discussed the aforesaid facts which were established on record pertaining to the interest free advance given to M/s. Hero Fibres Limited as well as loans given to its own Directors at interest at the rate of 10 per cent. On the other hand, the High Court has simply quoted from its own judgment in the case of 'Commissioner of Income Tax-I, Ludhiana v. M/s. Abhishek Industries Limited, Ludhiana' [ITA No. 110/2005 decided on 04.08.2006]. On that basis, it has held that when loans were taken from the banks at which interest was paid for the purposes of business, the interest thereon could not be claimed as business expenditure. **We are of the opinion that such an approach is clearly faulty in law and cannot be countenanced.** Insofar as loans to the sister concern / subsidiary company are concerned, law in this behalf is recapitulated by this Court in the case of 'S.A. Builders Ltd. v. Commissioner of Income Tax (Appeals) and Another' [2007 (288) ITR 1 (SC)]. (taking note of and discussing on the scope of commercial expediency)

SUPREME COURT HERO CYCLES SEC. 36(1)(III) – 379 ITR / (2015) 281 CTR 481

- In the process, the Court also agreed that the view taken by the Delhi High Court in 'CIT v. Dalmia Cement (B.) Ltd.' [2002 (254) ITR 377] wherein the High Court had held that once it is established that there is nexus between the expenditure and the purpose of business (which need not necessarily be the business of the assessee itself), the Revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the Board of Directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. It further held that no businessman can be compelled to maximize his profit and that the income tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own view point but that of a prudent businessman. ***Applying the aforesaid ratio to the facts of this case as already noted above, it is manifest that the advance to M/s. Hero Fibres Limited became imperative as a business expediency in view of the undertaking given to the financial institutions by the assessee to the effect that it would provide additional margin to M/s. Hero Fibres Limited to meet the working capital for meeting any cash loses.***
- Insofar as the loans to Directors are concerned, it could not be disputed by the Revenue that the assessee had a credit balance in the Bank account when the said advance of Rs. 34 lakhs was given. Remarkably, as observed by the CIT (Appeal) in his order, the company had reserve/surplus to the tune of almost 15 crores and, therefore, the assessee company could in any case, utilise those funds for giving advance to its Directors. On the basis of aforesaid discussion, the present appeal is allowed, thereby setting aside the order of the High Court and restoring that of the Income Tax Appellate Tribunal.

SUPREME COURT
M/S. MANGALORE GANESH BEEDI WORKS
AGREEMENT MADE- REVENUE APPROACH

- *"..In D. S. Bist & Sons v. CIT* [1984] 149 ITR 276 (Delhi) *it was held that the Act does not clothe the taxing authorities with any power or jurisdiction to re-write the terms of the agreement arrived at between the parties with each other at arm's length and with no allegation of any collusion between them. 'The commercial expediency of the contract is to be adjudged by the contracting parties as to its terms.'.."*

SUPREME COURT IN TAPARIA TOOLS CASE 372 ITR 605

- Held that there is no concept of differed revenue expenditure unless so specified in the Act

- **S. 36(1)(iii)/ 37(1): Normally revenue expenditure incurred in a particular year has to be allowed in that year and if the assessee claims that expenditure in that year, the Department cannot deny the same. Fact that assessee has deferred the expenditure in the books of account is irrelevant. However, if the assessee himself wants to spread the expenditure over a period of ensuing years, it can be allowed only if the principle of 'Matching Concept' is satisfied**

- It has been held repeatedly by this Court that entries in the books of account are not determinative or conclusive and the matter is to be examined on the touchstone of provisions contained in the Act [See – Kedarnath Jute Manufacturing Co. Ltd. v. Commissioner of Income Tax (Central), Calcutta [1972] 3 SCC 252; Tuticorin Alkali Chemicals & Fertilizers Ltd., Madras v. Commissioner of Income Tax, Madras [1997] 6 SCC 117; Sutlej Cotton Mills Ltd. v. Commissioner of Income Tax, Calcutta [1978] 4 SCC 358; and United Commercial Bank, Calcutta v. Commissioner of Income Tax, WB-III, Calcutta [1999] 8 SCC 338;

