Tax News

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INCOME TAX

Reminder For July 2011

Action Due	Due Date
TDS / TCS for the month of June 2011	07-07-11
PF for the month of June 2011	15-07-11
ESI for the month of June 2011	21-07-11
Due date for filing of TDS return for the quarter ended on 30th June 2011	15-07-11

SERVICE TAX

Action Due	Due Date
Service Tax for the month of June 11 in case of company	05-07-2011
Service Tax for the month of June 11 in case of a company for which e-payment is mandatory.	06-07-2011
Service tax for Quarter ending 30th June in case of assessee other than company that makes payment electronically.	06-07-2011
Service tax for Quarter ending 30th June in case of assessee other than company that does not make payment electronically.	05-07-2011

INCOME TAX

Important Changes/Notification

➢ **Exemption of interest on post office saving scheme:** As per new Notification of Income Tax Act, interest on Saving Account with Post Office u/s 10(15)(i) shall be exempted upto Rs. 3500/- in case of individual account and will be exempted upto Rs. 7000/- in case of Joint Account. *Notification No. 32/2011[F.No.173/13/2011-ITA.I]/S/O/1296(E), Dated 03.06.2011.*

➢ **Exemption u/s 139(1) to Specified Person from the requirement of furnishing a return of income for Assessment year 2011-12 : T**he Central Government hereby exempts the following class of persons, subject to the conditions specified hereinafter, from the requirement of furnishing a return of income under sub-section (1) of section 139 for the assessment year 2011-12, namely :—

Class of Persons

1. An Individual whose total income for the relevant assessment year does not exceed five lakh rupees and consists of only income chargeable to income-tax under the following head,—
(A) "Salaries";
(B) "Income from other sources", by way of interest from a savings account in a bank, not exceeding ten thousand rupees.

Conditions

2. The individual referred to in para 1,—
(i) has reported to his employer his Permanent Account Number (PAN);
(ii) has reported to his employer, the incomes mentioned in sub-para (B) of para 1 and the employer has deducted the tax thereon;
(iii) has received a certificate of tax deduction in Form 16 from his employer which mentions the PAN, details of income and the tax deducted at source and deposited to the credit of the Central Government;
(iv) has discharged his total tax liability for the assessment year through tax deduction at source and its deposit by the employer to the Central Government;
(v) has no claim of refund of taxes due to him for the income of the assessment year; and
(vi) has received salary from only one employer for the assessment year.

3. The exemption from the requirement of furnishing a return of income-tax shall not be available where a notice under section 142(1) or section 148 or section 153A or section 153C of the Income-tax Act has been issued for filing a return of income for the relevant assessment year. *NOTIFICATION NO. 36/2011, DATED 23-6-2011*

Supreme Court / High Court Judgments

Taxability of Interest earned under bills rediscounting scheme: Assessee, a Public Financial Institution under Section 4A of the Companies Act, 1956, was mainly engaged in the business of insurance other than life insurance. It also invested in shares, debentures, bonds, government securities etc. Further, it provided various types of loans and advances to different companies as well as Credit Institutions under different schemes like term loans, bill rediscounting, call money deposits, loans against

mortgage of property, loans to the State Governments for housing and firefighting equipment etc.

It was held that as per Sec 5 of the Income Tax Act, interest income chargeable to tax did not include all the interest received by a Credit Institution. Interest on loans and advances made to other Credit Institutions, accruing in the previous year, was specifically excluded. Similarly, in Sec 6 of the Act, that provided mode of computation of the chargeable interest, the interest on loans and advances made to Credit Institutions was explicitly excluded. Thus, the interest received by the assessee on loans and advances made under bill rediscounting scheme, from different banking companies, did not form part of chargeable interest and no tax was payable on such amount. *2011-TIOL-388-HC-KOL-IT in Income Tax.*

Capital gain in case of transfer of intangible assets: Assessee was a private limited company engaged in the business of healthcare, print media & electronic media communications. It entered into a 'Specified Assets Transfer Agreement' with another company for the sale of all its rights, titles and interest in specified assets of its Healthcare Journals & Communications business. These assets were (a) the periodicals (b) the products (c) the business intellectual property rights along with the goodwill (d) the customer database (e) the records (f) the editorial materials & (g) the contracts.

