Tax News

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INCOME TAX

Reminder for Dec 2013

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SERVICE TAX

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INCOME TAX

SC/ HC Judgments

- **Purchase of computer software:** The assessee was a marketing and development company of an international group owned by a US-based holding company. It set up its Branch Office in India to market the software. The assessee developed customized software to be used by the customers for designing highways, railways, airports, ports, mines, etc. The software was then licensed to an Indian customer and the branch office performed services involving peripheral installation and training.

  The Assessing Officer sought to tax the aggregate amount received by the Assessee during the year to tax at 20% as royalty under Section 44D read with Section 115A of the Income Tax Act. The assessee contended that software sold were goods (as held by the Supreme Court in the TCS case), and accordingly, only net profit would be chargeable to the PE as business income under Article 7 of the India- USA DTAA.

  On appeal, the ITAT noted that if the payment received by the assessee Company was for a copyright then it would classify as royalty both under the Income Tax Act, 1961 and under the DTAA. However, if the payment was for a copyrighted article then it would represent the purchase price of an article and could not be considered as royalty either under the Act or under the DTAA. The Tribunal held in favour of the assessee.

  On appeal to the High Court, the counsel for the Revenue submitted that in the present case, there was no sale of the software but it was mere licence to use the software and as such, the receipt from such a sale was receipt towards royalty. The counsel further contended that royalty was defined in Explanation 2 to Section 9(i)(vi) to include consideration for transfer of either one or more intellectual property rights mentioned therein and as such, there was no scope for an argument that computer software was not fully covered within the meaning of royalty. Contradicting the stand of the Revenue, the counsel for the Assessee company submitted that what was transferred was neither the copyright in the software nor the use of the copyright in the software, but what was transferred was the right to use the copyrighted material which was clearly distinct from the rights in a copyright. The High Court held:

  - The Supreme Court had held that copyright in a software program may remain with the originator of the program, but the moment copies are made and marketed, it becomes goods, which are susceptible to sales tax. Even intellectual property, once it is put on to a media, whether it be in the form of books or canvas (in case of painting) or computer discs or cassettes, and marketed, would become "goods". There was no difference between a sale of a software program on a CD, from a sale of music on a CD. In all such cases, the intellectual property has been incorporated on a media for purposes of transfer. Sale was not just of the media which by itself has very little value. The software and the media cannot be split up. What the buyer purchases and pays for is not the disc or the CD. The buyer is purchasing the intellectual property and not the media.

- The purchaser of computer software neither desires nor receives mere knowledge, but rather receives a certain arrangement of matter that will make his or her computer perform a desired function. This arrangement of matter, physically recorded on some tangible medium, constitutes a corporeal body. Once the "information" or "knowledge" is transformed into physical existence and recorded in physical form, it is corporeal property.
- In order to qualify as royalty payment, it is necessary to establish that there is transfer of all or any rights (including the granting of any licence) in respect of the copyright. In this case, the Licensing Agreement shows that the license was non-exclusive, non-transferable and the software had to be used in accordance with the agreement. Only one copy of the software was being supplied for each site. The licensee was permitted to make only one copy of the software and that also for backup purposes. It was also stipulated that the copy so made shall include assessee's copyright and other proprietary notices. All copies of the Software were the exclusive property of the assessee. The Software included a licence authorisation device, which restricted the use of the Software. The software was to be used only for Licensee's own business. Without the consent of the assessee the software could not be loaned, rented, sold, sublicensed or transferred to any third party or used by any parent, subsidiary or affiliated entity of Licensee. The Licensee was further restricted from making copies, decompile, disassemble or reverse-engineer the Software without assessee’s written consent. The Software contained a mechanism which assessee could activate to deny the Licensee use of the Software in the event that the Licensee was in breach of any provision of this Agreement. Thus in this case, there was no transfer of any copyrights and intellectual property rights to the purchaser of the Software.

- What has been transferred is not copyright or the right to use copyright but a limited right to use the copyrighted material, and it does not give rise to any royalty income. The case is decided in favour of the assessee. *2013-TII-50-HC-DEL-INTL.*

➢ **Income from House Property:** The assessee company derived income from sub lease of rental properties, maintenance charges, interest income on deposits, A.C. service charges and miscellaneous income. The assessee had shown the receipts from leasing out of property etc, as income from business, by claiming expenses towards salaries, wages, bonus, administrative expenses etc., for the relevant AYs. The AO held that the rental income from some of the properties was assessable as "income from house property". Consequently, the AO disallowed the expenses claimed and allowed deductions u/s 24 of the Act. The Tribunal ruled in favour of the Department. Upon appeal, the High Court held that:

- The AO, CIT, as well as the Tribunal have recorded a factual finding that the assessee closed down the manufacturing business with no evidence of revival, and the income from the land and building has to be treated as "income from house property".
- From the copy of the rental lease agreement, it is seen that the property which has been leased, is vacant land. No other document has been produced to show that the lease was in respect of the factory building, machinery and equipment.
- Since the assessee has stopped its business activities long back and is not carrying out any other business activity and the assessee has parted with the commercial assets and confined solely to receive some income by virtue of ownership thereof by lease, and the act of leasing was the outcome of the assessee's decision to get out of the business, we accept the case of the Revenue that the income receipt from letting out of the property was rightly assessed as "income from house property". *2013-TIOL-839-HC-MAD-IT.*

➢ **Exemption u/s 10B:** Assessee, a proprietor of M/s. Shyam Solutions, was engaged in the business of export of computer softwares. While filing the income tax return, it had claimed exemption u/s 10B. During assessment, AO opined that assessee had not brought back the entire amount to India, and to the extent the amount was yet to be brought in, the exemption could not be claimed. Also, penalty was imposed for concealment of income that was not brought into India. The Tribunal upheld the penalty. Upon appeal, the High Court held that:

- It appears that the accounts were duly audited and the exemption under Section 10B was claimed by furnishing the report in FORM No. 56G read with Rule 16E of the Income Tax Rules, 1962. So, all the facts were disclosed to the AO.
- It also appears that the claim denied by the AO under Section 10B was based on the facts disclosed in the return of income filed by the assessee.
- It is also evident that uncollected sums were export income from the software which was not approved by the clients. So, the assessee did not receive the same in time. As and when payment received, the same was disclosed to the Department. In view of above, the variation between the claim made by the assessee under Section 10B, vis-a-vis the claim disallowed in the assessment, occurred solely owing to bonafide reasons.
- No malafide intention or element of concealment is involved in this case, so it is out of the ambit of penal provisions contained in Section 271(1)(c). *2013-TIOL-832-HC-ALL-IT*.

- **Applicability of Sec 80I when manufacturing activity is performed by a third party:** Assessee was a cooperative society and had claimed Sec 80I deduction on income earned through transportation of Ammonia in specialized tankers. The HC held that:

  - Under section 80I, emphasis is on the profits and gains of industrial undertaking, which manufactures or produces an article or thing as specified. Transportation of ammonia, as in case of other products, may require specialized container vessels or wagons/transport vehicles, but the income derived would be earned from transportation.
  - Transport charges were separately paid, and were not income or profits derived from an industrial undertaking, which manufactured or produced articles or things. Transportation even in specialised vehicles or wagons, was a separate commercial activity. The said activity could be undertaken by a third person, other than the appellant. The third party transporters could have specialised vehicles or wagons for transportation of ammonia. The aforesaid activity of transportation was post-manufacture and relates to activities outside the four walls of the industrial complex or undertaking where manufacture or production took place.
- To examine whether the income was derived from an industrial undertaking, it is imperative to trace the source of profit or income to manufacture/production. Transportation, as noted above, is post-manufacture and takes place after the goods or articles have been manufactured in the industrial undertaking. They relate to activity of transportation of the said articles or goods from the factory to the place of the consumer/customer. It is a service and does not partake character and is not a part of manufacture. *2013-TIOL-826-HC-DEL-IT*.

- **Assets acquired by the merged entity pursuant to scheme of amalgamation: The** assessee was a public limited company engaged in the business of manufacturing and trading of readymade garments and accessories. Under a scheme of arrangement and merger sanctioned by the Delhi High Court u/s 394 of the Companies Act, proprietary concerns of the directors, M/s Vama Industries, Vikramaditya Exports and Meera Overseas had merged with the assessee. Imported motor cars were originally acquired by the proprietary concerns, but upon amalgamation, they became the properties of the assessee with effect from 1st April, 2004. The question raised was whether the assessee was entitled to claim depreciation as the imported cars were acquired by it after 1st April, 2001. Upon appeal, the High Court held that:

  - Explanation 7 to section 43(1) refers to acquisition of an asset under the scheme of amalgamation. This indicates that the Legislature has treated amalgamation as transfer of asset. Similarly, under sub-section 43(6), the use of the term "transferee company and transferor company" indicates that in cases of amalgamation, there is transfer of assets.

- The cars were not acquired and the assessee was not the owner of the motor cars prior to the said date. On merger of the three concerns with the respondent assessee, shares were issued as consideration to the proprietors of the business concerns. The shares issued were consideration for the transfer of the assets. It is immaterial, whether there was transfer of an undertaking, including the block of assets, which also included the imported motor cars.

- It is clear that the assessee had acquired the asset i.e. imported cars after the cutoff date i.e. 1st April, 2001 and, therefore, is entitled to depreciation and the prohibition in clause (a) to proviso to Section 32(1) would not apply. The tribunal has rightly decided the issue in favour of the assessee and against the Revenue. *2013-TIOL-815-HC-DEL-IT*.