ALLEGED ILLEGAL EXPENSE

- MUNDIAL EXPORT IMPORT FINANCE (P) LTD Calcutta high court 02.02.2016.
- *The questions of law which arise for determination in the instant appeal are as follows:- (i) Whether the damages of Rs.6,67,266/- paid by the Appellant to the Calcutta Port Trust as per Clause 22 of the Lease Agreement dated Octobe 21, 1982 by and between the appellant and Calcutta Port Trust is an expenditure covered by the Explanation to Section 37(1) of the Income Tax Act, 1961? (ii) Whether in the facts and circumstances of the case the payment of Rs.6,67,266/- to the Calcutta Port Trust by the Appellant was an expenditure incurred wholly and exclusively for the purposes of the Appellant's business and therefore allowable as deduction under Section 37(1) of the Income Tax Act, 1961, in determining the Appellant's income for the assessment year 2001-02? (iii) Whether the expenditure of Rs.6,67,266/- incurred by the Appellant as and by way of payment of damages to the Calcutta Port Trust for contravention of contractual obligation by way of encroachment of land adjacent to the demised land, belonging to the Calcutta Port Trust, is an expenditure capital in nature and thus not an allowable expenditure under Section 37 (1) of the Income Tax Act, 1961? (iv) Whether in coming to the conclusion that the payment of Rs.6,67,266/- by the Appellant to the Calcutta Port Trust was an expenditure covered by the Explanation to Section 37 (1) of the Act and/ or that such expenditure was capital in nature and, therefore, on both counts was not an allowable deduction under Section 37(1) of the Income Tax Act, 1961, the Tribunal has misdirected itself in law, has acted by an outright refusal to consider relevant matters and has taken into consideration irrelevant materials and whether the said findings of the Tribunal are perverse?*

ALLEGED ILLEGAL EXPENSE

- In Jamna Auto Industries, Yamunanagar –Vs- The CIT Haryana, Rohtak reported in (2008) 299 ITR 92 a full bench of Punjab and Haryana High Court elaborately dealt with the question of whether damages paid for breach of contract can be allowed as expenditure under Section 37(1) of the Act. In the aforesaid case the assessee had entered into an agreement with a German Firm for supply of certain goods. The said contract did not fructify, as the assessee did not have the requisite import license for the material intended to be imported. On a dispute being referred to an arbitrator, the assessee had to pay Rs.50,000/- to the
- said German firm in terms of the arbitral award. It was this amount which he claimed as deduction. In CIT –Vs- S.A. Builders Pvt. Ltd. reported in (2008) 299 ITR 88, the assessee was a contractor executing various works. The assessee claimed a deduction on account of compensation paid to the contractee for delaying the execution of works. The issue was whether the compensation paid can be allowed as a deduction. It was held that the compensation paid by the assessee was on account of breach of contract which does not fall within the category of payment of penalty for breach of any law but would be a compensation for breach of contractual obligation, accordingly, will fall in the category of allowable deduction.

ALLEGED ILLEGAL EXPENSE

- **The above issue was also dealt with by the Supreme Court in the Swedeshi Cotton Mills Co. Ltd. –Vs- CIT reported in (1998) 233 ITR 199.** The issue before the Supreme Court was regarding deductibility of liability incurred by the assessee for delayed payment of employee's contribution under Section 14B of the Employee's Provident Fund Act, 1952 and the penalty levied on the assessee under the Central Sales Tax Act.
- *The Supreme Court followed its earlier judgement in Prakash Cotton Mills Pvt. Ltd. –Vs- CIT reported in (1993) 201 ITR 684 and held that wherever an amount has been paid by way of damages, the compensatory payment made by the assessee entitles him to claim deduction from the income earned by him and where an element of penal levy is concerned, any such payment made for contravention of law is inadmissible. The Supreme Court in Standard Batteries (supra) reiterated the view taken in Prakash Cotton Mills Pvt. Ltd. -Vs- CIT reported in (1993) 201 ITR 684*.

CALCUTTA HIGH COURT ON ILLEGAL EXPENSE FINAL VIEWS

- We have already indicated that the payment was made to compensate the loss suffered by CPT due to occupation of land in excess of what was demised to the assessee. Therefore, the payment did not partake the character of penalty. The payment could not partake the character of a capital expenditure because contention of the CPT was that the prayer for lease of the land unauthorisedly occupied could not be examined before payment of the compensation. Therefore, the payment was altogether compensatory for the benefit already received by the assessee by user of the land which had or could have nothing to do with a grant of lease in future. For the aforesaid reasons the question No. 2 is answered in the affirmative and in favour of the assessee. No separate answer to question No.1 is necessary. The question No.3 is answered in the negative and the question No. 4 is answered in the affirmative. The appeal is allowed.

