Tax News

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INCOME TAX

Reminder for Feb-2013

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INCOME TAX

Important Circulars/ Notifications

- The Director General of Income Tax hereby extends the time limit for filing ITR-V forms relating to Income Tax Returns filed electronically (without digital signature Certificate) for AY2010-11(filed during FY2011-12) and for ITRs of AY 2011-12(filed on or after 1.4.2011) till 28th Feb, 2013. In respect of returns filed for AY 2012-13 for which ITR-V forms are yet to be received at CPC and time of 120 days has also elapsed, time limit for filing of ITR-V is extended upto 31st March 2013, or 120 days from the date of uploading of the electronic return data, whichever is later. Tis direction is issued to mitigate the hardship and grievance of the tax payers who have been prevented by reasonable causes to file the ITR-V in time. *Notification No. 01/2013 under CPR Scheme 2011, dated Jan 7, 2013.*
- The Central Board of Direct Taxes has issued a notification describing the Scheme for Centralised Processing of Statements of Tax Deducted at Source, 2013. The notification covers the following points:
  - Definitions
  - Centralised Processing Cell
  - Furnishing of correction statement of tax deducted at source
  - Processing of statements
  - Rectification of mistakes
  - Adjustment against outstanding tax demand
  - Appeal
  - No personal appearance at the Cell
  - Service of notice or communication

The details are in *Notification No. 03 /2013 [F.No. 142/39/2012-SO (TPL)] dated Jan 15, 2013.*

In this Notification, issues relating to taxation benefits on export of computer software, u/s 10A & 10B, have been examined and clarified. The issues covered are:

- Whether 'on site' development of computer software qualifies as an export activity for tax benefits.
- Whether receipts from deputation of technical manpower are eligible for deduction.
- Whether it is necessary to have separate master service agreement for each work contract.
- Whether R&D activities would be covered under 'computer software'.
- Whether tax benefits would continue to remain available in case of a slump-sale.
- Whether it is necessary to maintain separate books of account for units claiming tax benefits.

- Whether tax benefits can be enjoyed by an eligible SEZ unit consequent to its transfer to another SEZ.
- Whether new units set up in the same location would amount to expansion.
- Details are in Circular No. 01/2013 dated Jan 17, 2013.

SC / HC Judgments

Interest earned by a mutual association from deposits placed with member banks: The assessee, a mutual association, claimed that the interest earned by it on fixed deposits kept with the bank (which was a corporate member) was not taxable on the basis of mutuality. The AO rejected the claim though the CIT(A) and Tribunal upheld the claim. The High Court reversed the Tribunal and upheld the stand of the AO. On appeal by the assessee, the Supreme Court held:

- For a receipt to be exempt on the principles of Mutuality, three conditions have to be satisfied. First, there must be a complete identity between the contributors and participators. Second, the actions of the participators and contributors must be in furtherance of the mandate of the association. Third, there must be no scope of profiteering by the contributors from a fund made by them which could only be expended or returned to themselves.

- In this case, though the interest was earned from banks which were corporate members of the club, it was not exempt on the ground of mutuality because (i) the arrangement lacks a complete identity between the contributors and participators. With the funds of the club, member banks engaged in commercial operations with third parties outside of the mutuality, rupturing the 'privity of mutuality', and consequently, violating the one to one identity between the contributors and participators, (ii) the surplus funds were not used in furtherance of the object of the club but were taken out of mutuality when the member banks placed the same at the disposal of third parties, thus, initiating an independent contract between the bank and the clients of the bank, a third party, not privy to the mutuality & (iii) The Banks generated revenue by paying a lower rate of interest to the assessee-club and loaning the funds to third parties. The interest accrued on the surplus deposited by the club like in the case of any other deposit made by an account holder with the bank.

- A façade of a club cannot be constructed over commercial transactions to avoid liability to tax. Such setups cannot be permitted to claim double benefit of mutuality. *M/s Bangalore Club vs. CIT (Supreme Court)***.**

Despite TDS & Advance-tax, income is "undisclosed" if ROI not filed by due date: In this case the Supreme Court held that:

- Sec. 158B(b) defines the expression "undisclosed income" to mean that income "which has not been or would not have been disclosed for the purposes of this Act".

- The only way of disclosing income on the part of an assessee is through filing of a return and therefore an "undisclosed income" signifies income not stated in the return filed. It cannot be said that payment of Advance Tax by an assessee per se is tantamount to disclosure of total income.
- There can be no generic rule as to the significance of payment of Advance Tax in construing intention of disclosure of income. This depends on the time at which the search is conducted in relation to the due date for filing return. If the search is conducted after the expiry of the due date for filing return, payment of Advance Tax is irrelevant in construing the intention of the assessee to disclose income because it is a case where income has clearly not been disclosed. On facts, as the assessee had not filed the ROI by the date of search and the due date had lapsed, the income found was "undisclosed" even though advance-tax thereon had been paid.

