Tax News

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INCOME TAX

Reminder For September'10

Action Due	Due Date
TDS/TCS for the month of August'10	07-09-10
PF for the month of August'10	15-09-10
ESI for the month of August'10	21-09-10

SERVICE TAX

Reminder For September'10

Action Due	Due Date
Service Tax for the month of August'10 in case of company	05-09-10
Service Tax for the month of August'10 in case of company for which e-payment is mandatory	06-09-10

INCOME TAX

Recent decisions of Supreme Court / High Court

- **TDS on Interconnection services:**

Assessee - M/s Bharti Cellular Ltd - was a cellular service provider. It entered into Interconnect agreement with BSNL/MTNL, and paid port charges for availing such services. Under the National Standards, the assessee is required to connect its network with the network of BSNL (the service provider), and similar concomitant agreement is provided for, under which BSNL interconnects its network with the assessee.

The issue was whether or not, provisions of TDS are applicable to interconnection charges paid by cellular companies for availing technical services, and whether such port services provided by the PSU telecom companies to the assessee involved any human element, so as to make it qualify as technical services.

On the above issue the court held that:

- These issues need technical expert's assistance to conclude whether there was any human intervention when calls take place. Similarly, questions like - on what basis is the "capacity" of each service provider fixed under Interconnect Agreements? On what basis such "capacity" is allotted and what happens if a situation arises where a service provider's "allotted capacity" gets exhausted and it needs "additional capacity"? – need to be answered.
- The Interconnect Agreement in these cases is based on obligations and counter obligations, which is called a "revenue sharing contract". The assessee contended that Sec 194J of the Act is not attracted in the case of "revenue sharing contract" because there is only sharing of revenue and did not cover "fees" under Section 194J of the Act.
- The Assessing Officer (TDS) directed each of these cases to be examined by a technical expert from the side of the Department and to decide the matter within a period of four months. Therefore interest and penalty are not justified at this stage.

CIT Vs Bharti Cellular Ltd (2010-TIOL-65-SC-IT)

- **Consistency in accounting:**

An assessee who was a developer cum contractor adopted a consistent method of not taking into account the work in progress, but claimed it in the year when the work in progress was apparently paid for. It was held that any disturbance of the system would require adjustment of income for earlier years. Therefore it was not open to the assessee to disturb the consistent method of accounting followed by the assessee.

Krishna Gopal Kapoor and sons (2010) 325 ITR 214(All)

- **Taxability of forfeited amount paid for distribution rights:**

Assessee paid some amount for acquiring distribution rights of a product of a company, but company failed to produce the article and also did not repay the deposit which the assessee wrote off in its accounts and claimed as revenue expenditure. It was held by the High court that it was a capital expenditure.

Cochin Malabar Estates and Industries Ltd. v. CIT (2010) 325 ITR 129 (Ker)

Recent decisions of Tribunal

- **TDS U/S 194C**:

The issue was whether the liability to deduct tax at source u/s 194C arises on payments made towards reimbursement of expenses incurred for manufacturing of goods to be exported against a time deadline. Whether or not the arrangement between the assessee and the company lending its manufacturing facility was a contract and thus provisions of Sec 40(a)(ia) are applicable to the payments made for using the manufacturing facilities.

Assessee was in a business of export and due to heavy export orders that needed to be executed timely, the manufacturing facilities of M/s. Sarita Handa Exports were used for which the expenses in the nature of salaries, power & fuel and electricity were reimbursed to it.

The AO contended that it was a case of contract between two parties and therefore, provisions of section 40(a)(ia) were equally applicable to all contracts oral or written. Since the assessee had not deducted tax at source on reimbursement of expenses, the expenditure was not allowable as deduction.

But Tribunal held that since for the AY 2006-07 there was no provision to deduct TDS on contract amounts by the individuals or Hindu Undivided Family, the assessee was not liable to deduct tax at source u/s 194-C of the Act from the contractor for carrying out the work. Therefore, the assessee was not liable to deduct tax at source from the payments made by it to the company. Since the assessee was not liable to deduct tax at source, provisions of section 40(a)(ia) of the Act were not applicable.