B' BENCH, CHENNAI M/S HYUNDAI MOTOR INDIA LTD 7TH AUGUST, 2015

- As there is difference of opinion between the Members constituting the Bench with regard to one issue, following question is formulated and referred to the Hon'ble President for nominating Third Member: 1. "Whether, the expenditure incurred by the assessee by giving 100 cars to the Police Department of Tamil Nadu is an eligible expenditure under section 37 of the Income Tax Act or not? "
- When called upon to explain as to whether the management has taken any specific decision in the form of making it as one of the issues in the Board meeting or whether there is any communication between the top management and middle level management, learned counsel submitted that there is no such record available and in fact was not produced before the tax authorities. He also admitted that assessee has not even made any effort till date to draw attention of public by mentioning in their advertisements that cars manufactured by them are "best cars designed to protect the interest of public at large and used by police personnel". With regard to additional fittings for the specific use of the police personnel, no material was placed on record; the counsel merely contended that every car will have its logo 'Hyundai' and that itself will have advertisement value
- Having regard to the case law relied upon by both the parties and the ratios laid down therein, I am of the view that there is no commercial expediency in incurring this expenditure and therefore the view taken by the learned Judicial Member deserves to be upheld and I hold accordingly.

CIT VS. CHEMOSYN LTD (BOMBAY HIGH COURT)

- *(ii) The Tribunal has recorded the finding of fact that in view of the dispute between the two warring groups of shareholders the business of the assessee had suffered. After the settlement of the dispute there was a substantial increase in the sales. After settlement of the dispute new products were launched by the assessee-company. All this was evidence of the fact that the dispute between two groups of shareholders had affected the business of the company. The amount paid by the assessee for the purchase of its shares for subsequent cancellation was an expenditure incurred only to enable smooth running of the business. Thus, the expenditure was incurred for carrying on its business smoothly and was a deductible expenditure.*

M/S. AGGARWAL AND MODI ENTERPRISES (CINEMA PROJECT) CO. PVT. LTD

21ST JANUARY, 2016 (DELHI HIGH COURT)

- "Whether the Income Tax Appellate Tribunal was correct in law in reversing the order of the Commissioner of Income Tax (Appeals) and confirming the disallowance of the amount on account of liability of licence fee and on account of interest on arrears of licence fee payable to N.D.M.C. for running the business at Chanakya Cinema?
- *. The ITAT also appears to have drawn a distinction between a statutory liability and a contractual liability and opined that a deduction in respect of the contractual liability would be permissible "only when the disputes are settled." This is contrary to the legal position as explained in the above decisions of the Courts. Even where a challenge is laid to a liability arising under a contract, by a challenger initiating legal proceedings, such challenger can still for the purposes of its accounts and for the purposes of computation of its income tax liability claim the entire amount under challenge as an accrued liability as long as such amount is ascertainable. Corresponding adjustments would be made in the year in which the suit is finally decided or the disputes settled. That, however, would not preclude the Assessee from claiming it as an ascertained liability.*

SHREENATH MOTORS PVT.LTD BOMBAY HIGH COURT 3/7/2014

- In the facts of the present case, the authorities below have come to a categorical finding (i) that the expenditure incurred was not for the purpose of business of the Appellant-Assessee and was out of personal consideration and not out of any commercial consideration; (ii) that the Appellant-Assessee filed no evidence that it had framed any Rules or Regulations for incurring expenditure on the education of the son of the director or any other employee; (iii) that the Appellant-Assessee had not filed any details which would indicate that the said Mr Krishna KachKachalia was under any obligation to serve the Appellant-Assessee after the completion of management studies; (iv) that the Appellant-Assessee had paid education expenses of Mr Krishna Kachalia only because he happens to ::: be belonging to the family controlling the Appellant-Assessee; (v) that the expenditure incurred on the education of Mr Krishna Kachalia was not incurred for the purpose of business of the Appellant-Assessee and therefore could not be allowed as deduction in the hands of the Appellant. In view of these categorical findings of fact, we have no hesitation in holding that the deduction claimed by the Appellant-Assessee has been rightly disallowed by the authorities below and we find no infirmity in the impugned order passed by the ITAT.
- Sakal Papers Pvt.Ltd. v/s Commissioner of Income Tax, reported in (1978) 114 ITR 256 (Bom) distinguished

DELHI HIGH COURT IN KOSTUB LTD CASE

- : Held **ITA 10/2014**Pronounced on: 25.02.2014: *"Did the Tribunal fall into error of law in holding that the appellant's claim that the amount has been spent during the Assessment Year 2006-07, for the higher education of Sh. Dushyant Poddar, a son of its Director, was not liable as "business expenditure" under Section 37 of the Income Tax Act?"* Whilst there may be some grain of truth that there might be a tendency in business concerns to claim deductions under Section 37, and foist personal expenditure, such a tendency itself cannot result in an unspoken bias against claims for funding higher education abroad of the employees of the concern. As to whether the assessee would have similarly assisted another employee unrelated to its management is not a question which this Court has to consider. But that it has chosen to fund the higher education of one of its Director's sons in a field intimately connected with its business is a crucial factor that the Court cannot ignore. **It would be unwise for the Court to require all assessees and business concerns to frame a policy with respect to how educational funding of its employees generally and a class thereof, i.e. children of its management or Directors would be done. Nor would it be wise to universalize or rationalize that in the absence of such a policy, funding of employees of one class – unrelated to the management – would qualify for deduction under Section 37(1).** *We do not see any such intent in the statute which prescribes that only expenditure strictly for business can be considered for deduction*. Necessarily, the decision to deduct is to be case-dependent. **In view of the above discussion, having regard to the circumstances of the case, this Court is of the opinion that the expenditure claimed by the assessee to fund the higher education of its employee to the tune of `23,16,942/- had an intimate and direct connection with its business, i.e. dealing in security and investments.** It was, therefore, appropriately deductible under Section 37(1). The AO is thus directed to grant the deduction claimed. The appeal is allowed in the above terms. No costs.)