➢ **Application of Sec 54EC if assessee makes investment in tax-free bonds:** The assessee had sold 'Automatic Electric Load Monitoring System', and had invested the gain amount in Rural Electrification Bonds and claimed exemption under Section 54EC. The Assessing Officer found that short term capital gain was offered by the assessee in respect of Automatic Electric Load Monitoring System under Section 50 of the Act. The AO disallowed such exemption on the ground that the same was not available on short term capital gain and invocation of Section 54EC was permissible only on long term capital gain. The Tribunal held in favour of the assessee. Upon appeal, the High Court held that:

- The question to be addressed is whether the exemption permitted under Section 54EC for the depreciable assets, can also be claimed for short term capital gain.
- The exemption available under Section 54EC of the Act is available on short term capital gain arising from transfer of long term capital assets. There is no condition in the provision, which would preclude such interpretation. Admittedly, depreciable assets sold by the assessee were held by it for 10 years and therefore on such sale, investment in Rural Electrification Bond was made.
- Capital gain arising of long term capital asset, if invested in specified asset, the assessee is not to be charged capital gains tax. Exemption provided under Section 54EC of the Act, cannot be denied to the assessee only on account of the fact that deeming fiction is created under Section 50 of the Act. In other words, legal fiction created under Section 50 of the Act is though restricted to computation of capital gains, such deeming fiction cannot restrict application of Section 54EC which allows exemption of capital gains, if assessee makes investment in the specified assets. Thus, the assessee cannot be charged to capital gains when short term gains of long terms capital

assets get invested in the areas specified under the law. *2013-TIOL-806-HC-AHM-IT.*

- **Transfer of shares by holding company to wholly owned subsidiary at book value:** The assesse was a holding company. It had transferred shares held by M/s.EID Parry (India) Limited and M/s.Tube Investments of India Limited to its wholly owned subsidiary company at book value. Noting that the shares were quoted shares and were sold at the price less than the market value, the difference between the market value and the actual consideration was sought to be assessed as deemed gift under the provisions of the Gift Tax Act. The assesse contended that being a transfer from holding company to its subsidiary company, there was no transfer within the meaning of Section 47(iv), and so, there could be no deemed gift arising in this case. Upon appeal, the High Court held that:
  - A subsidiary company, even if 100% wholly owned by the holding company, is an independent entity. The assessee itself recognised that the transfer of shares to the subsidiary company was done at book value.
  - Under Section 47(iv), for the purpose of capital gains, the transfer of capital asset from the holding company to subsidiary company is not treated as a transfer. However, this Section would not apply to a case where no capital gain is involved.
  - Under Section 2(xxiv) of the Gift Tax Act, any transaction entered into by any person with intent thereby to diminish directly or indirectly the value of his own property and to increase the value of the property of any other person is also included within the meaning of transfer of property;.
  - When two companies are treated as two different entities, there arises no necessity for lifting the corporate veil to know the nature of transactions or the existence of two entities. Appeal of the assesse was dismissed. The *2013-TIOL-801-HC-MAD-IT.*

- **Sec 10A benefits to Software Technology Parks:** The assessee was a proprietory concern engaged in Electronic Data Transmission (Data Processing). The assessee's Unit was in operation ever since 1994, and was approved as Software Technology Park by the Government of India, and as 100% Export Oriented Unit for Computer Software since 2002. Considering its status as 100% Export Oriented Unit, the assessee claimed the benefit of deduction u/s 10A of the Act, starting AY 2003-04.

  For the AY 2005-06, the CIT observed that the assessee got registration as Software Technology Park only in 2002, whereas, it had commenced production in the Financial Year 1999-2000 itself. As such, the assessee unit was an existing unit wherein the plant and machinery were used for such purposes. By getting permission from the authority as Software Technology Park in 2002, the assessee had transferred the plant and machinery previously used to the Software Technology Park and the assessee had not registered ever since it commenced production in the Financial Year 1999-2000. In view of the above, the deduction granted was erroneous. Upon appeal by the assessee, the High Court held that:

- The mere fact that the assessee was in existence prior to its date of registration as Software Technology Park, would not disentitle the assessee from claiming deduction under Section 10A of the Act.

- Section 10A of the Act grants 100% deduction on profits and gains derived by an undertaking from the export of articles or things or computer software for a period of ten consecutive assessment years beginning with the assessment year relevant to the previous year in which the undertaking begins to manufacture or produce such articles or things or computer software

- Given the fact that the assessee is not formed by splitting up or transfer to a new business and got registration even since 2002, the fact that it has been in existence ever since 1999, does not go against the applicability of Section 10A of the Act. The Revenue's appeal is rejected. *2013-TIOL-763-HC-MAD-IT*.

Tribunal Judgments

➢ **Reimbursement of cost of software used by a shipping company: Assessee,** a Danish public limited company, was engaged in the business of operation of ships, chartering and other related activities of shipping in international traffic, which was covered under Article-9 of DTAA. Its shipping operation in India was carried out by Maersk India Pvt. Ltd.(MIPL) which was an agent of the assessee. The assessee, in its Return of Income, had shown gross freight earnings as not taxable under the DTAA, as the profits derived from the operation of ships in international traffic, was fully taxable in Denmark. The Assessing Officer observed that income earned by assessee from I.T. support services given to MIPL were taxable.