- Similarly, as TDS is also computed on the estimated income of an assessee for the relevant FY, it does not amount to disclosure of income, nor does it indicate the intention to disclose income if the ROI is not filed. *ACIT vs. M/s A. R. Enterprises (Supreme Court)*

Depreciation on Leased vehicles: The assessee, a NBFC, bought vehicles and leased it out to its customers. The vehicles were registered in the names of the customers. The AO held that as the vehicles were registered in the names of the customers and were used by them, the assessee was not eligible for depreciation u/s 32 as it was not the "owner" of the vehicles nor had it "used" the vehicles for purposes of business. The CIT(A) & Tribunal allowed the assessee's claim. However, the High Court reversed the Tribunal on the ground that the assessee was only a "financier" and not the "owner" of the vehicles and so was not eligible to claim depreciation. On appeal by the assessee, the Supreme Court held:

- Sec. 32 requires that the asset must be "owned, wholly or partly, by the assessee and used for the purposes of the business". The Department's argument that the assessee is not the "owner" of the vehicles is not acceptable because the lease agreement specifically provided that the assessee was the exclusive owner of the vehicle at all points of time and that it was empowered to repossess the vehicle (and not merely recover money) if the lessee committed a default. At the conclusion of the lease period, the lessee was obliged to return the vehicle to the assessee. Also, the assessee had the right of inspection of the vehicle at all times. As the assessee had a right to retain the legal title of the vehicle, it would be the owner of the vehicle in the eyes of law.
- The fact that at the end of the lease period, the ownership of the vehicle is transferred to the lessee at a nominal value not exceeding 1% of the original cost of the vehicle

does not make a difference. Also the fact that the Motor Vehicles Act deems the lessee to be the "owner" has no relevance.

- The Department's argument that the assessee had not "used" the vehicles is also not acceptable because the vehicle was "used" by the assessee in its business of leasing. Once it is held that leasing out of the vehicles is one mode of doing business by the assessee and the income derived from leasing out is treated as business income it would be contradictory, in terms, to say that the vehicles are not used wholly for the purpose of the assessee's business. *I. C. D. S. Ltd vs. CIT (Supreme Court)***.**

Gains on shares held in investment portfolio not assessable as business profits: The assessee maintained separate portfolios for shares in the trading account and for those in the investment account. This was accepted by the department in the earlier years. In AY 2007-08, the assessee sold all the shares in the investment portfolio and offered the gains to tax as long-term and short-term capital gains. The AO held that as the volume (Rs. 52 crores) and frequency of transactions was large, the LTCG & STCG were assessable to tax as business profits. The CIT(A) and Tribunal reversed the AO. On appeal by the department, the High Court held:

- The intent and purport of Circular No. 4 of 2007 dated 15.06.2007 is to demonstrate that a tax payer could have two portfolios, namely, an investment portfolio and a trading portfolio. In other words, the assessee could own shares for the purposes of investment and/or for the purposes of trading. In the former case whenever the shares are sold and gains are made the gains would be capital gains and not profits of any business venture. In the latter case any gains would amount to profits in business.

- On facts, the finding of the CIT(A) & Tribunal that the short term capital gains and long term capital gains were out of the investment account and were not related to the trading account does not call for any interference. *CIT vs. Avinash Jain (Delhi High Court)***.**

Payment by post-dated cheque relates back to date of handing over of cheque: In the year ended 31.3.2002, the assessee, a charitable trust eligible for exemption u/s 11, received a post-dated cheque dated 22.4.2002 from Apollo Tyres Ltd for which it issued a receipt. The AO held that the post-dated cheque had been accepted by the assessee to do undue favour to Apollo Tyres, whose directors were trustees of the assessee, and that there was a violation of sec 13(2)(d)(h), and that sec 11 exemption had to be denied. This was reversed by the Tribunal and the High Court on the ground that as the post dated cheque was given before 31.3.2002 and was duly honoured in April, 2002 when it was presented before the bank, the date of payment of the cheque should be treated as the date on which the cheque was received by the assessee. On appeal by the department, the Supreme Court held:

- Though the assessee trust issued a receipt in March 2002 when it received the cheque dated 22.4.2002, it was clearly stated in its record that the amount of donation was receivable in future and it was shown as donation receivable in the balance sheet as on 31.3.2002. Also Apollo Tyres Ltd did not avail any advantage of the said donation during the FY 2001-2002.