SECTION 40(A)(I) & (IA) TDS RELATED DISALLOWANCES

- Theory of doubtful penalization – Delhi high court JDS Apparels (& presumption of payment of tax by payee)
- Direct cost angle whether arguable? (notwithstanding section 30 to 38…)
- Short deduction not covered u/s 40(a)(ia) (Calcutta HC in S.K.Tekriwal ass fav. 361 ITR 432 & Kerala H.C. against)
- Paid vs payable P&H high court PMS Diesels 374 ITR rev fav (plus Gujarat, Calcutta, Karnataka & Kerala: rev fav.) & only ass fav decision Victor shipping Allahabad high court
- Narrow definition of royalty u/s 40(a)(i) – Mumbai ITAT SKOL Breweries case
- 30% disallowance to resident payee, immunity where resident payee includes in income whether can be extended to non resident payee also on basis of *non discrimination* clause (Delhi ITAT Mistubishi case & Delhi high cout in Herbalife case)

TDS PROVISIONS- LATEST VIEWS

Case Law	Proposition Held
Supreme court in Kotak Securities case	Fees for technical services requires human element and specialized element in services
VJM Media (P) Ltd 13/04/2016 Mumbai ITAT	Sharing of incremental advertisement revenue shall not fall within the provisions of section 194C.
Red Chillies Entertainment Pvt. Ltd. 31.05.2016 **"D" BENCH, MUM BAI**	...we are of the view that since the payment made by the assessee is in kind, the provisions of section 194J are not applicable ....(Gift to actors etc for movie Billu barber)
M/s. Neo Sports Broadcast Pvt. Ltd. Mumbai ITAT (01.04.2016) & M/s. Larsen & Toubro Ltd 29/04/2016 Mumbai ITAT & ITAT in Kotak Securities Ltd. vs. DCIT, 147 TTJ 443(Mum)	Bank guarantee commission not falls u/s 194A and sec. 194H

TDS PROVISIONS- LATEST VIEWS

- Delhi high court in Msons case Held Factoring & Discounting charges do not constitute interest u/s 2(28a) of the Act
- *Kolkatta ITAT in M/s Gourishankar Bihani v. DCIT in **ITA No.1127/Kol/2011 &*** Shri Ran Vi jay Singh **ITA No.2038-2039/Kol /2013** 27-05-2016: No tds payee exempt ; also refer M/s. Belvedere Estates Tenants Association kol ITAT case;
- Executive Officer, Jalandhar Improvement Trust Amritsar ITAT June 10, 2015 :"payments are out of legal obligations not amounts to works contract u/s 194C; (also refer Kol ITAT in West Bengal State Electricity Distribution Co. Ltd. 04.05.2016: licence fee does not fall within the purview of Section 194C);
- Repairs of medical equipment TDS u/s 194C not u/s 194J Mumbai ITAT in M/s DDRC SRL Diagnostic P Ltd.,(23.9.2015) (Asian Heart Institute & Research Centre Pvt. Ltd. 30/09/2015)
- Kol ITAT in case of Shri Sakhi Chand Buchasia 3.2.2016: Even otherwise, I am of the view that these charges are routine testing charges for testing the size of the stone ballasts, which cannot be said to be of technical nature. (Mumbai ITAT in Go Go International 28.08.2014 same views)
- 194H:CIT Vs. Intervert India Pvt. Ltd., 364 ITR 238 (Bom.) (ITA No.
- 1616 of 2011, dated 01/04/14.).

