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Estd. 1926

92nd Year

ज्ञानं परमं बलम्

A Monthly Journal of

The Chamber of Tax Consultants

THE CHAMBER'S JOURNAL

Vol. VII | No. 3 December 2018

YOUR MONTHLY COMPANION ON TAX & ALLIED SUBJECTS

Benami Act

Black Money Act

Income from Unexplained Sources

Benefit of Telescoping

Unexplained Expenditure

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CONTENTS

Vol. VII No. 3 | December – 2018

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The Chamber's Journal

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Editorial

The year 2018 is approaching its end; the year had been full of challenges for professionals due to the major tax reforms introduced by way of GST in the earlier years. The Government claims to be addressing the issues in a diligent manner from time-to-time – unfortunately, this remains to be the version of the Executive as problems and hitches on ground have ever since remained the same. If the authorities had lent a ear to the professionals prior to the introduction of the legislation, many problems being faced by the tax payers would not have arisen at all in the first place. It is unfortunate that we professionals being important stakeholders, have been left to harbour a feeling that this has been done by the bureaucracy to window dress their report card. In this process, the victim is the tax payer.

Another major issue which is experienced by the tax payers is with respect to e-way bills and the approach of the State Governments towards the same which defeats the very intention of GST, One Nation One Tax. It seems the State Government officials are not able to come to terms with the loss of 'their revenue'. The discretion available to them under IGST with respect to e-way bills is being misused by the State Government officials when the goods from the originating State pass through several other States to reach the destination State. These States through which the goods pass are creating hurdles which may push us back to the pre-CST regime.

Similarly, issues pertaining to input tax credit are not yet sorted out and this is certainly a hurdle in the path of 'ease of doing business'.

The Chamber has filed a writ against the recent CBDT Directive with respect to the Rating of Commissioners (Appeals). The Directive specifies three criteria, which if achieved, the Commissioner (Appeals) gets double points and hence boosts his rating. The criteria are – (1) – Further strengthening the order of AO. (2) Enhancing the taxable income viz., more than that assessed by AO. (3) Levying of penalty.

Such a directive holds the potential to prejudice the mind of AO and can induce him to base his order on this directive which in fact, can mar the fair and transparent assessment proceedings. While the introduction of e-assessment is highly welcome, as tax practitioner's time and unwanted personal interaction has considerably reduced, but the directives of above nature lead to suspicion in the minds of tax payers and tax practitioners that injustice done in assessment will continue in CIT Appeals also and may become more adverse and one will have to compulsorily take the matter till Tribunal. CIT appeals cannot be given such directive which prejudices their minds to employ so- called creative ideas to strengthen, enhance and levy penalty cropping up from AO's order. This is not acceptable and as torchbearer of the tax practising fraternity, the Chamber has taken lead in fighting for the cause of having fair and unbiased appellate proceedings.

The Special Story for the Chamber's Journal December issue is on Income from Unexplained Sources! We have touched upon the issues arising out of Prevention of Benami Properties Transaction Act, 1988 and Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act Act, 2015. The assessments for the previous year ending on 31st March 2017 during which the demonetisation of rupees 500 and 1000 notes was carried out will be taken up from January 2019 onwards. Thus, this issue will come in handy to our members to make effective representation before the authorities.

I thank all the esteemed professionals for sparing their valuable time to contribute to the Chamber's Journal December 2018 issue.

K. GOPAL
Editor

From the President

יהיה השינוי שאתה רוצה לראות בעולם

*In Hebrew means................****Be the change you want to see in the world!***

In our quest to cover various world languages, we have selected Hebrew, another old language of the world. And that is what we, at the Chamber believe in – To be the change through Professional growth!. In ***Mahatma Gandhi's words – "We must be the change, we wish to see in the world!"*** And while continuing to be the change, at the same time we should never stop learning, updating, contributing, imparting knowledge, and growing!.

The Japanese intellects have developed a concept termed 'Kaizen', which refers to 'Small but continuous improvement!' It is believed by the Japanese that continuous improvement is the path to perfection as they believe that with every time they improve, they learn something new. And hence, I would like to spread this message far and wide – *"It's no harm to go slow, as long as we are going and not stopping!"*

In Steve Job's words – *"The people, who are crazy enough to think they can change the word, are the ones who do!"*

The month of December also happens to house the festival, the ecstatic moment signifying the birth of the Prince of Peace, the *Messiah*, who pledged people into one of the oldest and the longest surviving religion of the world! Christmas is celebrated to remember the birth of Jesus Christ, who Christians believe is the Son of God. The name 'Christmas' comes from the Mass of Christ, and on this auspicious and celebrative occasion of Christmas, I would like to wish all my friends and members at Chamber, a Merry Christmas!

As we look at Christmas and invite a new year approaching, let us vow to take some new year resolutions promising to spread knowledge, keep learning, be the change, partner our Government in nation building and stitch out a new dawn for our country!

