Recent Judicial Pronouncements

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Case Study 1

Whether proviso to S.40(a)(ia) as substituted by Finance Act 2010 is Retrospective

Authorities

- **CIT vs. Virgin Creations** (Kolkata High Court) (ITAT No. 302 of 2011 - GA 3200/2011, dated 23/11/2011)
- **Alpha Projects V/s. DCIT** (ITA No.2869/Ahd/2011, dated 23/03/2012)
- **Rajamahendri Shipping & Oil Field Services Ltd. Vs. Addl. CIT** (ITA No.352/vizag/2008, dated 13/04/2012)
- **Piyush C Mehta vs ACIT** (ITA No.1321/Mum/2009, dated 11/04/2012)

Independent analysis of the provisions

S.40(a)(ia) - Amounts not deductible

Section 40 Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession",—

(a) in the case of any assessee—

xxx...

Contd…

(ia) any interest, commission or brokerage, rent, royalty, fees for professional services or fees for technical services **payable** to a resident, or amounts **payable** to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on which tax is deductible at source under Chapter XVII-B and **such tax has not been deducted** or, after deduction, has not been paid on or before the due date specified in sub-section (1) of section 139 :

Contd…

- Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid. (w.e.f. 01/04/2010)

Original Section 40(a)(ia) from 01/04/2005	**Retrospectively amended section from 01/04/2005 by Finance Act, 2008**	**Section as introduced by Finance Act 2010 w.e.f. 01/04/2010**
(ia) any interest, commission or …….. has not been paid **during the previous year, or in the subsequent year before the expiry of the time prescribed under sub-section (1) of section 200 :**	(ia) any interest, commission or …….. has not been paid,— **(A) in a case where the tax was deductible and was so deducted during the last month of the previous year, on or before the due date specified in sub-section (1) of section 139; or** **(B) in any other case, on or before the last day of the previous year:**	(ia) any interest, commission or …….. has not been paid **on or before the due date specified in sub-section (1) of section 139 :**

Original Section 40(a)(ia) from 01/04/2005	Retrospectively amended section from 01/04/2005 by Finance Act, 2008	Section as introduced by Finance Act 2010 w.e.f. 01/04/2010
Provided that where in respect of any such sum, tax has been deducted in any subsequent year or, has been deducted in the previous year but paid in any subsequent year after the expiry of the time prescribed under sub-section (1) of section 200, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.	Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted— (A) during the last month of the previous year but paid after the said due date ; or (B) during any other month of the previous year but paid after the end of the said previous year, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.	Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid.

Retrospectivity

- Whether section 40(*a*)(*ia*) as amended by the Finance Act, 2010 with retrospective effect from 1-4-2010 is clarificatory and/or explanatory and/or curative having retrospective effect from 1-4-2005?

Contd…

When can a statutory provision be said to be having a retrospective effect?

Whenever an amendment is made to a statutory provision to remove unintended consequences of that section and to make it workable, court have taken a view that such amendments are clarificatory and retrospective in operation.

Contd…

- Allied Motors (P.) Ltd. v. CIT [1997] 224 ITR 677
- CIT v. Alom Extrusions Ltd. [2009] 319 ITR 306
- CIT v. Gold Coin Health Food (P.) Ltd. [2008] 304 ITR 308
- CIT v. Kanji Shivji & Co. [2000] 242 ITR 124.
- CIT v. Varas International (P.) Ltd. [2006] 283 ITR 484

2010 amendment was to make the section workable and to remove unintended consequences

- After the retrospective amendment by Finance Act, 2008, the payments of TDS into Government treasury well within the time prescribed under section 200 r.w. Rule 30 were also hit and came to be disallowed u/s 40(i)(ia) which was not the intention of the legislature.

Act	Rule	Remarks
S. 40(a)(ia) as applicable from 01/04/2005 to 31/03/2010 after 2008 retrospective amendment, disallows expenditure except under following 2 circumstances: **A** TDS of March if paid before due date of filing return e.g. 30th September; **B** TDS of earlier months, if paid before last day of the previous year.	Rule 30 – IT Rules as effective from 2005 to 2009 prescribed the due date of payment into the Government treasury in case of various assessees under various sections.	**Rule 30(1)(b)(1)** – Amount credited in February gets due in on or before 30th April so assessee won't get the deduction even when the amount is paid within statutory time frame. **Proviso (a) to Rule 30(1)** also won't work as last quarter payment getting due on 15th April includes amount for Jan & Feb which would not be allowed as amount is not paid within previous year.