It was held that when assessee transferred brands, trademark and interests in a health periodical, held as intangible assets, the profit arising out of such transaction was to be treated as capital gains or business income. *2011-TIOL-371-HC-DEL-IT.*

Tribunal Judgments

➢ **Profits u/s 115JB during Sick period:** Assessee was a public sector undertaking. The company suffered losses for a number of years in the past and was declared a sick company as defined under the sick industries companies (special Provisions) Act, 1985. In the Assessment Year (AY) 2000-01, while computing the book profits as defined in Explanation to sec 115JA(2) of the IT Act, the company reduced the profits earned by it during the period of sickness in AY 1992-93 and AY 1993-94. The Assessing Officer (AO) disallowed the claim of the assessee. The CIT(A) affirmed the order of the AO.
The Tribunal held that the book profit of the assessee was to be computed with reference to each AY and the provisions of sec 115JA(2)(vii) cannot be applied for AY 2000-01 when the assessee was no more a sick company, as by then, its net worth had become equal or more than the accumulated losses. It was held by the Tribunal that profits earned during the period of sickness were not to be excluded from the ambit of book profit of non-sick years. *2011-TIOL-358-ITAT-HYD in Income Tax.*

➢ **Sec. 10A in case of forex fluctuation from external commercial borrowings**: It was held by the Tribunal that section 10A is not allowed in case where foreign exchange fluctuation was from the external commercial borrowings, not from any export activities. *2011-TIOL-352-ITAT.*

➢ **Applicability of Sec. 194C in case supply of materials:** Assessee, a State Government Public Sector company, was in the business of transmission of electricity to various sub-stations in the State through the network of transmission lines. Assessee entered into various agreements with various contractors for setting up of electrical sub-stations. The assessee further entered into separate agreements for supply of materials, erection and civil construction. While

deducting tax at source, the assessee excluded the payments towards supply of material. AO did not accept the claim of the assessee. The issues were:

(a) when assessee entered into agreements with sub-contractors for civil construction and erection of transmission towers, and also supplied materials, whether the assessee was liable to tax deduction at source on the supply portion,
(b) and when contractors compensated farmers for uprooting their trees for installation of towers on behalf of the assessee, and also undertook the work of haulage of felled trees to stores, whether it attracted provisions of Sec 194C.

It was held by the Tribunal that:

- the assessee cannot be considered 'in default', following the decision of ITAT in the case of KPTCL Bangalore Div, dated 10.3.2011, in which it was held that when the assessee was under no obligation to deduct tax u/s 194C of the Act towards the payments made on supply portion, then there was no question of charging of interest u/s 201(1A) of the Act;
- the assessee had assigned the contractors (i) to pay compensation to the farmers for losing their trees/crops etc. and (ii) to transport the cut logs to its storing places. The contractors had carried out these tasks on behalf of the assessee. The AO was asked to quantify the compensation paid which would not attract the provisions of s.194C of the Act and the balance amount would attract the provisions of s.194C of the Act. *2011-TIOL-333-ITAT-BANG in Income Tax*.

- **TDS liability in case of technical drawings procured from parent company:**

The assessee company was a 50-50 joint venture with M/s. Kunkel Wagner Progress Technologies,GmbH, Germany (KWPT). The parent company was in the business of manufacturing foundry moulding machines, sand preparation plants and allied equipments. These products were custom designed as per specifications of clients. The assessee company handled a part of the manufacturing activity of the parent company i.e., designing and manufacturing the conveying and handling equipments for the main plants designed by the parent company and erecting them at the sites of Indian plants.

The assessee during the year had paid an aggregate sum as consideration to KWPT from which no tax had been deducted at source. Issues involved were:

- When the subsidiary of a foreign company procured technical drawings from the parent company, was it necessary to deduct TDS from such payments.
- Was it necessary to examine whether the subsidiary constituted a PE and whether any income accrued to the foreign company in India.
- Whether the alternate argument of AO regarding expenditure being capital in nature, needed to be adjudicated.

