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ALL INDIA FEDERATION OF TAX PRACTITIONERS

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TWO DAY NATIONAL TAX CONFERENCE
HELD ON 15TH & 16TH FEBRUARY, 2014 AT LUDHIANA

INAUGURAL SESSION : (Seen from left to right) S/Shri Balbir Khanna; Harish N. Motiwalla, Secretary General, AIFTP; Arvind Shukla, Chairman, AIFTP-NZ; Dr. M. V. K. Moorthy, Dy. President, AIFTP; Hon'ble Mr. Justice S. K. Kaul, Chief Justice, Punjab & Haryana High Court; Hon'ble Mr. Justice J. S. Khehar, Judge, Supreme Court of India; Hon'ble Mr. Justice S. K. Mittal, Judge, Punjab & Haryana High Court; K. L. Goyal, Chairman, Conference Committee; Varinder Sharma, Ashok Juneja and Mukul Gupta, Vice President, AIFTP

Hon'ble Mr. Justice J. S. Khehar, Judge, Supreme Court of India addressing the gathering

Hon'ble Mr. Justice S. K. Kaul, Chief Justice, Punjab & Haryana High Court addressing the gathering

Hon'ble Mr. Justice S. K. Mittal, Judge, Punjab & Haryana High Court addressing the gathering

Section of audience

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Northern	0	941	17	0	958
Southern	1	873	13	5	892
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From the Editorial Board

Income Tax Appellate Tribunal – Oldest Institution – Top less for more than three years

Franks Committee on Administrative Tribunals and Enquiries has stated that the advantage which Tribunals had over Courts lay in cheapness, accessibility, freedom from technicality, expedition and expert knowledge of the members over the particular subjects. To achieve the said objective, the Income Tax Appellate Tribunal was set up on 25th January, 1941 as an Independent quasi judicial body to hear Second Appeals from the decisions of the Appellate Assistant Commissioner (now Commissioner of Income-tax (Appeals). Initially, the Tribunal was constituted with 3 Benches with Head Office at Bombay, the financial capital of India. With the increased litigation and in accordance with the motto "Sulabh Nyay – Satvar Nyay", Benches increased to 63 with 126 members, including the President.

Section 33 of the 1922 Act was enacted conferring power of Second Appeal before the Appellate Tribunal. Initially, Section 5-A of the 1922 Act provided that the Appellate Tribunal shall consist of Judicial Members and Accountant Members as defined. The 1961 Act contains sections 252 to 255 relating to appeals. The Tribunal is headed by one President. From 1.4.1972 power was conferred to appoint one or more Members to be the Vice President(s). From 1-4-1984, power to appoint one of the Vice Presidents to be the Senior Vice President stands conferred. It is functioning under the Ministry of Law & Justice not Finance, to maintain its independence.

A golden hand shake in between law and accountancy has been maintained. Over years it had applause from the judiciary, tax payers and the tax department. So much so that it used to be called as a model or mother Tribunal and other Tribunals have been formed on the same pattern. The Appellate Tribunal is final fact finding authority. Its finding on facts is final and no appeal lies to the Hon'ble High Court, except on substantial question of law. The powers are very wide but there is no power of enhancement. All questions, whether of law or a fact which relate to the assessment of an assessee may be raised before the Tribunal. In disposing of the appeal, the Tribunal has the power to give appropriate directions and to pass such orders as it thinks fit, after an opportunity of being heard to both the parties to an appeal. The powers include the power to annul an assessment order or set aside or remand. The powers have been expressed in the widest possible terms. It has power to grant stay and rectify its own order, with no right to review.

On account of the just, fair and independent dispensation of justice, without fear of the Revenue and being fair to all, it gained popularity and its functioning applauded. Senior stalwarts like Sarva Shri N. A. Palkhivala, Y. P. Trivedi, S. E. Dastur and many more, all over the country, derived pleasure in appearance and had high praise. However, with mistake in selections, appointment of some bad elements, the standard eroded and the old stalwarts started hesitating in accepting briefs. Due to certain unfortunate incidence which happened few years back, the golden image was shattered.

However, we can say with full pride that, we do have number of members, who are men of integrity and knowledge. We are of the considered opinion that, it is the duty and responsibility of the Bar to protect the members who are men of integrity, so that they can discharge their duty without any fear or favour. It is our desire to preserve the honour, dignity and to get unpolluted justice from the final fact finding body, which is the mother Tribunal. There are professionals who are men of integrity, knowledge and with great reputation, who are appearing before this august institution and higher forums regularly and few of them have been appearing before this institution for more than 50 years, they have witnessed the past glory of this institution, they are well conversant with the present atmosphere prevailing in the functioning of this institution, they are taking lead in preserving the independence of this prestigious institution.

President of this institution is administrative head and has full control over its members. Senior Vice-President and Vice-Presidents assist him in discharging the onerous duty. Shri Vimal Gandhi retired on 3-6-2010. Since last more than three years and nine months no President has been elevated. Hon'ble Shri R. L. Karwa continues as an officiating President. Appointment of Senior Vice-President and Vice-Presidents is in waiting. It seriously affects the administrative set up. In our view, by not appointing the President, Senior Vice-President and Vice-Presidents, the Government is sending a wrong message, that we have no competent person, who deserves to be appointed, to lead the institution. If that is so, how the citizens will gain the confidence of the institution.

As an acting President, one may not be able to take many bold decisions for better administration of justice. It is also to be noted that if this trend continues many competent and good professionals, who may be having the desire to serve the nation by joining the Bench may not come forward and make an application to be appointed as Members of the Tribunal, because there is neither elevation to High Court, they will not be promoted as Vice-President or President, nor they are entitled to practice before the Income Tax Appellate Tribunal. If Law Ministry does not take immediate steps to appoint President and his aides, the future of the Institution will be at stake and the Tribunal may not be able to retain its glory as one of the finest institutions of our country.

We have also come to know that exercise to fill up vacancies of more than 40 members is in offing, but unless and until a permanent President is appointed, the selection may be defective and not of men of integrity with expert knowledge. Faulty selection would not be in the interest of the nation.

Federation has always played a pivotal role in enhancing glory, reputation and image of the Institution. With the same motto it has made representation to all concerned with dire hope that the top institution is headed expeditiously by befitting permanent President in place of the officiating.

N. M. RANKA
Member, Editorial Board

FORTHCOMING PROGRAMMES

Date & Month	Programme	Place
5, 19-4-2014 & 3-5-2014	Workshop on MVAT Act & Allied Laws	Mumbai
28-6-2014	National Executive Committee Meeting (Southern Zone)	Chennai
28, 29-6-2014	National Tax Conference (Southern Zone)	Chennai

President's Message

First of all I would like to offer my greetings and good wishes on the auspicious occasion of 'Gudi Padwa' to everyone concerned with AIFTP.

Lok Sabha Elections of 2014 has already been declared and the electorate spirit particularly with new ten crore electorate is running very high expecting to set up of Government who will be committed to best governance of the country. Already "Aam Aadmi" i.e. General Public desires to have a sea change in the matter of good governance since they are grossly fed up with the present Government. So, we being responsible citizen of India should exercise our right to vote and we must 'vote' for the betterment of our motherland. The economists of the country have opined that our fundamentals are strong to withstand any set back and we have indeed a great potential to become number one of the world, provided we get a committed Government with a vision to take forward our country in the global context. This is surely possible with good governance coupled with corruption free society.

Recently, it has been publicly admitted by the CJI that there is a huge pendency of cases across all the courts in the country and the CJI is seriously concerned about this scenario. Hence, it is necessary in this behalf that all the stakeholders should sit down together and work out a time bound programme for eliminating this huge pendency of litigation. I therefore strongly feel that there is a urgency in the matter for judicial reforms coupled with fresh initiatives from the new Government which will occupy office after general elections. We, at AIFTP level, would like to get involved with the new Government to draw a plan with vision to sort out the mess of pendency and look at laws afresh and also weed out dead legislations which are of no use.

As informed earlier that next National Executive Committee meeting would be in the month of June, 2014. In fact we wanted to have the said meeting at some new place like Mangalore, so that we could increase our membership. However, logistically, it is difficult. Hence, we have decided to have the same at Chennai.

Meantime, may I request you to send your suggestions as well as your comments on the working of AIFTP by addressing to me personally.

Yours brotherly,

J. D. NANKANI
National President

Duties and Responsibilities of Independent Directors under the Companies Act, 2013

CA P. N. Shah

The Companies Act, 2013 (new Act) has been passed by Parliament in August, 2013. It received the assent of the President on 29th August, 2013 and is notified on 30th August 2013. It will come into force from the date to be notified by the Government. The new Act will replace the existing Companies Act, 1956 (existing Act). 98 Sections out of 470 Sections of the new Act have come into force from 12-9-2013. The provisions relating to Duties and Responsibilities of Independent Directors are contained in Chapter XI of the new Act. Draft Rules relating to some of the Sections in Chapter XI have been issued for public comments.

At present the concept of Independent Directors exists under SEBI Regulations. Therefore, it is obligatory for listed Companies to have specified number of Independent Directors. This concept does not exist under the existing Act. However, the New Act defines the term "Independent Director" and provides for specific duties and responsibilities of Independent Directors. Some of these important provisions are discussed in this Article.

1. Board of Directors

1.1 New Section 149 provides that the minimum number of directors in the case of a public company shall be three and in the case of a private company it shall be two. The maximum number of directors can be 15.

However, a company can provide for maximum number of directors as more than 15 by passing a Special Resolution. The Government can prescribe by Rules that in certain class of companies, there shall be at least one woman director. It is also provided that at least one of the directors shall be a person who has stayed in India for 182 days or more in the previous calendar year. Draft Rule 11.1 states that in every listed company there should be one woman director who should be appointed within one year from the date of this section coming into force. The Rule also provides that in every other public company where paid up Share Capital is ₹ 100 cr. or more or turnover is ₹ 300 cr. or more, a woman director shall be appointed within 3 years from the date on which this section comes into force.

1.2 The concept of "one person company" (OPC) is now introduced in the new Act. This term is defined in Section 2(62) to mean a company which has only one person as a Member. In such a company the minimum number of directors can be only one person who is a resident in India.

2. Concept of Independent Directors under SEBI Regulations

2.1 As stated earlier, under the SEBI Regulations, only a listed Company is required to have Independent Directors as provided in clause 49 of the Listing Agreement. This clause provides that a listed company shall have 50% of its Board of Directors as non-executive Directors. When the Chairman of the Board is a non-executive Director, at least one-third of the Board should have Independent Directors. If the Chairman is a promoter of the Company, or is related to any promoter or a person occupying management

position at the Board Level or one level below the Board, at least 50% of the Board should consist of Independent Directors.

2.2 The term "Independent Director" is defined in clause 49(iii) of the Listing Agreement. This definition is not as exhaustive as in the new Act. It is also provided that a nominee Director shall not be considered as Independent Director. Under Clause 49, the Board has to lay down a Code of Conduct for all Directors, including an Independent Director.

3. Concept of Independent Directors under the New Act

3.1 As stated earlier, the concept of Independent Directors does not exist under the existing Act. However, Section 149 of the New Act recognises the concept of an "Independent Director". This term is defined to mean a person —

(i) Who, in the opinion of the Board, is a person of integrity and possesses relevant expertise and experience.

(ii) Who possesses such other qualifications as may be prescribed. (Refer Para 3.5 below).

(iii) Who is or was not a promoter of the company, or its holding, subsidiary or associate company (hereinafter referred to as associate companies).

(iv) Who is not related to promoters or directors of the company or any of its associate companies.

(v) Who has or had no pecuniary relationship with any of the above persons/companies during the current or two immediately preceding financial years.

(vi) None of his relatives has or had pecuniary relationship or transaction with the above persons amounting to 2% or more of its gross turnover or total income or ₹ 50 lakhs (or such higher amount which is prescribed) – whichever is lower during the current or two preceding financial years.

(vii) Who or any of his relatives –

(a) Holds or held the position of a key managerial personnel or as employee of the company or any of its associate companies in any of the 3 financial years immediately preceding the year of his appointment.

(b) Is or has been an employee, proprietor or partner of the following during any of the 3 preceding financial years.

- A firm of Auditors, Company Secretaries or Cost Auditors of the company or any of its associate companies.
- Any legal or consulting firm which has or had transaction with the company in or any of its associate companies amounting to 10% or more of the gross turnover of the firm.

(c) Holds, together with his relatives, 2% or more of the voting power of the company, or

(d) Is a Chief Executive or Director of any non-profit organisation that receives 25% or more of its receipts from the company, any of its promoters, directors or its associate companies or that holds 2% or more of the total voting power of the company.

(viii) Who is not a Managing/Whole Time/ Nominee Director.

3.2(i) Every listed Company will be required to have atleast 1/3rd of the total number of directors as Independent Directors. The Government may prescribe the minimum number of Independent Directors in any class or classes of public Companies. Every such company will have to comply with this requirement within a period of one year from the commencement of the new Act. It will be the duty of every Independent Director to give a declaration u/s.149(7) at the first Board Meeting in which he participates and thereafter at the first Board meeting of every financial year in which he

participates that he meets with the above criteria of independent Director. He has to intimate status of his Independence from time-to-time. A Managing Director, whole-time Director or a Nominee Director will not be considered as an Independent Director.

(ii) Draft Rule 11.2 provides that a public company having paid-up capital of ₹ 100 crore or more, or having turnover of ₹ 300 crore or more or having aggregate outstanding Loans, Borrowings, Debentures, or Deposits exceeding ₹ 200 crore shall also have 1/3rd of the total number of directors as Independent Directors.

3.3 An Independent Director shall not be entitled to receive any remuneration other than a fee and reimbursement of expenses, for attending the meetings of the Board or any committee thereof or for any other purpose as decided by the Board. Such fees cannot exceed the amount as may be prescribed u/s. 197(5). He shall also be entitled to receive profit related commission as may be approved by the members. However, he shall not be entitled to receive the benefit of stock option. It may be noted that u/s. 197(1), commission on net profits payable to all Non-executive directors (including independent Directors) is limited to 1% of net profits of the company. If there is no managing or whole-time Director, this commission can be paid up to 3% of net profit.

3.4 An Independent Director can, subject to provisions of section 152, hold office for a term of 5 consecutive years. He can be appointed as such for a further term, not exceeding 5 years, if the members pass a special resolution and disclosure of such appointment is made in the Board Report. After the expiry of 10 years period he cannot be reappointed as an Independent Director. He can, however, be appointed as such Director after expiry of 3 years provided he was not directly or indirectly associated with the company in any other capacity. It may be noted that the period during which the Independent Director has held office as such Director before the commencement of the new Act shall not be counted for computing the period of 10 years, stated above. Further, an Independent Director shall not be liable to retire by rotation as provided in sections 152 (6) and (7). The appointment of Independent Director shall be approved by the company in General Meeting as provided in section 152(2). The explanatory statement annexed to the notice of General Meeting shall indicate the justification for choosing the Director for such appointment. This notice shall also include a statement that, in the opinion of the Board of Directors, such person fulfils the conditions in the Act for such appointment.

3.5 Draft Rule 11.3 provides for the qualifications of Independent Directors. As per this Rule, an Independent Director shall possess appropriate skills, experience and knowledge in one or more field of Finance, Law, Management, Sales, Marketing, Administration, Research, Corporate Governance, Technical Operations or Other Disciplines related to the Company's Business.

3.6 Section 149(12) provides that (i) an Independent Director and (ii) a Non-executive Director (other than a promoter or key management personnel) shall be held liable only in respect of such acts of omission or commission by a company which had occurred with his knowledge, attributable by the Board process. Further, he will also be liable for such acts which have occurred with his consent or connivance or where he had not acted diligently.

3.7 Any body, institute or association, having expertise in creation and maintenance of Data Bank, and as may be notified by the Central Government, shall maintain a list of Independent Directors. In this list, the names, addresses and qualifications of persons eligible and willing to act as independent Directors shall be listed. Such Data Bank shall be in accordance with the prescribed Rules. This list shall be placed on its website. Any company desiring to appoint an independent Director will be able to select the name from such Data Bank if such person qualifies for appointment as provided in section 149 (6)as discussed in para 3.1 above. The responsibility of exercising due diligence before selecting the name shall be that

of the company. The procedure for selection of the Independent Directors shall be in accordance with prescribed Rules. It may be noted that Draft Rule 11.4 provides for detailed procedure for maintenance of Data Bank.

4. Duties and Responsibilities of Independent Directors

4.1 Section 149(8) provides that the company and the Independent Directors shall comply with the provisions specified in Schedule IV. This Schedule lays down a "Code of Conduct" for Independent Directors. It is stated that the adherence with this code of conduct by Independent Directors and fulfilment of their responsibilities in a professional and faithful manner will promote confidence of the investment community, minority shareholders, regulators and companies in the institution of Independent Directors. The schedule provides for (i) Guidelines for professional conduct; (ii) Role and Functions; (iii) Duties; (iv) Manner of appointment, Reappointment, Resignation and Removal; (v) Separate Meetings of Independent Directors and (vi) Evaluation of Performance of Independent Directors by the Board of Directors. The Code of Conduct to be followed by the Company and the Independent Directors as given in Schedule IV is as under:

4.2 **Guidelines for professional conduct:**

An independent Director shall: (i) Uphold ethical standards of integrity and probity, (ii) Act objectively and constructively while exercising his duties; (iii) Exercise his responsibilities in a *bona fide* manner in the interest of the company, (iv) Devote sufficient time and attention to his professional obligations for informed and balanced decision making, (v) Shall not allow any extraneous considerations that will vitiate his exercise of objective independent judgment in the paramount interest of the company as a whole, while concurring in or dissenting from the collective judgment of the Board in its decision making; (vi) Not abuse his position to the detriment of the company or its shareholders or for the purpose of gaining direct or indirect personal advantage or advantage for any associated person; (vii) Refrain from any action that would lead to loss of his independence; (viii) Where circumstances arise which make an Independent Director lose his independence, the Independent Director must immediately inform the Board accordingly; and (ix) Assist the company in implementing the best corporate governance practices.

4.3 **Role and functions**

The Independent Directors shall: (i) Help in bringing an independent judgment to bear on the Board's deliberations especially on issues of strategy, performance, risk management, resources, key appointments and standards of conduct; (ii) Bring an objective view in the evaluation of the performance of board and management; (iii) Scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance; (iv) Satisfy themselves on the integrity of financial information and that financial controls and the systems of risk management are robust and defensible; (v) Safeguard the interest of all stakeholders, particularly the minority shareholders; (vi) Balance the conflicting interest of the stakeholders; (vii) Determine appropriate levels of remuneration of Executive Directors, key managerial personnel and senior management and have a prime role in appointing and where necessary recommend removal of executive directors, key managerial personnel and senior management; and (viii) Moderate and arbitrate in the interest of the company as a whole, in situations of conflict between management and shareholder's interest.

4.4 **Duties**

Independent Directors shall

(i) Undertake appropriate induction and regularly update and refresh their skills, knowledge and familiarity with the company; (ii) Seek appropriate clarification or amplification of information and, where necessary, take and follow appropriate professional advice and opinion of outside experts at the expense of the company; (iii) Strive to attend all meetings of the Board of Directors and the Board committees of which he

is a member; (iv) participate constructively and actively in the committees of the Board in which they are chairpersons or members; (v) Strive to attend the general meetings of the company; (vi) where they have concerns about the running of the company or a proposed action, ensure that these are addressed by the Board and, to the extent that they are not resolved, insist that their concerns are recorded in the minutes of the Board meeting; (vii) Keep themselves well informed about the company and the external environment in which it operates; (viii) Not to unfairly obstruct the functioning of an otherwise proper Board or committee of the Board; (ix) Pay sufficient attention and ensure that adequate deliberations are held before approving related party transactions and assure themselves that the same are in the interest of the company; (x) Ascertain and ensure that the company has an adequate and functional vigil mechanism and to ensure that the interests of a person who uses such mechanism are not prejudicially affected on account of such use; (xi) Report concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct or ethics policy; (xii) Acting within his authority, assist in protecting the legitimate interests of the company, shareholders and its employees; and (xiii) Not disclose confidential information, including commercial secrets, technologies, advertising and sales promotion plans, unpublished price sensitive information, unless such disclosure is expressly approved by the Board or required by-law.