Mrs.Sarita Handa Vs ACIT (2010-TIOL-440-ITAT-DEL)

- **Business Expenditure:**

It was held by the Tribunal that wrong classification and capitalization of expenses, would not disentitle the assessee from valid claim of revenue expenses. In the aviation crew training business, it needs frequent renovations, paintings and training requirements. False ceiling will constitute temporary structure apart from mock air-craft for training of employees which also have to be renewed from time to time. Polishing and painting also will constitute revenue expenses.

Frankfinn Aviation Services Pvt Ltd Vs DCIT (2010-TIOL-434-ITAT-DEL)

- **Allowability of commission paid to C&F agents through credit notes:**

The assessee paid the commission through credit notes to C& F agents, and made the actual payment subsequently. It was held that commission should be allowed on the basis of credit notes as the assessee was following mercantile system of accounting.

Meghdoot Village Products (P) Ltd. v. CIT (2007) (162 Taxman 25)

- **Depreciation:**

The issue arises 'whether air-conditioner, refrigerator and office equipments are in the nature of furniture and fixture or plant and machinery, for the purpose of applying rate of depreciation allowable under the Act. Whether Software Expenditure & up-gradation expenses for server are recurring expenditure having no enduring benefit and therefore, the expenses are to be allowed in full as revenue expenditure. Whether expenditure on Repairs and Maintenance of building are in the nature of capital expenditure so as to be disallowed.

Tribunal Held:

a. To decide whether the particular asset is plant or not, it should fulfill the function of a plant in assessee's trading activity or should be the tool of its trade, and if it is so, then it is plant, no matter that it is not very long-lasting or does not contain working parts such as a machine does and plays a merely passive role in the accomplishment of the trading purpose. In this view of the matter, assessee was entitled to rate of depreciation, applicable to the block of plant and machinery.

b. All the software programmes acquired by the assessee were necessary for operating the system and no new asset of enduring benefit came into existence. Also, the licence to use computer software was not transferred as such to the assessee. The server software, which was purchased by the assessee, was to be updated from time to time. Therefore software expenses should be treated as revenue expenditure.

The assessee has upgraded the server for better functioning of its business activities. Upgradation of the server did not bring any enduring benefit to the assessee. Considering the ownership and the function of such expenditure, this expenditure cannot be treated as capital and hence in view of the Delhi High Court's decision in the case of Sumitomo Corporation India Pvt. Ltd. Vs. CIT, it is to be allowed as revenue expenditure.

c. It was held that the assessee has spent the amount towards repairing and maintenance of the building which was already in existence. No new structure was put up. So it was allowed as revenue expenditure.

ACIT Vs Voith Paper Fabrics India Ltd (2010-TIOL-427-ITAT-DEL)

- **Capital Gain:**

The assessee was an owner of land and sold it to IOC. Assessee offered capital gain based on actual sale consideration received by it. However the registering authority valued the property according to the guidelines and asked to pay stamp duty accordingly. Assessing authority passed an order and demand tax on the basis of value adopted by registering authority instead of waiting for valuation of valuation cell. It was held that assessee must be given an opportunity to take advantage of the valuation report to be filed by the valuation department.

N. Meenakshi v. ACIT (2010) 326 ITR 229 (Mad).

- **Treatment of Depreciation to calculate book profits:**

Assessee made book profits u/s 115J of the Act. Assessee did not claim depreciation in its a/cs but in notes to accounts a precise amount of depreciation was mentioned to which assessee was eligible. Assessee claimed such depreciation in computation of book profits. It was held that it was allowed since the accounts for the purpose of book profits as computed in sub section (1A) of section 115J required that depreciation should correspond to the provisions of part II of schedule VI of the companies act.

Sain Processing and weaving Mills P. Ltd. v. CIT (2010) 325 ITR 565 (Delhi).

- **Remission of liability:**

There was an outstanding liability in the books of the assessee. The assessee failed to prove the existence and genuineness of such liability. It was held that where a liability, shown as a carried forward item of credit in the balance sheet in a later year is not found to be genuine, the proper course is to take reassessment proceedings for the year in which it was first credited, and not in a later year, since what was not genuine in a later year could not have been genuine in the year it was booked as a liability.