- When a post-dated cheque is issued, it will have to be presumed that the amount was paid on the date on which the cheque was given to the assessee and, therefore, it cannot be said that any undue favour was done by the assessee to Apollo Tyres Ltd. *CIT vs. Raunaq Education Foundation (Supreme Court)*.

ITAT Judgments

Transfer Pricing: L.G. Electronics Inc, a Korean company, set up a wholly owned subsidiary in India (the assessee) to which it provided technical assistance. The assessee agreed to pay royalty at the rate of 1% as consideration for the use of technical know-how etc. The Korean company also permitted the assessee to use its brand name and trade marks for products manufactured in India on a royalty-free basis. The AO, TPO & DRP held that as the Advertising, Marketing and Promotion ("AMP expenses") expenses incurred by the assessee were 3.85% of its sales and such percentage was higher than the expenses incurred by comparable companies (Videocon & Whirlpool), the assessee was promoting the LG brand owned by its foreign AE and hence should have been adequately compensated by the foreign AE. Applying the Bright Line Test, it was held that the expenses up to 1.39% of the sales should be considered as having been incurred for the assessee‘s own business and the remaining part on brand promotion of the foreign AE. The excess, after adding a markup of 13%, was computed at Rs. 182 crores.

On appeal by the assessee, the ITAT held that:

- The assessee's contention that in the absence of any mutual agreement between the assessee and its foreign AE, there is no "transaction" is not acceptable in view of the definition of that term in s. 92F(v) which includes an "arrangement or understanding". As long as there exists some sort of understanding between two AEs on a particular point, the same shall have to be considered as a "transaction", whether or not it is in written form.
- However, the department's contention that the mere fact that the assessee spent proportionately higher amount on advertisement in comparison with other entities shows an understanding is also not acceptable. On facts, as it was seen that the assessee not only promoted its name and products through advertisements, but also the foreign brand simultaneously, and the fact that the assessee‘s AMP expenses were proportionately much higher than those incurred by other comparable cases, lent due

credence to the inference of the transaction between the assessee and the foreign AE for creating marketing intangible on behalf of the latter.

- The assessee's contention that a distinction should be made between the "economic ownership" of a brand and its "legal ownership" and that AMP expenses towards the "economic ownership" of the brand, which are routine in nature, cannot be allocated as being for the benefit of the brand owner is not acceptable as it will lead to incongruous results. While the concept of economic ownership of a brand is relevant in a commercial sense, it is not recognized for the purposes of the Act.
- The assessee's argument that there is no "international transaction" is not acceptable because the definition of that term in s. 92B(1) is inclusive. Under clause (i) of the Explanation to s. 92B, a transaction of brand building is in the nature of "provision of service" by the assessee to the AE. Clause (ii) of the Explanation defines "intangible property" to include "marketing related intangible assets, such as, trademarks, trade names, brand names, logos". Consequently, brand building is a "provision of service". The fact that no consideration is paid by the foreign AE is irrelevant.
- While a provision from a foreign legislation cannot be imported into the Indian legislation, there is an inherent fallacy in the assessee's argument that the bright line test cannot be adopted to determine the ALP of the international transaction as it is not one of the recognized methods u/s 92C. The bright line test is a way of finding out the cost/value of the international transaction, which is the first variable under the TP provisions and not the second variable, being the ALP of the international transaction. Bright line is a line drawn within the overall amount of AMP expense. The amount on one side of the bright line is the amount of AMP expense incurred for normal business of the assessee and the remaining amount on the other side is the cost/value of the international transaction representing the amount of AMP expense incurred for and on behalf of the foreign AE towards creating or maintaining its marketing intangible. If the assessee fails to give any basis for drawing this line by not supplying the cost/value of the international transaction, and further by not showing any other more cogent way of determining the cost/value of such international transaction, then the onus comes upon the TPO to find out the cost/value of such international transaction in some rational manner. On facts, the cost/value of the international transaction was determined at Rs. 161 crore while its ALP (after the 13% markup) was Rs. 182 crore. The assessee was not entitled to claim a deduction for Rs. 161 crore and it was liable to be taxed on the markup of Rs. 21 crore.
- The assessee's contention that once the entire AMP expense is found to be deductible u/s 37(1), then, no part of it can be attributed to the brand building for the foreign AE notwithstanding the fact that the foreign AE also got benefited out of such expense is not acceptable because the whole purpose of transfer pricing is to provide a

statutory framework which can lead to computation of reasonable, fair and equitable profits and tax in India in the case of multinational enterprises. The TP provisions prevail over the general provisions. The exercise of separating the amount spent by the assessee in relation to international transaction of building brand for its foreign AE for separately processing as per s. 92 cannot be considered as a case of disallowance of AMP expenses u/s 37(1)/ 40A(2).

