Tax News

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INCOME TAX

Reminder for Nov-2012

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INCOME TAX

Important Circular / Notification

Income Tax rules: This Circular contains the rates of deduction of income-tax from the payment of income chargeable under the head "Salaries" during the financial year 2012-13 and explains certain related provisions of the Income-tax Act, 1961 and Income-tax Rules, 1962. The relevant Acts, Rules, Forms and Notifications are available at the website of the Income Tax Department- *www.incometaxindia.gov.in. Circular no. 8/2012 [F.NO. 275/192/2012-IT(B)], DATED 5-10-2012.*

TDS on Payments to Contractors: Representations have been received from various sections of the Industry on the difficulties faced in the matter of Tax Deduction at Source on Gas Transportation Charges paid by the purchasers of Natural gas to the sellers of gas. The matter has been examined by the Board.

The main stakeholders in this Industry are the - Owners/Sellers of the gas (which could be a Gas Distribution Company), Transporters of gas (which could be the Owners/Sellers of the gas or a third party/parties) and the Purchasers/ end-users of the gas. The Owner/Seller of the gas may transfer the ownership of the gas to the purchaser either at the point of delivery at the premises of the purchaser or at any intermediate point.

It is clarified that in case the Owner/Seller of the gas sells as well as transports the gas to the purchaser till the point of delivery, where the ownership of gas to the purchaser is simultaneously transferred, the manner of raising the sale bill (whether the transportation charges are embedded in the cost of gas or shown separately) does not alter the basic nature of such contract which remains essentially a 'contract for sale' and not a 'works contract' as envisaged in section 194C of the Act. Hence in such circumstances, provisions of Chapter XVII-B of the Act are not applicable on the component of Gas Transportation Charges paid by the purchaser to the Owner/Seller of the gas. The use of different modes of transportation of gas by Owner/Seller will not alter the position.

Transportation charges paid to a third party transporter of gas, either by the Owner/Seller of the gas or purchaser of the gas or any other person, shall continue to be governed by the appropriate provisions of the Act and TDS shall be deductible on such payment to the third party at the applicable rates. *Circular No. 9/2012 [F. No. 275/11/2012-IT(B)], dated 17-10-2012.*

National Institute of Ocean Technology, Chennai: It is hereby notified that the organization National Institute of Ocean Technology, Chennai has been approved by the Central Government for the purpose of clause (ii) of sub-section (1) of section 35 of the Income-tax Act, 1961 [said Act], read with rules 5C and 5E of the Income-tax Rules, 1962 (said Rules), from assessment year 2011-12 onwards in the category of "Scientific Research Association", engaged in research in science subject to certain conditions mentioned in the *Notification No. 45/2012 [F. NO. 203/51/2011/ITA-II], dated 29-10-2012.*

Amendment in Capital Gains scheme: In exercise of the powers conferred by sub-section (2) of section 54, sub-section (2) of section 54B, sub-section (2) of section 54D, sub-section (4) of section 54F, sub-section (2) of section 54G and sub-section (2) of section 54GB of the Income-tax Act, 1961 (43 of 1961) the Central Government has made amendments to the Capital Gains Account Scheme, 1988, the details of which, are given in *Notification No. 44/2012 [F.No. 142/21/2012-SO (TPL)], dated 25-10-2012.*

SC / HC Judgments

Receipt of Gifts on Capital account: The appellant was running 3 health clinics in Mumbai in the name of M/s. Kayakalp International. In March 1996, a search was conducted u/s 132 of the Act at the three clinics and residential premises of the appellant. During the course of the search, it was noticed that the appellant received substantial gifts from certain Non Resident Indians out of their Non Resident External Accounts during the assessment years 1994-95, 1995-96 and 1996-97. The AO completed the assessment for the block period 01.04.1985 to 26.03.1996, determining her total undisclosed income at Rs.2.11 crores. This was computed on the basis of unexplained cash credits, commission received on advertising, unexplained loans, undisclosed investments in properties, gifts from Resident Indians and Non Resident Indians etc. Upon appeal, the Tribunal deleted all additions made to the income by the AO except the following two additions: (a) Gifts received from Non Resident Indians from their NRE accounts and cash premium paid thereon for the assessment year 1994-1995 and 1995-1996 and (b) Commission received from an Advertiser for the assessment year 1993-94 up to 1996-1997. On further appeal by the Revenue, the High Court held that:

- Where the income has not been disclosed and the same has been revealed during the search proceedings, there, the block assessment as provided under Chapter XIVB of the Act would certainly apply.
- The burden of proof is on the assessee u/s 158BB(3) of the Act to satisfy the AO that the so called undisclosed income has already been disclosed in the return of income filed by the assessee. Mere mentioning of an amount as capital receipt in the Capital Account would not amount to a disclosure of income. This is so, as a capital receipt is not income and consequently not subject to tax.