CIT vs. GP International Ltd [2010] 325 ITR 25 (Punj & Haryana).

SERVICE TAX

Vital Notifications / Changes

Service tax on commission received by Primary Dealers dealing in Government Securities:

- In this notification, clarification has been given, whether or not, service tax is leviable on the underwriting commission received by the Primary Dealers for the auction of Government Securities:

- Underwriting service is taxable under section 65 (105) (z) of the Finance Act, 1994. The term 'underwriting' [section 65 (117)] has the meaning assigned to it in clause (g) of rule 2 of the SEBI (Underwriters) Rules, 1993.

- The term "underwriter" as in section 65(116) has been borrowed from rule 2 (f) of the SEBI (Underwriters) Rules, 1993.

- 'underwriter' or 'underwriting' is about dealing in securities of a body corporate.

- The related issue requiring resolution is whether dealing in government securities amounts to dealing in securities of a body corporate, particularly since government securities are issued by the Reserve bank of India, which is a 'body corporate' in terms of section 3 (2) of the RBI Act, 1934.

- Government securities are sovereign securities having zero default risk. RBI only manages the issue and also auction of Government Securities on behalf of the Government of India. In effect, Primary Dealers registered with the RBI (as opposed to registration with the Securities Exchange Board of India) deal in Government Securities, issued by the RBI on behalf of the Government of India, as a part of the central Government's market borrowing program. The general practice is that the RBI invites bids from the Primary Dealers, who in their bids indicate the amount to be underwritten and the underwriting fee expected by them. RBI examines these bids and decides the amount to be underwritten and underwriting fee to be paid to a Primary Dealer. Underwriting Fee is also known as Underwriting Commission in common parlance. Thus the conclusion drawn is that government securities are not securities of a body corporate.

- As the service tax law stands today, service tax liability does not arise on Underwriting Fee or Underwriting Commission received by the Primary Dealers during the course of the dealing in Government Securities.

Circular No.126/08/2010 – ST dated 10th August 2010.

Applicability of Service tax on commercial training and coaching:

Clarification was required, whether donations and grants-in-aid received from different sources by a charitable Foundation imparting free livelihood training to the poor and marginalized youth, will be treated as 'consideration' received for such training and subjected to service tax under 'commercial training or coaching service'. It was clarified that donation or grant-in-aid is not specifically meant for a person receiving such training or to the specific activity, but is in general meant for the charitable cause championed by the registered Foundation. Between the provider of donation/grant and the trainee there is no relationship other than universal humanitarian interest. In such a situation, service tax is not leviable, since the donation or grant-in-aid is not linked to specific trainee or training.

Circular No.127/09/2010 – ST dated 16th August 2010.

Service tax on on-going works contracts entered into prior to 01.06.2007:

It has been brought to the notice of the Board that the following confusions/disputes prevail with respect to long term works contracts that were entered into prior to 01.06.2007 (when the taxable service, namely, Works Contract came into effect) and were continued beyond that date:

- Prior to the said date services like Construction; Erection, Commissioning or installation; Repairs etc., were classifiable under respective taxable services even if they were in the nature of works contract. Would the classification of these activities undergo a change?

- Whether in such cases of continuing contracts, the Works Contract (Composition Scheme for payment of Service Tax) Rules, 2007 under Notification No. 32/2007-ST dated 22/05/2007 would be applicable?

- As regards the classification, with effect from 01.06.2007 when the new service 'Works Contract' service was made effective, classification of aforesaid services would

undergo a change in case of long term contracts even though part of the service was classified under the respective taxable service prior to 01.06.2007. This is because 'works contract' describes the nature of the activity more specifically and, therefore, as per the provisions of section 65A of the Finance Act, 1994, it would be the appropriate classification for the part of the service provided after that date.