Act	Rule	Remarks
S. 40(a)(ia) as applicable from 01/04/2010 disallows expenditure except TDS of previous year, if paid before due date of filing return e.g. 30th September.	Rule 30 – IT Rules as effective from 2010 prescribed the due date of payment into the Government treasury in case of various assessees under various sections.	Rule 30 becomes workable under all the circumstances.

'Mischief Rule' or "Heydon's Rule"

Four Tests:

- what was the common law before the making of the Act;
- what was the mischief and defect for which the common law did not provide;
- what remedy the Parliament has appointed to cure the defect; and
- the true reasons for the remedy.

- An explanatory Act is generally passed to supply an obvious omission or to clear up doubts as to the meaning of the previous Act. **Keshavlal Jethalal Shah v. Mohanalal Bhagwandas, AIR 1968 SC 1336 @ 1339.**
- If a statute is curative or merely declaratory of the previous law retrospective operation is generally intended. **CIT v. Podar Cement Pvt. Ltd. (1997) 226 ITR 625 @ 652 (SC).**

Case Study 2

Whether expenditure which is already paid before the end of the PY is outside the purview of provisions of S.40(a)(ia) of the Act

Merilyn Shipping & Transports

vs

ACIT

[2012] 136 ITD 23

(Visakhapatnam)(SB)

Paid vs Payable

- Disallowance u/s 40(a)(ia) could be made only of the amount remaining "payable" at the end of the year and not of that which had already been "paid".

- **N K Jewellers vs ITO** (ITA No.638/Ahd/2009, dated 27/04/2012)

Situations

- When expenditure is paid, tax is not deducted and also not paid;
- When expenditure is paid, tax is deducted but not paid;
- When expenditure is payable, tax is neither provided for nor deducted & paid;
- When expenditure is payable, tax is deducted but not paid;

Case Study 3

Whether short deduction of tax at source is hit by provisions of S.40(a)(ia) of the Act

DCIT

vs

S.K. Tekriwal

([2011] 15 taxmann.com 289 (Kol.))

- Section 40(a)(ia) has two limbs:
  - Non-deduction of tax at source
  - After deduction, non-payment thereof into the Govt. treasury
- Shortfall in deduction does not come within the purview of S.40(a)(ia) of the Act.

Case Study 4

Does amount disallowed u/s 40(a(ia) result into business income?

ITO vs Ramesh Industries (ITA No. 3148/Ahd/2008)

- Section 40(a)(ia) falls in chapter (iv) and under "the head computation of business income." Any addition proposed by the Assessing Officer by invoking a provision falling in chapter (iv) under the "Head computation of business income, particularly between section 28 to 43D, would be made under the "Head income from business and Profession" and not under the head "Income from other sources", unless specifically so provided.

Case Study 5

Can penalty u/s 271(1)(c) be levied on disallowance u/s 40(a)(ia)?

- **DCIT vs Anupam Rasayan India Limited** (ITA No.493/Ahd/2010, dated 04/04/2012).
- **ACIT Vs M/s Seaways Shipping Limited** (ITA No.80/H/2011 dated 17/06/2011)
- **ACIT vs Saraswati Construction Co.** (ITA 2865/Ahd/2010, dated 22/02/2011)

Case Study 6

Is a transport contractor liable to effect TDS when he hires trucks to transport goods of his client?

Gujarat Roadlines vs ITO (ITA No.3023/Ahd/2008)

- When an assessee, a transport contractor, hires trucks of others for transportation of goods of his clients, there is no agreement for carrying out any work between the owners of the truck and the assessee transport contractor so provisions of S.194C do not get attracted. Resultantly no disallowance can be made u/s 40(a)(ia) of the Act.

Case Study 7

- **Whether 3rd Proviso to S.80HHC(3) inserted by Taxation Laws (Second Amendment) Act, 2005 can be applied prospectively despite the same being made applicable retrospectively from 1/4/1998?**

Avani Exports vs CIT (SCA No. 7926 of 2006, dated 02/07/2012)

Facts

- The assessee challenged the constitutional validity and vires of retrospective insertion of conditions in third proviso to Section 80HHC(3) of the Income Tax Act, 1961 on the following amongst other grounds:

Issues

- Amendment is arbitrary and unreasonable;
- Amendment is in gross violation of Article 14 of the Constitution of India;
- Amendment in its present form does not entitle a single assessee to claim benefit of incentives under S. 80HHC, therefore the amendment makes the section completely unworkable;

Issues

- The burden to prove that the restrictions imposed by the amendment are reasonable is on the State;
- Amendment violates the principles of Promissory Estoppel and Legitimate Expectations;
- Amendment cannot have retrospective effect.