CTC EVENTS

This month will see a series of exciting events and seminars. A unique of its kind scheduled on the 10th December, 2018 on – Self Awareness Series Meeting by CA Varsha Shah on the subject of – ***"Work-Play-Inspire-Repeat!"*** Through excellent Life-building and Life-motivating lessons, it would be a great way for the members and students to find and pursue the right path, to see and understand life in a better way.

The Centre has notified National Financial Reporting Authority (NFRA) rules with monitoring and disciplinary powers over auditors of listed entities and large unlisted companies besides banks and insurance companies. NFRA – the newly set up independent regulator of the audit profession – has become the all-powerful body when it comes to disciplining auditors and overseeing the quality of service rendered by chartered accountants at large entities. ***A lecture meeting to throw light on the NFRA Rules*** has been scheduled on the 13th December, 2018.

The Centre also recently promulgated an ordinance to make changes to the Companies Act w.e.f. 2nd November 2018 with the aim to promote ease of doing business, ensure better corporate compliance and expedite insolvency proceedings. A lecture meeting to discuss the ***Compulsory Dematerialisation of Shares and Companies Amendment (Ordinance), 2018 has been scheduled on the 20th December, 2018***.

This month also sees our annual event of ***Intensive Study Course on FEMA*** on the 14th, 21st and 22nd December, 2018 ***which will be inaugurated by Mr. S. S. Mundra, Ex-RBI Dy. Governor,*** speakers from RBI, Foreign Exchange Department and stalwarts of our profession as speakers and Brains' trustees.

As much as we promote the culture of imparting knowledge, at CTC we equally promote to show case the talents possessed by our members. CTC takes pride in announcing a ***musical event – "Surila Yarana!"*** on the 11th January, 2019 for the members, by the members and to the members. It will be a grand musical evening of togetherness followed by ***dancing to the tunes of famous Bamboo beats*** and their troupe performing garba, bhangda and popular Bollywood songs followed by dinner.

Playing cricket is like running an organization – It needs team work, motivation, strategy, flexibility, risk assessment and good captaincy. To lighten the mood post tax season, CTC is organising the 5th edition of the ***CTC Box Cricket Tournament*** on the 12th January, 2019.

The CTC, this month announces the most-awaited event of the year – ***The Dastur Essay Competition, 2019***. We, at the CTC believe that young students are the future leaders of our nation. Members are requested to encourage students to participate in this Essay Competition. We have similar event of ***Debate Competition*** jointly organised with H. R. College of Commerce and Economics on 18th and 19th January, 2019.

We have received an overwhelming response to our ***5th International Study Tour to East Europe*** and we have closed registration within one week. We are looking at increasing group size from 45 to 80 passengers.

We have also finalised venue and dates for ***13th RRC on International Taxation at Surat*** from 20th to 23rd June, 2019. All other RRCs are receiving good enrolments and are almost full.

REPRESENTATIONS

Chamber has filed writ petition in Bombay High Court on new CBDT directive related to ranking of Commissioner Appeals, which states that Commissioner Appeals will get double points if he fulfils these three criteria (1) Further strengthening the order of AO. (2) Enhancing the taxable income viz., more than that assessed by AO. (3) Levying of penalty. Such a directive can defeat the conduct of appellate proceedings in unbiased manner. The Chamber places on record the hard work put in by seniors like Mahendra Sanghvi, Vipul Joshi, assisted by Dharan Gandhi, Abhitan Mehta, Apurva Shah and others in Law & Representation Committee in making Chamber raising its voice as a representative of tax fraternity and tax practitioners with an objective to have unbiased appellate proceedings *de hors* of such directive. Above all, Chamber is blessed with guidance of our Senior Past President Shri Sohrab Dastur saheb who guided us on the above petition.

Special Story for the month on ***"Income from unexplained Sources"*** designed by Bhadresh Doshi and his team deserves compliments, as it covers entire gamut of topics including Benami Law, Black Money Law etc. I thank all authors for timely contribution of their articles.

We have very few copies of our Publications left and members are requested to buy before they are sold out.

Thank you,

Hinesh R. Doshi
President

The Chamber of Tax Consultants

Vision Statement

The Chamber of Tax Consultants (The Chamber) shall be a powerhouse of knowledge in the field of fiscal laws in the global economy.

The Chamber shall contribute to the development of law and the profession through research, analysis and dissemination of knowledge.

The Chamber shall be a voice which is heard and recognised by all Government and Regulatory agencies through effective representations.

The Chamber shall be pre–eminent in laying down and upholding, among the professionals, the tradition of excellence in service, principled conduct and social responsibility.

Dr. Rakesh Gupta *FCA, FCS, AICWA, MBA, LLM, PhD*
& Somil Agarwal *ACA, ACS, AICWA, LLM (U.K)*

Deemed Income – Doomed Implications!!!