- As regards applicability of composition scheme, the determining factor would be whether such a contract satisfies rule 3 (3) of the Works Contract (Composition Scheme for payment of Service Tax) Rules, 2007. This provision requires that the option to choose the scheme be exercised prior to payment of service tax in respect of a particular works contract. Once such an option is made, it is applicable for the entire contract and cannot be altered. Therefore, in case of a contract where the provision of service commenced prior to 01.06.2007 and any payment of service tax was made under the respective taxable service before 01.06.2007, the said condition under rule 3(3) was not satisfied, and thus, no portion of that contract would be eligible for composition scheme. On the other hand, even if the provision of service commenced before 01.06.2007 but no payment of service tax was made till the taxpayer opted for the composition scheme after its coming into effect from 01.06.2007, such contracts would be eligible for opting of the composition scheme.

Circular No. 128/10/2010-ST dated 24th August 2010.

Recent decisions of SCs/HCs

- **Taxability in case consulting engineer services provided by a foreign service provider:**

Assessee was a foreign company, which entered into a technical assistance agreement with one M/s. Stanzen Toyotetsu India Private Limited (Indian company). It provided consultancy/technical assistance and transfer of technical know-how relating to the manufacture of automobile components to the Indian company.

It was held that definition of the 'Consulting Engineer' u/s 65 (31), was amended w.e.f 1/5/2006 and the charge of service, on service received from outside India, under Section 66-A of the Act, was amended w.e.f. 18/4/2006. Therefore, as the assessee was a foreign company and a service provider, from the date of the aforesaid amendments, the service receiver would be liable to pay the service tax and the assessee was not liable to pay any tax prior to that.

2010-TIOL-584-HC-KAR-ST in Service Tax.

Recent decisions of CESTAT

- **Taxability of activity of procuring customers from foreign principal:**

It was held that where assessee was not engaged in collecting and receiving goods of the foreign principal but it was engaged in procuring the customers for the foreign principal, the nature of activities of the assessee would not come under the scope of C& F agent.

Acer India Pvt. Ltd. v. CST (2010) 6 Taxman.com 43.

- **Taxability of airport services eg royalty for space etc.:**

M/s Cochin International Airport Ltd, (CIAL) was provider of various categories of services to the Air Passengers and was duly registered with the Central Excise Department in relation to services such as Storage & Warehousing, Cargo Handling, Tour Operator and Airport Service and was paying Service Tax at the appropriate rate and also filing the ST-3 Returns for the respective periods in time. "Airport Services" has been defined as "any service provided to any persons by airport authority or any person authorized by it, in an Airport or a Civil enclave". Under Section 67 of the Finance Act 1994 as amended, the value of any taxable service shall be the gross amount charged by the service provider for such service, rendered by him.

On verification of the financial accounts of CIAL, it was noticed that it had accounted income from various agencies for providing different categories of services as given below:

A. Royalty charges

B. Licence fee on: *(1) advertising (2) cargo agents building (3) car park (4) for space (5) from shops (6) for garbage disposal (7) restaurant/ snack bar (8) from telephone operators (9) vending machine (10) catering services (11) facilitation counter*

C. *Income from entry ticket charges*

D. *Income from guest room*

E. *Income from issue of commercial pass*

F. *Income from courtesy coach parking*

G. *Income from surcharge on pre-paid taxi*

On scrutiny of the Service Tax Returns furnished by M/s. CIAL it was noticed that it had not taken into consideration the service charges received by it as royalty, licence fee, and other income stated above, for the purpose of arriving at the taxable value of the service provided by it for payment of service tax. As a result, various show cause notices were issued.

The lower authorities confirmed the demand and upheld the imposition of penalties and the interest demanded on the appellants. The matter is before CESTAT. The Tribunal observed:

1. Royalty Charges: Tax liability on the royalty charges collected by the appellants from M/s Air India for the services rendered by M/s Air India at the CIAL. As per the said agreement entered by the appellant with Air India, Air India has been given exclusive contract to perform ground handling services including passengers handling, ramp handling and cargo flight handling including loading of cargo etc. The appellant is required to provide facilities like runway for landing and take off, Security services, Passenger facilities etc. It is also seen that Air India is collecting service tax from various Airlines and is discharging service tax liability on such amounts collected by them for the services rendered by M/s Air India. It is abundantly clear from the certificate dated 28/1/2008 issued by M/s Air India that as per the CBEC circular dated 17.9.2004, services provide to various air lines and other facilities at the airport which needs to be managed by the appellant, has been contracted out to Air India and they have discharged the service tax liability on gross amount collected. It is not in dispute that the said services have been rendered by M/s Air India in the place of the appellants. This being the factual matrix, the royalty charges collected by appellants from M/s Air India can be construed as an amount for lease or rental charges for functioning in the appellant's area.