CABLE CORPORATION OF INDIA
18/11/2015 MUMBAI ITAT

- *We have considered rival contentions and found that the compensation/ damages has been paid by the assessee in terms of consent terms filed before the Hon'ble Bombay High Court. Pursuant thereto, the debt became a judgment debt.* ***It is an accepted principle of law that there could be no deduction of tax at source from a judgment debt for which reliance can be placed on All India Reporter Ltd. v/s Ramchandra D. Datar, 41 ITR 446 (SC), Islamic Investment Co. v/s UOI 265 ITR 264.*** *Further, There is also no question of treating the said amount as penalty under the Negotiable Instruments Act as no penalty could be prescribed under the said Act.*

PUNJAB & HARYANA HIGH COUR T GURDAS GARG VS. CIT IN ITA NO.413 OF 2014, DATED 16.7.2015

- *It is important to note some of the findings of fact by the CIT (Appeals). The identity of the payees i.e. the vendors in respect of the lands purchased by the appellant, was established. The sale deeds were produced. The genuineness thereof was accepted. The amount paid in respect of each of these agreements was certified by the Stamp Registration Authority. The CIT (Appeals) held the transactions to be genuine. Accordingly, the CIT held that the bar against the grant of deductions under Section 40A(3) of the Act was not attracted. 5. It is important to note that the Tribunal did not upset these findings including as to the genuineness and the correctness of the transactions. It is also important to note that the Tribunal noted the contention on behalf of the appellant that there was a boom in the real estate market; that it was necessary, therefore, to conclude the transactions at the earliest and not to postpone them; that the appellant did not know the vendors and obviously therefore, insisted for payment in cash and that as a result thereof, payments had to be made immediately to settle the deals. The Tribunal did not doubt this case. The Tribunal, however, held that the claim for deduction was not sustainable in view of Section 40A(3) as the payments which were over `20,000/- were made in cash. The Tribunal, therefore, disallowed the same only on a construction of Section 40A(3). The Tribunal restricted the ambit of the proviso to the circumstances mentioned in Rule 6DD of the Income Tax Rules, 1962.*

PUNJAB & HARYANA HIGH COUR T GURDAS GARG VS. CIT IN ITA NO.413 OF 2014, DATED 16.7.2015

- *At the cost of repetition, the Tribunal h as not disbelieved the transactions or the genuineness thereof. Nor has it disbelieved the fact of payments having been made. More important, the reasons furnished by the appellant for having made the cash payments, which we have already adverted to, have not been disbelieved. In our view, assuming these reasons to be correct, they clearly make out a case of business expedienc In the circumstances, the order of the Tribunal in this regard is set aside. The payments cannot be disallowed under Section 40A(3) of the Act.*
- **Dreamland Colonizers Pvt. Ltd- Chandigarh ITAT (15.02.2016**)- expenses incurred in cash were genuine which were paid to the seller for purchase of land and there were practical expediency because of which the payments have to be made in cash. (Gurdas garg supra applied);
- **Dhuri Wine, Chandigarh ITAT 09.10.2015** expenses incurred in cash were genuine Which were paid to distilleries through Excise Department for purchase of liquor and there were practical expediency because of which the payments have to be made in cash
- **Amritsar ITAT Rakesh Kumar , Muktsar vs Assessee on 9 March, 2016 :** In the present case, the genuineness of payment has not been doubted as Assessing Officer himself has held that sale deeds of properties were registered with the Revenue Department of Govt. Therefore, the case of the assessee is fully covered by the above decision of Hon'ble Punjab and Haryana High Court

HON'BLE GUJARAT HIGH COURT IN THE CASE OF ANUPAM TELE SERVICES VS. ITO 2014 366 ITR 122 (GUJ)

- *"In Attar Singh Gurumukh Singh vs. ITO (1991) 191 ITR 667 (SC), the Supreme Court observed that section 40A(3) of the Income-tax Act, 1961, must not be read in isolation or to the exclusion of rule 6DD of the Income-tax Rules, 1962. The Section must be read along with the rule, and if read together, it will be clear that the provisions are not intended to restrict the business activities. There is no restriction on the assessee in his trading activities. Section 40A(3) only empowers the Assessing Officer to disallow the deduction claimed as expenditure in respect of which payment is not made by crossed cheque or crossed bank draft. The payment by crossed cheque or crossed bank draft is insisted on to enable the assessing authority to ascertain whether the payment was genuine or whether it was out of income from undisclosed sources. The terms ofsection 40A(3) are not absolute. Considerations of business expediency and other relevant factors are not excluded. Genuine and bona fide transactions are not taken out of the sweep of the section. "*

SECTION 40A(3)