Sections namely 68, 69, 69A, 69B, 69C and 69D fall under Chapter VI titled as "Aggregation of Income and Set off or Carry Forward of Loss". These sections deal with unexplained cash credit, unexplained investment, unexplained money, unexplained expenditure etc. etc., as deemed income. Since these sections are there on the statute for a long time, we may not reproduce them but section 115BBE which is of recent origin & has been amended quite often is being reproduced before any discussion takes place:

Section 115BBE introduced by the Finance Act, 2012 w.e.f. 1-4-2013 & amended from time to time, which stands as on date:-

Tax on income referred to in section 68 or section 69 or section 69A or section 69B or section 69C or section 69D.

115BBE. *[(1) Where the total income of an assessee,—*

(a) includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D and reflcted in the return of income furnished under section 139; or

(b) determined by the Assessing Officer includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, if such income is not covered under clause (a),

the income-tax payable shall be the aggregate of—

(i) the amount of income-tax calculated on the income referred to in clause (a) and clause (b), at the rate of sixty per cent; and

(ii) the amount of income-tax with which the assessee would have been chargeable had his total income been reduced by the amount of income referred to in clause (i).]

(2) Notwithstanding anything contained in this Act, no deduction in respect of any expenditure or allowance [or set off of any loss] shall be allowed to the assessee under any provision of this Act in computing his income referred to in clause (a) [and clause (b)] of sub-section (1).

Controversy as to head of Income

Section 14 of the Act, provides for computation of total income under the five heads of income i.e., Salaries, House Property, Profit and Gains of Business or Profession, Capital Gains, Other sources. Controversy is as to under which head of income such deemed income should be assessed. This is relevant because once income/loss is computed under a particular head of income, provisions of inter-head adjustment as prescribed u/s. 71 are to be explored and given effect to. Section 71 provides for the set-off of loss from one head against income from another with certain exceptions. If there was loss under the head 'business' and income from 'other sources' in the same year, section 71 provided the set off of loss from 'business' against income from 'other sources'. Reason for such controversy arose as a result of certain judicial decisions which is expedient to discuss at this stage.

Hon'ble Gujarat High Court in the case of *Fakir Mohmed Haji Hasan vs. Commissioner of Income-Tax (2001) 247 ITR 290,* interpreting the scope and describing the scheme of Sections 69, 69A, 69B and 69C of the Act, observed:

"The scheme of sections 69, 69A, 69B and 69C of the Income-tax Act, 1961, would show that in cases where the nature and source of investments made by the assessee or the nature and source of acquisition of money, bullion etc., owned by the assessee or the source of expenditure incurred by the assessee are not explained at all, or not satisfactorily explained, then, the value of such investments and money or the value of articles not recorded in the books of account or the unexplained expenditure may be deemed to be the income of such assessee. It follows that the moment a satisfactory explanation is given about such nature and source by the assessee, then the source would stand disclosed and will, therefore, be known and the income would be treated under the appropriate head of income for assessment as per the provisions of the Act. However, when these provisions apply because no source is disclosed at all on the basis of which the income can be classified under one of the heads of income under section 14 of the Act, it would not be possible to classify such deemed income under any of these heads including income from "other sources" which have to be sources known or explained. When the income cannot be so classified under any one of the heads of income under section 14, it follows that the question of giving any deductions under the provisions which correspond to such heads of income will not arise. If it is possible to peg the income under any one of those heads by virtue of a satisfactory explanation being given, then these provisions of sections 69, 69A, 69B and 69C will not apply, in which event, the provisions regarding deductions etc., applicable to the relevant head of income under which such income falls will automatically be attracted.

The opening words of section 14 "save as otherwise provided by this Act" clearly leave scope for "deemed income" of the nature covered under the scheme of sections 69, 69A, 69B and 69C being treated separately, because such deemed income is not income from salary, house property, profits and gains of business or profession, or capital gains, nor as it income from "other sources" because the provisions of sections 69, 69A, 69B and 69C treat unexplained investments, unexplained money, bullion etc. and unexplained expenditure as deemed income where the nature and sources of investment, acquisition or expenditure, as the case may be, have not been explained or satisfactorily explained. Therefore, in these cases, the source not being known, such deemed income will not fall even under the head "income from other sources". Therefore, the corresponding deductions which are applicable to the incomes under any of these various heads, will not be attracted in the case of deemed incomes which are covered under the provisions of sections 69, 69A, 69B and 69C of the Act in view of the scheme of those provisions."

This decision was simply followed by Hon'ble Punjab & Haryana High Court in the case of *Kim Pharma P. Ltd. vs. CIT 258 ITR 454* but without its own independent reasoning.