4.5 **Manner of Appointment**

(i) Appointment process of independent Directors shall be independent of the company management. While selecting Independent Directors the Board shall ensure that there is appropriate balance of skills, experience and knowledge in the Board so as to enable the Board to discharge its functions and duties effectively.

(ii) The appointment of Independent Director(s) of the company shall be approved at the meeting of the shareholders.

(iii) The explanatory statement attached to the notice of the meeting for approving the appointment of Independent Director shall include a statement that in the opinion of the Board, the Independent Director proposed to be appointed fulfils the conditions specified in the Act and rules made thereunder and that the proposed Director is independent of the management.

(iv) The appointment of Independent Directors shall be formalised through a letter of appointment, which shall set out: (a) The term of appointment; (b) The expectation of the Board from the appointed Director; the Board-level committee(s) in which the director is expected to serve and its tasks; (c) The fiduciary duties that come with such an appointment along with accompanying liabilities; (d) Provision for Directors and Officers (D and O) insurance, if any; (e) The Code of Business Ethics that the company expects its Directors and employees to follow; (f) The list of actions that Director should not do while functioning as such in the company; and (g) The remuneration, mentioning periodic fees, reimbursement of expenses for participation in the Boards and other meetings and profit related commission, if any.

(v) The terms and conditions of appointment of Independent Directors shall be open for inspection by any member.

(vi) The above terms and conditions shall also be posted on the company's website.

4.6 **Re-appointment**

The re-appointment of Independent Director shall be on the basis of report of performance evaluation.

4.7 **Resignation or removal**

(i) The resignation or removal of an Independent Director shall be in the same manner as is provided in sections 168 and 169 of the Act.

(ii) An Independent Director who resigns or is removed from the Board of the company shall be replaced by a new Independent Director within a period of not more than one hundred and eighty days from the date of such resignation or removal, as the case may be.

(iii) Where the company fulfils the requirement of Independent Directors in its Board even without filling the vacancy created by such resignation or removal, as the case may be, the requirement of replacement by a new Independent Director shall not apply.

4.8 **Separate meetings:**

(i) The Independent Directors of the company shall hold at least one meeting in a year, without the attendance of Non-independent Directors and members of management;

(ii) All the Independent Directors of the company shall strive to be present at such meeting;

(iii) The meeting shall: (a) Review the performance of Non-Independent Directors and the Board as a whole; (b) Review the performance of the Chairperson of the company, taking into account the views of Executive Directors and Non-Executive Directors; and (c) Assess the quality, quantity and timeliness of flow of information between the company management and the Board that is necessary for the Board to effectively and reasonably perform their duties.

4.9 **Evaluation of performance**

(i) The performance evaluation of Independent Directors shall be done by the entire Board of Directors, excluding the director being evaluated.

(ii) On the basis of the report of performance evaluation, it shall be determined whether to extend or continue the term of appointment of the Independent Director.

4.10 Reading the above provisions it will be noticed that very onerous duties and responsibilities are cast on Independent Directors. It is difficult to comprehend whether the corporate sector will be able to find the required number of Independent Directors to comply with these requirements.

5. Some Procedural Provisions

It may be noted that some procedural provisions relating to Independent Directors are as under:

(i) Section 152(3) provides that all directors (including Independent Directors) of a Company (including a Private company) shall obtain Director Identification Number (DIN).

(ii) Section 167(1)(b) provides that a Director (including an Independent Director) of a Company (including a Private Company) shall vacate his office if he does not attend all the meetings of the Board held during a period of 12 months, with or without seeking leave of absence of the Board. It may be noted that under section 173(2) participation of directors in a Board Meeting through video conferencing or other audio visual means is permitted.

(iii) U/s. 173(3) at least 7 days notice is required for Board Meeting. If shorter notice is given, at least one Independent Director should be present at the meeting. If no Independent Director is present at such meeting, the decisions taken by the Board should be circulated to all Directors. These decisions shall be final if they are ratified by at least one Independent Director.

(iv) Where Audit Committee is required to be appointed by a listed or other specified Company under section 177, it should have atleast 3 Directors. Majority of Directors in this committee should be Independent Directors.

(v) Section 178 is a new section which provides for appointment of nomination and Remuneration Committee of the Board.

This Committee should consist of 3 or more Non-Executive Directors. Out of this at least 50% should be Independent Directors. This section is applicable to a listed company and to other specified companies.

(vi) A listed company or other specified company has to appoint a Corporate Social Responsibility (CSR) Committee of Board. This committee should consist of 3 or more Directors, out of which at least one Director shall be an Independent Director.

(vii) The Board Report to Members should give a statement of declaration given by Independent Directors u/s. 149(6).

(viii) Section 197(5) provides that a Director (including an Independent Director) shall be entitled to receive such fees, as may be prescribed, for attending a Board Meeting. Draft Rule 13.2 provides that such fees shall not exceed ₹ 1 lakh per meeting as the Board may decide. It is also provided that different fees for Independent Directors and other Directors can be fixed within this limit.

(ix) Chapter XI (Sections 149 to 172) contains various provisions relating to duties and responsibilities of Directors (including Independent Directors). In this Chapter some of the sections provide that penalty of varying amounts can be levied on the Company for non-compliance with the provisions of the Section. There are also provisions for prosecution of defaulting officers and levy of penalty on them. Therefore, the Key Officers will have to be very careful about compliance with the provisions of these sections.

6. To sum up

6.1 Reading the above provisions, it is evident that it will be difficult to find adequate number of persons who will qualify to be Independent Directors. The duties and responsibilities which have been cast on the Independent Directors by the provisions of Schedule IV are so onerous that many persons who have joined the Board of some Companies may not decide to continue in such a position under the new Act. Once this position is accepted, an Independent Director will have to be ever vigilant about the activities of the Company in which he has accepted this assignment.

6.2 Particular reference may be made to the definition of the term "Independent Director" given in Section 149. This definition is so complex that the Company will have to make detailed study of the background of the person who is to be appointed as an Independent Director. Again, the status of his compliance with the above definition will have to be consistently reviewed by the Company Secretary from time-to-time.

6.3 Some of the provisions relating to Independent Directors are subject to Rules being prescribed by the Government. Therefore, the concerned director and the Company Secretary will have to study such Rules and amendments to the rules from time-to-time to ensure that the Rules are complied with.

6.4 The Duties and Functions of Independent Directors are explained in Schedule IV. Reading these provisions it appears that the Independent Director will have to acquire knowledge of the technical, financial, managerial as well H.R. functions of the Company and report to the Board about deficiencies in the functioning of the staff in each of these fields. He will have to suggest remedial steps to be taken and also see that they are promptly implemented. In other words, the role of an Independent Director under the new Act will be that of a "SUPER WATCHDOG" who has to ensure that those in the day-to-day management (including all Directors on the Board) are functioning in the best interest of the stakeholders, minority shareholders, regulators, workers, customers and public at large. Considering the duties and responsibilities cast on the Independent Directors, many companies may not be able to adequately compensate them for the time and energy put in by them.

Note: *The relevant sections and rules have not been brought into force. Therefore, above article is subject to any amendments made hereafter.*

[Source : Article published in paper book at 17th National Convention held on 26th & 27th December 2013 at Mumbai]

Indian Professional Firms – Road Ahead

CA T. N. Manoharan

Introduction

Indian professional firms, both in the accounting and legal field, are constituted by small and medium firms and hardly there are a few hundreds of firms that can boast of more than 10 partners. Many of these firms have grown only when the family members qualify as professionals but the trend is changing where non-family members constitute a firm and grow as an entity to compete with the multinational accounting and legal professional firms. Although size has no correlation to quality, in the emerging scenario, size would be of relevance to scale up to the growing economic needs and globalised competitive market. Therefore, Indian professionals need to measure up to the expectations of the service seekers both in the Indian context as well as in the international arena. While it is not difficult to comprehend both the opportunities in the anvil and the challenges that are facing the Indian professional firms, it is not so easy to identify the measures that need to be adopted to overcome those challenges and reap the benefits by capitalising on the opportunities. In this article, an attempt is made to deduce these aspects in a practical manner so as to provide food for thought for the readers and persuade them to act in a proactive manner.

Opportunities

Besides the traditional areas of practice, both the accounting and legal professionals in India have tremendous opportunities in the field of consultancy services. While the accounting professionals can contribute in terms of business, finance and capital advisory services, legal professionals can render services relating to drafting, vetting, documentation and compliance oriented services. The wide range of services that flows in the consultancy field include services relating to project appraisal and funding by way of private equity or other means; IPO; Valuation; Due Diligence; Merger and Acquisitions; Risk assessment; Debt syndication; Restructuring of business; ERP implementation; Internal audit; System audit; Knowledge process outsourcing (KPO) and Wealth Management. Knowledge in these areas would bring immense opportunities and there is no dearth of work for a professional who has the skill set to venture in these areas.

The basic difference between the statutory work and consultancy work is that in the case of the former, a client is compelled to engage a Chartered Accountant to prevent penal consequences for non-compliance whereas, in the case of the latter, the client approaches on his own volition for value addition. Similarly, a lawyer is engaged to represent a client in the courts due to the exclusivity in terms of eligibility to represent whereas, on the consultancy front, he is approached to provide value addition to business collaborations and transactions. In the case of statutory work, the client perceives it to result in an expenditure whereas, in consultancy, the benefit accrues either in the form of increase in revenue or reduction in expenditure thereby enhancing his willingness to pay adequate compensation for the services. Therefore, the ability of the professional to do proper

billing of services commensurate to the time and expertise utilised is far greater with reference to consultancy services than billing for statutory work.

Challenges

Indian professional firms are facing many challenges in view of globalisation and unprecedented recession in the economy. These challenges demand reorientation in the approach and attitude of the professionals in public practice. The emerging areas of opportunities indicated above call for different skill sets, knowledge and delivery mechanism. There is one significant difference between the consultancy field and the traditional areas of practice encompassing statutory audit or appearance in the Court and that is the competitive environment. A Chartered Accountant or a legal professional in India has to compete with Multinational entities, corporate bodies and other professionals in the Management Consultancy field.

In order to ensure quality and timely delivery of services and to be in the reckoning, Indian professional firms have to re-orient themselves to provide for acquisition of skill sets by partners and associates; they need to create verticals paving way for specialisation within the firm; they must not only keep adding new talent but continuously endeavour to retain such talent within the firm; they need to aim at geographical spread and reach to cater to clients having regional or national presence; they ought to invest in infrastructure; they should also be prudent and proficient in billing the value for their services without underselling them and above all, they need to cherish and uphold values and ethics.

Knowledge and skill sets

In the present day world, knowledge is power. Across the globe, we find knowledge driven economies are growing faster. Therefore, every Indian professional would do well to constantly update the knowledge and consciously acquire the skill sets required for effectively applying such knowledge in the day-to-day activities. Soft skills such as communication skills, negotiation skills, presentation skills and linguistic skills would be of immense strength to a professional for the delivery of his knowledge oriented services. Appropriate support can be drawn from technological skills and managerial skills by periodical and proper orientation and training.

Knowledge in the new areas of consultancy work may be acquired by studying the relevant literature and accessing information through web. Attending workshops and training programmes focusing on specific topics would be useful. Participating in the execution of work by other professionals or mentor firms will help to provide the confidence required to handle assignments independently. Templates of reporting would serve as a model in the initial implementation of work. Mid-size firms can even afford to organise periodical in-house training programmes for partners and the senior staff. Individual empowerment by undergoing specialised post qualification courses seems to be inevitable. Every professional who has the competence in the consultancy field should groom and train others to create teams within the organisation.

Positioning of divisions

Indian professional firms should be in a position to create divisions demarcating the areas of operation into different verticals. For example, a Chartered Accountancy firm can segregate the areas of practice into audit and assurance division; tax and allied services division and consultancy division. Even if there are three partners, each one should attempt to specialise so as to head and lead one of these divisions. In the emerging scenario, specialisation is the order of the day.

A specialist in audit, another one in tax and yet another professional having proficiency in consultancy can come under one roof to constitute a strong small and medium professional firm and render multifarious services to the client. With the emergence of Limited Liability Partnership since 2008 and the scope for having Multi-disciplinary Partnership firms involving professionals from accounting and legal field, there is enormous scope to expand and grow and also to build multi layer teams in each vertical created within the firm.

It is common knowledge that Indian entrepreneurs are consolidating their businesses to grow big and face global competition. Multinationals are establishing subsidiaries of large size in India. Foreign banking Companies operating in India through Branches in India will soon be converting those Branches into domestic subsidiary companies. Takeovers, mergers, amalgamations and collaborations are the order of the day. Professionals should also become conscious of this factor and gear up to restructure their firms by mergers and consolidations, reorient their skills and expand their firm size as well as profile of the services rendered. When an enterprise or a business group grows and correspondingly the professional firm rendering service to that enterprise/group does not, the chances of replacement of that firm by a bigger firm as a service provider cannot be ruled out. Therefore, capacity building of Indian professional firms in terms of positioning divisions and reaching out with geographical spread are important.

Human Resource Development

India can be proud of having the demographic advantage in the global arena. In the Indian context, it is no longer the problem of unemployment but it is the problem of un-employability. Even for the educated youth with whatever qualification, these days, orientation and training seems to be inevitable. Many of them are raw products coming out of the Institutions and Universities with a certain qualification; some are semi-finished and only a few are well developed competent ones. Therefore, good amount of time needs to be invested in grooming, nurturing and training them with orientation programmes at the inception as well as at periodical intervals.

Attracting new talent in the profession to join a small or a medium size firm appears to be a challenging task. Every Indian professional firm should have a plan of succession so that such firms continue to exist and grow. A professional firm should identify talent and offer due recognition, salary and status so as to attract and also take steps to retain young professionals in the firm to grow and stabilise with job satisfaction and leadership skills. Retention is possible only by providing wider exposure; opportunity to handle work of greater magnitude and also providing right ambience resulting in a sense of belonging. A firm needs to provide the social status for every professional associated with it and it should also take care of fulfilling or facilitating the fulfilment of his social needs such as housing, conveyance, education, etc. of the partners and audit managers and their families. While humans are mortals, firms can exist eternally with proper succession planning and execution. Institution building with perpetual succession is essential for the posterity of next generation CAs to inherit the legacy.

Geographical spread

Another challenge faced by firms is to execute any work across the region/country due to lack of pan India presence. Similarly, getting assignment of certain works would depend on the extent of geographical presence of such firm in as many locations as possible. Expansion and growth coupled with the above outlined empowerment only can enable a

firm to handle work that is spread across the length and breadth of the nation and even abroad. This situation demands that every such firm should identify professionals / firms in different geographical locations and develop an understanding for mutual reference and sharing of resources, particularly human resources, for execution of works.

Initially, this could be by affiliation or merely an association for convenience but gradually it can take shape as a formalised network arrangement. Once the reliability and compatibility is established after mutually collaborating for a few years, then merger can be contemplated by converting the firms within the network in other locations as a branch. Junior professionals who work with the firm for a minimum period of 3 to 5 years can be upgraded as partners subject to acceptability and compatibility. By this approach, a small and medium firm can evolve itself into a bigger firm by developing branches in many centres. The aim should be to render all services under one umbrella and make the firm a one stop solution for a client in our field. No doubt, this is easy to say but challenging to accomplish. But, if there is a sustained approach, systematic planning and undiminished enthusiasm, this can be gradually but certainly made to happen.

Infrastructure

Generally, infrastructure takes a back seat and it is a non-priority item for many Indian professional firms. This mind set should drastically undergo a change. Every firm should aspire to have stability in the place of operation and allocate a percentage of earnings every year for acquiring modern gadgets and tools. Further, every firm should spend in installing and documenting Systems, Procedures and Controls to secure and enhance operational efficiency. Knowledge database should be developed leading to industry-wise specialisation and also in select areas like transfer pricing. In the light of various reforms and legislations in the offing, such as convergence with IFRS; XBRL implementation; Direct Tax Code; Goods and Services Tax legislation and a new Company Law, appropriate investment in software solutions and tools; books and periodicals; equipments of latest technology becomes inevitable.

Billing Standards

It can be said without fear of contradiction that many Indian professional firms are unable to expand by recruiting young professionals for two reasons. One is the inability to pay near to market salary and secondly, not being able to guarantee partnership and provide lucrative practice with variety of work exposure in view of the limited areas of operation. While the second one can be addressed by tackling the challenges identified above, the first one can be handled only by proper billing of the services rendered. Under selling of services cripples the growth potential of a small and medium professional firm.

Service rendered, in many cases, is not properly identified and added on to the billing. Invariably, it is the practice of annual billing or common fee package for multifarious services that paves the way for under-selling of the services. Many do not even consider the man-hours spent as one of the important ingredients for billing. Of course, in deserving and exceptional cases, rendering of services for a low cost or free of charge may be justified but that policy or approach should not be extended to all clients. A professional who renders services backed by knowledge, values and competence always does the billing with absolute confidence unmindful of losing the client. He not only demands greater value for services, but also commands respect and credibility.

Quality and Values

Most important challenge to any small and medium professional firm is to ensure quality in anything it does and to adhere to the ethical norms laid down for the profession. The first one can be ensured by building quality team in the organisation and the later by imbibing values and appreciating that growth should not be at the cost of ethics. Adherence to Values is a challenging task these days as many players around us in the system do not attach any significance to this aspect.

Aspiration to become rich in the shortest possible time can be the root cause for deviation from established principles and best practices. We read in history that Gautama Buddha deserted all the prosperity and left the Palace in search of peace. On the contrary, many in today's world seem to be joining the race in search of prosperity and in the process desert peace. Prosperity is welcome but not at the cost of peace of mind. Contentment is too great a virtue to be given up. No one is poor if he is contended and the one who lacks it can never be considered rich irrespective of the wealth that he may possess.

Some members of the profession strive and survive on account of the goodwill created by our forefathers. Many members contribute to and enhance such goodwill by their exemplary conduct, impeccable integrity and qualitative delivery of services. Unfortunately, the conduct of a few members has diminishing effect on the goodwill of the profession. We need to introspect as to which category we should belong to and the answer is obvious. Fee based approach in everything we do would be fatal in the long run whereas value based approach would enhance our reputation. Mahatma Gandhi said that there is enough for every one's need but not for the greed. The Father of the Nation also indicated that 'ends' do not justify the 'means'. It might pay to be unethical in the short run, but in return one loses self-esteem and peace of mind, which is too precious a price one should dread to pay and suffer.

Lord T. B. McCauley said, "the measure of man's real character is what he would do if he knew he would never be found out". Everyone aspires to grow and reach greater heights. It will be nice to always bear in mind that ability may take us to the top but it requires character to stay there. Quality in service without compromising on ethical values begets not only prosperity in the long run but undoubtedly helps us to build image and command respect. In matters of innovation and empowerment, one should swim with the current, but in matters of values and principles, one should stand like a rock.

Conclusion

There is tremendous scope for the accounting and legal profession in India to grow and expand. Business entrepreneurs, these days, require professional firms to do the hand holding in the establishment of their business as well as in the expansion and restructuring plans. They expect professionals to be part of the decision making process instead of merely providing inputs for decision making. If only Indian firms can address the above discussed challenges with vision, zeal and right attitude, they can accomplish their goals competitively and make a mark in the profession. By the year 2020, India is expected to emerge as a strong economic power in the comity of Nations. By the same year, even if a few hundreds of Indian professional firms can grow and emerge as Multinational firms, it would be a milestone to reckon in the annals of the Indian history about which all of us can be proud of. Let us join hands to co-author, along with the Government, an enchanting future of India by building a credible economy.

[Source : Article published in paper book at 17th National Convention held on 26th & 27th December 2013 at Mumbai]

Issues under Capital Gains covering share transactions and exemptions

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I. General Introduction

The present section 45(1) of the Income-tax Act, 1961 correspondences to section 12B(1) of the 1922 Act. In *Navinchandra Mafatlal v. CIT (1954) 26 ITR 758 (SC)* considered and upheld the constitutional validity of the amendments made by the Act XXII of 1947. The SC held that the term income in Entry 54 in List I of the Seventh Schedule to the Government of India Act, 1935, should be given its widest connotation so as to include the capital gains. Once again under the Income tax Act, 1961 the power of the legislature to levy tax on capital gains is upheld by the court on account of Entry 82 of the Seventh Schedule of the Union List (Constitution of India).