- *In Commissioner of Income Tax v. Smt. Shelly Passi , the Panjab and Haryana High Court took the view that the cash deposited to the bank account of a recipient does not fall within the purview of section 40A(3)* 350 ITR 227
- T&AP high court in case of Grandhi Venkata Ramana, We have already observed that the prohibition contained in Section 40A(3) of the Act is not absolute and dozens of exceptions are carved out by the rule making authority. At least in the exceptions contained in the rule, the payment by the assessee, as well as receipt by the payee are in cash. *In the instant case, the payment no doubt was in cash but it was deposited into the bank account of the recipient. It is not a case where the cash was paid by the assessee and was received by the recipient. An instance of cash being credited to the account of the recipient stands on a higher footing, compared to the different heads, under Rule 6DD of the Rules when payment of cash, even to the banks and other statutory agencies, is recognized, there is no reason why the deposit of cash into the bank account of a recipient cannot be regarded as qualifying for allowances.* Further, the objective under the Act is to ensure that the income of an assessee is levied tax and every step is taken to ensure that no part of the income escapes the taxation. The prohibition contained under Section 40A(3) of the Act is more a matter, which genuinely falls in the realm of the Banking Regulation Act. A provision of that nature cannot be understood just in grammatical manner. fSection 40A(3) of th e Act. I.T.T.A.No.244 of 2003 28-10-2014

PRABI R KUMAR MULLICK KOL ITAT ON SEC. 40A(3) ORDER DATED 01-06-2016

- As there are two different orders on the grounds of appeal favouring and against the assessee. The Hon'ble Apex Court directs to take the view favourable to the assessee. Therefore considering the facts of the case in totality and object of the section 40A(3) of the Act, we are of the considered view that this case does not require the reference to the Special Bench. Hence in our considered view this case does not require to be referred to the Special Bench

PRABI R KUMAR MULLICK KOL ITAT ON SEC. 40A(3) ORDER DATED 01-06-2016 *A.Y. 2008-09*

- *11.3 It is pertinent to note that the primary object of enacting section 40A(3) were two folds, firstly, putting a check on trading transactions with a mind to evade the liability to tax on income earned out of such transaction and, secondly, to inculcate the banking habits amongst the business community. Apparently, this provision was directly related to curb the evasion of tax and inculcating the banking habits. Therefore, the consequence, which were to be fallen on account of non-observation of Section 40A(3) must have nexus to the failure of such object. Therefore, the genuineness of the transactions being from vice of any device of evasion of tax is relevant consideration. With regard to the purpose of bringing the provisions of section there is no doubt about the identity of the party. The ld. AR has directly deposited the cash in the account of the companies and has produced the sales bills of the company. The AO has also verified the transactions from the companies by issuing notice under Section 133(6) of the Act. So in the instant case, there is no evasion of tax by claiming the bogus expenditure in cash.*

SECTION 41(1) – RECENT VIEWS

- Karnataka high court in CIT vs Alvares & Thomas in ITA 658/2015 (24/03/2016)
- The sine qua non of section 41(1) is i) remission/cessation of trading liability ii) Some benefit is taken by assessee in respect of such trading liability. *Even if the party could not be traced and could not be verified, section 41(1) cannot be invoked. Cessation has to as per law.* Delhi high court decision in Vardhman matter relied & followed

V. S. DEMPO & COMPANY LTD BOMBAY HIGH COURT GOA BENCH 9TH APRIL, 2015 TAX APPEAL NO. 62 OF 2006

- The principal amount of loan having been taken for purchase of capital amount was on capital account and therefore no occasion to apply Section 41 (1) of the Act in respect of that could arise. The issue in fact stands concluded in favour of the respondent by the decision of this Court in *Mahindra and Mahindra Ltd* (2003) 261 ITR 501*(supra) and M/s. Xylon Holding (supra) in* the context of the submission made by the revenue before us.

M/S. CABLE CORPORATION OF INDIA LTD. MUMBAI BENCH "C 12.11.2014 SECTION 43B

- *. Section 43B per se does not provide the manner in which the payment of interest is to be made, it only provides that the deduction is allowable on the sum payable mention in clauses (a) to (f), if such sum is actually paid by the assessee. The said section creates fiction that certain liabilities, irrespective of the method of accounting followed by the assessee, would be allowed as deduction only on actual payment. ...There is no prohibition or embargo that the sum actually paid will not cover payments through allotment of shares. The shares are tradable commodity and has a value which can be sold in the market as per the value of the share on the date of sale. It is easily convertible into money as and when required. Once there is no such prohibition u/s 43B for discharging the payment of interest liability and claiming of deduction thereof, by converting the payment through allotment of shares, then how the assessing officer sans any legal provision or any judicial authority could have entertained " reason to be believe" that such a deduction is not allowable.*