- AO and the Tribunal had found that the amounts shown as gifts were not genuine gifts, but were mere credits taken so as to evade payment of income tax. Therefore, the non-genuine gifts to the appellant was undisclosed income

and covered by the definition provided in Section 158B(b) of the Act.

- The appellant had contended that only the evidence found during the search can be a basis for block assessment. U/s 158BB(1) of the Act, an AO has to compute the undisclosed income for the block period in accordance with the provision of the Act on the basis of evidence found, as a result of a search or other documents or materials available with the AO and relatable to such evidence. Thus, information available with the AO prior or after the search is also certainly evidence which can be used to compute the undisclosed income for the block period. *2012-TIOL-820-HC-MUM-IT.*

Lease amounting to Sale of Property: Lease deed was executed between the assessee ("lessees") and the "lessor" under which the lessor leased a factory shed to the assessee for a term of thirty years, and collected the advance rent for the entire period. The next day, a document was executed between the parties stating that the lessor granted the assessee an option to purchase the premises for a further consideration of Rs.2,90,000/- after five years. In effect, there was no further consideration to be paid, as the amount was to be adjusted against the advance rent already paid as aforesaid.

The position, therefore, was that the assessee was put in possession of the property and had virtually the entire control of the property. The entire payment under the lease had been made. The consideration under the Agreement had also been paid for it was to be adjusted against the advance rent already paid. Nothing substantial remained to be done by the assessee to purchase the property, except to have the formal documentation drawn up and registered.

The AO denied the assessee, deduction in respect of the lease rent. The CIT(A) upheld the order of the AO. He, however, held that the expenditure was in the nature of a premium and directed the AO to allow depreciation after capitalizing the expenditure. The Tribunal held that the arrangement between the parties conferred the benefit of ownership upon the assessee without the actual sale during the current accounting year. The Tribunal held that the assessee had acquired a capital asset and the expenditure had to be treated as capital expenditure. The Tribunal, however, held that as per the terms of the lease deed, the assessee was not the owner of the premises and therefore, was not entitled to depreciation under section 32. Upon further appeal, the High Court held that:

- The entire arrangement between the parties, seen as a whole, clearly indicates that the parties never intended entering into an agreement of lease. They intended to and did enter into an agreement of sale of the property by the lessor to the assessee. It is inconceivable that a party, who has paid the entire consideration in advance, would not exercise the option to purchase the property after 5 years. The lease agreement was just a feeble attempt at indicating that the sale had not taken place on 29th March, 1982 itself (lease date).
- The AO rightly denied the assessee, deduction in respect of the lease rent. There appears to be contradictory findings by the Tribunal. On the one hand, the Tribunal held that the assessee had acquired a capital asset and

the expenditure in doing so had to be treated as capital expenditure. On the other hand, the Tribunal held that the assessee being a lessee cannot be said to be the owner of the property and was, therefore, not entitled to depreciation. Section 32 indeed entitles an assessee, who is the owner of a property, to depreciation. The arrangement between the lessor and the assessee was, in effect, an agreement of sale of the property by the lessor to the assessee. The assessee is, therefore, the owner of the property having acquired the same on 29th March, 1982, itself and so the assessee would be entitled to depreciation. *2012-TIOL-817-HC-MUM-IT.*

Sale of shares to sister concern: The assessee was engaged in business of sale and purchase of shares and government securities. The AO noticed that the assessee had earned significant profit on sale of shares of ALPS industries out of its opening stock. This profit was sought to be set off mainly against the loss on sale of shares of J.P. Industries and Himachal Futuristic Company Ltd (HFCL). The assessee had purchased the shares of J.P. Industries and HFCL and sold them after a month at a significant loss. The shares were purchased from M/s A. Nitin Capital Services and again sold back to it at a loss. The AO held that the sale and purchase of shares of J.P. Industries and HFCL were a sham transaction and disallowed the loss claimed by the assessee.

On appeal, the CIT (A) held that the purchase had been made at a higher price and not the prices quoted on the BSE. The sales have been made on dates when the price of the shares was at its lowest in the market. The appellant had also not been the beneficiary of the dividend by these companies which went to M/s A. Nitin Capital Services. Also, the close family connection between the 2 firms indicated that it was not a transparent transaction. The transaction appeared to be an attempt to create losses in share dealing to reduce the profit made on sale of share.