The section 45 brings to charge capital gains and its ingredients are:

a) Existence of a capital asset, owned by the assessee;

b) A transfer of such asset during the previous year;

c) There should be profits and gains from transfer of such assets, and

d) Such profits and gains must accrue or arise to the assessee.

Shares and securities are an important part of a person's portfolio. The reason being on account of the fact that equity offers better return in comparison with the traditional instrument of investment. Stock market is now becoming more safer place in view of SEBI and other regulators who are keeping watch over manipulations. Also technology have helped individuals easy accessibility to the stock market.

The term share is not defined in the Income-tax Act, 1961 (the "Act"). Shares are included in the definition of goods in the Sale of Goods Act, 1930. Thus, under the Indian common law, shares are regarded as movable property. The dictionary meaning of the term is one of the equal parts into which a company's capital is divided, entitling the holder to a proportion of the profits.

Section 2(4) of Securities Contracts, (Regulation) Act, 1956 defines securities to include securities" include:-

i) shares, scripts, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;

(ia) derivative;

(ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes;

(ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;

(id) units or any other such instrument issued to the investors under any mutual fund scheme;

(ie) any certificate or instrument (by whatever name called), issued to an investor by

any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be;

(ii) Government securities;

(iia) such other instruments as may be declared by the Central Government to be securities; and

(iii) rights or interest in securities;

Under the Act, capital gain/ loss arise on the transfer of capital assets [S. 2(14)] (investments, in common parlance), which does not include stock-in-trade. While stock-in-trade is also not defined in the Act, it is commonly used to denote goods kept in hand by a businessman for the purposes of its trade or typical subject or commodity a person, company, or profession uses or deals in. It is this lack of express definitions of such important terms and expressions that has given rise to considerable litigation. The most common cause of litigation with respect to share transactions is the classification of profits from them as business income/loss or capital gain/ loss.

Short-term capital asset is defined u/s. 2(42A) and capital asset which are not short-term capital assets are defined u/s. 2(29A) as long-term capital assets.

Asset includes part of an asset as well [see *National Product v. CIT (1987) 163 ITR 632 (Karn)* and *Dilip Chinubhai Shah v. CIT (2002) 253 ITR 680 (Guj.)*]

Another cause of this dispute is that shares held for a period exceeding 12 months are classified as long-term and if sold on a recognised stock exchange are exempt from tax. While those held for twelve months or less are taxable at the rate of 15%.

While sale of shares constituting investment results in capital gain/loss, Sale of shares constituting stock-in-trade results in business income/loss. While all transactions have the underlying objective of making a profit, their true intention *vis-à-vis* capital gain or business income can be gathered from the surrounding circumstances and more importantly the intention of the assessee, which is a matter in the exclusive knowledge of the assessee.

The traditional thought behind investing was to deploy surplus funds in order to earn extra income over and above that from conventional sources of one's business or profession. With limited avenues and manners available for investing, the distinction between investment and business was perhaps discernible. With increase in disposable incomes and savings, the traditional concept of investment has undergone an overhaul.

Deploying surplus funds in the equity markets has since long been an instrument of making investments for the purpose of earning regular dividend and in the anticipation of selling them high. The traditional paper-based trading in the Indian equity markets has given way to modern exchange based trading resulting in ease of operation and liquidity. As a result, the number of transactions in any given portfolio today would be far higher than those two decades back. Furthermore, the increased investor awareness, availability of research tools and investor being more proactive automatically result into higher activity that translates into higher transactions.

While the mindset of the average Indian has kept pace with the changing times to suit his needs, the law has yet to catch up. It has failed to take into account the various factors which affect the intention, nature and manner of making investments. It is majorly due to this disparity between the changing times and law that gives rise as disputes as to what constitutes investment and what business. While the age old proverb "do not put all your

eggs in one basket" traditionally applied to investors dividing their savings in different classes like fixed deposits, gold, shares, etc., the contemporary view is to diverse their equity portfolios across companies of different sectors, sizes, business portfolios, etc. This translates into higher holdings in shares and number of transactions.

Absentis statutory guidance, the task of finding out the correct nature of transactions rests with the judicial authorities. The circulars issued by the CBDT serve as guiding principles for them to base their pronouncements upon.

i) CBDT instruction No. 1827 dt. 31-8-1989

ii) Circular No. 4/2007 dt. 15-6-2007 (2009) 291 ITR (St.) 384

Since lot of jurisprudence has developed on what constitutes investment and what business, *qua* share transactions, without statutory intervention, it may not be possible to dilute the distinction between the two. Such intervention, however, is required to reduce litigation and attain finality on this issue. Till that time, the principles evolved by the Courts would have to be given due consideration.

There have been several cases on this issue, but the application of the law to the facts of the case can still result in difficulty. The difficulty arises because often, there would be no single test which can be applied to conclusively determine the issue. Several factors are taken into account, and these facts would need to be weighed against each other before arriving at the conclusion. The issue which needs to be analysed are primarily:

1. What is the primary business/profession of the assessee.
2. What is the intention of the assessee at the time of purchase of the shares?
3. Is the purchase and sale made for realising profit, or for retention and appreciation in its value?
4. What is the past history of the assessments made by the Department?

The answer to this issue often would depend on numerous factors, none of which is absolutely conclusive one way or the other.

II. Factors that impact classification

The question whether transactions of sale and purchase of shares were trading transactions or whether these were in the nature of investment was a mixed question of law and fact, as observed in the case of *CIT v. H. Holck Larsen [1986] 160 ITR 67 (SC)*. The totality of all the facts will have to be borne in mind and the correct legal principles are to be applied to these.

In the year 1989, the CBDT issued guidance on the issue of treatment of shares held as stock-in-trade and shares held as investment. Based on the judgments of Courts, the following factors were enunciated in the said Instruction.

S. No.	Factor	Investment	Stock-in-trade	Issues that arise from such classification
1	Purchase and sale are allied to or incidental to usual trade or business	No	Yes	One needs to look at the primary source of income derived by the assessee. One needs to see the past history of an assessee.

S. No.	Factor	Investment	Stock-in-trade	Issues that arise from such classification
2	Nature and quantity	Quantity is low	Quantity is high	The instruction is silent on the aspect of nature. The quantity of transactions depends on a number of factors such as availability of funds. E.g. a person having high income may undertake higher number of transaction as compared to a person with low income.
3	Repetition of transaction	No/Less	Yes/High	It is common knowledge that if a person wants to acquire (or sell) a major stake in a company, the same may not always be possible in a single tranche due to non-availability of the required number of floating stock (or buyers) at a given time. In such a case, it is inevitable that "repetition" may take place.
				Also, the decision to invest or divest further is a commercial decision depending on the share price, anticipation of price movement. E.g. a person, as per his changing financial goals and with a view to earn returns, may consistently buy (or sell) shares. While he may intend only to churn his portfolio in order to suit his immediate needs and risk, he could be regarded as a trader in shares.
4	Intention of purchase	To earn income	To sell at profit	Typically, dividends account for only a nominal return on the shares. The more lucrative aspect of share transactions is the possibility of an increase in price. In as much as this, every person would want to sell the shares at profit, sometimes even at the cost of dividend. Hence, by this classification.
5	Share dealings	Dealing with capital asset	Dealing in capital assets	
6	Manner of earning income	Outright sale divided	Deriving income from exploitation of assets	If this test is to be applied, even long-term capital gains on which no dividend is received should be regarded as business income.
7	Entry on books	Shown as investment	Shown as stock-in-trade	It is a settled principle that entries in the books of account does not affect the tax liability of that item as per the decision of the Supreme Court in the case of *CIT v. Bazpur Co-operative Sugar Factory Ltd. [1988] 172 ITR 321 (SC).* However considering the conduct of the assessee over a period of time entry in books of account will held in knowing the real intention of the assessee. Maintenance of separate books of account is a decisive factor.

III. Some of the important decisions on this issue are as follows

1. Length of time: Earlier year accepted by dept.

i) *Gold Co. Ltd. v. CIT [1973] 92 ITR 121 (Cal.) (HC)*

The length of time, nature of dealings, method of dealings, how proceeds of sale are dealt with by assessee, these ingredients and other factors are some of matter that would determine question whether a particular transaction is in realisation of investment or a sale in ordinary course of business.

ii) *CIT v. S. Ramaamirtham [2008] 306 ITR 239 (Mad.)*

The assessee had been holding shares for a long time and had been utilising the surplus funds only for the investments. In earlier years also, the assessee had been showing only capital gains on similar transactions and that was accepted by the Revenue.

iii) *Shri Bharat K. Kenia vs. Addl. CIT ITA No. 6544/M/2008 dated 15-5-2009.*

Principle of consistency in holding of shares as an investment which is always accepted by Department in past. The position cannot be allowed to change, merely because on same set of facts a different view is possible.

iv) *SMK Shares & Stock Broking Pvt. Ltd. ITA No. 799/M/2009 dated 24-11-2010.*

The uniformity in treatment and consistency under the same facts and circumstances is one of the fundamentals of the judicial principles which cannot be brushed aside. Assessing officer himself accepted the assessee as investor in earlier years. All these factors outweigh the test of frequency of transaction being undertaken by the assessee in deciding the true intention of assessee.

v) *Hardik Bharat Patel v. DCIT, ITA Nos. 2274 & 8013/M/2011, Bench "H", dated 1-5-2013.*

The Tribunal observed that the department itself has accepted the short-term capital gain shown by the assessee while passing assessment under section 143(3) for assessment year 2006-07 and for assessment year 2009-10. Both these assessments were completed under section 143(3) and similar transactions were made and they were accepted. Different yardstick adopted for these two years under consideration, which was not justified. The assessee is a salaried person and shown all the purchases of shares under the head investment portfolio, therefore, they have to be treated under the head investment portfolio and capital gain whether short- term or long-term capital gain has to be assessed.

In the case of Ashvinkumar K. Kapadia, similar issue was decided by the Tribunal and this order of the Tribunal has also been affirmed by the Hon'ble jurisdictional High Court in ITA No. 5510/2010, *vide* order dated 28-9-2011. While deciding the issue in favour of the assessee, the Hon'ble High Court followed the decision in the case of Gopal Purohit.

vi) *Addl. CIT v. Mr. Tejas B. Trivedi, ITA No. 5412/Mum/2009 dt. 9/7/2010*

The Tribunal observed that the assessee was consistently showing the shares as investment and valued them at cost. The department in the past under scrutiny assessment has accepted the capital gain declared by the assessee, thereby treating the assessee as investor.

2. Two separate portfolios: Own expertise and capabilities

i) *Gopal Purohit v. JCIT [2009] 122 TTJ 87 (Mum.)*

CIT v. Gopal Purohit (2011) 336 ITR 287 (Bom.).

Department SLP dismissed. (2011) 334 ITR 308 (St.)

A person investing in shares is bound to study the newspapers, business magazines, watch the business channels and use websites and other tools to keep a track of the developments which are happening on day-to-day basis and which may happen in the near future and for this, he may have assistance of the financial planner or investment consultant or may by his own expertise and capabilities do it on his own. Hence, employment of such infrastructure cannot turn an investment activity into a business activity.

ii) *CIT v. Suresh R. Shah [2013] 256 CTR 104 (Mad.) (HC)*

It is open for the assessee to maintain two separate portfolios one for investment and other for maintaining business activities of shares.

iii) *CIT v. Suresh R. Shah (2013) 258 CTR 376 (Bom.)(HC)*

There is no bar for an assessee to maintain two separate portfolios.

3. Intention of the assessee

i) *CIT v. National Finance Ltd. [1962] 44 ITR 788 (SC)*

ii) *Khan Bahadur Ahmed Allauddin & Co. v. CIT [1966] 62 ITR 490 (AP)*

Where shares were acquired merely with intention of obtaining a managing agency and not of dealing in shares and shares were sold at loss to another company under same management, the loss was held to be not a trading loss.

iii) *Dalhousie Investment Trust Co. Ltd. v. CIT [1967] 66 ITR 473 (SC)]*

Mere fact that an investment company periodically varies its investments does not necessarily mean that the profits resulting therefrom are trading profits.

iv) *Gondhara Transport Co. (P.) Ltd. v. CIT [1972] 84 ITR 294 (P&H)*

Where assessee-transporter suffered loss on sale of shares of another transport company, which it had purchased to eliminate competition, such loss was held to be capital loss.

v) *Janak S. Rangwala v. ACIT [2007] 11 SOT 627 (Mum.) (Trib.)*

It is the intention of the assessee which is to be seen to determine the nature of transaction conducted by the assessee. Though the investment in shares is on a large magnitude but the same shall not decide the nature of transaction. Similar transactions of sale and purchase of shares in the preceding years have been held to be income from capital gains both on long-term and short-term basis.

vi) *Vinod K. Nevatia v. ACIT (2011) 49 DTR 16 (Mum.) (Trib.)*

Primarily, it is the intention with which an assessee starts its activity which is the most important factor which has to be considered keeping in view the adjoining circumstances. Mere intention to liquidate the investment at higher value does not imply that the intention was only to trade in security.

vii) *Accra Investments (P) Ltd. vs. ITO [2013) 359 ITR 116 (Bom.) (HC)*

Assessee, engaged in the business of investment, subscribed to 20% of the issued shares of a company with a right to nominate manager of the investee company. The shares were not freely transferable. Held, on facts, that the profit on sale of these shares was capital gains.

viii) *Trinetram Consultants Pvt. Ltd. v. Dy. CIT (2013) 143 ITD 634 (Mum.)(Trib.)*

The Tribunal held that when assessee earned gain on purchase and sale of equity shares and Mutual funds and its intention was to purchase shares and Mutual funds for holding then as investment, gain in question was assessable under head Capital Gain.

4. Volume and number of transactions; quantum of investments

Frequency, volume, and value of transactions cannot be the only criteria for determining the nature activities carried on. The Circular No. 4/2007 dated 15-6-2007 itself makes it clear. This Circular supplements the earlier Instruction No. 1827 dated August 31, 1989.

i) *Suresh Kumar Seksaria v. ACIT [2010] 1 ITR 783 (Mum.) (Trib.)*

The volume and number of transactions is not decisive in understanding the true nature of the transactions. The volume and number will depend upon the quantum of investments being made. If funds invested are huge, obviously the number of transactions and volume will become high.

ii) *Shantilal M. Jain v. Asst. CIT (2011) 132 ITD 466 (Mum.)(Trib.)*

In this case assessee had traded in 85 scripts in 188 transactions with high frequency and regularity. Despite large volume, etc. of share transactions, AO bound by Rule of Consistency to treat share gains as STCG. Though it is the case of the revenue that due to volume, magnitude, frequency, continuity, regularity, the ratio between purchase and sale clearly indicate that income on account of purchase and sale of shares should be treated as income from business and not as income from STCG, the AO has, from A.Y. 2005-06 to 2009-10 (except for the impugned year & 2006-07), consistently accepted the income as being STCG. In these circumstances, the Rule of consistency as propounded by the Bombay High Court in Gopal Purohit is squarely applicable and the income has to be treated as STCG.

5. Borrowed funds: Use of borrowed funds

The use of borrowed funds for the purpose of buying and selling shares has often been considered by Courts and Tribunals as indicative of activity in the nature of business as against investment.

i) *CIT v. Niraj Amidhar Surti 2010-TIOL-736-HC-AHM-IT*

Merely because the shares had been purchased from borrowed funds obtained on high rate of interest would not change the nature of the transaction from investment to one in the nature of an adventure in the nature of trade.

ii) *CIT v. S. Ramaamirtham [2008] 306 ITR 239 (Mad.)*

The assessee had been holding shares for a long time and had been utilising the surplus funds only for the investments. In earlier years also, the assessee had been showing only capital gains on similar transactions and that was accepted by the Revenue.

iii) *Spectra Shares & Scripts Pvt. Ltd. vs. CIT (2013) 91 DTR 289 (AP)(HC).*

Assessee a non-banking finance company, made all investments with its own fund earned substantial dividend valued closing stock at cost it was held that Assessing officer was right in treating the sale of share under head Capital Gain. Commissioner's action in revising such an order held bad in law.

6. Frequency of transactions

i) *ITO v. Rohit Anand [2009] 34 SOT 242 (Tri.) (Del.)*

The volume of transaction includes the appreciation in shares also and such appreciation has been offered for tax. If volume of transaction is the criteria, what is to be examined is how frequently the transaction is done, whether the transaction is settled in the course of the day of trading itself or in the settlement period itself so as to avoid payment of full purchase price.

7. Calculating the number of transactions

The Revenue authorities usually take into account the number of transactions entered into by the assessee for the purpose of determining whether the assessee is an investor or a trader. For example, a person places an order on the stock exchange to buy 10,000 shares of X Limited. However, due to the illiquidity of the stock, the same are available to him only in 50 smaller transactions, the Revenue authorities usually consider the number of transactions as 50.

i) *Nehal V. Shah v. ACIT, ITA No. 2733/M/2009 dated 15-12-2010.*

In this case, the Mumbai bench of the Tribunal held that when a person places single order on the computer based trading system and the desired number of shares is obtained by him in a series of tranches, the whole transaction ought to be considered as a single transaction. A single transaction would be split by the computers trading of the stock exchange into many smaller transactions.

8. 30 days Theory

Off late, the Tribunals have been taking a view that shares held for a period of less than 30 days are business assets while those held for 30 days or more are investments. This view does not find a place on the statute books, but to settle disputes of this kind, the Tribunals have evolved this principle, wherever appropriate having regard to the facts and circumstances of the case.

i) *Sanjeev Chawla v. Jt. CIT dt. 13-8-2010; Bench "I" Mumbai ITAT ITA No. 5614/M/2009.*

ii) *Sugamchand C. Shah v. ACIT (2011) 37 DTR 345 (Ahd.)(Trib.)*

iii) *Dev Ashok Karvat v. DCIT (2012) 17 Taxmann.com 271 (Mum.)(Trib.)*

iv) The Delhi High Court in case of *CIT v. Sahara India Housing Corporation Ltd.* (Delhi High Court) Source : www.itatonline.org, laid certain guidelines

(a) Whether the initial acquisition of the subject-matter of transaction was with the intention of dealing in the item or with a view to finding an investment?;

(b) Why and how and for what purpose the sale was effected subsequently?;

(c) How the assessee dealt with the subject-matter of transaction during the time the asset was with the assessee. Has it been treated as stock-in-trade or as an investment in the balance sheet?

(d) How the assessee returned the income from such activities and how the department dealt with the same in the preceding and succeeding assessments?;

(e) Whether the deed of partnership or memorandum of association, if the assessee is a firm or a company, authorises such an activity?

(f) Most importantly, what is the volume, frequency, continuity and regularity of transactions of purchase and sale of the goods concerned?

While there are many more Tribunal decisions which one can analyse, if one looks at the general trend of these decisions, one can perhaps deduce the following:

1. It is important to understand from the facts what the intention of the assessee

was in carrying out the transactions. All the relevant facts have to be considered for this purpose. It is therefore important to highlight all the relevant facts at the assessment stage itself.

2. The volume of transactions is not determinative of the issue – the mere deployment of large amounts as investments could also result in large volumes.

3. If the assessee himself treats certain transactions as trading transactions and others as investments, and clearly maintains the distinction between the two, differential tax treatment of the 2 types of transactions is clearly permissible.

4. If the transactions in shares have been treated in earlier years as giving rise to capital gains, the treatment in subsequent years for similar transactions would not change merely on account of the tax exemption/concessional taxation rate.

IV. Portfolio Management Schemes

1) A new mode of investment has off late arisen for investors. It has now become very common for investors to entrust their funds or securities to portfolio managers, who carry out the investment activity on their behalf. Most portfolio managers now insist on a minimum portfolio size of only ₹ 10 lakhs.

2) In case of large investors, the portfolio managers obtain a power of attorney, open a demat account as well as a bank account in the name of the investor, and carry out the transactions in the name of the investor.

However, for smaller investors, portfolio managers had been operating on a pooled basis till a couple of years ago, whereby the portfolio manager deposited the funds received from investors into a common account held in the name of the portfolio manager for a particular scheme, purchased and sold shares for that particular scheme in his own name, with the shares being credited and delivered from a demat account in the name of the portfolio manager for the particular scheme. The portfolio manager, in the books of account of the particular scheme, kept track of the share of investments and bank balance of each investor, which when totalled for all the investors at any point of time, constituted the total investments held in that particular scheme and the bank balance in that particular scheme. The transactions of purchases and sales were allocated on a *pro rata* basis depending upon the funds available of each investor.