BOGUS PURCHASES ISSUE – LATEST VIEWS

- Adamji & Company Mumbai ITAT Date of Order – 27.05.2016
- *CIT v/s Nikunj Exim Enterprises Pvt. Ltd., 372 ITR 619*
- Held by ITAT in above order: ...*Therefore, unless, the assessee had made purchases he could not have effected corresponding sales. Therefore, before treating the purchases made by the assessee as bogus, the Assessing Officer should have conducted necessary enquiry keeping in view the aforesaid fact. Without conducting any enquiry, the Assessing Officer solely relying upon the investigation made by the Sales Tax Department cannot make the addition, that too, on the basis of untested material. The decisions relied upon by the learned Authorised Representative referred to above fully support this view. Therefore, in the aforesaid facts and circumstances, we are of the view, the addition made on account of estimation of profit by treating the purchases as bogus has no legs to stand..... (7* **17.03.2016- Mumbai ITAT in** Ashok Talreja (HUF)Prop. S.P. Enterprises,) (& Shri Mohammad Taufiq Navlakhiya - 12.02.2016)
- Also refer Bombay high court in case of Eagle Impex **30th SEPTEMBER, 2015 (The main grievance of the Respondent with regard to the impugned order is that the Respondent had failed to produce the parties from whom the purchases were made. Mr. Pinto, learned Counsel appearing for the Appellant was not able to support the aforesaid submissions with the aid of any case law.)**
- *Gujarat high court in VARSHABEN SANATBHAI PATEL **13/10/2015 – REOPENING QUASHED on issue of bogus purchases***
- Concealment penalty : Delhi high court FORTUNE TECHNOCOMPS (P) LIMITED (**13.05.2016**) ass fav. (refer *116 ITR 416 Cal HC)* & Gujarat high court M/S.RUCHI Developers **01/02/2016 (ass fav)**

BOMBAY HIGH COURT IN CASE OF MONICA INDIA :16TH APRIL, 2016

- *....The contention of Mr. Chhotrary that the seller had not shown the aforesaid consideration of Rs.1.78 Crores as his receipt of sale of the goods and, therefore, the buyer of the goods i.e. espondentAssessee cannot claim the same as a deduction is not sustainable. The remedy, if any of the Revenue to bring to tax the income of Rs.1.78 Crores in the hands of the seller of the goods. ....In any case, the buyer of the goods cannot be made liable to tax on the consideration paid by him to the seller of goods only because the seller of goods has failed to take it into consideration as a part of his income while discharging its obligation to pay tax under the Act. Thus, there is no merit in the first submission made on behalf of the Revenue.....*

PRIOR PERIOD ANGLE

- Saurashtra Cements and Chemicals Industries 213 ITR 523 where Hon'ble Gujarat High Court held that the expenses pertaining to the transactions of earlier years do not become liability payable in earlier year unless it can be said that liability was determined and crystallized in the year on the basis of maintaining account of mercantile basis.

GUJARAT HIGH COURT LATEST VIEWS ON REVENUE NEUTRALITY BETWEEN PAYER & PAYEE

- TAX APPEAL NO. 209 of 2015 /PWS ENGINEERS LIMITED/ 06/06/2016
- *"(ii) Whether on the facts and in the circumstances of the case, the Tribunal was right in law and in overlooking the fact that the entire exercise was revenue neutral in nature because the company as well as the Directors were taxable at the same rate and that the Directors had paid off the taxes and taking into consideration it ought not to have confirmed any part of the disallowance made by the authorities ?"*
- **Held**

GUJARAT HIGH COURT LATEST VIEWS ON REVENUE NEUTRALITY

- .....In fact, the assessee had demonstrated before CIT(Appeals) that the tax liability of the company on such disputed remuneration amount was exactly the same as the tax the four Directors had paid to the Revenue. To these factual aspects, even the Revenue has, at no stage raised any dispute. We may therefore, proceed on the basis that the element of excessive remuneration represents that income of the company which was eventually taxed in the hands of the Directors at the same rate at which; had it not been so distributed; would have been taxed in the hands of the company. In that view of the matter, the question of revenue neutrality would immediately arise. A certain income has already been taxed in the hands of the Directors. Permitting the Revenue to tax the same income again at the same rate in the hands of the principal payer would amount to double taxation. **Only on this count, we answer question in favour of the appellant-assessee and against Revenue, allow the Appeal and set aside the order of the Tribunal.** The Tax Appeal is disposed of accordingly.