The assessee submitted that the amount received from MIPL was only recovery of proportionate cost incurred by the assessee for maintenance and up-gradation of a software used in the shipping operations, and therefore, it was in the nature of reimbursement of cost not chargeable to tax in India. It was also submitted that the payment received from MIPL neither constituted *"royalty"* nor "fees for technical services" either under the Act or under the DTAA. Upon appeal, the Tribunal held that:

- The main controversy is with regard to the treatment of amount recovered from MIPL towards software usage which has been developed and maintained by the assessee. This software is a tool and integrated part of shipping operations only. Usage of software cannot be segregated from activities of overall shipping operations, so as to hold it as rendering of any independent technical service.

- Article-9(1) of Indo Denmark DTAA provides that if any activity is directly linked with carrying on shipping operations and results into some kind of an income, then it has to be treated as a part of such shipping operations only. Any kind of receipts recovered by way of software usage / development cost from MIPL cannot be taxed in India under Article-9(1) of DTAA.
- Further, this receipt also cannot be taxed as fees for technical services or royalty independently because in the present case, the assessee is not rendering any service of managerial, technical or consultancy to its agent or group entities. Such a recovery of a cost cannot be held to be fees for technical services. **Revenue's appeal was dismissed. 2013-TII-198-ITAT-MUM-INTL.**

➢ **Adjustment under TNMM method when capacity utilization is low: The** assessee, Indian subsidiary company of M/s Merloni TermoSanitari SpA-Italy (MTS), is a 100 per cent export oriented unit engaged in the manufacture of water heaters. The assessee company was incorporated in November 2004 and started the commercial production of water heaters, etc. in April 2005. The assessee was required to incur certain fixed operating costs and had created huge capacity to cater to the growing demand of water heaters in the export market. However, being the first year of operations, and not being able to generate the required sales, its fixed operating costs were not absorbed due to low capacity utilisation and the assessee had suffered operating losses during the year. Being the initial year of commercial operation, the assessee had declared losses in its return. In the subsequent two years, however, the assessee had earned profits. The assessee had various international transactions with its AEs, including purchase of components and raw materials, sale of water heaters and spare parts besides payment of management fees. The case was referred to the TPO.

The assessee had benchmarked its international transactions on the basis of the Transactional Net Margin Method (TNMM) as the most appropriate method, using operating profits / operating sales as the profit level indicator (PLI). The assessee excluded fixed costs while calculating the operating profits, as it was a start-up company with low capacity utilization in the first year. The assessee concluded that its international transactions were at ALP and no adjustment was required in the value of its international transactions. The TPO accepted TNMM as the most appropriate method but he used the financial data of the comparable companies only for the relevant financial year. Also, while calculating the profit level indicator, the TPO considered operating profits/total cost as the PLI as against operating profits/operating sales as used by the assessee. The adjustments sought by the assessee on account of low capacity utilization and abnormal start-up costs were also denied on the ground that for the purpose of comparability analysis under the TNM method, only those adjustments could be allowed which were in accordance with Rule 10B(1)(e). Upon appeal, **the Tribunal held that:**

- The assessee is a unit which has been set-up during the year and its capacity utilization is only 21%, which has resulted in losses, while its profit margins have been compared with entities established over the years. Ostensibly, such a comparability analysis does not provide a level playing field. In our view, the aforesaid factor is required to be adjusted so as to facilitate a meaningful comparability analysis between the international transactions of the assessee and the comparable uncontrolled transactions.
- As per the Revenue, such an adjustment to the profit margin of the assessee is not permissible under Rule 10B(1)(e). As per the Revenue, in sub-clause (iii) adjustments to the net profit margin are permissible but it is only in relation to the net profit margins of the comparable uncontrolled transactions, and not with respect to the margin of the tested party, and thus the claim of the assessee cannot be allowed. The plea of the Revenue is misdirected.

- The whole objective of adopting the most appropriate method for the purpose of comparability analysis is to examine whether the price charged is comparable to an uncontrolled transaction of similar nature. Therefore, keeping in mind the aforesaid objective, the net profit margin of the tested party drawn from its financial accounts can be suitably adjusted to facilitate its comparison with other uncontrolled entities/transactions as per sub-clause (i) of rule 10B(1)(e) of the Rules itself. The absence of such a specific provision in rule 10B(1)(e)(iii) of the Rules does not operate as a bar, so long as the adjustment sought to be made in the profit margin of the tested party are based on cogent and sufficient reasons and seeks to make the comparability analysis with comparable uncontrolled transactions more meaningful. The appeal of the assessee is upheld. **2013-TII-170-ITAT-PUNE-TP.**

➢ **Section 54F:** The assessee, an individual, had received a plot of land from her father through gift deed. The assessee constructed a bungalow on the said land. The bungalow was dismantled to construct 8 flats. Four flats were retained by assessee for her own use and the remaining 4 flats were sold. On the 4 flats sold, assessee worked out LTCG on sale of land and short term loss on sale of construction of flats and offered the same for tax. The AO considered the construction of flats to be as an adventure in the nature of trade, and therefore treated the income as "business income" and not "capital gains”. The AO also observed that the 4 flats retained by the assessee for her own use were independent units on two different floors, and therefore could not be considered to be a single unit for the purpose of claiming exemption u/s 54F and therefore held that assessee was not eligible for deduction u/s 54F.