At regular intervals, the portfolio manager provided each investor with a statement showing that particular investor's proportionate shares purchased and sold, the proportionate income earned by that particular investor, and the proportionate shareholding and bank balance of the particular investor.

3) How should these transactions of the portfolio manager on a pooled basis on behalf of the investor be taxed in the hands of the investor? In particular, other than the aspect of whether such transactions constituted a business or not in the hands of the investor, some of the interesting issues that arose were:

Given the provisions of section 45(2A), were the gains on such transactions taxable in the hands of the investor or in the hands of the portfolio manager?

Given the fact that the portfolio manager was the registered shareholder through the depository, could the investor still contend that when the dividends are passed on to him by the portfolio manager, they retained the character of dividends? If not, how would such dividend passed on by the portfolio manager to the investor be

treated for tax purposes in the hands of the investor?

If the transactions were such that they constitute a business, considering the fact that section 45(2A) applies only to capital gains, can it be said that the investor is carrying on a business through the portfolio manager? Or is it really the portfolio manager who is carrying on the business and agreeing to pay a percentage of profits to the investors for the funds provided? Can the investors and the portfolio manager be treated as constituting an Association of Persons (AOP)?

Considering the fact that the contracts with the share brokers were in the name of the portfolio manager, can the investor claim (either for the purpose of exemption or for the purposes of deduction) that STT has really been paid by him on those transactions?

4) The answers to these questions can be found in the nature of the relationship between the investor and the portfolio manager. The SEBI (Portfolio Managers) Regulations, 1993 define a portfolio manager as any person who, pursuant to a contract or arrangement with a client, advises or directs or undertakes on behalf of the client (whether as a discretionary portfolio manager or otherwise) the management or administration of a portfolio of securities or the funds of the client, as the case may be. Clause 15(2) of the regulations clearly provides that the portfolio manager shall act in a fiduciary capacity with regard to the client's funds. The portfolio manager is an agent of the investor, and though he may carry on certain transactions in his own name, such transactions are in his capacity as an agent of the investor.

Therefore, on general principles, such transactions are the transactions of the investor carried out through an agent, the income from such transactions is liable to tax as the income of the investor, and would take its colour from the circumstances surrounding the actions of the investor. Similarly dividends received by the portfolio manager is received by him in his capacity as an agent of the investor, and accordingly such dividends are taxable (or exempt) in the hands of the investor as dividends. Similarly, STT paid by the portfolio manager is paid by him in his capacity as an agent of the investor, and therefore should be regarded as payments by the investor himself. Accordingly, the investor is entitled to claim exemption or deduction on account of such STT.

A relationship between the portfolio manager and an investor cannot be regarded as constituting an AOP, because the entire transactions are carried out by the portfolio manager to whom the funds have been entrusted by the investor as an agent of the investor. Therefore, all actions are those of an investor through his agent. There is no commonality of purpose between the portfolio manager and the investor, since the portfolio manager is seeking to earn his fees for the work done on behalf of the investor, while the investor is seeking to maximise the return on his investments. It is merely a common interest in ensuring that the value of the investments appreciates so that the investor gets the maximum yield on his investments while the portfolio manager earns the maximum fees. The Andhra Pradesh High Court in the case of *Deccan Wine and General Stores v. CIT 106 ITR 111,* had held that there must be a common design to produce income and common interest or production of income are not enough to constitute an AOP. However, this decision may no longer be valid, given the amendment to section 2(31), whereby an explanation has been inserted to clarify that an association

of persons shall be deemed to be a person whether or not it was formed or established or incorporated with the object of deriving income, profits or gains. What would be therefore the position today?

Fortunately, SEBI, *vide* SEBI (Portfolio Managers) (Amendment) Regulations, 2008 dated 11th August, 2008, has amended regulation 16(8) to provide that a portfolio manager cannot hold securities in its own name beyond a period of 6 months from the date of the amendment regulations. This time limit was extended by a further 3 months, and therefore, the practice of pooling of investments by portfolio managers has been discontinued from May 2009, and currently all clients securities holdings are in demat accounts in the names of clients. However, SEBI has clarified that funds of all clients can be kept in a combined separate bank account, with clear segregation of each client's funds through back-office records, with proper reconciliation and reporting to clients to ensure that funds of one client are not used for another client.

The manner of operation of portfolio managers also does create problems at times for investors from the perspective of classification as capital gains or business income. A few of the questions which arise in this regard are:

1. Does the appointment of a portfolio manager by an investor amount to creation of an infrastructure by the investor, giving the transactions the colour of business transactions?

2. The frequent churning of the portfolio by the portfolio manager increases the number of transactions, besides at times resulting in a low holding period. Does this change the nature of the transactions from capital gains to business income?

3. Often portfolio managers take client instructions as to whether they desire their portfolio strategy to be aggressive, defensive or balanced. Does such categorisation matter for the purposes of deciding whether transactions are in the nature of investment or business? For instance, does the choice of an aggressive investment strategy resulting in high risk, high reward, mean that the transactions constitute a business?

Generally, the investor has no choice as to the method of valuation of investments which the portfolio manager follows in submitting statements to the investor, as the portfolio manager follows a standard practice for all clients. Most portfolio managers do follow the principle of computing the gains on sale of the investments on a FIFO basis, since most of the clients are investors in shares and this facilitates computation of their capital gains. The opening balance and closing balance of shares is normally computed on a market value basis, to facilitate computation of the portfolio management fees. This generally does not create any difficulty for an investor, who computes his capital gains on the same basis and for whom the valuation of the shares held is not really relevant for tax purposes. The problem really arises if the transactions of the portfolio manager are classified as a business by the client for his tax purposes. The question then arises as to whether the method of valuation followed by the portfolio manager is binding on the client, or whether he can choose to follow a different method of accounting. The portfolio manager, in the statements given to the client, is merely rendering accounts to the client as an agent, and therefore the method of accounting followed in rendering such accounts should not be relevant for taxation purposes of the client. In any case, the manner of computing cost of bonus shares would differ in such a case, as the method of averaging would have to be followed by the client, though the portfolio manager may compute the gains by taking the cost of such shares at nil.

Most portfolio managers compute the annual portfolio management fees either as a flat amount or a fixed percentage of the opening or closing

value of the assets under management, besides an incentive for a return exceeding a particular level. For example, a portfolio manager may quote a fee of 1% of the assets under management, with 20% of the annual returns in excess of 6% of the assets. SEBI has now mandated the high watermark principle, under which the shortfall in return in one year has to be made good in the subsequent year before becoming eligible for the incentive fee. Those clients treating the portfolio transactions as business transactions have no difficulty in claiming such fees as a deductible expenditure, other than facing the question of whether tax has been deducted at source in respect of such fees in case they are liable to tax audit in the earlier year. Generally, tax would be deductible at source under section 194J as fees for technical services in such cases.

The deductibility of portfolio management fees is an issue faced by investors. Can an investor claim deduction for the portfolio management fees that he pays from the computation of his capital gains which is liable to tax? Can an investor claim that the fees paid to the portfolio manager are either for purchase of shares or for sale of shares, and are therefore either part of the cost of acquisition or expenses in connection with transfer? Since the income earned through the portfolio manager consists of long term capital gains, short-term capital gains as well as dividend, what would be the extent of such fees that could be claimed as a deduction? How can an investor claim the fees in respect of shares which are not yet sold as at the year end?

An activity of sale of shares and securities carried on by any businessman/professional, in addition to their regular business/profession, gain arising due to the same, under which head same shall be taxed?

Whether it shall be taxed as a Capital gain or under the head business income?

i) *Apoorva Patni v. Addl. CIT (2012) 24 Taxmann.com 223 (Pune)(Trib.).*

The assessee declared the capital gains in respect of investments made through the PMS providers. The Assessing Officer assessed the long-term as well as short-term gains as business income. On appeal Commissioner (Appeals) upheld the contention of assessee. On further appeal to Tribunal by revenue, the Tribunal held that by engaging PMS provider, assessee was looking for appreciation and maximisation of wealth and not merely encashing of profits as trader, gain from such activity was liable to be considered as derived from activity of investment and not trading hence liable to be assessed as capital gains (A.Y. 2006-07).

ii) *Slil Shah Family (P.) v. ACI [2013] 144 ITD 390 (Mum.)(Trib.)*

The Tribunal considering the nature of transaction through Portfolio Management Services providers which had resulted into capital gains, STCG and LTCG as eturned by the assessee. It was held that the Assessing Officer should accept the capital gains as returned by the assessee.

Other case Law:

- *ITO v. Rohit Anand (Del. ITAT) 34 DTR 89*
- *Sugamchand C. Shah v. ACIT (Ahd.) (ITAT) 37 DTR 345*
- *ITO v. Radha Birju Patel, (Mum.)(Trib.)*
- *Smt. Nalini Navin Bhagwati v. ITO (Mum.) (Trib.)*
- *ARA Trading & Investment Pvt. Ltd. v. DCIT (2011) 47 SOT 172 (Pune).*

Currently, the issue of share transactions through portfolio management scheme is pending before the Special Bench of the Delhi Tribunal in the case of M/s. Suraj Overseas Pvt. Ltd. For the time being, it appears that this controversy would be settled once the Special Bench decides the issue.

V. Section 50: Provisions of section 50 versus provisions of section 50C

i) The provisions of section 50 come into picture where the relevant block of

depreciable assets has ceased to exist on account of the transfer of all the assets comprised in that block or on account of the net sale proceeds of some of the assets of the block exceeds the depreciable value of the relevant block comprising the opening written down value of the block together with the cost of additions, if any, during the relevant previous year. Section 50 only modifies the "cost of acquisition" in case of depreciable assets for computing capital gains whereas the expression "the full value of consideration received or accruing as a result of transfer of the asset" used in section 48 remains the same and hence the fiction contained in section 50C(1) applies in full force for computing the short-term capital gains also as provided in section 50. This position gets support from two facts – (i) section 50 is already part of the statute at the time of insertion of section 50C and the operation of section 50C is not excluded through any limiting cause and (ii) by obtaining the provision of section 50C if and when section 50 is applicable. Applying the provisions of section 50C in the context of section 50 does not amount to extension of the legal friction created in section 50C beyond its legitimate field and there is no conflict between the two legal fictions contained in section 50 and section 50C as they operate in different fields. Further, section 50C is applicable to all capital assets relating to which computation is to be made under section 45 and no distinction is made between a depreciable asset and a non-depreciable asset in section 50C. *[ITO v. United Marine Academy (2011) 138 TTJ (Mumbai)(SB) 129].*

ii) *ITO v. United Marine Academy [2011] 130 ITD 113 (Trib.) (Mum.) (SB)*

The deeming fiction created in section 50C thus operates in a specific field which is different from the field in which section 50 is applicable. Provision of section 50C to the transfer of depreciable capital assets covered by section 50 is applicable in computing the capital gain arising from the said transfer by adopting the stamp duty valuation.

iii) Section 50 makes special provision for the computation of capital gains in the case of depreciable assets. There is no explicit requirement in the statutory provision to the effect that the new asset should also be used in a business carried on by the assessee.

The Tribunal held that sec. 50 makes special provision for the computation of capital gains in the case of depreciable assets. There is no explicit requirement in the statutory provision to the effect that the new asset should also be used in a business carried on by the assessee.

Lalbhai Kalidas & Co. (ITAT Tribunal Mumbai) ITA No. 5832/M/2011 for A.Y. 2007-08 dtd. 8-11-2013 before Bench "A".

a) *Artic v. Asst. CIT (1999) 68 ITD 462 (Mum.)*

b) *Orient Cartons P. Ltd. v. Dy. CIT (1997) 57 TTJ 302 (Mum.)*

c) *Oceanic Invt. Ltd v. ACIT (1997) 57 TTJ 549 (Mum.)*

d) *Chhabria Trust v. Asst. CIT (2003) 87 ITD 181 (Mum.) (S B)*

e) *Fluorescent Fixtures (P.) Ltd. v. ITO (2009) 34 SOT 48 (Mum.).*

VI. Exemptions

Sections 54-54GB deal with exemptions i.e. circumstances when the capital gains earned by an assessee can be partly or wholly exempted. The idea behind granting of these exemptions is to lessen the burden of the assessee who could be suddenly saddled with a high tax liability, when in fact, he may desire only to improve the quality

of his existing asset. E.g. if a person lives in an old ancestral residential house and owing to its condition, he wants to purchase a new house, the gain on sale of his ancestral house could be substantial. While most of his cash inflow would be utilised towards purchasing the new house, he may not have sufficient funds to discharge his tax liability. In order to avoid this practical and genuine problem, the exemption provisions seek to offer some respite to the assessees.

The main purpose of section 54 is to give relief in respect of profits on the sale of a residential house. There is no special Rule for interpreting exemption provisions. Both Rules of strict as well as liberal construction require to be invoked at different stages as had been pointed out in *Union of India v. Wood Papers Ltd. AIR (1991) SC 2049*.

"A Caravan may be residence within this provision" *Markins v. Elson (1978) TLR 634 UK*.

In *CIT v. Aravind Reddy (TN) (1979) 120 ITR 46 (SC) (48*)

The Supreme Court succinctly summed up the object, purpose and symmetry of the section in the following words:

> "If you sell your house to make a profit, pay Caesar what is due to him. But, if you buy or build another, subject to the conditions of section 54(1), you are exempt."

Time and again, controversies have arisen as regards the claims of assessees for exemption. Some of the controversies are discussed below:

I. Section 54: Profit on transfer of house property used for residence

Benefit of section 54 is confined to sale of a residential house after 36 months and reinvestment in a residential house. Reinvestment benefits is available both for purchase and construction of the house. Purchase has to be either one year before or two years later. Construction has to be completed within three years of the sale of the asset in respect of which benefit of reinvestment is claimed.

Both the section 54 and 54F are available to the Individuals and HUFs only

There have been many decisions on purchase/construction of the house. Some important issues are dealt hereunder:

i) Bar on number of houses to be constructed

This controversy arises mainly because the wording used in section 54 is "constructed, a residential house". The tax authorities have time and again given a hyper-technical interpretation to these words and contended that the word "a" implies that the assessee must purchase or construct one and only one house.

a) *CIT v. Gita Duggal [2013] 357 ITR 153 (Delhi) (HC)*

b) *CIT v. Raman Kumar Suri [2013] 212 Taxmann 411 (Bom.) (HC)*

The fact that the residential house consists of several independent units cannot be permitted to act as an impediment to the allowance of the deduction under section 54. It is neither expressly nor by necessary implication prohibited.

c) *ITO v. Ms. Sushila M. Jhaveri [2007] 107 ITD 327 (Trib.) (Mum.) (SB)*

The word "a" means "any" which means "many" or "more than one".

d) *Smt. V. R. Karpagam v. ITO [2013] 143 ITD 126 (Trib.) (Chennai)*

"A residential house" under section 54F (and also section 54) cannot be construed to mean singular house. Singular shall include plural.

e) *CIT v. D. Ananda Bassappa (2009) 309 ITR 329 (Kar.)*

f) *CIT v. Smt. K.G. Rukminiamma (2011) 331 ITR 211 (Kar.)*

2. Acquisition of tenancy rights in flat – Whether covered?

i) *Yogesh Sunderlal Shah v. ACIT [2012] 139 ITD 194 (Trib.) (Mum.)*

For the purpose of exemption u/s 54, the assessee has to buy the property as owner and not as perpetual tenant. The agreement showed that the assessee was tenant and not owner of the flat. Hence, exemption could not be granted to the assessee.

ii) *Vinod V. Chhapia v. ITO (2013) 56 SOT 465 (Mum.)(Trib.)*

Tenancy Right transfer – Taxability in the hands of the landlord – held to Income from Others Sources.

Amount received by the assessee landlord for mere consent of tenancy rights from old tenant to new tenant cannot be said to be for transfer of capital assets and accordingly, the amount cannot be brought to tax under "capital gains"

iii) *Ajit M. Pendukar v. ITO ITA No. 3225/M/2009 "G" Bench dt. 19-12-2012.*

Conversion of Tenancy rights into ownership – Ownership flat sold – What is the cost of Tenancy right to be considered for determining capital gains. Matter set aside to A.O.

3. Whether payment for car parking covered under the scope of section 54?

- Parking space ultimately makes the residential habitable;
- Parking is an integral part of the house;
- Cost of parking is recovered from the flat buyer as cost of flat itself.

4. Whether completion of construction/ occupation of house necessary?

While the statute does not speak of completion of construction or its occupation as prerequisites for availing the deductions, the statute does prescribe for withdrawal of deduction if the purchase/construction is not complete within the prescribed time.

CIT v. Mrs. Hilla J. B. Wadia [1995] 216 ITR 376 (Bom.) (HC)

In this case, it was held that the intention of the Legislature was to promote and encourage investment in the new residential asset and completion of construction or occupation was not a must.

Allotment of a flat by DDA under the Self-Financing Scheme shall be treated as construction of the house [Circular No. 471, dated 15-10-1986]. Similarly, allotment of a flat or a house by a co-operative society, of which the assessee is the member, is also treated as construction of the house [Circular No. 672, dated 16-12-1993]. Further, in these cases, the assessee shall be entitled to claim exemption in respect of capital gains even though the construction is not completed within the statutory time limit. [*Sashi Varma v. CIT (1997) 224 ITR 106 (MP)*]. Delhi High Court has applied the same analogy where the assessee made substantial payment within the prescribed time and thus acquired substantial domain over the property, although the builder failed to hand over the possession within the stipulated period. [*CIT v R.C. Sood (2000) 108 Taxmann 227 (Del)*].

Also see other decisions on the similar issue.

CIT v. Anilaben Upendra Shah (2003) 262 ITR 657 (Guj.)

Vinod Kumar Jain v. CIT (2010) 195 Taxmann 174 (P&H)

Charanbir Singh Jolly v. 8th ITO (2006) 5 SOT 89 (Mum.)

Smt. Lata G. Rohra v. Dy. CIT (2008) 21 SOT 541 (Mum.)

5. Cost of improvement

In terms of s. 48(ii), cost of improvement is allowable as deduction while computing the cost of original asset sold giving rise to the issue that whether the expenditure incurred in making the house habitable also qualifies for exemption u/ss. 54/54F.

– This issue came up for consideration in the following cases

1. *Mrs. Gulshanbanoo R. Mukhi v. JCIT 88 ITD 649 (Mum.)*
2. *Sonia Gulati vs. ITO 115 Taxmann 232 (Mag.) (Mum.)*
3. *Saleem Fazelbhoy v. DCIT (2006) 9 SOT 601 (Mum.)*

And in all these cases it has been held that the investment in residential house would not only include the cost of purchase of the house but also the cost incurred in making the house habitable. An inhabitable premise cannot be equated with a residential house. Therefore, the investment in house would be complete only when such house becomes habitable. Accordingly, the expenditure incurred on making the house habitable should be conserved as investment in purchase of the house, subject to the conditions that the payments are made within the period prescribed u/s. 54/54F.

However one may take adequate care in distinguishing the expenditure incurred on making house habitable and the expenditure on renovation just to make the house more comfortable which may be claimed as cost of improvement u/ss. 48(ii) at the time of sale.

6. Condition of exemption not fulfilled

Owing to the present circumstances in the housing sector, residential apartments are rarely ready within a period of three years. This gives rise to substantial difficulty for the assessees as not only do they not get possession of their flats which they purchased in good faith but also face the possibility of withdrawal of exemption. It is desirable that the limit of two/three years be increased to factor in delays in construction, obtaining approvals etc.

Moreover, the Revenue authorities seek to withdraw the exemption in the year in which exemption is claimed rather than taxing such amount in the year in which the two/three years' window for purchase/construction expires. This results in higher interest liability for the assessees. In most cases, the assessees would contend that exemption should be taxed in the third year.

However, it is not uncommon for assessees for merely postponing their tax liability to the third year, to invest in plots, etc. without any intention to actually construct a house thereon. Since this would involve an abuse of a beneficial provision, the tax authorities must be circumspect while dealing with such situations. However, in genuine cases where the delay in construction of house cannot be attributed to the assessee, the Revenue authorities must take a reasonable stand and tax, if at all, the capital gains in the third year.

i) *Sri Prasad Nimmagadda v. DCIT [2013] 56 SOT 473 (Hyd.) (Trib.)*

Assessee's claim of exemption under section 54 of the Act could not be denied in the year in which exemption is claimed in view of proviso to section 54 and the Assessing Officer must verify whether the assessee has offered the capital gain for taxation in the subsequent AY in which the period of three years expires.

ii) *Pushp Devi Tibrewala (Smt.) vs. ITO (2013) 58 SOT 41 (Hyd.)(Trib.)*

Assuming the construction is not completed within 3 years, the exemption can be withdrawn when 3 years expires.