- In principle, it is necessary that properly comparable cases should be chosen before making comparison of the AMP expenses incurred by them. However, the argument that only such comparable cases should be chosen as are using the foreign brand is not acceptable. The correct way to make a meaningful comparison is to choose comparable domestic cases not using any foreign brand. Also, several factors have to be considered for determining the cost/value of the international transaction of brand/logo promotion through AMP expenses. *L.G.Electronics India Pvt. Ltd vs. ACIT (ITAT Delhi Special Bench)*.

Capital Gains: The assessee owned a plot of land a part of which was acquired by the Municipality for development purposes. The assessee was entitled to receive TDR/ FSI in lieu of the land acquired. The assessee sold the development rights to the said property for Rs. 20 lakhs and computed capital gains on that basis. However, for purposes of stamp duty, the property was valued at Rs. 1.19 crores. The AO held that the value of the property as adopted by the stamp duty authorities had to be taken as the consideration u/s 50C for purposes of capital gains. This was reversed by the CIT(A). On appeal by the department, the Tribunal held:

- Sec. 50C applies only to the transfer of "land or building" and not to the transfer of all "immovable property". Accordingly, though FSI and TDR is "immovable property" as held in *Chedda Housing Development vs. Babijan Shekh Farid*, 2007 (3) MLJ 402 (Bom), it is not "land or building" and so cannot be the subject matter of sec. 50C.
- The property acquired for development (in lieu of which the FSI/TDR was granted) also cannot be considered even though the property continues to stand in the assessee's name in the property records. The property should be valued by the DVO net of the land transferred to the Developer by the assessee after considering the acquisition made by the Govt & the Municipal Corporation and also excluding the value of TDR or additional FSI included in the consideration shown in the Development Agreement. *ITO vs. Prem Rattan Gupta (ITAT Mumbai)*.

Transfer of immovable property held through company: The assessee held shares in a company called Kamala Mansion Pvt. Ltd. The company owned flats in a building known as Om Vikas Apartments, Walkeshwar Road, Mumbai. The shares were sold by the assessee for Rs. 37.51

lakhs and capital gains were offered on that basis. The AO & CIT(A) held that by the sale of shares in the company, the assessee had effectively transferred the immovable property belonging to the assessee and that it was an indirect way of transferring the immovable properties being the flats in the building. He accordingly 'pierced the corporate veil', invoked s. 50C and computed the capital gains by adopting the stamp duty value of the flats. On appeal by the assessee, the Tribunal held:

- Sec. 50C applies only to the transfer of a "capital asset, being land or building or both", "assessed" by any authority of a State Government for stamp duty purposes. The expression "transfer" has to be a direct transfer as defined u/s 2(47) which does not include the tax planning adopted by the assessee. On facts, the subject matter of transfer is 'shares' in a company and not land or building or both. The assessee did not have full ownership on the flats which are owned by the company. The transfer of shares was never a part of the assessment of the Stamp duty Authorities of the State Government. Also, the company was deriving income which was taxable under the head 'income from property' for more than a decade. Consequently, the action of the AO & CIT(A) to invoke s. 50C to the tax planning adopted by the assessee is not proper and does not have the sanction of the provisions of the Act. *Irfan Abdul Kader Fazlani vs. ACIT (ITAT Mumbai)***.**

Valuation of shares of a closely held company: The assessee held 50% of the shares in L&T Infocity Ascendas Ltd ("LTIAL") while the rest were held by L&T Infocity Ltd. The assessee and L&T Infocity sold their entire holding in LTIAL to Ascendas Property Fund India ("APFI"), an AE of the assessee for a consolidated price of Rs. 79 crores. The assessee also held shares in Ascendas (India) IT Park Ltd ("AITPL") which was also separately sold to APFI. The assessee claimed that the shares were sold at arms' length price on the basis that (a) with regard to LTIAL, a third party (L&T Infocity) had sold its holding at the same price as that of the assessee and so the price was supported by "internal CUP" and (b) with regard to AITPL, the valuation was determined by a CA in accordance with the Controller of Capital Issues (CCI) Valuation guidelines.

The TPO/AO & DRP held that the transfer of shares in LTIAL by L&T Infocity to APFI was not an "uncontrolled comparable transaction" and so it was not as per the "internal CUP" method. With regard to the transfer of shares in AITPL, it was held that the valuation based on CCI guidelines was not acceptable. Instead, the valuation of both sets of shareholdings was determined on the basis of the "Discounted Cash Flow (DCF)" method for valuation of an enterprise and an addition of Rs. 239 crores was made. On appeal by the assessee, the Tribunal held:

- Sec. 92C(1) provides that the arm's length price in relation to an international transaction shall be determined by any of the methods set out therein. There may be difficulties in ascertaining the fair market value, but such difficulties should not be a reason for not adapting the prescribed methods. Some subtle adjustments in the methodology prescribed for evaluation of an international transaction are required to be done.