Since expenses on demolition were not accounted by the assessee in her books, the AO made an addition of Rs 2 lacs considering the same to be unexplained expenditure made out of income from undisclosed sources. He also noted that the demolition of bungalow would have resulted into generation of timber, steel, copper from electric wires, doors, windows etc. Since no income was reported by the assessee on account of sale of the aforesaid items, he estimated its sale to be of Rs 1 lacs and added it to the income. Upon appeal, the Tribunal held that:

- The assessee was merely an individual who got the property as gift, demolished it and reconstructed it. This transaction cannot be treated as business or adventure in nature of trade, and so the addition to income as "business income" needs to be deleted.

- Since the construction took place prior to the date of transfer, the assessee is not eligible for deduction u/s 54F.

- With regard to the addition made on account of demolition expenses and income from sale proceeds of items extracted from old bungalow, no addition can be made only on the basis of estimation. We thus direct its deletion. *2013-TIOL-947-ITAT-AHM.*

- **Write off of TDS amount as short receipt:** The issue was that when assessee received payments after TDS, and such deduction was deposited in Treasury, whether assessee could still write off such sum as short receipt, merely because it did not receive TDS Certificates from payers. The assessee claimed deduction for this sum, by contending that it was not in a position to recover the TDS certificate from the parties, who deducted tax at source. It was claimed that this amount was nothing but short recovery of the revenue receipts from the payers. The A.O. refused this claim on the ground that it was nothing but payment of income tax which cannot be allowed as deduction. The CIT(A) approved the action of the A.O. On appeal, the Tribunal held that:

  - The parties, on deduction of tax at source, made the payment to the assessee for the remaining amount and duly deposited tax at source with the treasury. Once the assessee received the net amount and further the amount of TDS certificates also stood deposited in the Government exchequer, the position of the assessee vis-à-vis the parties stands neutralized as nothing remains due from them. In such a situation, there can be no question of incurring any business loss or treating the amount of TDS certificates not received as short receipts.

  - Since this amount represents tax deducted at source by the parties on behalf of the assessee, the same is in the nature of TDS receivable. It is settled position that tax payment is not a charge against, but application of income. Section 40(a)(ii) clearly provides that any sum paid on account of taxes on the profits or gains of any business or profession, is not deductible. *2013-TIOL-937-ITAT-MUM.*

- **Business loss:** The assessee was engaged in the business of real estate development. The AO observed that the assessee had started a real estate project and had booked expenses incurred on the project under the head work in progress, as during the year nothing was sold. The assessee had earned an interest income partly from the loan given to sister concern and partly from bank deposits and after claiming various expenses, a nominal net profit was declared. The AO treated the interest income as income from other sources and disallowed the expenses debited in the P&L Account treating them as not related to earning of interest income. Also, the AO held that by not recognizing the income following the percentage completion method, the assessee was deferring its tax liability.

  On Appeal, the Tribunal held that:

  - The income was earned out of surplus funds advanced by the assessee to its sister concern which was not a business activity of the assessee.
  - Even if the income was treated under the head 'income from other sources' still the total income of the assessee would be computed after setting off losses under other sources.
  - The expenses of rent, electricity, printing, telephone conveyance, security expenses, filing fee etc. are common expenses which are required to run a business. So these expenses are allowed to be deducted.

  - The AO cannot force assessee to change the method of accounting specially in a case where in earlier years the method employed by assessee was accepted by Department. *2013-TIOL-925-ITAT-DEL.*

- **Expenses for acquiring shares from parent for allotting ESOP to employees:** Assessee, an Indian subsidiary of a foreign company, was primarily engaged in the marketing and distribution of healthcare products. It filed its Return of Income claiming deduction of certain expenses. The AO observed that employee of the assessee had received shares of parent foreign company on discounted price (ESOP), and the difference between the fair market price and discounted price had been paid by the assessee to its parent company. This difference had been claimed by the assessee as revenue expense. The AO was of the opinion that in the garb of ESOP allotment, the assessee had provided benefit to the parent company and had claimed deduction of capital expenses. Upon appeal, the Tribunal observed that:

- There is no dispute that the liability has accrued to the assessee during the previous year. The only question to be decided is as to whether it is the expenditure of the assessee or that of the parent company.

- The foreign parent company has a policy of offering ESOP to its employees to attract the best talent as its workforce. In pursuance of this policy, the parent company allowed the assessee to issue its shares to the employees. The shares were in fact acquired by the assessee from the parent company and there was an actual outflow of cash from the assessee to the foreign parent company. The difference between the fair market value of the shares and the price at which shares were issued to the employees was met by the assessee. So, there is no basis on which it could be said that the expenditure in question was a capital expenditure of the foreign parent company.