7. No exemption under section 54 if land only is sold

The house property concerned must be building or land appurtenant to building. The basic test was whether the land appurtenant to building could be used independent of the user of the building. If so, it cannot be said to be land appurtenant to building. Further, the basic requirement is that the capital gain should arise from the transfer of building or land, the income of which is chargeable under the head Income from house property. If the land alone is sold, the provisions of section 54 will have no application inasmuch as the income from land is not chargeable under the head Income from house property. *[CIT v. Zaibunnisa Begum (1985) 151 ITR 320 (AP)].*

Another important issue for consideration is whether the sale consideration is whether the sale consideration can be apportioned between the cost of the land and the building and the computation of capital gain be made accordingly. In other words, whether the bifurcation of sale proceeds is permitted for computing capital gains in respect of land and building separately.

This issue came for consideration before various courts and it has been held that the sale consideration should be bifurcated on a scientific basis to arrive at an apportionment between land and building for claiming benefit u/ss. 54/54F.

Refer :

(1) *CIT v. C. R. Subramanian (2000) 242 ITR 342 (Kar)*

(2) *CIT v. Dr. D. L. Ramachandra Rao (1999) 236 ITR 11 (Mad)*

(3) *CIT v. Vimalchand Golecha (1993) 201 ITR 442 (Raj.)*

II. Capital gain on transfer of land used for agricultural purposes [Section 54B]

Any capital gain (short-term or long-term), arising to an assessee (individuals and HUF), from the transfer of any agricultural land which has been used by the assessee or his parents for at least a period of 2 years immediately preceding the date of transfer, for agricultural purposes, shall be exempt to the extent such capital gain is invested in the purchase of another agricultural land within a period of 2 years after the date of transfer to be used for agricultural purpose, provided the new agricultural land purchased, is not transferred within a period of 3 years from the date of its acquisition.

a) *Asha George (Smt.) v. ITO (2013) 351 ITR 123 (Ker.) HC*

b) *ACIT v. N. Raghu Varma (2013) 24 ITR 616 (Hyd.)(Trib.)*

III. Section 54EC: Capital gain on transfer of long-term capital assets not to be charged on investment in certain bonds [Section 54EC]

Any long-term capital gain, arising to any assessee, from the transfer of any capital asset on or after 1-4-2000 shall be exempt to the extent such capital gain is invested within a period of 6 months after the date of such transfer in the long-term specified asset provided such specified asset is not transferred or converted into money within a period of 3 years from the date of its acquisition.

- The exemption u/s. 54EC is available to any assessee as against the exemption available to "Individuals or HUFs u/s. 54/54F.
- The exemption u/s. 54EC is available only if the assessee has invested the whole or any part of the Long-term capital gain within six months from the date of transfer of the Long-Term capital asset.
- Such investment has to be made only in the Long-Term specified assets which means any bonds redeemable after 3 years.

- If these bonds are transferred or converted into money at any time within a period of three years from the date of its acquisition, then the amount of capital gain not so charged under s. 45 originally would be chargeable as Capital Gains in the previous year in which such bonds are transferred or converted into money.
- If any loan is taken against the security of these bonds, then it shall be deemed that the bonds have been converted (otherwise than by transfer) into money on the date on which such loan, or advance is taken.
- Once the claim of exemption is made under this section, then no claim for deduction can be made for the investment made either u/s. 88 or 80C as the case may be.

1. Limit of ₹ 50 lakh

a) *ACIT v. Raj Kumar Jain & Sons (HUF) [2013] 153 TTJ 49 (Trib.) (URO) (Jp.)*

Deduction under section 54EC for investment in the specified bonds must be restricted to ₹ 50 lakhs.

b) *ITO v. Rania Faleiro (Ms.) [2013] 142 ITD 769 (Panaji) (Trib.)*

The assessee had sold a property on 5-2-2008. Assessee invested a sum of ₹ 50 lakhs out of sale consideration in Capital Gains Bonds on 31-3-2008. Assessee thereafter invested a sum of ₹ 50 lakhs on 30-6-2008 in Capital Gains Bond. Assessee claimed exemption under section 54EC on the amount of ₹ 1 crores. Assessing Officer allowed only ₹ 50 lakhs. The language of section 54EC is clear and unambiguous and it leads to the interpretation that the assessee can make the investment in two different financial years provided in a financial year the investment made did not exceed ₹ 50 lakhs. Accordingly the assessee was entitled to exemption in respect of both investments in capital gain bonds.

c) *Aspi Ginwala & Ors. v. ACIT (2012) 52 SOT 16 (Ahd.)(Trib.)*

As per proviso to section 54EC, where assessee transfers his capital asset after 30th September of the financial year he gets an opportunity to make an investment of ₹ 50 lakhs each in two different financial years and is still able to claim exemption up to ₹ 1 crore. Exemption u/s 54EC is duly available where there is a delay in making investment due to non-availability of the bonds

2. Applicability to sale of business assets treated as short-term capital assets.

As per section 50, business assets on which depreciation is allowed, is treated as short-term capital assets, and gain on their sale is taxable as short-term capital gains. A question arises whether benefit of exemption under section 54EC which is available only on sale of long-term capital assets.

i) *CIT v. Ace Builders (P) Ltd. [2006] 281 ITR 210 (Bom.) (HC)*

In the present case, the asset sold was a long-term capital asset, but was treated as short-term capital asset under the deeming provision of section 50. Held, there is nothing in section 50 to suggest that the fiction created therein is not only restricted to sections 48 and 49 but also applies to other provisions. Therefore, the exemption under section 54E of the IT Act cannot be denied to the assessee on account of the fiction created in section 50.

The above decision was followed by the Bombay High Court in a subsequent case of *CIT v. Legal Heirs of late Dr. (Mrs.) S. R. Pandit [Income-tax Appeal No. 775 of 2005]* and a Special Leave Petition of the Revenue authorities was rejected by the Supreme Court on March 23, 2007.

IV. Section 54F

- S. 54F provides for exemption from taxation of a Long Term Capital Gain arising from transfer of a Long Term Capital Asset other than the Residential House.
- Both the section 54 and 54F are available to the Individuals and HUFs only

1. Whether the new residential house must necessarily be in the name of assessee.

   i) *CIT v. Kamal Wahal [2013] 351 ITR 4 (Delhi) (HC)*

   Held that for the purposes of section 54F, the new residential house need not be purchased by the assessee in his own name nor is it necessary that it should be purchased exclusively in his name.

   ii) *DIT (IT) v. Jennifer Bhide (Mrs.) [2012] 349 ITR 80 (Karn.) (HC)*

   Assessee, out of sale proceeds of residential property, purchased another residential property and specified bonds. Exemption under sections 54 and 54EC could not be denied to her to the extent of 50% on the ground that new property and bonds were purchased in the names of assessee and her husband when admittedly no consideration followed from the husband.

   iii) *Prakash v. ITO 312 ITR 40 (Bom.)(HC)*

   Purchase in the name of Adopted Son not allowed.

2. Whether the term "residential house" necessarily implies element of habitability.

   i) *Usharani Kalidindi (Smt.) v. ITO [2013] 25 ITR 409 (Hyd.) (Trib.)*

   The house for which exemption is claimed must be inhabitable and should have had basic amenities like a place for cooking, toilet and bathroom, approach road within plot. Exemption could not be granted when there was no evidence of grant of electricity or telephone or water connection.

   ii) *Ashok Syal v. CIT (2012) 209 Taxmann 376 (P&H)*

   Construction of new house S. 54.

   It was further recorded that a house was one which could be used by the assessee for his residence and putting up of tin sheds for being used by somebody to reside without there being basic living amenities like bathroom, kitchen, electricity, etc., would not pass the definition/test of "dwelling unit" or a "house". In view of the above, no illegality could be found in the findings recorded by the Tribunal. Accordingly, it is held that the property was not a house and the assessee was not entitled to the benefit u/s. 54.

   iii) *CIT v. Sambhanandan Udaykumar (2012) 345 ITR 389 (Kar.)(HC)*

   Section 54F of the Act is a beneficial provision of promoting the construction of residential house. Therefore, the said provision has to be construed liberally for

achieving the purpose for which it was incorporated in the statute. The intention of the Legislature was to encourage investments in the acquisition of a residential house and completion of construction or occupation is not the requirement of law. The words used in the section are 'purchased' or 'constructed'. For such purpose, the capital gain realised should have been invested in a residential house. The condition precedent for claiming benefit under the said prevision is the capital gain realised from sale of capital asset should have been parted by the assessee and invested either in purchasing a residential house or in constructing a residential house. If after making the entire payment, merely because a registered sale deed had not been executed and registered in favour of the assessee before the period stipulated, he cannot be denied the benefit of section 54F of the Act. Similarly, if he has invested the money in construction of a residential house, merely because the construction was not complete in all respects and it was not in a fit condition to be occupied within the period stipulated, that would not disentitle the assessee from claiming the benefit under section 54F of the Act. The essence of the said provision is whether the assessee who received capital gains has invested in a residential house. Once it is demonstrated that the consideration received on transfer has been invested either in purchasing a residential house or in construction of a residential house even though the transactions are not complete in all respects and as required under the law, that would not disentitle the assessee from the said benefit.

3. Failure to construct new house property within the specified time.

In case the assessee fails to construct the new residential property for which exemption is claimed within the prescribed time, an issue arises whether the exemption is to be withdrawn for the year in which it was allowed or is to be treated as income of the year in which the time limit for fulfilment conditions expires.

i) *Anu Agarwal (Smt.) v. ITO [2013] 55 SOT 294 (Chd.) (Trib.)*

In the instant case, no plans for construction of house were made. Therefore, there is no question of getting the same approved. Apart from this, assessee admitted that assessee has no evidence to prove that assessee wanted to start construction. If the tax is allowed to be postponed merely on the basis of purchase of plot then no assessee would pay correct taxes during the year and postpone the payment of taxes by merely purchasing the plot and that cannot be intention of the provisions of section 54F.

4. Residential house purchased outside India – whether entitled to exemption:

i) Where non-resident Indian sold property in India and purchased residential property in U.K. and claimed deduction under section 54, it was held that it was not necessary that residential property showed be purchased in India itself. [*Mrs. Prema P. Shah, Sanjiv P. Shah v ITO (2006) 282 ITR (AT) 211 (Mumbai)*]. However, a contrary view has been

given in respect of section 54F in the case of *Leena J. Shah v. ACIT (2006) 6 SOT 721 (Ahd)*.

ii) *Vinay Mishra v. ACIT [2013] 141 ITD 301 (Trib.) (Bang.)*

The words 'in India' cannot be read into section 54F, when Parliament in its legislative wisdom has deliberately not used the words 'in India' in section 54F, thereore exemption under section 54F cannot be denied on ground that residential house acquired was situated outside India.

5. Exchange of old flat for a new one

i) *Jatinder Kumar Madan v. ITO [2012] 51 SOT 583 (Mum.) (Trib.)*

Acquisition of new flat under a development agreement in exchange of old flat amounts to construction of new flat for purpose of claiming deduction under section 54.

ii) *Veena Gope Shroff (Smt.) vs. ITO (2013) 58 SOT 36 (Mum.) (Trib.)*

New flat received in exchange of old flat. Constructed by builder amounts to construction.

6. Delay in deposit of money in capital gains scheme.

i) *Sunil Sachdeva v. ACIT [2013] 56 SOT 321 (Trib.) (Delhi)*

The assessee on 30-7-2008, prior to the due date for filing of return under section 139(1), had issued instruction to its bank to transfer the relevant amount from savings bank account to the special capital gain account maintained with the same branch of the said bank. In this regard, the assessee also furnished a certificate from the bank confirming this factual position. Assessee having issued necessary instructions to the aforesaid bank in which both the accounts (i.e., savings bank account as well as special capital gain account) were maintained for transfer/deposits, the assessee proceeded to file his return of income on the same date i.e. 30-7-2008. The instructions of the assessee were acted upon by the bank only on 31-7-2008. Held, there was sufficient compliance with the mandate of section 54F by the assessee, and benefit could not be denied on this ground.

ii) *CIT v. Ms. Jagriti Aggarwal (2011) 339 ITR 610 (P&H)(HC)*

Sub-s. (4) of s. 139 is in fact, a proviso to sub s. (1) and provides for extension of period of due date for filing the return in certain circumstances and, therefore, exemption under s. 54 was allowable where the assessee had purchased new property before the extended due date of filing of return as per s. 139(4) and filed return within such extended time.

7. Deemed value cannot be considered for the prupose of section 54EC (50C).

Nila V. Shah (Mrs.) v. ITO (2013) 83 DTR 218 (Mum.)(Trib.)

8. Voluntary demolition of House will not amount to transfer and assessee is not eligible for exemption.

CIT v. Mrs. Abhay B. Parikh; ITA No. 1583 dt. 24/1/2013 (Bom.)(HC)

[Source : Paper presented at 17th National Convention held on 26th & 27th December 2013 at Mumbai]

Whether claim for deduction, not made in the return, can be made subsequently

CA A. K. Srivastava

Income-tax Act, 1961, is a complicated piece of legislation. It is a ritual to amend the Act every year, generally through the Finance Act of the year. Sometime the Act is also amended through Amendment Act. No other Act undergoes as much amendments as Income-tax Act does. At times, there may be valid reasons for such amendments but of late it is noticed that many amendments are made to overcome judicial decisions.

2. Section 139 of the Act governs the filing of return of income. Sub-section (I) requires the specific category of persons to furnish their return of income, in the prescribed form and verified in the prescribed manner, by a specified date. The person is also required to provide such other particulars as may be prescribed. Certain exceptions to the general rule have been provided.

3. Sub-section (3), requires a person,who has incurred loss under the head "Profits and Gains of business or profession" or under the head "Capital gains" and claims the loss or any part thereof to be carried forward, under the relevant provision, to file the return of income by the due date as prescribed under sub-section (I).

4. Sub-section (5) of section 139, permits a person, who has filed the return of income as required under section 139(I) or in pursuance of notice under sub-section (I) of section 142, to file a revised return, if the assessee discovers any omission or wrong statement therein. The revised return is to be filed at any time before the expiry of one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier.

5. Article 265 of the Constitution of India lays down that no tax shall be levied except when authorised by law. Following this Article, only legitimate tax can be recovered and even a concession by a tax-payer does not give authority to the tax collector to recover more than what is due from him under the law.

6. **CBDT's Circular No. 14(XL-35) dated 11-4-1955**

In the said circular, the CBDT observed that:

"3. Officers of the Department must not take advantage of ignorance of an assessee as to his rights. It is one of their duties to assist a taxpayer in every reasonable way, particularly in the matter of claiming and securing reliefs and in this regard the Officers should take the initiative in guiding a taxpayer where proceedings or other particulars before them indicate that some refund or relief is due to him. This attitude would, in the long run, benefit the Department for it would inspire confidence in him that he may be sure of getting a square deal from the Department. Although, therefore, the responsibility for claiming refunds and reliefs rests with assessee on whom it is imposed by law, officers should :-

(a) Draw their attention to any refunds or reliefs to which they appear to be clearly entitled but which they have omitted to claim for some reason or other;

(b) Freely advise them when approached by them as to their rights and liabilities and

as to the procedure to be adopted for claiming refunds and reliefs."

6. The intention of this circular is not that tax due should not be charged or that any favour should be shown to anybody in the matter of assessment, or that where investigations are called for, they should not be made. Whatever the legitimate tax it must be assessed and must be collected. The purpose of this circular is merely to emphasise that we should not take advantage of an assessee's ignorance to collect more tax out of him than is legitimately due from him."

The above circular has been judicially noted and approved in many judgments and has been relied upon in support of the assessees' claim.

7. An assessee, after filing the return, may at a later stage, realise that a claim or deduction allowable under the Act has been omitted or the quantum thereof is not correct. If the return has been filed by the due date as prescribed and a period of one year from the end of the relevant assessment year has not elapsed, he may revise the return by filing a revised return.

8. If however, the assessee, filed the return after the due date, he would not be entitled to file a revised return as held in *Jagdish Kumar Sinha v. CIT 220 ITR 67 (SC).* In case the assessee filed the return by due date, but a period of one year from the end of the relevant assessment year has elapsed, subsequently notices that proper deduction was not claimed, still he can not revise the return. What can the assessee do in such a situation? Should he be denied the proper deduction or some respite is available to him?

9. **Goetze (India) Ltd. v. CIT 284 ITR 323 (SC) judgment dated 24-3-2006**

The assessee filed its return of income on 30-11-1195 for A.Y. 1 995-96. During assessment proceedings it sought to claim a deduction by way of a letter dated 12-1-1988. The deduction as disallowed by the Assessing Officer on the ground that there was no provision under the Income-tax Act to make amendment in the return of income otherwise than by revising the return.

In appeal before the CIT(A), the assessees' claim was allowed. However the ITAT allowed Departments' appeal against the order by CIT(A). The assessee in appeal before the Supreme Court relied upon the Apex Court' decision in *National Thermal Power Co. Ltd. v. CIT (1998) 229 ITR 383 (SC)* to contend that it was open to assessee to raise the points of law even before the Tribunal.

The Apex Court held that the claim of deduction not made in the return cannot be entertained by the assessing officer otherwise than by filing a revised return. The court also held that the decision does not impinge upon the powers of the Tribunal under section 254 of the Act.

The judgment in Goetze's case has opened the flood gate to litigation.

10. **Distinction between a Fresh Claim and Revised Claim**

A distinction needs to be made between a fresh claim made during the assessment proceeding through a letter and revision of return. In a case where no claim was made in the return , the judgment in Goetze's' case is generally relied upon by the assessing officer, ignoring the Circular No. 14(XL-35) cited above. However, where necessary evidence in respect of a claim is already on record but the quantum of deduction needs revision due to various factors, the assessees' claim through a letter ought to be accepted. In such cases there is already a claim by the assessee and there being no fresh claim the judgment in Goetze's case, with due respect shall not be applicable.

The Allahabad High Court in *CIT v. Dhampur Sugar Ltd. 90 ITR 236 (All.)* made a distinction between revised return and a correction of return. It held that:

"There is distinction between a revised return and a correction of return. If the assessee files some application for correcting a return already filed or making amends therein, it would not mean that he has filed a revised return. It will retain the character of an original return. but once the revised return is filed, the original return must be taken to have been withdrawn and to have been substituted by a fresh return for the purpose of assessment."

11. **Appellate Authorities jurisdiction to entertain fresh claim – Judgments subsequent to Goetze**

Goetze judgment gave a tool in the hands of the assessing officer to deny the benefit of deduction not claimed in the return, but made by way of letter/revised computation, even though necessary information was available before the assessing officer in the assessment proceeding. Aggrieved by the action of the assessing officers, the assessees have agitated the issues before Appellate Authorities. Some of the judgments are cited hereinafter.

- *Commissioner of Income Tax v. Jai Parbolic Springs Ltd. (2008) 306 ITR 42 (Del.)*

The assessee claimed 1/5th of expenditure on account of customer introduction charges in the return of income and treated the balance as deferred revenue expenditure. The assessing officer allowed the claim. In appeal before the CIT(A), by way of additional ground of appeal, the assessee claimed the entire expenditure as allowable deduction. The CIT(A) allowed the claim. The ITAT, in appeal by the department, restored the issue to the assessing officer to consider and decide the issue after examining the details. The assessing officer, in the fresh order did not allow the claim on the ground that it was not made in the return. Both the CIT(A) and the ITAT held that the claim was allowable and allowed the same.

The Hon'ble Delhi High Court held that:

"17. In *Goetze (India) Limited v. Commissioner of Income Tax 284 ITR 323 (SC)* wherein deduction claimed by way of a letter before Assessing Officer, was disallowed on the ground that there was no provision under the Act to make amendment in the return without filing a revised return. Appeal to the Supreme Court, as the decision was upheld by the Tribunal and the High Court, was dismissed making clear that the decision was limited to the power of assessing authority to entertain claim for deduction otherwise than by revised return, and did not impinge on the power of Tribunal."