On appeal by the assessee, the Tribunal held that merely because there was some minor difference between the market price and the negotiated price, the transaction could not be termed as sham. The Tribunal was considerably influenced by the assessment order made in the case of M/s A. Nitin Capital Services. It was, therefore, held that once the transactions were accepted as genuine in the hands of M/s A. Nitin Capital Services, they could not be held to be bogus in the hands of the assessee. The Tribunal, therefore, allowed the appeal. Aggrieved, the Revenue appealed before the High Court. The High Court observed that:

- The shares were held for a very short period. There was no evidence of any delivery being effected or any consideration actually having passed between the parties. The assessee relied almost entirely on book entries. The sale of shares was done when their value had dipped to half of their purchase price. At the time of purchase as well as at the time of sale, it was only the sister concern M/s A. Nitin Capital Services which was involved in the transaction.
- The reasoning of the Tribunal that the acceptance of M/s A. Nitin Capital Services' claims in its returns would lead to the inference that the transactions with the assessee were genuine, cannot be accepted.

- Revenue's appeal is allowed. AO's order, as modified by the CIT (A) is restored. *2012-TIOL-810-HC-DEL-IT.*

Tribunal Judgments

Agent of a foreign institution: The assessee was registered as a public charitable trust u/s 12AA of the I-T Act. It was also registered in terms of section 2(15) for carrying on the activities of education in a charitable manner. The assessee was one of the many institutes established by ICS, London for regulating and supporting the profession of ship-broking throughout the world. Students aspiring to become the members of the Institute had to pass a number of examinations. The Institute in Madras was registering students to write the examinations conducted by ICS, London. It collected registration fees from the students and provided necessary academic support so that the students could qualify in the examinations. The assessee institute was maintaining a faculty to provide educational support and counseling to the registered students.

The AO contended that the institute was only an agent of ICS, London, working on commercial terms. It was like a tutor running a coaching centre, and so its activities could not be called as educational. The Tribunal held that:

- The Memorandum of Association and other Bye-laws and particulars of the assessee Institute, show that it is an institution registered in India for all purposes of law.
- The relationship with ICS London is not commercial or business or trade related. It is something like a collaboration of Oxford University with one of the Indian Universities. In the modern world, international affiliation and recognition are necessary, so almost all the modern professions in the world are having similar arrangements. There is no reason to hold that the assessee is an agent or branch of a foreign Institute.
- The assessee is not running a coaching centre for a particular examination. There is nothing on record to show that the assessee is engaged in any commercial or professional activities in India by way of consultancy or professional advice and it is not earning any income by way of carrying on any trade or commerce. The income of the assessee is the fees collected from the students and the expenses are incurred for running the Institute for imparting professional education to its registered students. The income of the assessee is not utilized for the benefit of any individual. Hence the assessee cannot be construed as an agent of a foreign institution. *2012-TIOL-588-ITAT-MAD***.**

Claiming Sec 10A benefits for demerged company: Assessee had set up an STPI unit which was demerged and transferred to another company after due approval by the High Court. Assessee - now the demerged company - had been claiming deduction u/s 10A in respect of the income of the STPI unit from Assessment Year 2002-03 onwards. AO disallowed deduction claimed u/s 10A stating that STPI unit was started only by splitting up of existing infrastructure and the undertaking formed by splitting up of business already in existence was not eligible for deduction. STPI unit was demerged and transferred, and thus was not eligible to deduction. The assessee contended that it had shown the income of the

undertaking for the period 1.4.2004 to 30.9.2004 as its income and had claimed deduction u/s 10A on such income which was correctly allowed by CIT (A), in as much as the same was not claimed or allowed as a deduction in the hands of the resulting company. The ITAT held that:

- In the present case the STPI undertaking of the assessee stands transferred in a scheme of demerger before the completion of the specified 10 year period and therefore provisions of section 10A(7A) of the Act apply. Clause (a) of section 10A(7A) specifically mandates that no deduction shall be admissible in the hands of the demerged company for the previous year in which the demerger takes place. In the instant case, the assessee is the demerged company and is to be denied deduction.
- As per section 2(19AA), an STPI unit is seen as a distinct and separate business entity by the Income Tax Act which mandates that separate set of books of accounts be maintained for the STPI. The I.T. Act also does not regard the demerger as a sale, and allows the resulting company to continue to enjoy the benefits bestowed u/s 10A. By virtue of the fact that the STPI undertaking is transferred to the resulting company as a Going Concern, it is the resulting company that is going to enjoy the profits or losses of the STPI unit as on 31.3.2005.
- It is necessary that the income of the undertaking for the entire year from 1.4.2004 to 31.3.2005 is deemed to be the income of the resulting company and no part of it be deemed to belong to the assessee. The benefit of sec 10A has to be available completely and no portion of it is to be denied on the ground that the same has not been claimed by the right person. *2012-TIOL-573-ITAT-BANG.*