It was held by the Tribunal that:

- The assessee was not only procuring material from parent company but had also exported software to the parent company. There was obviously a territorial nexus of the parent company in India;
- It had not been examined whether the assessee which had transactions with its parent company during the year, would constitute a PE. It had also not been examined whether the parent company had other transactions and activities in India. The taxability of the disputed amount in India in the hands of the parent company had to be examined carefully. Since the AO did not consider

the matter properly therefore the matter was sent back. *2011-TII-92-ITAT-MUM-INTL.*

- **Taxability of receipts earned by non-resident assessee from Indian customers by relaying TV programmes:**

The assessee was a non-resident company and a wholly owned subsidiary of Asia Satellite Telecommunications Holdings Limited of Hong Kong. The AO had held that the receipts earned by the assessee outside India were liable to tax as these had accrued and arisen in India.

According to the Revenue, the relaying of the programmes in India amounted to the assessee's operations being carried out in India. The amount paid to the assessee by its customers amounted to royalty under Explanation 2 to sec. 9(1)(vi) or alternatively represented consideration for the right to use industrial, commercial or scientific equipment.

In appeal before the Tribunal, the assessee submitted that its receipts could not be deemed to have accrued in India and the Delhi High Court had, in the assessee's own case, held that no activities were carried out by the assessee in India and provisions of section 9(1)(i) were not attracted in the assessee's case.

The Tribunal held that following Delhi High Court's judgment in assessee's own case, the assessee's activities did not fall in the scope of provisions of sec. 9(1)(i) of the I.T. Act, therefore, such receipts of agreement were non-taxable. *2011-TII-93-ITAT-DEL-INTL.*

- **Transfer Pricing:**

The assessee, a subsidiary of M/s Sapient Corporation, USA, rendered customized software development services to associated enterprises and also provided post-sales support services.

The assessee determined the arms' length price of the international transactions of software development and related services by applying TNMM as most appropriate method. The assessee had benchmarked its international transactions with 10 comparable companies with an average operating profit ratio (OP/TC) of 9.31%. Since the operating profit margin of the assessee at 12.5% was higher than the average operating profit margin earned on similar transactions with unrelated third parties, the international transactions were claimed to be at arms' length.

The TPO, however, rejected five loss making comparables identified by the assessee. On appeal, the ITAT held that:

- when the loss making companies had been taken out from the list of comparables by the TPO, then companies which showed super profits should also have been excluded.

- Zenith Infotech was mainly a software product company, while the assessee was engaged in rendering software development services. Since software product company typically had higher margins, it was not correct to include it as a comparator.

- Since the OP/TC of the appellant at 12.5% was within (+/-) 5% of OP/TC margin of 3 comparable companies at 13%, no adjustment was required on account of difference in arm's length price of the international transaction. *2011-TII-50-ITAT-DEL-TP.*

SERVICE TAX

Important Changes/ Notification:

- **Extension of date :** Through Notifications, the effective date of exemption for Transport of goods by rail, and taxable service provided to any person in relation to transport of goods, etc., has been extended form July 2011 to January 2012. *Notification No.40/2011-Service Tax dated 14-Jun-2011, Notification No.39/2011-Service Tax, Notification No. 38/2011-Service Tax*.

SC/HC Judgments

- **Security service as input service**: The assessee, manufacturer of soda ash, provided residential quarters for its workers, where security services were also provided. The issue was whether the security service provided by the respondent at the residential quarters, would be included in the term 'input service' as defined in rule 2(l) of the Cenvat Credit Rules.

As per the Service Tax Act, 'input service' has been defined in section 2(l) as service used by the manufacturer whether directly or indirectly or in relation to the manufacture of final products and clearance of final products from the place of removal. The High Court held that the security service provided by the manufacturer in the residential quarters maintained for the workers did not have any direct or indirect relation in the activity of manufacture of the final product.