- *CIT v. Ramco International 221 CTR 491 (P&H)*

The assessee did not make a claim for deduction u/s. 80IB in the return. The assessee however filed Form 80CCB and other relevant documents during assessment proceedings. The claim was disallowed by the assessing officer. The CIT(A) allowed the claim. The ITAT upheld the order by CIT(A). The High Court upheld the ITAT order.

- *CIT v. Bharat Aluminium Ltd. 303 ITR 256 (Del.)*

The assessee submitted a revised computation of income which was not signed by the person who had signed the original return of income. The assessing officer did not accept the revised computation on the ground that it was not signed in accordance with section 140(c) of the Act. The Hon'ble court relying on the decision in *Dhampur Sugar Ltd. 90 ITR 236 (All.)*, wherein it distinguished between the original return and revised return, held that original return was required to be signed as per section 140(c), whereas the revised computation could be signed by the authorised person.

- *CIT v. Natraj Stationery Products (P) Ltd., (2009) 312 ITR 222*

The assessee had asked for re-computation of deduction under section 80-IB. Relying on Goetze (India) Ltd. (supra) the Revenue rejected the claim. As the assessee had not made any new claim the court held that the said decision may not be squarely applicable. It held that the

Courts have taken a pragmatic view and not the technical view as what is required to be determined is the taxable income of the assessee in accordance with the law. In this sense, assessment proceedings are not adversarial in nature.

- *Commissioner of Income Tax v. Rose Services Apartment India P. Ltd., [2010] 326 ITR 100 (Delhi)*

Relying upon the decision of the Supreme Court in National Thermal Power Co. Ltd. 229 ITR 383 (SC), the Court rejected the plea of the Revenue that the Tribunal could not have entertained the plea, holding that the tribunal was empowered to deal with the issue and was entitled to determine the claim of loss, if at all, under one section/provision or the other.

- *CIT v. Jindal Saw Pipes Ltd., [2010] 328 ITR 338 (Delhi)*

Decision in Goetze (India) Ltd. (supra) was relied upon by the Revenue but the contention was not accepted, observing that the Tribunal's jurisdiction is comprehensive and assimilates issues in the appeal from the order of the CIT (Appeals) and the Tribunal has the discretion to allow a new ground to be raised.

- *Universal Subscription Agency (Pvt.) Ltd. v. JCIT I 59 Taxmann 64 (All.)*

It was held that the decision of the Apex Court in Goetze's case has not laid down as a matter of law that there is a bar for the assessing officer to entertain the claim for deduction otherwise than by filing a revised return.

- *CIT v. Pruthvi Brokers & Shareholders Pvt. Ltd. – 349 ITR 336 (Bom.)*

The assessee filed a ROI in which it omitted to make a claim for payment of SEBI fees. The claim was made by a letter during the assessment proceedings. The AO rejected the claim on the ground that he had no authority to allow any deduction which had not been claimed in the ROI. The assessee raised the claim before the CIT(A) who allowed and this was confirmed by the Tribunal. The department filed an appeal to the High Court claiming that as per Goetze 284 ITR 323 (SC), the assessee was not entitled to make an additional claim for deduction other than by filing a revised return. The High Court dismissing the appeal held that:

It is well settled that an assessee is entitled to raise not merely additional legal submissions before the appellate authorities, but is also entitled to raise additional claims before them. The appellate authorities have the discretion whether or not to permit such additional claims to be raised. It cannot, however, be said that they have no jurisdiction to consider the same. That they may choose not to exercise their jurisdiction in a given case is another matter. The exercise of discretion is entirely different from the existence of jurisdiction. Goetze was confined to a case where the claim was made only before the AO and not before the appellate authorities. The Court did not lay down that a claim not made before the AO cannot be made before the appellate authorities. The jurisdiction of the appellate authorities to entertain such a claim has not been negated by the Supreme Court in this judgment.

- *Chicago Pneumatic India Ltd. v. Deputy Commissioner of Income Tax (2007) 15 SOT 252 (Mumbai)*

It has been held that even though the assessee did not revise its claim under sections 80HH and 80-I, in the revised return, the IT authorities were obliged to consider the revised figures placed before them during assessment.

- *Thomas Kurian v. Assistant Commissioner of Income Tax (2007) 106 ITD 158 (Coch.)*

AO being a quasi-judicial authority, once having noted in the assessment order that assessee had export turnover, was duty bound to ask the assessee as to why he had not claimed deduction under section 80HHC. The matter was remanded to the AO to decide assessee's claim for deduction under section 80HHC.

- *Solaris Bio Chemicals Ltd. v. Deputy Commissioner of Income Tax – ITA No. 987 (Delhi) of 2011 – Order dated 13-7-2012*

Where assessee only sought to claim higher depreciation during assessment proceedings, without revising the return, it was held that no revised return of income was required to be filed.

There are a host of other judgments/orders on the issue wherein same stand been taken. A few of them are:

- *Pradeep Kumar Harlalka v. ACIT 12(3), Mumbai - ITA No. 4501/Mum./2010 - dated 1-8-2011 – Deduction u/s. 80C*
- *ACIT v. M/s N H K Spring India Ltd. - ITA No. 285/Del./2012 - dated 29-8-2012 - Deduction u/s 40(a)(ia).*
- *Sri Lakhan Singh v. Sri Lakhan Singh - ITA No. 1025/Bang/2011 - dated 24-8-2012 – Deduction u/s. 32 Depreciation*
- *Xerox India Limited v. DCIT-ITA No. 1580/ Del/ 2010 – dated 8-11-2013. – Deduction u/ss. 37 and 43B.*
- *Deputy Commissioner of Income Tax v. Smt. Achla Sabharwal – ITA No. 4417/Del/2013 – dated 24-1-2014 – Deduction u/r. 9B(2) & Sec. 32 Depreciation*

Conclusion

12. In view of the judgments/orders, the CIT(A) and Tribunal have power to allow deduction for expenditure to assessee to which it was otherwise entitled even though no claim was made by the assessee in the return. The assessee if entitled to a particular claim, which it missed in the return, may claim during appellate proceedings. The assessee should however ensure that all necessary evidence is submitted during assessment proceedings and is available in record.

[Source : Article published in souvenir at National Tax Conference held on 15th & 16th February 2014 at Ludhiana]

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Situs of sale under Central Sales Tax Act 1956 with reference to Works Contract

Sandeep Goyal, *Advocate*

Levy of tax on composite contract in the shape of works contract has always been a matter of dispute and has led to huge litigation before every level of adjudication including the Apex Court. The very fact that the transaction includes the supply of goods as well as labour, has resulted in complications on account of levy as well as calculation of quantum of taxable turnover for the purpose of levy of VAT/Sales Tax. Not only the bifurcation of the goods and services is required to be made for the purpose of calculation of works contract but the other factors like situs of sale, the time of accrual of sale, the receipts relating to the works contract, the TDS deducted on the payments, the amount of work certified by the engineers and many other factors lead to serious disputes which have always been a bone of contention between taxpayer and the revenue. It is seen of late that the assessing officers have adopted different methods for different persons and in some cases for different years of the same assessee and have levied the tax in a highly arbitrary manner by not following the law laid down by courts from time to time.

Situs of sale

One of the most problematic area for the levy of tax on works contract is to determine the situs of sale of goods which have been incorporated in the works contract by the contractor. It has been observed by the Hon'ble Supreme Court in the case of *Builders Association of India v. Union of India in (1989) 73 STC 317 (SC)* that even though the State Governments are competent to levy tax on the sale of goods which have been sold in the course of works contract but the levy of tax would be governed by the same restrictions as are applicable for the levy on goods in general in the contract of sale. The Hon'ble Supreme Court observed that such a levy is subject to the restrictions which are contained in Entry 54 of List II of 7th Schedule appended to Constitution of India.

Accordingly, the State Governments are not competent to levy tax on the transfer of property in goods involved in the works contract if such sales are in the course of export out of/import into India, sales which have taken place outside the State and the sales which have taken place in the course of inter-State trade and commerce as defined under section 3(a) of the Central Sales Tax Act, 1956.

Some of the States had evolved a unique method of levying the tax on such goods which are sold in the course of inter-Statetrade and commerce by including some provisions in their respective local Acts, which were the deeming fictions. The States had provided that the situs of sale would be deemed to be in that State where the transfer of property has been passed on to the buyer and if at that time the goods are in a particular State then the tax would be levied in that State. Such provisions were challenged before the Hon'ble Supreme Court of India in the landmark case of *Gannon Dunkerley and*

Company v. State of Rajasthan (1993) 88 STC 204 (SC). In the said Constitutional Bench judgment, the Hon'ble Supreme Court had laid down various principles with regard to the computation of levy of tax in a transaction evolving works contract and had also struck down the provisions contained in various State Acts whereby it was presumed that the situs of sale would be inside the State if the goods were in the State at the time of transfer of property in the goods. The Hon'ble Court ruled that whether a deemed sale resulting from transfer of property in the goods involved in the execution of a particular works contract amounts to a sale in the course of inter state trade or commerce or an outside sale or a sale in the course of import has to be decided in the particular terms of a contract. It was observed that the definition of situs of sale in the sales tax legislation of the State would have no bearing on the chargeability of tax on sales in the course of inter-State trade or commerce since it falls outside the field of legislative competence of the State Legislature and will have to be excluded while assessing the tax liability under the State legislation. It was held that the State Legislature while enacting the Sales Tax law for the State cannot make a departure from the principles of Section 3, Section 4 and Section 5 of the Central Sales Tax Act which have overriding effect on the State Sales Tax laws read with Article 286 of the Constitution.

In a case relating to job work which constituted works contract, was subject matter of litigation before Punjab and Haryana High Court wherein the State had levied tax on the material used in the dyeing of fabricated cloth by pressing into operation the deeming provision whereby such sales were presumed to be intra-State sale as the goods were in the State when the transfer of property in the goods had taken place. It was held by the Hon'ble Court that in a case where the grey cloth is sent by contractees from outside the State of Haryana and is processed in the State of Haryana into finished cloth by being subjected to processes such as bleaching, dyeing. sizing and printing and is thereafter sent back to the contractees outside the State the movement of cloth is occasioned by the contract of sale and the transaction amounts to inter-State sale within the meaning of section 3 of the Central Sales Tax Act. Since there was no levy of tax on works contract under the Central Sales Tax Act, the State was not found competent to levy tax on such transactions even by applying the law under the Central Sales Tax Act.

Some of such decisions had led to the amendment in Central Sales Tax w.e.f. 11-5-2002 when section 2(g) of the Central Sales Tax was amended so as to include the transfer of property in the goods involved in execution of a works contract as to be sales. By way of making this specific amendment in the definition of sales, the scope of sales had been enlarged and the States became competent to charge tax on such transactions. The question of determination of the situs of sale still remains a problematic area as the State of origin as well as the State where the goods are being consumed both claim that those States are competent to levy tax on such sales. The States from where the goods had originated claim such transaction as to be inter-State sale whereas the State where the goods were consumed, claim the same as to be intra-State sale as according to them the goods have not moved in pursuance to the contract of sale which has taken place inside the State. For the determination of the situs of the sale involving works contract, it is important to see the facts of each contract as well as the actual execution thereof. In a given case where the goods have moved in pursuance of a specific contract and have been used for that very contract then such transaction would be inter-State sale and the State from where the goods have originated would be competent to levy tax on such transactions. Similarly, in the course of an import, if the goods have been

brought inside the customer frontiers of India for the purpose of being used in a particular contract and were specifically imported for this purpose, then it would amount to a transaction in the course of import and no tax would be leviable on such purchase. In this regard, the Hon'ble Supreme Court of India in the case of *lndure Ltd. [(2010) 34 VST 509* has held that the State Governments are not competent to levy tax in such a scenario.

In other words, in the following circumstances, the tax would be leviable as on inter-State sale from the State of origin under section 3 on Central Sales Tax Act, 1956.

(1) In the case of movable property when the finished goods are sent to a different State in pursuance to a contract of sale, the said works contract would be treated as an inter-State sale.

(2) In a case where the goods are manufactured or assembled by the contractor in accordance with the conditions of the contract and for the purpose of contract only, then the transfer of goods from manufacturing facility to the State where these are incorporated in the works contract would be treated as inter state sale.

(3) Where the goods are procured on inter-state purchase basis and are subsequently sold as in transit sale under Section 3(b) read with section 6(2) of the Central Sales Tax Act and the delivery of the goods is taken by the contractee himself.

In sum and substance, the inter-State works contract would take place where the goods have moved from one place to another specifically for the purposes of execution of a works contract in another State and where the delivery has been given directly to the contractee. However, in a case where the goods are sent by the contractor from his own place in one State to another, the sale would be considered as inter-State sale irrespective of the fact that the delivery and possession of the goods remained with the contractor in the State where the works contract had been executed. However, in a case where the goods are received by the contractor which are not specifically meant for use in a particular contract but are used by him out of stock then it would amount to a local sale.

Appropriate State for collection of tax

It is seen that in case of inter-state sale, there had been a lot of dispute as to which State would collect the tax. In the case of works contract, this dispute has arisen all the more. In practice, it is seen that all the State Govts. who are connected with a transaction of inter-State sale in works contract invariably demand the tax on the same in one manner or the other. However, in terms of section 9(1), it is only the State of origin , i.e. from where the movement of goods start, who is entitled to collect tax on the same. However, in a case where the sale is a subsequent sale under section 3(b), the levy of tax has to be determined with reference to 1st proviso to section 9(I) which provides for two different conditions. In the first condition, the tax is to be collected by the State from where the registered dealer who has made the second sale, has obtained or could have obtained the forms (C Forms) in connection with the purchase of such goods. In case where the subsequent sale has been made by an unregistered dealer, tax is to be calculated by the State from where such subsequent sale has been affected.

It has come to light that the Assessing Authorities have not understood the concept of section 9(1) in the real sense. In fact, most of the Assessing Authorities do not even refer to Section 9(1) which authorises the collection of tax by their State as there is no other provision under the Act by virtue of which the Assessing Authority becomes competent to levy tax. In a case of subsequent sale, the

Assessing Authorities have been observing that subsequent sale made under section 3(b) is rejected on the ground that there was no subsequent sale and therefore the same does not fall under section 3(b). However, while doing so, the Assessing Authorities lose sight of the fact that in case of rejection of second sale as 3(b) sale, then the said sale would be treated as a sale under section 3(a) and it is only the State from where the movement of goods has started who would be competent to collect tax on such sales.

For example, if there is first sale by dealer A in Mumbai to dealer B in Punjab, who makes a subsequent sale of the same goods to dealer C in Punjab. Even though all the formalities with regard to Form C and E-1, etc. are fulfilled but the Assessing Authority of dealer B in Punjab rejects the sale on the ground that there was a pre-existing contract between B and C before the movement of goods (even though it is immaterial) and holds that the subsequent sale does not fall under section 3(b). In such a scenario, the only State who is competent to levy the tax on the sale between B and C would be the State of Maharashtra and not the State of Punjab as section 9(1) provides for the collection of tax by such State. State of Punjab can collect tax only in case the Assessing Authority holds that the sale between B and C is a subsequent sale covered under section 3(b) but dealer B has failed to produce C forms from dealer C or E-1 forms from dealer A. Such like misunderstandings on the part of Assessing Authorities have led to unnecessary litigation before the courts.

The Haryana Tax Tribunal has, however laid down certain guidelines with regard to the determination of tax in such a scenario in the case of *Enexco Teknologies India Ltd., Gurgaon v. State of Haryana in Sales Tax Appeal No.370 of 2009-10.* The guidelines by the Hon'ble Tribunal are as under:

1. Situs of sale both in case of a sale, as defined in the Sale of the Goods Act, 1930, and a sale taking place by the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract, is to be determined in accordance with the provisions of sections 3, 4 and 5 of the Central Sales Tax Act.
2. A sale or purchase (of goods) is taxable under the Local Sales Tax Law (Haryana Value Added Tax Act) only if it is a sale or purchase inside the State as defined in section 4 of the Central Sales Tax Act Act and is not an inter-State sale or purchase as defined in section 3 or an export/ import sale or purchase as defined in section 5 of the said Act.
3. A sale in the course of inter-State trade is either section 3(a) sale, when such sale occasions the movement of the goods from one State to another, or section 3(b) sale, when it is effected by transfer of documents of title to the goods in the course of the movement of the goods from one State to another.
4. After first sale in the course of inter-State trade, a second sale effected by transfer of documents of title to the goods during the course of the movement of the goods is a subsequent sale in the course of inter State trade. A subsequent sale can be only section 3(b) sale as it can be effected only by transfer of documents of title to the goods. Such sale can be effected any number of times duringthe course of the movement of the goods. Existence of a prior agreement with the subsequent purchaser with or without the consent of the first seller will not come in the way of subsequent sale being an inter-State sale under section 3(b).
5. An inter-State sale, which is not a subsequent sale, is taxable in the State, *vide* section 9(1) of the Central Sales Tax Act, from where the inter-State movement of the goods commenced.
6. A subsequent inter-State sale is exempt from tax, vide section 6(2) of

the Central Sales Tax Act, subject to production of both (i) a certificate in Form E-1 (given by the first seller in the course of inter-State trade to the purchasing dealer/E-11 (Given by the subsequent seller in the course of inter-State trade to the purchasing dealer) and (ii) declaration in Form C (Sale to a registered dealer/certificate in Form D (Sale to a Government Department).

7. In case E- l/E-11 and C/D forms are not produced, the subsequent inter-State sale is taxable in the State, *vide* proviso to section 9(1) of the Central Sales Tax Act, from where the selling dealer (suffering the tax) obtained or could have obtained, the declaration in Form C for the purchase of the goods in the course of inter-State trade.

Levy of tax on real estate transactions under the provisions of VAT

The recent ruling of Hon1ble Supreme Court of India in the case of *L&T v. State of Karnataka (2013) (65 VST I)* on a reference by two Member Bench, has categorically laid down the law relating to the transactions involving the development and sale of buildings and flats by real estate developers. Even though there had been a judgment of Hon'ble Supreme Court of India in the case of *K. Raheja, (2005) 141 STC 298,* but still a general understanding amongst all the persons was that the real estate transactions are not taxable as it does not constitute works contract but is a sale of chattel as a chattel. The result of this continuous dispute was that the Hon'ble Supreme Court in the case of *L&T (2008) (17 VST 460)* in which a two Judge Bench of Hon'ble Supreme Court of India doubted its earlier judgment of K. Raheja and referred it to the larger Bench observing that the earlier decision of the Hon'ble Apex Court appears to be wrong.

The Larger Bench of the Hon'ble Supreme Court repelled the contentions raised by the builders in this regard and held that the activity of construction is covered by the term 'works contract' as the term 'works contract' is nothing but a contract in which one of the parties is obliged to undertake or to execute works . It was held that even though the ultimate transaction between the parties may be sale of flat but it cannot be said that the characteristics of works contract are not involved in that transaction. The Hon'ble Bench summarises the legalposition in para 101 as under:

(i) For sustaining the levy of tax on the goods deemed to have been sold in execution of a works contract, three conditions must be fulfilled (one) there must be a works contract (two) the goods should have been involved in the execution of a works contract and (three) the property in those goods must be transferred to a third party either as goods or in some other form.

(ii) For the purpose of Article 366(29A)(b), in a building contract or any contract to do construction if the developer has received or is entitled to receive valuable consideration, the above three things are fully met. It is so because in the performance of a contract for construction of buildings, the goods (chattels) like cement, concrete, still, bricks, etc., are intended to be incorporated in the structure and even though they lost their identity as goods but this factor does not prevent them from being goods.

(iii) Where a contract comprises of both a works contract and a transfer of immovable property, such contract does not denude it of its character as works contract. The term "works contract" in Article 366(29A)(b) takes within its fold all genre of works contract and is not restricted to one specie of contract to provide for labour and services alone. Nothing in article 366(29A)(b) limits the term "works contract".

(iv) Building contracts are species of the works contract.

(v) A contract may involve both a contract of work and labour and a contract for sale. In such composite contract, the distinction between contract for sale of goods and contract for work (or service) is virtually diminished).