Application of Trust money: Assessee was a registered trust set up under the Ministry of Commerce & Industries. The entire corpus was provided by Govt. of India to promote India Brand Overseas. Assesee spent a significant sum for participation in Hannover Fair in Germany. AO was of the opinion that since this amount was applied outside India it attracted section 11(1)(a) & 11(1)(b) and was taxed accordingly. On appeal, the CIT(A) observed that the assessee had spent the amount outside India and did not have CBDT's exemption, so the AO was correct in disallowing the amount.

On appeal, the AR contended that the assessee had participated in the fair as an agent of the Ministry and had got the grant from the Ministry's sponsored body Engineering Export Promotion Council for setting up Indian Pavilion in the fair. Grant for specific purposes had been held as tide up grants and so the said amount cannot be taxed by treating it as application outside India. The Tribunal held that:

- It is not in dispute that the amount was spent for participating in Hannover Fair in Germany and for such participation, the entire control was with the Ministry.
- Section 11(1)(a) of the Act requires that the income of the trust should be applied not only to charitable purposes, but also applied in India to such purposes.
- If as AR says, the income of the trust can be applied even outside India so long as the charitable purposes

are in India, then there is no need for a trust which tends to promote international welfare in which India is interested, to apply to the CBDT for exemption. Hence, disallowance in this regard could validly be made. *2012-TIOL-537-ITAT-DEL*.

Turnkey Contract: The assessee entered into a contract with ONGC for fabrication and installation of on-shore and off-shore oil facilities and pipelines. The assessee claimed that though the contract was one, it had to be sub-dividend into two parts, one for designing, fabrication and supply of material and the other for installation and commissioning of the project. It was claimed that the work relating to the former was carried out exclusively in Abu Dhabi and hence no income relating to receipts for that part of the contract was liable to tax in India as the there was no PE in India.

The AO & DRP rejected the claim on the basis that (a) the contract was a "turnkey" one where the entire risk of completion & commissioning was on the assessee & it was not divisible into different components, (b) the assessee had a project office in India which was a PE, (c) the assessee had a Dependent Agent PE, (d) there was a "construction and installation PE" under Article 5(2)(h) & (e) ownership of the equipment transferred to ONGC only after issue of the certificate of acceptance of the entire work. It was also held that s. 44BB was not applicable and the profit was estimated at 25% of gross receipts. On appeal by the assessee, the Tribunal held:

- The assessee's project office in India constituted a PE. It also had a 'Dependent Agent PE' and also a 'construction and installation PE' under Article 5(2)(h).
- However, though the contract was on a 'turnkey' basis, it had to be regarded as a divisible contract because the consideration for various activities had been stated separately. Also, ONGC had the discretion to take only the platform erected by the assessee in Abu Dhabi without having installation thereof. The segregation of the contract revenues into offshore and onshore activities was made at the stage of awarding the contract.
- The PE was in respect of the installation and commissioning work done in India and the activities carried outside India were not attributable to the said PE.
- The work of installation of the platform done inside India did not fall u/s 44BB because the activity could not be regarded as a 'facility in connection with the prospecting for, of extraction or production of, mineral oils'. *National Petroleum Construction Company vs. ADIT (ITAT Delhi), October 12, 2012.*

India-USA DTAA -Managerial services: The assessee was a company engaged in the business of IT enabled services. It provided voice based call center services to clients in USA, and for that the telecom infrastructure was provided by Tata Communication and Reliance Communications at India and Verizon in the USA. Novatel was a telecom voice service provider in USA and Novatel was helping the assessee for connecting to the USA Telecom network. All the calls received from the USA or made to the USA required the help of a local telecom

voice service provider in the USA and Novatel was providing this service to the assessee. The assessee had made payments towards voice charges to Novatel. According to the Assessing Officer (AO), such payment represented fee for technical services and tax was required to be deducted at source therefrom u/s 195 of the IT Act. As no TDS was effected, the AO disallowed the entire expenditure incurred in terms of section 40(a)(i).

CIT (A) held that the sum had to be treated as deemed income in the hands of the Novatel and the provisions of section 40(a)(i) of Income-tax Act r. w. s. 195(1) of Income-tax Act became applicable.