- For the assessee it was an employee cost which is a revenue expenditure, and had to be allowed as deduction. *2013-TIOL-919-ITAT-BANG.*

➢ **Expenditure for acquiring controlling stake in loss-making company:** Assessee was a holding investment company. It had made huge investment in M/s Ambuja Cement Ltd., to acquire the controlling interest in it. Assessee, under section 14A, claimed expenditure. The AO noticed that the business of the assessee was not yet set up and started, therefore, disallowed various expenses claimed in its P&L A/c. Furthe, the assessee had also not disclosed any dividend income from its investment with M/s Ambuja Cements Ltd., as appeared in the balance sheet of the company. Therefore, AO disallowed the expenses claimed in the P&L A/c. On appeal, the Tribunal held that:

- In the present case AO has disallowed the entire expenditure by holding that business of the assessee had not started. However, being a holding company, the business had indeed started when it acquired the shares of M/s Ambuja Cement Ltd.

- Assessee has invested in the company which was not showing profits. The assessee acquired controlling interest in the company just to run it properly. The assessee has submitted that till date no dividend has been earned by the assessee as assessee is doing the business in these companies from the amounts invested through shares. The assessee's case is not a case of disallowance under section 14A. Therefore, the disallowance made under section 14A is being deleted. *2013-TIOL-903-ITAT-DEL.*

➢ **Expenditure incurred towards channel placement charges:** The assessee company was broadcasting news through its four news channels, viz., Aaj Tak, Headlines Today, Dilli Aaj Tak and Tez. The assessee had incurred expenses in respect of channel placement charges which are in the nature of distribution expenses. However, the

AO was of the opinion that the same was for sales promotion and attracted the rigours of fringe benefit tax (FBT). On appeal, the CIT(A) upheld the order of the AO. Upon further appeal, the Tribunal held that:

- Expenditure was incurred by the assessee for channel placement which is made to third persons and there is no employer-employee relationship between the assessee and the recipient.
- In respect of payment to third persons, FBT is not applicable because no fringe benefit is enjoyed by the employee/recipient. The payment is in the nature of expenditure incurred for the purpose of business by the assessee and in the hands of the recipient it is taxable as income.
- The assessee has incurred the expenditure for broadcasting of its channels on the desired bands. Therefore, the expenditure is for the broadcasting of its channels and not for sales promotion or publicity. *2013-TIOL-860-ITAT-DEL.*

SERVICE TAX

Important Circulars/ Notifications

- **Amendment to notification no. 25/2012**: The following clause has been added to the notification No.25/2012-Service Tax dated the 20th June, 2012, namely:-

  "19A. Services provided in relation to serving of food or beverages by a canteen maintained in a factory covered under the Factories Act, 1948 (63 of 1948), having the facility of air-conditioning or central air-heating at any time during the year." *Notification No. 14/2013-Service Tax New Delhi, 22nd October, 2013.*

- **Income-tax deduction from salaries during FY2013-14:** In the Circular No.08/2012 dated 05.10.2012, the rates of deduction of income-tax from the payment of income under the head "Salaries" under Section 192 of the Income-tax Act, 1961(hereinafter 'the Act'), during the financial year 2012-2013, were intimated. The present Circular contains the rates of deduction of income-tax from the payment of income chargeable under the head "Salaries" during the financial year 2013-2014 and explains certain related provisions of the Act and Income-tax Rules, 1962 (hereinafter the Rules). The relevant Acts, Rules, Forms and Notifications are available at the website of the Income Tax Department- *www.incometaxindia.gov.in. Circular No. 08 /2013 New Delhi, dated the 10th October, 2013*

CESTAT JUDGMENT

- **Market research on behalf of overseas customers:** The appellant was engaged in conducting market research on behalf of certain customers situated abroad. After conducting the market research, the results were communicated to the clients abroad and consideration for the said service received in convertible foreign exchange. Since the results of such market survey were being sent abroad and the amount was being received under the convertible foreign exchange, the appellant contended that the service was being exported and hence no tax was leviable in India.

  Revenue contended that the whole of the service was provided in India and just because the results of the service had been communicated abroad, it was not implied that the service had been provided abroad. The taxing event is not the consumption of service but the provision of service and since the service had been provided in India, it was liable to pay service tax. Upon appeal, the Tribunal observed:

  In view of the Board Circular dated 25.4.2003, the services rendered by the appellant have to be considered as export of service and would not be liable to service tax. *2013-TIOL-1667-CESTAT-MUM.*

- **Method of disbursement of salary cannot determine nature of transaction:** The appellant employed personnel belonging to its group company in Germany for a specific period. During this period, the appellant entered into agreements with the personnel for their employment. Since the personnel employed were foreign nationals, about 25% of the salary was paid in India in Indian currency and the balance 75% was paid by the group company in Germany to the credit of accounts of the personnel employed and thereafter, debit notes were raised on the appellant by the foreign entity towards reimbursement of the salary paid in Germany. For the income earned in India by the personnel, the appellant also discharged the Income Tax liability showing the personnel employed as their own employee.