- To a transaction of sale of shares in a closely held company, none of the six methods prescribed in s. 92C & Rule 10B apply. Accordingly, while determining the most appropriate method, the modern valuation methods fitting the type of underlying service or commodities cannot be ignored. Fixing enterprise value based on discounted value of future profits or cash flow is a method used worldwide. The endeavor is only to arrive at a value which would give a comparable uncontrolled hprice for the shares sold. From this view-point, the DCF method adopted by the TPO is in accordance with s. 92C(1).

- The assessee's argument, with regard to the sale of shares in LTIAL, that the price is at ALP as per the CUP method as a third party (L&T Infocity) sold the same shares at the same price to the same buyer is not acceptable because the sale of shares by L&T Infocity to APFI cannot be said to be uncontrolled. The fact that a common agreement for sale of the shares for a consolidated sum was entered into by the assessee with L&T Infocity shows that the transaction was not independent but was a joint effort.

- The assessee's argument, with regard to the sale of shares in AITPL, that the TPO was bound by the CCI guidelines on valuation of shares is also not acceptable because the CCI guidelines were issued for a totally different purpose and cannot be transported into a pricing methodology prescribed for fixing ALP. *Ascendas (India) Pvt. Ltd vs. DCIT (ITAT Chennai)***.**

Comparables cannot be ignored on ground of abnormal profits/losses if they are functionally comparable: The assessee provided software research & development services to its USA based AE and was remunerated on a 'cost plus' basis. The assessee claimed that applying the TNMM and using operating profits to cost as the Profit Level Indicator ("PLI"), its PLI of 9.98% was at arms length. The TPO & DRP rejected the assessee's claim and computed the ALP at 24.35% and made an adjustment of Rs. 6.20 crores. The Tribunal held:

- The Turnover filter is an important criteria in choosing the comparables because significant differences in size of the companies would impact comparability even if there is no functional difference in their activities.

- U/s 92C & Rule 10B(2), there is no bar to considering companies with either abnormal profits or abnormal losses as comparable to the tested party, as long as they are functionally comparable. It is for the Assessee to demonstrate existence of abnormal factors. On facts, as the assessee has not shown any factors for abnormal profits, no comparable can be excluded for that reason.

- Though the functions performed by offshore service providers and onsite service providers is the same, i.e. development of computer software, under Rule 10B(2)(b) one has to have regard to the functions performed, taking into account assets employed or to be employed and the risks assumed by the respective parties to the transactions. Thus assets and risk profile, pricing as well as prevailing market conditions are different in predominantly onsite companies from predominantly offshore companies like the assessee. Since, the entire operations of the assessee took place offshore i.e. in India; it should be compared with companies with major operations offshore.
- The TPO is entitled to collect information u/s 133(6) though if it is sought to be used against the assessee, it must be furnished to the assessee and his objections taken into account. If the assessee seeks an opportunity to cross examine the party, the opportunity should be provided so that he can rebut the stand of that particular company. *Trilogy E-Business Software India vs. DCIT (ITAT Bangalore)***.**

Profit from sale of land converted into industrial unit: The assessee company was engaged in the business of manufacturing of specialized chemicals and in development of real estate and was owner of certain land allotted to it by Govt of Maharastra. The land was allotted to the assessee on condition that the assessee will obtain necessary approval from land revenue authorities for using the land for industrial purpose within the stipulated time. After obtaining approval, the assessee converted the land into stock in trade and then sold the same and offered the gain as capital gain. The AO during the course of assessment proceedings observed that the assessee had converted the land after a long gap and at the relevant time the land was rural agricultural land and hence the same could not have been converted into stock in trade.

The AO adopted the value of land as per stamp duty value. On appeal, the ITAT held that:

- the claim of the assessee that the land was not meant for agricultural use nor any agricultural activity had been carried on by the assessee on the said land after the date of acquisition has not been disputed. The agricultural land has not been defined in the Act. In a previous case, the Supreme Court held that for a land to be agricultural, it was required to be shown its connection with agricultural purpose and user. Also, it was held that the entry in the revenue records was not a conclusive evidence in determining the true nature of land. In the present case, no connection of the land to the agricultural purposes or user was established.

- Argument of the DR that since land was beyond Municipal limits the same has to be considered as agricultural could not be accepted as it is not the location of the land but its connection with agricultural purpose and user which makes it agricultural.