In further appeal to the Tribunal, the assessee contended that since the recipient did not have any PE in India, the telecom voice service fee was not chargeable in India. It was argued that the amount paid for such services could neither be treated as FTS nor royalty and as such, no tax was to be deducted at source on payment for telecom services provided by Novatel. The amount paid to Novatel was not its income accruing in India u/s 9(1)((vii) or section 9(1)(vi) or under DTAA between India and USA. Thus, the liability to TDS u/s 195 would not arise in the hands of the assessee. The Tribunal held that:

- The income of the non-resident – Novatel was in the form of service charges payment. As claimed by the assessee, the non-resident – Novatel – had not rendered any services of managerial, technical or consultancy in nature which expressly did not cover under the expression 'fees for technical services'.
- The payment made to a non-resident in respect of telecom voice services availed outside India cannot be termed as 'fees for technical services'.
- It was decided that the assessee had no obligation whatsoever to deduct tax at source when the payments made to Novatel and as such, no disallowance u/s 40(a)(i) of the Act was called for. *2012-TII-164-ITAT-BANG-INTL.*

SERVICE TAX

Important Circular / Notification

Extension of Date of Submission of Return: In exercise of the powers conferred by sub-rule(4) of rule 7 of the Service Tax Rules, 1994, the Central Board of Excise & Customs has extended the date of submission of the return for the period 1st April 2012 to 30th June 2012, from 25th October, 2012 to 25th November,2012. The circumstances of a special nature which have given rise to this extension of time are as follows:

- ACES will start releasing the return in Form ST3 in a quarterly format, shortly before the due date of 25th October, 2012.
- This will result in all the assesses attempting to file their returns in a short time period, which may result in problems in the computer network and delay and inconvenience to the assesses. *F.No.137/99/2011-Service Tax, 15th October, 2012.*

CESTAT JUDGMENT

- **Export of Services by SEZ unit:** The appellant was a unit in the Special Economic Zone and registered as a service provider under the category of "Business Auxiliary Services". It exported taxable output service under the Export of Service Rules, 2005 without payment of service tax. This resulted in accumulation of unutilized credit of service tax availed on input service for which it filed a refund claim, for the period October to December, 2010.

  The lower adjudicating authority opined that the input service procured by the appellant from the Domestic Tariff Area were exempted unconditionally vide Notification no. 9/2009-ST dated 03.03.2009 and, therefore, the appellant should not have paid any duty. Holding that seeking refund of input service tax credit for the activities undertaken within the SEZs is not consistent with the scheme of refund under rule 5 of the CENVAT Credit Rules, 2004, the refund claim was rejected. Upon appeal, the Bench observed:

- The appellant is eligible for refund of service tax paid which was not required to be paid under section 11B of the Act, provided that the appellant filed the refund claim within the prescribed time-limit and the bar of unjust enrichment did not apply.
- In the instant case, as the appellant has exported the output service, hence the principle of unjust enrichment does not apply.
- The only point that needs to be seen is whether the appellant made the refund claim within a period of one year from the date of payment of duty, and so the case is sent back to the lower authority to examine this point. *2012-TIOL-1478-CESTAT-MUM.*

Rent paid for job worker's unit: The applicant cleared semi-finished goods to its job worker and after due processing the goods were returned without payment of duty. The applicant paid rent of the premises of job worker and availed credit of the service tax paid. The jurisdictional authorities objected to this availment on the ground that the job worker premises is not registered with the department as the premises of the manufacturing unit (applicant).

Accordingly, a demand notice seeking reversal of Cenvat credit was issued and the same was confirmed by the adjudicating authority along with imposition of penalty and interest. Before the CESTAT, the applicant submitted that the activity undertaken by the job worker is in relation to the manufacturing activity and, therefore, credit of the rent paid by the applicant in respect of the premises of the job worker is available (to the applicant). The Revenue representative justified the demand by submitting that the job worker is an independent manufacturer and, therefore, the service tax paid in respect of the rent of job worker's premises is not available as Cenvat credit. The Bench observed:

- The premises for which the rent is paid is not part of the manufacturing unit as per the ground plan of manufacturing unit submitted by the applicant.

- The job worker is an independent manufacturer and he is working under Notification 214/86. Job worker being an independent manufacturer is liable to pay duty in respect of the activity which amounts to manufacture.

- In the present case, the job worker is not paying duty and he is working under the Notification and hence the applicant has not made out a case of waiver of total duty. *2012-TIOL-1332-CESTAT-MUM.*

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