(vi) The dominant nature test has no application and the traditional decisions which have held that the substance of the contract must be seen to have lost their significance where transactions are of the nature contemplated in Article 366(29A). Even if the dominant intention of the contract is not to transfer the property in goods and rather it is rendering of service or the ultimate transaction is transfer of immovable property, then also it is open to the States to levy sales tax on the materials used in such contract if such contract otherwise has elements of works contract. The enforceability test is also not determinative.

(vii) A transfer of property in goods under clause (29A)(b) of Article 366 is deemed to be a sale of the goods involved in the execution of a works contract by the person making the transfer and the purchase of those goods by the person to whom such transfer is made.

(viii) Even in a single and indivisible works contract, by virtue of the legal fiction introduced by Article 366(29A)(b), there is a deemed sale of goods which are involved in the execution of the works contract. Such a deemed sale has all the incidents of the sale of goods involved in the execution of a works contract where the contract is divisible into one for the sale of goods and the other for supply of labour and services. In other words, the single and indivisible contract, now by the Forty-sixth Amendment has been brought on par with a contract containing two separate agreements and States have now power to levy sales tax on the value of the material in the execution of works contract.

(ix) The expression "tax on the sale or purchase of goods" in Entry 54 in List II of the Seventh Schedule when read with the definition clause (29A) of Article 366 includes a tax on the transfer of property in goods whether as goods or in the form other than goods involved in the execution of works contract.

(x) Article 366(29A)(b) served to bring transactions where essential ingredients of "sale" defined in the Sale of Goods Act, 1930 are absent within the ambit of sale or purchase for the purposes of levy of sales tax. In other words, transfer of movable property in a works contract is deemed to be sale even though it may not be sale within the meaning of the Sale of Goods Act.

Taxing the sale of goods element in a works contract under Article 366(29A)(b) read with Entry 54, List II is permissible even after incorporation of goods provided tax is directed to the value of goods and does not purport to tax the transfer of immovable property. The value of the goods which can constitute the measure for the levy of the tax has to be the value of the goods at the time of incorporation of the goods in works even though property passes as between the developer and the flat purchaser after incorporation of goods.

Even though the conclusion given byApex Court is binding in so far as the dealers are concerned but at the same time, there are some unanswered questions even after the aforesaid judgment which still bothers the tax professionals, the dealers affected by it and the common man who has to bear the burden of this tax. Some of those issues are summarised as under:

1. It appears that a specific argument had been raised before the Hon'ble Bench that in case the contention of the States is to be accepted that the transfer of flats after construction would amount to works contract, then the levy of stamp duty on the entire value of building at the time of its sale is not legally justified as it would amount to levying the tax on the same transaction as a sale of movable as well as immovable property which would be contradictory to each other. It appears that the Hon'ble Supreme Court has not dealt with this issue which has bearing on the entire controversy.
2. Even though it has been held. by the Hon'ble Apex Court that the builders are the contractors and are covered under the definition of works contract but it has also been held that the levy of tax would start from the date when the prospective buyer enters into an agreement with the real estate developer.It has also been clearly held that no tax would be payable in case the agreement is entered into after the completion of contract as it would amount to sale of immovable property. This position has resulted into levy of tax upon customers who make the booking in advance whereas no tax would be levied on the person who buys the property after its completion. This position has resulted into an anamalous situation as the burden of tax on a person who books the property in advance would be more than the person who buys the property after its completion.
3. It has come to notice that the appropriation of tax liability upon the customers is a daunting task. It becomes almost impossible to appropriate the element of tax between the customers as the actual liability of tax for each customer would be different. In-so-far as the builder is concerned,it is almost next to impossible to find out as to how much exact liability should be recovered from every single customer as the project undertaken by him is joint in nature.
4. It has not been clarified as to what would be the position with regard to the common areas as the property in goods involved in the execution of those common areas is never passed on to the prospective buyer even though the cost of such goods is always recovered from the prospective buyers.

The aforesaid questions have arisen after the judgment of Hon'ble Supreme Court of India but it appears that the tax-payers are bound to be involved in another round of litigation on the issue of levy of tax on the flats built by builders for the prospective buyers.

[Source : Article published in souvenir at National Tax Conference held on 15th & 16th February 2014 at Ludhiana]

Questions & Answers

N. M. Ranka, *Sr. Advocate*

DIRECT TAXES

DTAA

Q.6 *Payment is made to a non-resident/Foreign Company not having Permanent Account Number by and such payment is subject to a specified withholding rate in DTAA with that particular country.*

Ans. Query is incomplete. Unable to understand.

Penalty

Q.7 *Will penalty be levied u/s. 271(1)(c) for disallowance made u/s. 14A and addition made on account of section 50C?*

Ans. Section 14A mandates that no deduction shall be allowed in respect of expenditure incurred in relation to income which does not form part of the total income under the Act. Method for allocating expenditure has been prescribed. First duty is of the assessee to compute his income and in the light of section 14A. On failure without reasonable explanation, penalty would be attracted as it would amount to furnishing of in accurate particulars of income u/s. 271(1)(c) Explanation 1. In *Mak Data P Ltd. v. CIT (2013) 358 ITR 593 (SC),* it is stated "Explanation 1 to Section 271(1)(c) of the IT Act, 1961, raises a presumption of concealment, when a difference is noticed by the Assessing Officer, between the reported and assessed income. The burden is then on the assessee to show otherwise, by cogent and reliable evidence'. It applied *Union of India v. Dharmendra Textile Processors (2008) 306 ITR 277 (SC)* and *CIT v. Atul Mohan Bindal (2009) 317 ITR 1 (SC).*

Section 50C is special provision for full value of consideration in specified cases. It is a deeming provision whereby the stamp duty valuation is deemed as full consideration against real consideration received by the owner. Hence, no penalty would be exigible u/s. 271(1)(c). (Refer *CIT v. Madan Theatres Ltd. (2013) 260 CTR 75 (Kolkata).*

Income/Business or House Property

Q.8 *Whether income from activity of providing residential accommodation to any person as paying guest by a limited company owning residential flat would be treated as business income or income from house property?*

Ans. While providing residential accommodation, if food and other facilities are also provided to the paying guest, it would be business income. As per Memorandum/ Articles of Association providing residential accommodation should be one of the objects. Thus it would be more like running a hotel.

Capital Gain

Q.9 *i. Can Short Term Capital loss on sale of shares taxable u/s 111A of the Act be set off against short term capital gains on sale of capital asset other than shares or securities?*

ii. Is it mandatory for assessee to set off of loss from future and options against income from other business in same assessment year?

Ans. (i) Section14 contains Heads of Income and Capital Gains falls in 'E'. Section 70 deals with set off and carry forward and set off.

Section 70(2) provides that where the result of computation made for any assessment year in respect of any short term capital asset is a loss, the assessee shall be entitled to have such loss set off against the income, if any, as arrived at in respect of any other capital asset. Hence answer is in affirmative.

(ii) No

Tax Deducted at Source

Q.10 *Section 194 IA provides that no deduction under the said section shall be made where consideration for the transfer of an immovable property is less than fifty lakh rupees.*

If A & B purchase property for ₹ 60 lakhs, each one pays ₹ 30 lakhs to Mr. Vendor. Whether A & B have to deduct TDS?

Issue is whether limit of ₹ 50 lakhs is to seen vis-à-vis co-owner or qua property.

Ans. Section 1941A(2) says, if the consideration for the transfer of an immovable property is less than fifty lakh rupees, no deduction need be made. If there is a single sale deed for consideration of ₹ 60 lakhs, though A&B pay ₹ 30 lakhs each, deduction has to be made by the joint transferees. However, if there are two separate, distinct, independent sale deed for consideration of ₹ 30 lakhs for half share in favour of 'A' and another deed for half share in favour of 'B', deduction need not be made on account of the overriding provision of Section 194-1A(2). To avoid litigation it is also advisable to execute Sale Deeds on different dates and present for registration on different dates. The limit has to be seen on the basis of the document executed/registered. A vendor can sell in parts, to different persons and on different dates. There is no aggregation provision.

Full Bench of Karnataka High Court in (2013) 359 ITR 83 have exhaustively dealt with the issue and have held that section 45(4) would be inapplicable when the firm did not transfer any right in the capital asset in favour of the retiring partner; it did not cease to hold the property and consequently its right to property was not extinguished; no property was transferred to the retiring partner and existing capital assets remained intact with the firm.

It referred to the judgment of the Bombay High Court in the case of *CIT v. A. N. Naik Associate (2004) 265 ITR 346* and extensively dealt with on page 99 the distinguished factor. In the light of the case of A. N. Naik Associate (supra) it is desirable to execute retirement deed with care and caution. Case of Sudhakar Shetty does not appear to laying of correct law (Refer *CIT (Addl.) v. Mohanbhai Panabhai (1987) 165 ITR 166 (SC); CIT v. R. Lingmallu Raghukumar (2001) 247 ITR 801 (SC); Prashant S Joshi v. ITO (2010) 324 ITR 154 (Bom.) etc.)*

Capital Gain

Q.11 *There are number of judgments of Supreme Court and High Courts that when partner retires from partnership firm and when excess amount is paid over and above his capital account balance, the same is not liable to tax.*

However Mumbai Tribunal in the case of Sudhakar Shetty 130 ITD 197 has taken the view that the same is liable to capital gains tax, what is your valued opinion for the same?

i. In CIT v. Dynamic Enterprises 95 DTR 97 (Karn.) (FB)- is held that when a partner takes away only money towards the value of his share in the firm, there is no transfer of capital asset and consequentially no profits or gains are chargeable to tax u/s. 45(4).

ii. If property in partnership firm is to be transferred, new partners who want to enjoy the property are admitted to partnership and old partners retire who are paid cash, is there any tax liability?

Ans. As discussed hereinbefore there is no tax liability when any amount is paid in full and final settlement of account to the retiring partner. However, precaution should be taken. It should not be a colour, device or camouflage and on a single day.

Section 14A

Q.12 *Recently Third Member in the case of DH Securities Pvt. Ltd. (www.itatonline.org) has taken the view that section 14A gets attracted to a case even where shares are held as stock-in-trade some High Courts are taken contrary view. What is your view in the matter. Also please explain third member case of jurisdictional Tribunal is against and judgment of other High Court is in favour, what is binding on assessee.*

Ans. View expressed in DH Securities Pvt. Ltd. does not appear to be good law as shares are trading assets/stock-in-trade, gain or loss wherein would be assessable u/s. 28 of the Act. Income has to be computed after deduction of expenditure for purposes of business. When the view of any High Court being superior Court, is in favour of the assessee, he should carry the matter to the jurisdictional High Court by way of appeal u/s. 260A. It would become a substantial question of law.

Section 50C

Q.13 *Stamp duty is generally paid by the buyer who may not contest the value adopted by the State stamp valuation authority. Seller may not be aware of the buyer paying the additional stamp duty as demanded by the Stamp Valuation Authority.*

a) Can the seller request the AO to refer the valuation to DVO?

b) If the AO does not entertain the request for referring the matter to DVO then what is the remedy available to the assessee?

c) If the DVO values at a higher value then the value adopted by Stamp Valuation Authority then which value can the AO adopt?

Supposing that the AO had referred the matter to DVO in respect of the said property under the WT Act for the asst. year preceding the year in which the land is sold and the DVO has valued the property (for the purpose of WT) at a rate which is more than the value which is assessed by Stamp Valuation Authority then which value can the AO consider for the purpose of capital gains – value adopted by DVO under WT Act for the year preceding the year in which the land is sold or the value adopted by the Stamp Valuation Authority

Ans. (a) Yes the vendor, who is liable to capital gain may request his A.O. to refer the valuation to DVO u/s. 50C(2)(i) of the Act.

(b) Assessee can prefer an appeal and the CIT(A) shall direct and remand to A.O.

(c) A.O. has to adopt the value determined by the stamp valuation authority and cannot enhance as that of the DVO. He has to adopt lesser value if computed by the DVO against value of the stamp authority.

(d) Value adopted for W.T. assessment would not be considered u/s. 50C of the Act. Value adopted by the stamp valuation authority is statutory and is of binding nature.

Stay of disputed demand

Q.14 *Can the A.O. relying on instructions No.1914 and 1922 insist on minimum 50% payment of disputed tax liability in case where the assessee has applied for keeping the demand in abeyance on the basis of instruction No. 96 issued by the Dy. Finance Minister and considered by many High Courts in their decisions? If the AO insists on 50% payment then what is the remedy left with the assessee?*

Ans. Instructions Nos. 1914 and 1922 are not in accordance with law. There is no provision in the statutes for payment of 50% of the disputed demand. Such instructions are not binding on the assessee. Instruction No. 96 is of binding nature. The Rajasthan High Court in *Maharana Shri Bhagwat Singhji v. ITAT (1997) 223 ITR 192* observed that the relevant factors for deciding the stay applications primarily are a *prima facie* case, balance of convenience, financial status

of the petitioner, hardship and also the interest of the Revenue. It referred to the instruction No. 96 (F.No. 1/6/69-(ITCC) dated August 21, 1969. It has been recently followed and repeated in *Maheshwari Agro Industries v. Union of India & Others, reported in (2012) 346 ITR 375 (Raj).* Observations on page 419 are eye opener.

Same view has been expressed by the other High Courts in the following cases:-

(i) *Valvoline Cummins Ltd. v. DCIT (2008) 307 ITR 103 (Delhi);*

(ii) *N. Rajan Nair v. ITO (1987) 165 ITR 650 (Ker.);*

(iii) *Mr. R. Mani Goyal v. CIT (1996) 217 ITR 641 (All.);*

(iv) *I.V.R. Constructions Ltd. v. ACIT (1998) 231 ITR 519 (AP);*

(v) *Taneja Developers and Infrastructure Ltd. v. ACIT (2010) 324 ITR 247 (Delhi) – the Hon'ble Court also held that the circular has not been superseded;*

(vi) *Vikrambhai Punjabhai Palkhiwala v. S.M. Ajbanj (1990) 182 ITR 413 (Guj.);*

(vii) *Jain Cycle Spares and Co. v. CIT (2004) 267 ITR 60 (MP);*

(viii) *Soul v. Dy. CIT (2010) 323 ITR 305 (Delhi).*

The assessee must make detailed stay petition before the AO and CIT(A) covering the above aspects. After exhausting administrative remedy with the higher authorities, writ would be the only efficacious remedy.

[Source: Brains' Trust Queries replied at Brains' Trust Session at 17th National Convention on 27-12-2013 at Mumbai]

Questions & Answers

CA. H.N. Motiwalla

Query No. 1 : Penalty under Section 271(1)(c) when assessed under S. 115JB

Whether penalty under section 271(1)(c) of the Act can be levied in a case where tax has been paid by the assessee under section 115JB of the Act and amount of tax payable as book profit is the same even as per order of assessment, with reference to variation in the amount of loss or income determined as per normal provisions of the Income-tax Act?

Answer

In *CIT v. Nalwa Sons Investments Ltd., [327 ITR 543 (Del.)]* the facts were the assessee filed return declaring loss of ₹ 43.47 crores. Thereafter, the revised return exhibiting the income at ₹ 3.87 crores were filed under provisions of section 115JB of the Income-tax 1961. The assessment was framed under section 143(3) at loss of ₹ 36.95 crores, after making certain additions as per normal provisions and book profit at ₹ 4.07 crores under section 115JB of the Act.

The Court observed that under the scheme of the Act, the total income of the assessee is first computed under the normal provisions of the Act and tax payable on such total income is less than certain percentage of book profit, then, such book profit shall be deemed to be the total income and tax shall be payable on such deemed income.

Further, the Court has also noted that the Explanation 4 to section 271(1)(c) of the Act, which gives the meaning of the term "the amount of tax sought to be evaded". That is where the income in respect of which particulars have been concealed or inaccurate particulars have been furnished has the effect of reducing the loss declared in the return or converting that loss into positive income, the tax sought to be evaded shall be the tax that would have been chargeable on the amount of such income if it were the total income.

After considering the scheme as well as Explanation 4 to section 271(1)(c) of the Act the Delhi High Court held that, no doubt there was concealment but that had its repercussions only when the assessment was done under the normal procedure. In the instant case, the assessment as per normal procedure was, not acted upon. On the contrary, it is deemed income assessed under section 115JB of the Act which became the basis of assessment. Tax is paid on the income assessed under section 115JB of the Act. Hence, when the computation was made under section 115JB of the Act, the aforesaid concealment had no role to play and was totally irrelevant. Therefore, the concealment did not lead to tax evasion at all. Therefore, penalty cannot be imposed on the basis of disallowance or addition made under normal provisions.

Query No. 2 : Section 50C – Stamp Duty value exceeds the actual consideration

X purchased a vacant site (2400 sft) of rural area of Andhra Pradesh for ₹ 10,000/- in the financial year 1995-96 and paid Stamp Duty as per above consideration. Now X wants to sell it to Y for ₹ 2,00,000/- i.e. actual consideration. But Stamp Duty has to pay for ₹ 16,00,000 i.e reckoner value of ₹ 16,00,000/-. What steps X and Y should take?

Answer

Section 50C(1) if the Act provides that in case where the value adopted or assessed by the stamp valuation authority in respect of a transfer of land or building or both for the purpose of payment of stamp duty exceeds the consideration received or accrued by the assessee for such transfer, the value so adopted or assessed shall be deemed to be the full value of the consideration received or accruing for such transfer.

Section 50C(2), provides for the valuation of the capital asset to be referred to a valuation officer where the assessee claims that the value adopted by the stamp authority is in excess of the fair market value of the property. The valuation of the capital asset cannot, however, be referred to a valuation officer where the value adopted or assessed by the stamp authority has been disputed in appeal or revision or in reference before any authority, Court or the High Court.

So, in this case, Y has to challenge the value adopted or assessed by the stamp authority in appeal or revision or in reference before any authority, Court or High Court.

If Y does not dispute the said valuation before any authority or Court or High Court then, X can claim before the Assessing Officer that the value so adopted or assessable by stamp duty authority is in excess of fair market value of the property as on date of transfer, be referred to the valuation officer.

Query No. 3 : Applicability of TDS u/s. 195

X purchased a vacant site in Andhra Pradesh from Y (Non-Resident) for sale consideration of ₹ 25,00,000/-, in the Financial Year 2010-11, without deducting TDS. Whether section 195 of the Income-tax Act, 1961 would be applicable?

Answer

The objective of this section is to ensure that the tax on the income of non-residents and foreign companies is deducted at source, so that the department is not put to the trouble of recovering it from such persons whose connections with India, may be transient or whose assets in India, may not be sufficient to meet the tax liability.

If income is chargeable in the hands of Y (non-resident) tax has to be deducted as per the provisions of section 195 of the Act. The Supreme Court in *GE India Technology Centre Pvt. Ltd. v. VIT [327 ITR 456]* has held that the obligation to deduct tax at source arises only when there is a sum chargeable under the Act i.e. payment which has an element of "income" chargeable to tax in India.

However from July 1, 2012 sub-section (7) has been inserted in section 195 to provide that a person responsible for paying a non-resident in relation to a specified class of persons or cases which are notified by the Board shall make an application to the Assessing Officer to determine whether tax is to be deducted or not.

Query No. 4 : Can Jain being of minority community continue in the status of HUF?

As per F. No. 4-2/2014 –NCM., G.O.I. Ministry of Minority Affairs, dated February 6, 2014, Jain Community are covered under section 2(c) of National Commission of Minority Act 1992 as minority. So, can Jain continue with HUF under the Income-tax Act?

Answer

There is no restriction on Jains to be assessed under the status of "HUF" under the Direct Tax laws, even though Jain community has been declared as a minority community.

No separate definition of the expression HUF has been attempted in any of the Direct Tax laws because the term has a definite connotation under the Hindu Law. The Supreme Court in *Surjit Lal Chhabda v. CIT [101 ITR 776]* and the Bombay High Court in *CIT v. Gomedalli Lakshmi Narayan [3 ITR 367]* have declared that the expression HUF must be construed in the sense in which it is understood under the Hindu Law.