Judgment of the High Court

- The amendment is held to be violative of Article 14 of the Constitution of India. High Court found that discrimination based on two classes, first, whose assessments have become final and secondly, whose assessment are pending, definitely violates Article 14 of the Constitution of India as there is no rationale nexus with the object of the amendment, and, therefore, such classification fails the test of Article 14 of the Constitution, being a case of 'palpable arbitrariness'.

Judgment contd...

- Hon'ble the Court further held that it is for the Revenue to prove that the restrictions imposed by the amending Act are reasonable. It was held that in the fact of the present the Revenue has failed to discharge that burden by pointing out the reason for making classification based on the above stated discrimination which have no reasonable connection with the object of amendment.

Judgment contd...

- Hon'ble the Court further held that in order to overcome adverse decision of the any Court of Tribunal, the legislature cannot delete a valid piece of legislation and incorporate a totally new one with retrospective effect.

Judgment contd...

- Hon'ble the Court held that "If after inducing a citizen to arrange his business in a manner with a clear stipulation that if the existing statutory conditions are satisfied, in that event, he would get the benefit of taxation and thereafter, the Revenue withdraws such benefit and imposes a new condition which the citizen at that stage is incapable of complying whereas if such promise was not there, the citizen could arrange his affairs in a different way to get similar or at least some benefit, such amendment must be held to be arbitrary and if not, an ingenious artifice opposed to law."

Judgment contd...

- Hon'ble the Court held that "Moreover, we find that the present amendment has been made at a point of time when the application of section 80HHC has already been exhausted and the same was not even in the statute book. In such situation, it is not permissible to take away the benefit already granted through a concluded scheme by introducing fresh amendment by virtue of which an expired scheme has been revived with benefit conferred upon only a limited section and snatching the same from some other sections."

Judgment contd...

- Hon'ble Court further held that substantive amendment cannot have retrospective operation in so far as the same is operating against the assessee. In other words, the amendment in so far as it grants benefit to the assessees having export turnover below 10 crs would not be affected.

Case Study 8

- **Whether Export Incentive are eligible for deduction u/s 10B after SC's judgment in the case of Liberty India (317 ITR 218)**

Maral Overseas Ltd.

vs.

ACIT

136 ITD 177 (SB) (Ind)

Facts

- 'A' received export entitlements and incentives, on which it claimed deduction u/s 10B of the Act after forming the same as part of business profit.

- AO declined holding such income was not derived from 100% export oriented undertaking, therefore, not eligible for claim of deduction u/s 10B(1) read with section 10B(4) of the Act.

Findings of the Special Bench

- S. 10B(1) refers the profits and gains as are derived by a 100% EOU, yet the manner of determining such eligible profits has been statutorily defined in S.10B(4) of the Act
- As per the formula stated above, the entire profits of the business are to be taken which are multiplied by the ratio of the export turnover to the total turnover of the business.

Findings Contd...

- Ss.4 does not require an assessee to establish a direct nexus with the business of the undertaking and once an income forms part of the business of the undertaking, the same would be included in the profits of the business of the undertaking.

Findings Contd...

- Law is settled in P.R.Prabhakar 284 ITR 584 (SC) to hold that straight jacket formula given has to be followed to determine eligible deduction. (80HHC)
- Liberty India (317 ITR 218) not applicable as provisions of 10B are different from 80IA wherein no formula has been laid down for computing eligible deduction.

Findings Contd...

- Once an income forms part of the business of the eligible undertaking, there is no further mandate in the provisions of section 10B to exclude the same from the eligible profits.
- Mode of determining eligible deduction u/s 10B is similar to S.80HHC, except Explanation (baa) to S.80HHC for exclusion of certain income from "profit of business", which is however, conspicuous by its absence in section 10B.

Case Study 9

- **Can higher profits in the eligible unit be made a ground to re-determine its profit while computing deduction u/s 80IC of the Act**

Cadial Healthcare Ltd. vs. ACIT ITA No. 3140/Ahd/2010, dated 25/05/2012.

Facts of the Case

- 'A' claimed deduction u/s 80IC for its Buddi manufacturing unit after debiting direct and allocating indirect expenditure such as marketing, corporation and interest.
- AO observed that other indirect expenditure such as advertisement, research and other significant marketing expenditure have not been allocated to Profit & loss account of Buddi manufacturing unit and accordingly eligible profit for the said unit has been escalated to claim more deduction.

Facts Contd...