  The Central Excise department was of the view that the transaction involved comes within the purview of ‘Manpower Supply or Recruitment Agency services' and for the amount remitted to the German entity for payment of salary to the personnel employed in India, a show-cause notice was issued demanding Service Tax thereon. The appellant contended that the personnel employed by it remained its employees during the period of the agreements and, therefore, there is no supply of manpower by the German entity. Since the employees are foreign nationals, part of their salary is paid in Germany through the group company. Upon appeal, the CESTAT Bench observed:

  - The global employees working under the appellant are working as its employees and having employee-employer relationship.

- There is no supply of manpower service rendered to the appellant by the foreign company. The method of disbursement of salary cannot determine the nature of transaction. The appellant's appeal is upheld. *2013-TIOL-1640-CESTAT-MUM.*

➢ **Adjustments in respect of volume discounts and other rebates:** Applicant provided port service and paid Service Tax, after adjusting for the amount, which it thought did not qualify to be taxed as per provisions of Rule 6(3) of the Service Tax Rules, 1994.

The Revenue submitted that the adjustment can be done only in respect of the service which was not provided by the service provider and the amount of service tax had been refunded to the person from whom it was received. In the present case the applicant was giving some volume discounts and other rebates and the ST paid on such amount was adjusted against the payment of service tax for subsequent period, which was not permissible. The appellant contended that in respect of the amount of adjustment, verification was conducted by the Deputy Commissioner of Service Tax, and as the applicant had refunded the amounts of service tax collected from the service recipient by way of credit notes, therefore, the adjustment was permissible and the demand was not sustainable. The CESTAT Bench observed:

- As per the provisions of Rule 6(3) of the Rules, the adjustment in respect of excess service tax paid is only in respect of the services which are not provided by the service provider.

- In the present case, the adjustment is not in respect of services which are not provided rather it is by way of discounts and rebates. In view of this, total waiver of service tax cannot be upheld. *2013-TIOL-1633-CESTAT-MUM.*

➢ **Online registration fee:** The appellant was registered as provider of "on-line information and database access or retrieval or both". It was observed that the registration fee collected by the appellant was not declared in the ST-3 returns filed by it. Before the CESTAT Bench, the Revenue representative submitted that the registration fee collected by the respondent was part of the value of taxable service provided, on which the respondent was liable to pay service tax. Since the registration fee was not refundable and was to be adjusted in the first purchase of the goods by the clients and if no purchase was made the registration fee was not to be refunded, so service tax was payable on it.

In the matter of the demand being time barred as held by the lower appellate authority, it was submitted that the registration fee collected from the client was never declared to the department nor reflected in the ST-3 returns filed by the respondent and it was only during verification of records that the fact came to notice. The Bench held:

- The registration fee is required to be added to the gross value of taxable service on which the respondents are liable to pay service tax.
- By not disclosing the fact regarding collection of registration fee in the ST3 returns, the allegation against the appellant, of suppression with intent to evade tax is also sustainable. *2013-TIOL-1598-CESTAT-MUM***.**

➢ **Commission received from Multilevel Marketing:** The appellant entered into an agreement with M/s Fashion Suitings Pvt. Ltd., Bhilwara, Rajasthan (FSL) for the purpose of selling the company's product as per the RCM - Right Concept Marketing - Business Marketing Plan. According to terms and conditions of the agreement between the parties, a distributor gets commission on the supply made by FSL and also a share in the commission for introducing new customers. Thereafter, when a new customer starts using FSL products they in turn will propagate FSL products to other persons and the distributor gets commission in respect of purchases made by such introducees, down the line. He shares the commission with others on such purchases. Consequently FSL sales are boosted. Minimum purchases, in terms of RCM products prescribed by the company from time to time, is compulsory for a distributor during the month in which he desires to have the commission credited in his account. Company is obligated to remit consideration to the distributor for selling the company's product as per terms of conditions specified in the agreement.

The Department contended that the commission received by the appellant under this scheme, constituted consideration paid by the service receiver FSL, and so service tax was payable on it. Upon appeal, the Bench observed:

- This is a clear Multilevel Marketing Service Scheme. The consideration/commission received by the appellants from FSL is the result of the marketing/promotion of FSL products by the appellants and constitutes a service (Business Auxiliary Service), as defined under Section 65 (19) of the Act.

- Hence service tax is payable on the commission paid to the appellant. *2013-TIOL-1582-CESTAT-DEL.*

➢ **Finishing services for new / old building:** The applicant had undertaken interior work at 9th floor of a multi-storey building in Mumbai, and the Department had ruled that as per Sec 65(25b) this was a taxable Service ('Commercial or Industrial Construction service'). The applicant contended that it had only undertaken interior renovation of a *part* of the building, and so it could not be held liable for providing commercial or industrial construction service, hence the demand is not sustainable. Upon appeal, the Bench observed:

- As per the definition, construction of new building or civil structure, or part thereof, is covered under the scope of taxable service.