- The land was non-agricultural on the date of conversion on 31.3.2000 and, therefore, a capital asset. The conversion into stock-in-trade was supported by Board Resolution for which no dispute has been raised. The assessee was also involved in real estate activities and therefore conversion of the non-agricultural land has to be considered as stock-in-trade of the business of the assessee. The conversion of land into stock-in-trade had been duly declared by the assessee in the return for the assessment year 2000-01. The notes to the audited accounts also mentioned this fact and differences between cost of land and market value had been credited into capital reserve. Therefore, there is nothing illegal about the conversion of land by the assessee into stock-in-trade. *2013-TIOL-63-ITAT-MUM.*

Loan advanced by JV partner converted into share premium: Assessee was a joint venture between 'F' and 'O', a Government owned trading organization from Russia. Assessee was not doing any activity for last six years due to heavy losses. AO made addition for loan converted into shares, share application money and for liabilities converted into share capital and premium. Assessee contended that it received outstanding share application money and other loans from foreign collaborator. Due to heavy losses, promoters agreed to convert share application money and other loans outstanding in the books of account for enhancement of share capital to the extent of authorized capital available and balance as share premium account enabling the company to get it closed under Simplified Exit Scheme as the company had already disposed off its trawlers in the previous years.

Assessee submitted that provisions of section 41(1) were not applicable in its case. This Section provides that where an allowance or deduction is granted to the assessee in any previous year in respect of any loss or liability, and subsequently, the assessee receives any amount in respect of such expenditure, or the liability is extinguished, then the amount so received or extinguished shall be charged to tax in the previous year in which the amount is received or the liability is extinguished. This was not true in the present case. The Tribunal held that:

- the loan was taken for acquiring the capital asset in the form of trawlers. This loan was taken from a joint venture partner in the company. This amount was converted into the shares and share premium. This amount was not taken to the profit & loss account. Thus, this amount has not changed its character from capital to revenue. The assessee has not derived any benefit out of this conversion of one liability to another liability. There was no waiver of the loan, therefore, conversion of the loan into share capital shall not constitute a trading receipt.

- Thus, the addition made u/s 41(1) is deleted. *2013-TIOL-15-ITAT-DEL.*

Reimbursement of costs to a third party for manufacturing steel: The assessee companies - Kalyani Ltd and Mukund Ltd - were engaged in the business of steel manufacturing. To manufacture steel in economical and cost effective manner the assessees had entered into a Strategic Alliance Agreement [SSA], incorporated a company HSL, and invested in the same as per the SSA. As per terms of the SSA, both the assessees had agreed to reimburse HSL all the expenses incurred in course of business. Accordingly, the expenses incurred towards hot metal making and steel rolling activities were allocated to the assessee and the expenses incurred on steel making activities were allocated to ML. The common expenses and corporate expenses were reimbursed in predetermined ratios.

In the course of the assessment u/s 133A, the AO was of the view that payments made by the assessee were in nature of fees for technical services and thus the assessees were liable to deduct taxes u/s 194J. Based on the above the AO treated both the assesses as assessee in default u/s 201(1A) for non-withholding of taxes on costs reimbursed to HSL.

Upon appeal, the Tribunal held that:

- As per the terms of SAA, the assessee and ML have reimbursed the expenses incurred by HSL in performance of its obligations, on cost to cost basis and the same is evident from the P&L account and debit notes raised by HSL on the assessee and ML. Therefore, the said payments did not comprise of any income component.

- Thus, the reimbursement of such expenses cannot be categorized as in the nature of fees towards professional and technical services. Hence, the assessee as well as ML were not liable to deduct tax at source u/s 194J of the Act. *2013-TIOL-09-ITAT-BANG.*

- Recent Discussion - The payments made to third party, towards services availed for operating and maintaining an integrated steel plant cannot be said to be reimbursement merely because the said third party charged at cost. Unlike as required u/s 195, element of income is not essential for deduction of tax u/s 194C. In case, the third party has no income or not liable to tax, there is a provision under the Act to obtain a certificate u/s 197 for no deduction of tax.