- AO further observed that the products manufactured by Baddi unit were the products which the assessee company was purchasing from suppliers on Principal to Principal basis (P2P) before setting-up of the Baddi Unit.
- AO was of the view that the assessee company was generating substantial profit on account of brand value and marketing expenditure incurred on those products and therefore such cost ought to have been allocated to Baddi Unit.

Case of the Revenue

- AO was of the view that the profit of 'A' was on account of three reasons; viz
  - (a) manufacturing assets ;
  - (b) brand assets and
  - (c) marketing assets
- Eligible undertaking was having only manufacturing assets and not brand / marketing assets. Hence, the profit only to the extent of manufacturing assets could be said to be derived from eligible undertaking, which was only eligible for deduction u/s 80IC of the Act.

Findings of the Tribunal

- 'A' has maintained separate Profit & loss account for eligible unit.
- AO is not empowered to disturb P&L account merely because profit of eligible unit is higher than other units, particularly when accounts of eligible unit is separately maintained and more so w/o pointing any defects in such books of accounts so maintained.

Findings contd...

- S.80IC viz-vis S.80IA(8) of the Act do not provide for segregation of profits as suggested by AO.
- If there is no inter-unit transfer, then AO has no right to determine FMV or ALP of the goods sold in the market.

Case Study 10

Can a fresh ground, not raised before the lower authorities, be raised in the Memo of Appeal for the first time before ITAT

All Cargo Global Logistics Ltd. Vs. DCIT (Special Bench Mumbai Tribunal) (No.5018 to 5022, 5059/Mum/2010, dated 21/05/2012)

Facts

- A raised raised the ground (*in Form 36*) that u/s 153A, the AO was not entitled to make additions which were not based on incriminating material found during the search. *This ground was not raised before the AO or the CIT (A).* Since this ground was not raised before the lower authorities, it was an additional ground and could not be entertained.

Findings

- As per S.253(1) a person can be "aggrieved" only if a ground had been raised and it is decided against him. (**Pokhraj Hirachand 49 ITR 293 (Bom)**)
- A fresh ground taken in the appeal memo can still be considered as "additional ground" for which leave is required from the Tribunal.

Findings Contd...

- Three elements while dealing with Grounds of Appeal before the Tribunal:
  - the grounds taken in the memorandum of appeal;
  - the grounds for which leave is allowed by the Tribunal and;
  - grounds taken by the respondent for supporting the order of the CIT(A).

Findings Contd...

- The Tribunal is not confined only to issues arising out of the appeal before the CIT(A) but has the discretion to allow a new ground to be raised, if the same is a pure question of law for which facts are on record. (**NTPC 229 ITR 383 (SC))**
- Additional ground should be allowed to be raised if it is necessary to assess the correct tax liability.

Case Study 11

Once assessment is framed u/s 143(3), can it be said that AO has applied his mind to all the issues, whether explicitly mention in the body of the AO or not.

Rubamin

vs

Love Kumar

(SCA No.16901 of 2011, dated 30/04/2012, Gujarat High Court)

Facts

- For AY 2005-06, original assessment was framed u/s 143(3) of the Act
- Notice u/s 148 of the Act came to be issued on 15/09/2009 on the ground that commission was paid without effecting TDS therefore the same should have been disallowed u/s 40(a)(ia) of the Act.

Arguments of the Assessee

- Petitioner submitted that it was not at all liable to effect TDS as certificate u/s 197 of the Act was available with it.
- Had it been called for the same could have been placed on record

Arguments of the Revenue

- Revenue submitted that during the original assessment stage this aspect of disallowance u/s 40(a)(ia) of the Act was not at examined so no opinion on the same.
- More over this being a reassessment within 4 years, even if there is an omission, the same can be remedied u/s 147 of the Act.

Findings

- There was no escapement of income at all (certificate u/s 197)
- There is no tangible material on record to justify the reopening
- Merely because AO does not express his findings in the AO, the same can not be taken as a ground to conclude that income has escaped assessment

Findings contd...

- If the AO does not apply his mind and commits a lapse, there is no reason why the assessee should be made to suffer the consequences of that lapse.
- Since all the facts were before the AO, at the time of framing the original assessment, and later a different view was taken by him or his successor on the same facts, it clearly amounts to a change of opinion.

Other decisions supporting this view

- Rotary Club of Ahmedabad vs ACIT (336 ITR 585)(Guj)
- Ganesh Housing Corp. Ltd. vs DCIT (341 ITR 312) (Guj)
- CIT vs. Kelvinator of India (256 ITR 1)(Del)(FB) & Eicher (294 ITR 310) now affirmed by SC in 320 ITR 561 (SC).