FIDUCIARY SHARES & STOCK P. LTD- EXPLANATION TO SEC. 73- DEEMED SPECULATIVE TRANSACTION

- 13.05.2016 order
- *Held In our humble view, drawing support from the judicial pronouncements cited at paras 5.6.3 to 5.6.9 of this order (supra) we are of the considered opinion and hold that the amendment inserted in Explanation to section 73 of the Act by Finance (No. 2) Act, 2014 w.e.f. 01.04.2015 is clarificatory in nature and would therefore operate retrospectively from 01.04.1977 from which date the Explanation to section 73 was placed on the statute since this amendment to section 73 of the Act* ***'.... or a company the principal business of which is the business of trading in shares .....'*** *brings in the assessee whose principal business is trading of shares. Therefore, the loss incurred in share trading business by such companies, i.e. like the assessee will not be treated as speculation business loss but normal business loss, and hence the same loss can be adjusted against other business income or income from any other sources of the year under consideration...*

SECTION 14A

- **Recent notification dated 2/6/2016 (disallowance cant exceed expense claimed)**
- Satisfaction must Delhi high court Taikisha Case 370 ITR 338 (not recorded by AO cannot be recorded by CIT-A Delhi ITAT in case of Azimuth Investments Ltd.)
- Exempt income must _ Delhi high court Holcim & Cheminvest cases (disallowance cannt exceed dividend income)
- Bombay high court in HDFC case 366 ITR 505

DELHI HIGH COURT IN BHARTI OVERSEAS CASE INTEREST ELEMENT SEC. 14A DISALLOWANCE

- *The object behind Section 14A (1) is to disallow only such expense which is relatable to tax exempt income and not expenditure in relation to any taxable income. This object behind Section 14A has to be kept in view while examining Rule 8D (2) (ii). In any event a rule can neither go beyond or restrict the scope of the statutory provision to which it relates. Rule 8D (2) states that the expenditure in relation to income which is exempt shall be the aggregate of (i) the expenditure attributable to tax exempt income, (ii) and where there is common expenditure which cannot be attributed to either tax exempt income or taxable income then a sum arrived at by applying the formula set out thereunder. What the formula does is basically to "allocate" some part of the common expenditure for disallowance by the proportion that average value of the investment from which the tax exempt income is earned bears to the average of the total assets. It acknowledges that funds are fungible and therefore it would otherwise be difficult to allocate the sum constituting borrowed funds used for making tax-free investments. Given that Rule 8 D (2) (ii) is concerned with only 'common interest expenditure' i.e. expenditure which cannot be attributable to earning either tax exempt income or taxable income, it is indeed incongruous that variable A in the formula will not also exclude interest relatable to taxable income.*

SECTION 40(B) REMUNERATION

- Whatever may be the nature of transaction, whether it is recorded in the books of account or not recorded in the books of account, the source of generating additional income for investing in the stocks of the assessee is only the business transactions. Other than the business transactions, the assessee has no other source of income. Since the assessee has offered additional income of `30 lakhs when the discrepancies found in the stocks, the same was classified as unexplained income under Section 69 of the Act. This does not mean that the income was not generated from the business. This Tribunal is of the considered opinion that the income was generated in the business of the assessee-firm, therefore, it has to be necessarily considered for computing the remuneration of the partners under Section 40(b) of the Act

- Chennai ITAT in case of M/s Roshan 07.04.2016 **ITA No.393/Mds/2013**

SUPREME COURT
DALMIA PROMOTERS & DEVELS.(P) LTD
SEPTEMBER 16, 2015 CONSISTENCY

- *Shri Jaideep Gupta, learned senior counsel appearing on behalf of the Revenue has argued before us that in Tuticorin Alkali Chemicals & Fertilizers Ltd. vs. Commissioner of Income-tax [227 ITR 172], this Court has held that in such a situation such income would have to be treated as interest from other source and not as business income. This is resisted by the learned counsel appearing on behalf of the assessee.*

  We are not going into this issue inasmuch as this appeal can be disposed of on the ground that consistency does demand that there being no change in circumstances, the income for the year 1993-94 would also have to be treated business income as for the previous three years.

LOSS SET OFF APPROACH

- Hon'ble Supreme Court in the case of CIT v. Manmohan Das (1966) 59 ITR 699 (SC) wherein has held whether the loss in any year may be carried forward to the following year and set off against the profits and gains of the subsequent year under section 24(2) has to be determined by the Income-tax Officer who deals with the assessment of the subsequent year. A decision recorded b the Income-tax Officer who computes the loss in the previous year that the loss cannot be set off against the income of the subsequent year is not binding on the assessee.

KEY TAKE AWAYS

- Business head aims to tax *real* business profits & not hypothetical/artificial and theoretical income;
- Head of income must be carefully decided;
- Revenue needs to establish an receipt is taxable income;
- Assessee needs to establish an expense is incurred and *otherwise* allowable under the law;
- Revenue neutrality is important is income recognition/accrual and expense claim;
- For disallowing an expense, it must be incurred and so claimed by assessee;
- Book entries are not conclusive to taxation;
- Sec. 115JB cannot include capital receipts;
- Consistency is hallmark of taxation;
- Business Agreements cannot be re-written by revenue
- Valuation of stock by itself cannot result in income taxable;

Thank You

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