SERVICE TAX

Important Circular / Notification

- Clarification has been issued in respect of notices/ reminder letters issued for life insurance policies. Under the Point of Taxation Rules 2011, the point of taxation generally is the date of issue of invoice or receipt of payment whichever is earlier. The invoice mentioned refers to the invoices as issued under Rule 4A of the Service Tax Rules 1994. No tax point arises on account of such reminders. Thus it is clarified that reminder letters/notices for insurance policies not being invoices would not invite levy of service tax. In case of issuance of any invoice, point of taxation shall accordingly be determined. This clarification is only for the life-insurance sector. *Circular No.166/1/2013 –ST, dated Jan 1, 2013.*

SC/HC JUDGMENTS

- **CAG has no power to audit records of private assesses:** The question was whether CERA, an audit wing of the Principal Director of Audit (Central), Kolkata under the Comptroller and Auditor General of India, has power and/or authority and/or jurisdiction to audit the accounts, service tax records or other documents of the petitioner company, which is not an undertaking of the Central Government or any State Government. The High Court noted that:

- None of the statutes, namely, the Companies Act, 1956, the Income Tax Act, 1961, the Central Excise Act, 1944 or the Finance Act, 1994 as amended from time to time, contain any provision for audit by the Comptroller and Auditor General of India or any audit team subordinate to the Comptroller and Auditor General of India, of any company incorporated or existing under the Companies Act 1956, except a government company within the meaning of Section 619 of the said Act.

- Sub-section (2) of Section 94 also does not empower the Central Government to frame rules for audit of the accounts of an assessee by any audit team under the Comptroller and Auditor General of India.

- Thus, impugned notice cannot be sustained and the same is liable to be set aside. *2013-TIOL-38-HC-KOL-ST*.

CESTAT JUDGMENT

- **Services provided by a Trust, acting as an intermediary:** Appellant was a Trust (Sanstha) consisting of farmers and transporters. The farmers undertook harvesting of sugar cane and the truck owners undertook transportation of these from the farmers' fields to the factory in *Kolhapur*. The bills for the service rendered to the sugar factory were routed through the Sanstha and the payment was received from the sugar factory to the Sanstha for further distribution to the farmers and the transporters.

The department took a view that the activity undertaken by the appellant fell under the category of 'Manpower Recruitment and Supply Services' and accordingly a Service Tax demand was raised. Before the CESTAT, the Sanstha submitted that -

- It was a charitable Trust and only a facilitator for the transaction between the farmers on one side and the sugar factory on the other. The farmers enter into an agreement with the sugar factory for harvesting of sugar cane and rates are fixed for harvesting and supply of sugarcane by the two parties. Similarly, for the transport of sugar cane from the farmer's fields to the sugar factory the transporters enter into an agreement with the sugar factory. The appellant comes into picture only as a facilitator and there is no agreement between the Sanstha and the sugar factory.

- Based on the details given by the sugar factory regarding quantum of cane received, bills are raised by the appellant and from the bills raised it can be easily seen that the charges are based on the tonnage of sugarcane supplied and not on the basis of labour employed.

- The payments are made directly to the accounts of the farmers and the transporters by the sugar factory, who routes these payments through the appellant-Trust and they do not retain any amount and the amounts are straightaway credited to the bank where the farmers and the transporters hold accounts.

- The appellant Trust did not hold any bank account at all and it had not undertaken any banking transaction during the impugned period. Therefore, the allegation that the appellant-Trust supplied labour to the sugar factory was not borne out from the documents available on record.

The CESTAT Bench observed that the appellant had made a strong case, for grant of interim stay. *2013-TIOL-190-CESTAT-MUM.*

- **Service Tax on Toll charges:** Appellant was engaged in construction of highways. The Public Works Department (PWD) of Government of Maharashtra awarded the contract for this purpose, and authorised the appellant to collect toll from the users of the road at various places. The department was of the view that the appellant was required to discharge service tax liability on this activity under the category of "Business Auxiliary Service" and a show cause notice was issued. The appellant referred to the Board Circular no. 152/3/2012-ST dated 22/02/2012. The CESTAT observed -

- From the above circular it is clear that if on the basis of an agreement between the State authority and the concessionaire for construction of roads, the contractor is authorised to collect the toll charges from the users of the roads for the services rendered and the entire activity is done on Build-Own/Operate-Transfer basis, there is no service tax liability.

- Construction of roads has been specifically excluded from the scope of service tax levy both under "Commercial and Industrial Construction Service"and "Works Contract Service". Further repair and maintenance of roads have also been exempted from service tax retrospectively in this year's budget. Thus the intention of the Government is to keep out road construction activity from the purview of service tax. So Service tax cannot be levied. *2013-TIOL-136-CESTAT-MUM.*

➢ **Payment made for use of trade secret:** The appellant is a manufacturer of Ion exchange resins. An employee who was working with *M/s Purolite International Ltd.*, a competitor of the applicant, left the job and provided trade secret for manufacturing of ion exchange to the applicant. *M/s Purolite International Ltd*. filed a suit in the USA court and the applicant was charged with using the trade secret of M/s Purolite International Ltd. Court proceedings were initiated against the applicant.