Basic Issues

- **Reasons for Reassessment**
  - **In writing;**
  - **Must show how income has escaped assessment;**
  - **Failure of the A to be recorded in the Reasons;**
  - **A has a right to ask for a copy of the same.**
- **GKN Driveshafts (India) Ltd. v. ITO 259 ITR 19 (SC)**
  - **Notice; return; reasons; objections; order on objections; challenge to reopening if no then normal reassessment proceedings.**

Line of Action

- Notice of reopening
- Time gap between the notice and end of the assessment year to which the same pertains
  - Within 4 years:
    - Change of opinion, if original u/s 143(3)
    - Is reopening permissible when return is not subjected to 143(3) assessment ?
  - Beyond 4 Years:
    - If original u/s 143(3), Proviso to S. 147
    - Is reopening permissible when return is accepted u/s 143(1)

Case Study 12

Whether an order u/s 263 giving a direction to carry out further investigation to frame assessment order afresh is a valid order.

Income Tax Office

vs

D G Housing Projects Ltd.

20 Taxmann.com 587 (Del)

Facts

- For AY 04-05, the A sold an immovable property incurring LTCL of Rs. 35.71 lakhs after indexation. The said property was purchased by the A in 1997 for Rs.69.63 lacs and was sold in 2003 for Rs.70 lacs. The AO accepted the said computation of income.

Facts contd...

- In S 263 proceedings, CIT observed that full value of consideration receivable has not been properly examined by the AO and therefore the assessment order was erroneous and prejudicial to the interest of the revenue.

Facts contd...

- On appeal, ITAT set aside the order and held that the CIT had not held and come to the conclusion or given a finding that the actual receipt of consideration was more than what was declared in the return.

Findings

- Where the AO has formed a wrong opinion or finding on merits, the CIT has to come to the conclusion and himself decide that the order is erroneous, by conducting necessary enquiry before passing the order u/s 263.

Findings contd...

- The CIT is entitled to collect new material to show how the order of the AO is erroneous. The CIT cannot remand the matter to the AO for further enquiries or to decide whether the findings recorded are erroneous without a finding that the order is erroneous and how that is so.

Controversies

- In a set aside proceedings u/s 143(3) r.w.s. 263, can the assessing officer go beyond the issues raised by the CIT in revision order? **CIT vs. D. N. Dosani [280 ITR 275 (Guj)]**
- Can a subsequent SC decision or retrospective amendment in law make assessment order erroneous? **CIT vs. G. M. Mittal Stainless Steel P. Ltd. 263 ITR 255 (SC) [Contrary view Star India Ltd vs ACIT (Mum)]**

Controversies

- **“Lack of inquiry” vs. “Inadequate inquiry”**
  - Inadequate inquiry would not by itself give occasion to the CIT to pass orders under section 263 of the Act
  - "Lack of inquiry" can give jurisdiction u/s 263 to the CIT.

CIT vs. Sunbeam Auto Ltd. [332 ITR 167 (Del)]

CIT vs. Vikas Polymers [194 Taxmann 436 (Del)]

CIT vs. Anil Kumar Sharma [335 ITR 83 (Delhi)]

Controversies

- An intimation under section 143(1) is not amenable to revisional jurisdiction of CIT under section 263.

CIT vs Kartar Singh & Co Pvt. Ltd. [300 ITR 440 (P&H)]

Vinod Kumar Rai v CIT [116 ITD 72 (Agra) (TM)]

Case Study 13

Whether mere rendering of technical services without making available technical knowledge and knowhow would satisfy the 'make available' condition under DTAA.

CIT vs. De Beers India Minerals (P) Ltd.

[2012] 21 taxmann.com 214 (Kar)

&

DIT vs. Guy Carpenter & Co. Ltd.

[2012] 20 taxmann.com 807 (Del)

What is not 'make available'

- It is not enough that the services offered are the product of intense technological effort and a lot of technical knowledge and experience of the service provider have gone into it.
- Similarly, the use of a product which embodies technology shall not *per se* be considered to make the technology available.

‘Make Available’

- To satisfy the 'Make available‘ test of DTAA, the following twin tests must be satisfied simultaneously:
  - Rendering Services; and
  - Making technical knowledge available

‘Make Available’

- To satisfy the 'make available' condition, it is imperative that the technical knowledge or skills of the service provider should be imparted to and absorbed by the receiver so that the receiver can deploy similar technology or techniques in the future without depending upon the provider.

‘Make Available’

- If only technical services are rendered and the technical knowledge is withheld from recipient of the services, the 'make available' condition under DTAA is not satisfied and consideration for such technical service is not liable to be taxed in terms of DTAA.

Thank You