Mulla, in his seminal work on Hindu Law, stated that the Hindu Law applied to the following:

(i) Hindus, not only by birth but Hindus by conversion;

(ii) Illegitimate children where both parents are Hindus;

(iii) Illegitimate children where father is Christian and mother a Hindu and if children are brought up as Hindus;

(iv) Jains, Buddhists in India, Sikhs, Nambudri Brahmins except so far as such law is varied by custom and to Lingayats;

(v) A Hindu by birth who having renounced Hindusism has reverted to it;

(vi) Sons of Hindu dancing girls;

(vii) Brahmos, Arya Samajists, and Santhals of Chhota Nagpur;

(viii) Hindus who make a declaration that they are Hindus for the purpose of Special Marriage Act;

(ix) Kutchi Memons who had settled in Madras and Travancore, etc., and regulated their affairs according to Hindu law in matters of succession, inheritance and property including the Hindu concept of coparcenary and survivorship. Therefore, accordingly to *CED v. Hajee Abdul Sattar Sait [(86 ITR 53 (SC)]* such Kutchi Memons being mass converts were governed in matters of property, succession and inheritance by the rules of Hindu law including the rules as to joint family property, its distribution according to the rule of survivorship and the right of a son by birth.

Query No. 5 : Assessment on Executors

Please explain the procedure for e-filing of return of a deceased's estate till final distribution of assets i.e. maturity of Section 54EC Bonds, Tax Saving FDR., P.O. deposits etc., (section 168 (1) (a). Whether he will have to apply for separate PAN or PAN of deceased will serve the purpose. The basic exemption will also be available for ₹ 2,00,000/- or not applicable to deceased?

Answer

Section 168 of the Act applies to executors as well as to administrators or other person administrating the estate of a deceased person.

Sections 159 and 168 of the Act deal with assessments on legal representatives. Section 159 of the Act is meant to enable the revenue to make an assessment on legal representation in respect of the income which accrued to or was received by the deceased, while section 168 of the Act authorises an assessment on the legal representative in respect of the income which accrues to him after the death, the estate being vested in him. Though the assessment is on the executor or executors, as the case may be, for all practical purposes it is the assessment of the deceased *[CIT v. G.B.T. Sheth and Another – 133 ITR 192 (MP)].*

Hence, the executor has to e-file return under the PAN of the deceased and would be entitled for basic exemption.

Questions & Answers

C. B. Thakar, *Advocate*

INDIRECT TAXES

Query No. 1 : Administrative charges and contract value

All the expenses incurred by the Contractor inclusive of his own establishment expenses like salary to his Staff are to be borne by Developer with 5% service charges (profit).

These expenses are charged separately and the details are submitted to Developers. There is an Agency Agreement between Contractor and Developer by virtue of which the Contractor gets 5% and hence it cannot form that part of sale price.

Whether re-imbursement of these expenses can be added to sale price for Taxation purpose under MVAT Act, 2002?

Reply

Referring to the facts given by you, it can be said that the position as to whether contractor is acting in dual capacity, one as contractor (i.e. principal to principal) and as agent for administrative expenses is required to be seen. This can be ascertained from your agreements etc..

Query No. 2 : Import/Export sales vis-à-vis FTZ

Whether sale from Free Trade Zone to the unit situated in same Free Trade Zone is taxable or exempt?

Reply

What is contemplated by Free Trade Zone is not clear. It appears that the reference is to SEZ/100% EOU etc. Normally, such sales are also taxable under MVAT Act, 2002. However, exemption can be claimed under Notification bearing No. VAT 1505/CR 121/Taxation-1, dated 1-4-2005.

In general a question may arise whether sale to unit in Special Economic Zone (SEZ) by Domestic Tariff Area Unit (DTA) or by SEZ to DTA amounts to sale/purchase in course of Export/ Import? The issue arises as SEZ is given special status by Special Economic Zones Act, 2005 (SEZ Act, 2005).

Sale in course of Export/Import under Sales Tax Laws

As per Article 286 of the Constitution of India no tax can be levied on sale/purchase taking place in course of Export and Import. The said terms are defined in sections 5(1) and (2) of CST Act, 1956. The said definitions are reproduced below for ready reference.

"5. When is a sale or purchase of goods said to take place in the course of import or export:

(1) A sale or purchase of goods shall be deemed to take place in the course of the export of the goods out of the territory of India only if the sale or purchase either occasions such export or is effected by a transfer of documents of title to the goods after the goods have crossed the customs frontiers of India.

(2) A sale or purchase of goods shall be deemed to take place in the course of the import of the goods into the territory of India only if the sale or purchase either occasions such import or is effected by a

transfer of documents of title to the goods before the goods have crossed the customs frontiers of India."

The accepted meaning of above section is that the goods should be going out of Indian Territory or should be coming from outside Indian Territory. Unless this fact is present, the argument of sale in course of export/import is almost not tenable. In relation to SEZ there is special enactment i.e. SEZ Act, 2005. In the said Act, SEZ is given special status as foreign territory for various purposes. The transactions with SEZ unit by DTA (either sale or purchase) are to be routed through import/export formalities like filing of Bill of entry etc. Therefore, a debate arises as to whether it can be said to be sale in course of export/ import for purposes of Sales Tax Acts.

In light of above definition of sale in course of export/import in sections 5(1)/5(2) reproduced above, it can very well be stated that there is no possibility to consider sale/purchase transactions with SEZ as in course of export/import. The said is also now well settled by judgment of Hon. Allahabad High Court. Reference can be made to judgment in case of *M/s. India Exports v. State of U.P. & Others (Civil Misc. W.P. No. 1488 of 2009 decided on 11-2-2011 (All).*

In this case the facts were that the petitioner was a unit in SEZ. It cleared its manufactured goods i.e. furniture for sale to DTA unit. The petitioner was claiming this sale to DTA as its export or in other words sale in course of import and not liable to sales tax. The Sales Tax authorities levied CST as applicable to normal sale and hence this writ petition before Hon. High Court. Before High Court section 53(1) of SEZ Act was relied upon. The said section is reproduced below for ready reference.

"Section 53 in the Special Economic Zones Act, 2005.

"53. Special Economic Zones to be ports, airports, inland container depots, land stations, etc., in certain cases. A Special Economic Zone shall, on and from the appointed day, be deemed to be a territory outside the customs territory of India for the purposes of undertaking the authorised operations.

(2) A Special Economic Zone shall, with effect from such date as the Central Government may notify, be deemed to be a port, airport, inland container depot, land station and land customs stations, as the case may be, under section 7 of the Customs Act, 1962 (52 of 1962): Provided that for the purposes of this section, the Central Government may notify different dates for different Special Economic Zones."

The important arguments of petitioner were as under:

(i) Sale from SEZ to DTA are sales in the course of import on which Central Sales Tax is not leviable under Article 286 and Section 5 (2) of the Central Sales Tax Act and for which no exemption notification is required.

(ii) Rule 47(1) of the SEZ Rules requires buyer of DTA to submit import license and Rule 47(4) provides for valuation and assessment of goods cleared for DTA to be made in accordance with Customs Act and Rules; Rule 48(1) requires the buyer of DTA to file a Bill of Entry for home consumption applicable to goods imported into India and Rule 48(2) provides for valuation of goods for customs duty in accordance with the provisions of the Customs Act. The territory of SEZ under these Rules shall be deemed to be territory outside the territory of India and thus any goods removed from SEZ to DTA shall be deemed to be goods imported from outside the territory of India. Section 5(2) of the Central Sales Tax Act deems sale and purchase of goods in the course of import only if the sale and purchase either occasions such import or is effected by a transfer of documents of title to the goods before the goods have crossed the customs frontiers of India. The customs frontiers of India under Section 2 (ab) of

the Central Sales Tax Act means crossing the limits of the area of a customs station in which imported goods or export goods are ordinarily kept before clearance. There is no liability for payment of Central Sales Tax in respect of the sale and purchase of the goods in the course of import into the territory of India.

(iii) The customs duty is levied only on the goods imported into India, from territory outside India. Section 12 of the Customs Act, 1962 read vide Entry 83 of List-1 of 7th Schedule of the Constitution of India, vide in re Sea Customs Act AIR 1963 SC 1760 (page 191) under Section 53(1) and Section 53 (2) of the SEZ Act, the authorised operations in SEZ are deemed to be imports to SEZ as custom station, which covers port, airport, etc. The importer from SEZ to DTA is required to have import licence and to file a bill of entry. The deeming fiction in SEZ Act and Rules read with Customs Act and Central Sales Tax Act makes the special transaction as import, exempt from Central Sales.

(iv) The SEZ are deemed to be territory outside customs territory of India and thus they cannot be treated as part and parcel of any particular State in India. In the transaction of sale from SEZ to DTA there is no moment of goods from one State to another, calling for imposition of Central Sales Tax.

(v) The deeming fiction has to be given full play and affect and regulations assuming all facts on which fiction can operate.

Hon'ble Allahabad High Court has held that the sale is taxable as any other sale within India. After referring to statement of Objects and Reasons for SEZ Act, 2005, Hon'ble High Court observed as under:

20. We do not find any substance in the argument of Shri Bharat Ji Agrawal that the Central Sales Tax cannot be levied on the sales made by the petitioner from SEZ unit to a unit in DTA. The SEZ unit under the SEZ Act, 2005 is deemed to be territory outside the territory of India under Sections 51, 53 (1) for a limited purpose; Sub-section (2) provides that SEZ shall with effect from the date of notification by the Central Government be deemed to be a port, airport, inland container port, land station and land customs station under Section 7 of the Customs Act.

21. The SEZ Act, 2005 has taken into consideration and has provided for amendment of the various taxing statutes, or modified them, for fulfilling the object and purpose of the Act. Section 7 provides for exemption from tax, duties or cess on any goods or services exported out of or imported into or produce from DTA by unit in SEZ or a developer subject to terms and conditions as may be prescribed and be exempt from the payment of tax, duties or cess under all enactment specified in the First Schedule. Section 27 of the SEZ Act, 2005 applies Income Tax Act with certain modifications in relation to developers and intrepreneurs carried out authorised operations in SEZ and modifications are specified in Second Schedule. Section 57 amends the enactment specified in the Third Schedule, which are amended by SEZ Act, 2005. The Central Sales Tax is not included in any of these Schedules.

Hon'ble High Court also observed that deeming clause in one statute cannot apply to other unless so specified in the said statute or can be inferred. That being not the position in above facts and circumstances of the case, Hon'ble High Court held that the claim of sale in course of export/ import is not tenable and confirmed levy of tax.

In light of above, it can be said that a sales to FTZ and sales from FTZ can not amount to sale in course of import/export. Therefore, unless there is exemption granted under the Local Act, no exemption will be eligible. Under CST Act, there is facility of 'I' form for tax free purposes under CST Act.

Quest – Opinion

Vinayak Patkar
Advocate

Query – C Form

Our query is regarding the issue of C form to M/s. Kavita Industries Limited (KAVITA). We have submitted the following documents along with our brief for opinion:

I. Details of sale-in-transit transactions relating to the year 2010-2011.

II. Notification of Award for ex-works supply contract dated 10-7-2009 of Power Grid Corporation of India Limited (PGCIL).

III. Purchase Orders of Common Goods Limited (CGL) for purchase of oil.

IV. Invoices of KAVITA.

V. Transport Receipts of Adhunik Transport Organisation Limited (Adhunik).

The facts informed by you are as follows:

a. The PGCIL has awarded the Supply Contract for Auto Transformer Package for Chullier (Palakad) Sub-station by their Work Order dated 10-7-2009.

b. One of the items required for this package is the oil.

c. CGL, Maharashtra has placed Purchase Order for such oil on KAVITA, Maharashtra vide their order dated 4-11-2010.

d. KAVITA supplied the oil vide their various invoices.

e. The oil was consigned by KAVITA directly to PGCIL, Palakad.

f. The CGL has effected sales u/s. 6(2) of the Central Sales Tax Act, 1956.

g. The CGL is required to issue Form C to KAVITA. Though the oil was directly delivered to PGCIL, Palakad site, the CGL is not registered under the CST. Act, 1956 in the State of Kerala *qua* Oil.

h. The CGL, Maharastra is registered under that Act *qua* oil. However, the second sales so effected to PGCIL have not been reported in the returns filed in the Maharashtra State but were reported in the State of Kerala.

On these facts, the CGL desires to know from which State they can obtain C forms for these transactions:

Opinion

A. KAVITA has directly dispatched the goods to PGCIL Kerala site. Therefore, two successive sales have taken place when the goods have been delivered to PGCIL. The Gujarat High Court in the case of Haridas Mulji Thakkar reported in 84 STC 317 has elaborately discussed the nature of such sales. The facts involved in that case and the observations of the Hon'ble Court are reproduced below :

"The respondent-dealer was a distributor of carbon dioxide manufactured by a concern in Bombay. The respondent received orders from its purchasers in Gujarat. The respondent placed orders with the Bombay supplier which in turn sent the goods directly to the purchasers f.o.r.

Bombay, the transport receipts in their names, according to the instructions of the dealer. The price charged by the respondent was higher than that charged by the Bombay supplier. Delivery of the goods was taken by the purchasers, the purchasers paying the freight charges. The question before the court was whether the sale by the respondent to the purchasers in Gujarat was an inter-State sale within the meaning of section 3(b) of the Central Sales Tax Act, 1956 and not a local sale, liable to tax under the Gujarat Sales Tax Act, 1969.

Held, that there were two deliveries which synchronised in point of time even though both the sales were separate in point of fact and in the eye of law. When the Bombay supplier transported the goods to Gujarat and took out receipts in the name of the purchaser/ purchasers in Gujarat, there was constructive delivery in favour of the respondent-dealer. At the same time there was constructive delivery of the same goods in favour of the purchasers. While effecting the second delivery, the Bombay supplier acted as agent of the respondent. The moment the goods were transported and the transport receipts were taken in the name of the Gujarat purchasers, the property in the goods stood transferred in their favour. The sale was by transfer of documents of title to the goods while the goods were in movement from one State to another although there was no actual endorsement thereon by the respondent. The second sale was, therefore, an inter-State sale within the meaning of section 3(b) of the Central Sales Tax Act, 1956.

B. In this case, as the Hon'ble Court observed, when the Bombay supplier transported the goods to the State of Gujarat and took out transport receipts in the name of the purchaser there was a constructive delivery in favour of the assessee/petitioner. At the same time there was constructive delivery of the same goods in favour of the purchaser. In other words, such constructive deliveries are immediate on taking out the transport receipt in the name of the purchaser. In your case, the transport receipts have been taken out by KAVITA in the State of Maharashtra. Therefore, the constructive delivery or the first sale has taken place in this State.

C. Section 23(2) of the Sale of Goods Act,1930 states, 'Where in pursuance of the contract, the seller delivers the goods to the buyer or to a carrier or other bailee (whether named by the buyer or not) for the purpose of transmission to the buyer, and does not reserve the right of disposal, he is deemed to have unconditionally appropriated the goods to the contract.

D. Rule 12(6) of the Central Sales Tax Rules, 1957 states that Form C referred in Section 8(4) should be one obtained by the purchasing dealer in the State in which the goods covered by such form are delivered.

E. In our considered opinion, therefore, CGL has to obtain the C form for this transaction pertaining to the purchase of oil from the State of Maharashtra.

F. This transaction can also be viewed from another angle. Assuming that the ratio of the Gujarat High Court judgment as regards constructive delivery is not applicable in CGL's case, still, in our view the C form can be obtained from the State of Maharashtra. Explanation to Rule 12(6) in clear terms states that where, by reason of the purchasing dealer not being registered under Section 7 in the State in which the goods covered by Form C are delivered (and therefore) he is not able to obtain the said form from that State, Form C may be the one obtained by him in the State in which he is registered. CGL is not registered in the State of Kerala *qua* oil. However, their registration certificate in the State of Maharashtra covers oil. In view of the above referred explanation they can obtain such form from the State of Maharashtra.

G. You may revise the returns.

Tax World

SALES TAX

D. H. Joshi, *Advocate*

1. Misc.: Important circular issued by the CCT, Kerala

The Commissioner Commercial Taxes, Kerala, issued Circular No. 02 / 2014 on the subject of Kerala Value Added Tax Information System (KVATIS)–IT policy of the Dept. In this circular, Dept.'s vision and mission, objectives, e-governance infrastructure, project management, etc. are explained.

No. ITMC – 38101 / 13 CT (Kerala Tax Reporter) Vol. 22 Page 14

2. VAT u/s. 9-B of MPCT Act – Trade / Cash Discount

In the present case, the assessee received trade discount and cash discount from the selling dealer by way was credit notes. In the assessment of selling dealers, no deduction was allowed for the said discounts given, but for levy of VAT u/s. 9-B in the case of appellant-purchaser, these discounts were reduced from purchase price applying its decision in *Titan Industries (2012) 20 STJ 39 (M.P.-Bd)*, Appellate Board held that in the assessment of the selling dealer, the target discount given by way of credit note is not deductible from sale price. Therefore, while levying tax u/s. 9-B on the appellant-purchaser it is not justified to reduce the same from purchase price. Hence, the case remanded to AO to pass a fresh order on this point after verification of bills.

Amit Enterprises, Bhopal v. CCT, M.P. (2014) 24 STJ 179 (M.P.-Bd)

3. Works Contract – Printed labels – Whether simple sale ?

In the present case decided by Madras High Court, the facts for consideration were in respect of labels supplied by the assessee on which certain particulars were printed as per requirement of a particular customer. The labels, by themselves, could not be sold in open market. It was not the case of the State that persons who manufacture spurious goods under the very same brand name, had an opportunity to buy these labels, so as to pass off their goods as that of the customers of the assessee respondent. The assessing authority had no evidence before him to come to a conclusion that the labels printed by the assessee are marketable, though actually not marketed. There was also no evidence to show that printing of labels is not incidental, but primary. Without any evidence, the assessing authority went on presumptions. On facts, the Division Bench of the High Court held that in the facts of the present case, the ratio in Anandam Viswanathan case (1989) 73 STC 1 (SC), squarely applies, and the Tribunal and the Single judge were right in holding that the printed labels supplied by assessee to his customers constituted a works contract and not an outright sale.

State of Tamil Nadu v. Premier Litho Works and Anr. (2014) 24 STJ 150 (Mad.)

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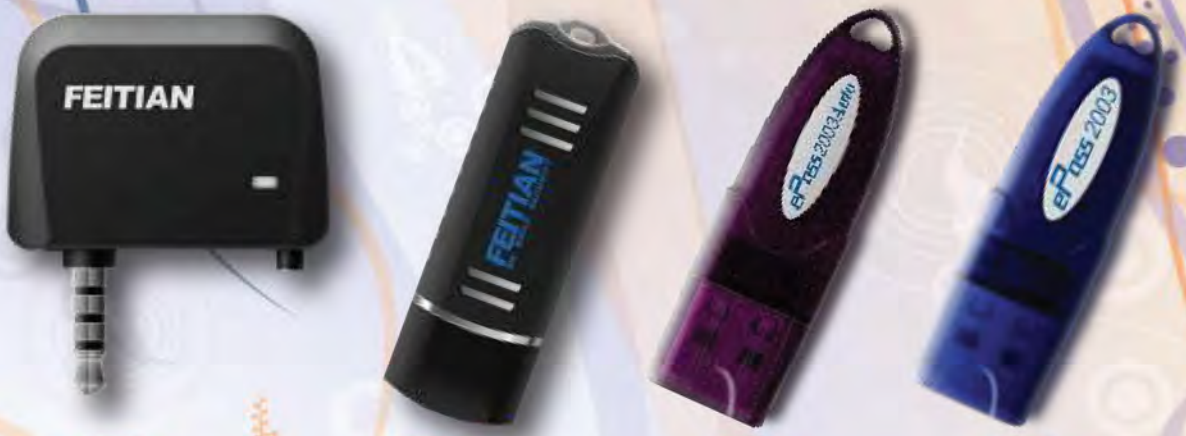

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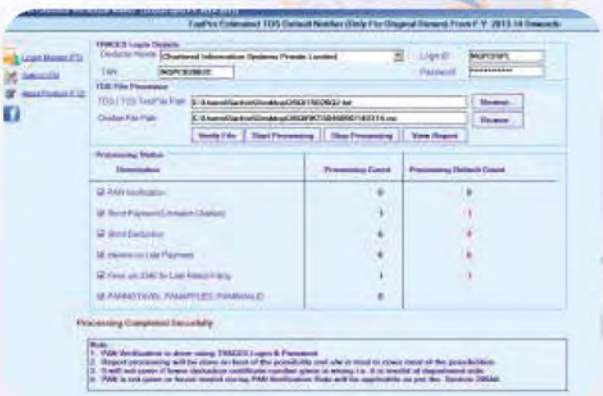

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