Not to escalate the matter further and be saddled with damages of astronomical proportions, the applicant entered into an agreement with M/s Purolite International Ltd., to settle the dispute out of court. As per the settlement, it paid consideration for the use of trade secret and became the co-owner of the Purolite's technology. Revenue took a view that the consideration paid by the applicant to Purolite is covered under Intellectual Property Service under reverse charge mechanism and, therefore, the applicant is liable to pay service tax on the entire consideration. Upon appeal by the appellant, the CESTAT Bench observed -

- The intellectual property right means any right to intangible property namely trademarks, designs, patents, but does not include copyright. While framing the charge against the applicant, the adjudicating authority has not specified specifically under which part of the Intellectual Property Right applicable in India the applicant is covered.

- In view of the above observations, the impugned demands are not sustainable. Therefore, prima facie the applicant has made out a case for waiver of pre-deposit of the entire demand. *2013-TIOL-94-CESTAT-MUM.*

Services of guidance on business matters: The applicant was providing various services to its members such as general guidance on the various facts of business, representation of members' problems and views at local, state and central govt. level, networking and information sharing opportunities, free access to commercial reference library etc. The applicant was charging the members a one-time registration fee and also recovering annual subscriptions from them for providing the aforesaid services. The department determined that the said "services" were classifiable under category of "Club or Association service" of the Finance Act, 1994 and service tax was leviable on the same.

The applicant submitted that it was a company registered under Companies Act. As per the definition of the club or association service, it did not include any person or body of persons engaged in the activities of trade unions, promotion of agriculture, horticulture or animal husbandry. Since the applicant was engaged in promotion of agriculture, and in public service, therefore, by way of the exclusion clause of the definition of the service, applicant was not liable to service tax. The Bench observed -

- The applicant was already paying service tax on the club or association service, so there was no prima facie case in its favour.

- The applicant relied on the decision of the Jharkhand High Court in the case of Ranchi Club Ltd. where it was held that service tax was not liable on the members of the club, as the club was giving service to its member and club was formed on the principle of mutuality and, therefore, any transaction by the club with its member was not a transaction between two parties. However, in the present case, the applicant had not been able to give any evidence to prove that applicant was a Member's club.

- Holding so, the CESTAT directed the applicant to make a pre-deposit for obtaining Stay in the matter. *2013-TIOL-56-CESTAT-MUM.*

Difference between 'renting' and 'leasing': Appellant was a body established under the Uttar Pradesh Industrial Development Act, 1976 to develop certain notified areas as a planned industrial township. One of the functions of GNIDA was to allocate and transfer, by sale or by lease, plots of land for industrial, commercial or residential purposes. GNIDA charged both one-time lease charges at the time of initial handing over of the land and also charged annual lease charges at different rates for land given for different purposes.

Revenue determined that service tax was payable on such "lease charges" received as per provisions of section 65 (105) (zzzz) read with section 65 (90a) of Finance Act, 1994. Appellant argued that it was doing a statutory sovereign function and not a service and that long term lease was like sale and not akin to renting made taxable under section 65(105)(zzzz), and hence the demand was not maintainable. The Bench observed:

- The key question to be considered was whether long term lease like one for 90 years, would be covered by the meaning of "renting" or "leasing" used in section 65 (105) (90a). The ordinary meaning of "renting" would not cover long term leasing. The inclusive definition given in section 65 (105) (zzzz) including renting, letting, leasing and licensing in the same type of services would suggest that the word "leasing" used in the said section did not cover long term leasing where a property was given to a person with rights to transfer, assign and mortgage the rights. Such transfers were more akin to sale, and less to renting of property. Such view was supported by the decision of Delhi High Court in the case of Krishak Bharati Co-operative Ltd Vs. Dy. CIT *(2012-TIOL-515-HC-DEL-IT)* holding that payments made to GNIDC was an expenditure in the nature of capital expenditure, and not a revenue expenditure.

- A government authority, doing an activity as per a mandate in an Act of the legislature, cannot take away the character of service from the activity. If that is not the case transportation functions done by Indian Railways would not amount to service. So may be the case of insurance service provided by Life Insurance Corp of India mandated to do so under LIC Act, 1956. However it is recognized that sovereign functions done by a government authority like certifications done under Weights and Measures Act, issue of passport etc cannot be considered as taxable service. The concept as to what are sovereign functions also is changing. Developing a township according to a plan which will be conducive to society at large and maintaining municipal functions in such township has to be considered prima facie to be sovereign functions and not a commercial activity of the government.

- CESTAT further observed that since the appellant is an Authority set up by a State Government they should not be put to hardship that may be caused by ordering pre-deposit in a matter involving basic legal issues. Holding so, the Bench granted waiver of pre-deposit and ordered a Stay in the matter. *2013-TIOL-44-CESTAT-DEL*.

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