   Hence it was held that the service tax liability on amounts collected from M/s Air India in any form would not arise.

2. Royalty charges collected from M/s Thomas Cook, Atlas Jewellery and M/s BPCL**:** The agreement clearly indicates that the amounts are paid by M/s BPCL, Thomas Cook and Atlas Jewellery for the space allotted to them by CIAL on lease for a specified term. From the agreement which has been entered with M/s BPCL, that particular piece or parcel of land in the Air Port area has been given to them for construction/fabrication of tanks wherein the aviation fuel is

stored. The said agreement could clearly be classified as an agreement for lease or rent. On perusal of the agreement between the appellant and Thomas Cook Ltd., it is found that the said agreement is for operation of foreign exchange counters within the airport enclave. It is seen that as a consideration for the licence granted, the said Thomas Cook pays a fixed amount of Rs 5000/- as license fee and a further amount as percentage on gross foreign exchange turnover recorded by them in the Air Port. It is also seen that this licence is for a specified period. From the agreement, it is seen that all the licensees are required to pay municipal rates and taxes and other statutory levies by the State or any other Authority under the law. This would indicate that the licensees i.e. M/s Thomas Cook, Atlas Jewellery etc., have taken the area on lease and as per the CBEC Circular dated 17.9.2009, such charges would not be subject to service tax as the activity of letting out premises is not rendering services.

3. Licence fee charged by the appellant on advertising, cargo agency, car parking, space, shops, restaurant/snack bar, telephone operator, vending machines, catering services facilitation counter are also on the same lines. These charges cannot be considered as the charges which have been collected by the appellant from other service providers for services rendered definitely with the airport services. The entire tenor of the agreements entered by the appellant with the other parties clearly speak of letting out/leasing out the space in the Cochin International Air Port for a specified term, renewable or being leased out to any other bidder.

4. As regards the service tax liability on the garbage disposal, the said garbage disposal is collection of garbage like waste material, discarded items scrap from the Air Port premises. Though there is no agreement provided for this, the explanation given by the appellant in the appeal indicates that these are nothing but sale of garbage from the Air Port premises. Even this activity would not be liable to service tax.

5. As regards courtesy coach parking and surcharge on prepaid taxi, these activities would definitely be covered as services which are being rendered by the appellant. There is no justifiable reason given by the appellant for non inclusion of this amount for discharge of the service tax liability. As regards the tax liability on the income from the guest room**,** the guest room charges are realized from the passengers who are accommodated in the guest rooms due to contingencies. This accommodation is provided only to the passengers who have been issued with boarding passes and tickets and this facility is not open to others. The amount so collected would definitely fall within the purview of the services provided under the category of Air Port Services.

6. Service Tax liability on income from entry ticket charges and income from issue of commercial passes: These charges are charged by the appellant for restricting the entry to public into the Air Port. The said income is not in respect of any services rendered by the appellant as an Air Port Authority. This amount collected and shown as income could not be construed as services rendered, and therefore, is not liable to service tax**.**

2010-TIOL-1043-CESTAT Bangalore.

- **Commercial coaching service**:

The assessee was engaged in providing commercial coaching service to students, collecting advance coaching fee for the period July 2003 to March 2004. This service became taxable w.e.f 1st July 2003. The assessee neither took registration nor deposited the service tax on the advance received for taxable services provided by it. It was held that in a situation where the payment for the service to be provided had been received in advance, the liability to pay tax would be on 5th of the month immediately following the calendar month in which service was provided.

Ashok Singh Academy v. CCE (2010) 29 VST 579 (New Delhi).

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