With reference to the view of the Bombay High Court in the case of *Manikgarh Cement*, the Court held that while outdoor catering services provided by the manufacturer to its workers was mandatory and therefore covered within 'input service', the act of providing residential quarters by the manufacturer to its employees was voluntary. Providing further security service in such residential quarters was also voluntary, so it was not an 'input service'. *2011-TIOL-383-HC-AHM-ST in Service Tax.*

CESTAT Judgments

- **Tennis club registered as charitable institute:** The appellant, a non-profit organization registered under Bombay Public Trust Act, was engaged in providing service of health club/sports activities to its members. The department raised a demand alleging that as per Section 65(25)(a), the 'Club' is required to pay Service Tax, because a "club or association" is defined as any person or body of person providing services, facilities or advantages, for a subscription or any other amount, to its members.

Assessee submitted that since they are a non-profit organization and a certificate has been issued by Assistant Charity Commissioner indicating that they have to be treated as a charitable trust, they need not pay any Service Tax. Furthermore, since they are not providing any chargeable services, they were exempt. To this submission, the Bench observed that the appellants were providing services such as health club, organizing tennis matches by renting the ground, renting the place for party purpose, organizing tournaments etc. and the same could not be called as non-chargeable services.

Thereafter, it was submitted by the appellant that there were several decisions in their favour holding that the services provided by the association or a club to its members cannot be considered as a service.

After considering the various submissions, CESTAT held that the appellants are covered by the definition of club or association and the activities also are covered by taxable service. No evidence showing acute financial difficulty had been given. The appellant was therefore directed to make a pre-deposit of 25% of the Service Tax demanded and report

compliance. *2011-TIOL-742-CESTAT-AHM in Service Tax.*

- **Handling, transportation, and supervision charges taxable under cargo handling services:** The assessee, a public sector undertaking, was engaged in the business of warehousing fertilizer and other items, and was registered with Service Tax Authorities for payment of tax on "Storage and Warehousing" charges.

It was observed that the assessee was recovering supervising charges from its customers at a certain percentage of handling and transportation charges. Department raised a demand alleging that assessee was required to pay service tax on the supervision charges (in addition to the service tax paid on handling and transportation charges), under "Cargo Handling Service". After this demand, assessee started paying tax on such services also.

However, when the Department raised a demand for previous years as well, the assessee contested that:

- It was a "cargo handling agency" because it was in the business of warehousing of goods for which it was already paying service tax.
- As a corporation owned by the Rajasthan State it did not want to enter into dispute on this issue with the Union of India and as soon as the issue was pointed out by the Department, it started paying tax for the charges collected by it and paid to the contractor who was providing the service. So there should not be any tax liability for the extended period.

CESTAT held that considering the status of the assessee as a PSU and its conduct after the matter was pointed out, and the fact that the audit by the Department on previous occasions did not point out this issue, though it was collecting charges during such period also, it was clear that the assessee did not have any intention to evade the impugned tax. Therefore the demand would be sustainable only to the extent of demand covered by the normal period of time of one year. Interest under sect. 75 would be payable on the sustainable portion of the demand. Penalty under sec. 76 would be maintainable in respect of the period within normal period, while penalty under sec. 78 would not be maintainable. *2011-TIOL-724-CESTAT-DEL in Service Tax.*

- **Taxability of repair charges of coffee machine provided by the employer:** The assessee was providers of software development and support services and these services came into the taxable net w.e.f 16 th May, 2008. The issue was whether repair of coffee vending machine was input service for CENVAT credit as vending coffee was a catering service quite essential, especially for employees working in IT companies.

CESTAT held that maintaining the coffee machine in working condition was very essential, especially for the employees working round the clock as in the case of IT companies. Therefore, repair of the coffee vending machine was an eligible input service in or in relation to the output service provided by the assessee, and, therefore, it was rightly entitled to the service tax paid on the repair of the coffee vending machine. *2011-TIOL-719-CESTAT-MUM in Service Tax.*

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