- In respect of repair, alteration, renovation or restoration, it is specifically mentioned that it is in relation to building or civil structure. There is no mention in the definition 'part thereof' in sub-clause (d) of the definition. In view of this, prima facie we find that the applicant has a strong case in its favour. *2013-TIOL-1576-CESTAT-MUM***.**

➢ **Services received in India by person situated in India, having PE abroad:** The appellant was engaged in providing various services including Software Development & Consultancy Service. It had branch offices in three countries outside India, which provided services to overseas customers. The consideration for the services rendered abroad were received by the branches who raised bills on the customers. After deducting the expenditure incurred for rendering the services abroad, excess of income over expenditure of the branches was remitted to their head office in India.

The Department was of the view that the services rendered by the overseas branches on behalf of the parent-company fell under the category of 'Business Auxiliary Service' and accordingly, the entire amount received by the overseas branches was liable to service tax. The Appellant submitted that the branches were not independent entities and they were part of the appellant's organization and, therefore, if the branches had undertaken service to the overseas customers, it was not to be considered as service received by the appellant as there cannot be a service to self. Even if it was held that the appellants had rendered the service, since service had been rendered to the overseas customers, it amounted to export of service. The Bench observed:

- The provisions of Section 66A are attracted only when services are received in India by a person situated in India even if such persons may have permanent establishment abroad. In the present case, the appellant had provided services through their branches abroad to customers located abroad. Therefore, it was not a case of the appellant receiving the services but it was a question of rendering services abroad. Therefore, prima facie, provisions of Section 66A are not attracted.

- If the services rendered abroad had been subject to local taxation, the question of levying service tax in India on the very same transactions would not arise. The appellant has assured that it would provide evidence regarding payment of GST/VAT on the services rendered abroad if given the opportunity.

- Even if the appellant had received the service from abroad from its branches, since the service had been consumed by the clients abroad, it would amount to export of service under Rule 3 of the Export Service Rules, 2005 in which case also there would not be any service tax liability.

- The matter has to go back to the adjudicating authority for consideration afresh. *2013-TIOL-1568-CESTAT-MUM.*

➢ **Electroplating of connector components on job-work:** The appellant was engaged in the manufacture of various electric and electronic goods. Besides undertaking manufacture on its account, it had also undertaken job-work of electroplating of connector components for M/s. Tyco Electronic Corporation India Pvt. Ltd. The appellant was availing the benefit of Notification No.8/2005 on the ground that it was engaged in the manufacture of these goods and was supplying the same to M/s. Tyco Electronic. However, the department took a view that the appellant should have discharged service tax on the electroplating cost including the cost of electroplating materials used by the appellant.

The appellant contested that the contention of the revenue that the process does not amount to manufacture and therefore it has to be classified as a service under 'business auxiliary service' is not correct. Electroplating of electrical contacts on job work basis is a process incidental or ancillary to the completion of manufacture and amounts to manufacture. As per Section 16(6) of the Schedule to the Central Excise Tariff Act, conversion of an article which is incomplete or unfinished but having the essential character of the complete or finished article, shall amount to manufacture. Upon appeal, the Bench observed:

- As per Sec 16 (6) of the Central Excise Tariff, the activity performed by the appellant was 'manufacture', and therefore it was not liable to pay service tax in view of the specific exclusion in the definition of 'business auxiliary service' which provides that if the process amounts to manufacture, no service tax would be liable to be paid.

- Notification No.8/2005-ST provides for exemption from service tax to the goods produced on behalf of the client, provided, such exemption is allowed only when such goods are used by the principal manufacturer, or further manufacture of other goods on which appropriate duty of excise is payable. The Notification also defines 'appropriate duty of excise' and that it cannot be 'nil' rate of duty, or duty of excise wholly exempt. The Notification when read with the 'appropriate duty of excise' would mean that only when the goods manufactured by the principal manufacturer attract 'nil' rate of duty as per tariff or unconditional full exemption, the benefit of Notification No.8/2005 is denied. In this case, the 100% EOU viz., M/s. Tyco Electronics to whom the appellants have supplied the goods on job work basis is eligible for exemption Notification No.24/2003-CE dated 31.3.2003. It is the stand of the department that this notification exempts 100% EOU from payment of duty and therefore the appellant is not eligible for the benefit of Notification No.8/2005-ST. We find that Notification

No.24/2003-CE dated 31.3.2003 has a proviso which reads as under:

"Provided that the exemption contained in this notification in respect of duty of excise leviable under Section 3 of said Central Excise Act shall not apply to such goods if brought to any other place in India."

This clearly shows that this is not an unconditional exemption notification. Exemption is available only if the goods are not brought to any other place in India. Since exemption under Notification No.24/2003 is not an unconditional exemption, we find that the appellant has a case for eligibility for exemption under Notification No.8/2005 also even if it is assumed that the process does not amount to manufacture. *2013-TIOL-1493-CESTAT-BANG*.

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