Hon'ble Gujarat High Court in a subsequent decision titled as *Krishna Textiles vs. CIT 310 ITR 227* observed that:

The decision of this Court in the case of Fakir Mohmed Haji Hasan vs. CIT (supra) would not render much assistance to the Revenue as in that case, the Court was really concerned with the unexplained investment under s. 69 of the Act and other provisions, namely, ss. 69A, 69B and 69C are not under consideration. The onus to prove is different under each of these provisions, more particularly, under s. 69C, the onus is on the Revenue to prove that the income really belongs to the assessee. Moreover, proviso to s. 69C which has come into force w.e.f. 1st April, 1999 was not considered while laying down the general propositions with regard to ss. 69A, 69B and 69C of the Act. Hence at the most, these *observations are merely in the nature of an obiter so far as s. 69C is concerned and it cannot be considered as a ratio laid down by this Court.*

Hon'ble Gujarat High Court in a subsequent case titled *DCIT vs. Radhe Developers India Ltd. 329 ITR 1* observed in para 22 as under:

The decisions of this Court in the case of Fakir Mohmed Haji Hasan (supra) and Krishna Textiles (supra) are neither relevant nor germane to the issue considering the fact that in none of the decisions the legislative scheme emanating from conjoint reading of provisions of ss. 14 and 56 of the Act have been considered. The Apex Court in the case of D.P. Sandu Bros. Chembur (P) Ltd. (supra) has dealt with this very issue while deciding the treatment to be given to a transaction of surrender of tenancy right. The earlier decisions of the apex Court commencing from case of United Commercial Bank Ltd. vs. CIT (1957) 32 ITR 688 (SC) have been considered by the Apex Court and, hence, it is not necessary to repeat the same. Suffice it to state that the Act does not envisage taxing any income under any head not specified in s. 14 of the Act. In the circumstances, there is no question of trying to read any conflict in the two judgments of this Court as submitted by the learned counsel for the Revenue.

Section 56(1) provides that income of every kind which is not to be excluded from the total income shall be chargeable to income tax under the head 'income from other sources'. Deemed income under sections 68, 69 etc. are therefore to be assessed under the head 'income from other sources' as per this mandate. But decisions of *Fakir Mohmed Haji Hasan vs. Commissioner of Income-Tax (2001) 247 ITR 290 (Guj) & Kim Pharma (P&H), supra*, held otherwise. Gujarat High Court in the subsequent decision of *Radhe Developers, supra*, brought the incorrectness of the proposition of law to the fore albeit obliquely since this decision too was the decision of a bench of coordinate strength, their Lordships could not do more except to indicate that law as explained by the Supreme Court decisions have gone unnoticed by the previous bench.

Thus, taking into account the above mentioned judicial decisions, it can be concluded that Act does not contemplate taxing any income under any head not specified in section 14. Deemed income u/ss. 68, 69 etc. would have therefore to be assessed under the head Income from other sources. This becomes further clear when we read the disability under sub-section (2) of section 115BBE which provides that there would not be allowed any deduction in respect of any expenditure or allowance or set-off of any loss against such deemed income. Had such income not been falling under the head Income from Other sources, where was the need for the legislature to provide such disability under sub-section (2) of section 115BBE. But for the prescribed head of income covering the deemed income, there was no occasion for claiming any deduction of expenditure, allowance or set off of loss against deemed income u/s. 68, 69, 69A. In fact, Hon'ble Income Tax Appellate Tribunal in the case of Satish Kumar held that in the absence of any provision in section 115BBE as to the denial of the set off of any loss prior to A.Y. 2017-18, benefit of the set off of loss could not be denied in earlier years. Other decisions of the Tribunal are also to the similar effect that the words added "or set off of any loss" in section 115BBE (2) are with prospective effect. All these decisions show that deemed income are to be assessed under the head 'income from other sources'. Had it not been like this, where was the occasion to claim any deduction on account of expenditure or allowance or set off of loss against the deemed income & where was the need for providing for the denial of set off or claiming deduction u/s. 115BBE. If legislature intended to treat deemed income under sections 68, 69 etc., as income without any prescribed head, there was no need to bring sub-section (2) to section 115BBE. In fact, section 115BBE does not seek to disturb this position of law as it merely prescribes the rate of tax applicable on such deemed income. Therefore, by creating disability under sub-section (2) of section 115BBE legislature too has given enough indication that such deemed income was assessable under some head of income out of the five heads. Since these incomes u/s. 68, 69, 69A etc. are deemed incomes due to the fact that its nature & source remain unexplained, the obvious head of income under which such income would fall is income from other source as per the mandate of section 56(1). Controversy that deemed income is in the nature of orphan child without any head of income, in our considered opinion, is thus misplaced.

Controversy as to prospective or retrospective effect to amendment to sub section (2) of section 115BBE

Sub-section (2) of section 115BBE provided that no deduction in respect of any expenditure or allowance shall be allowed to the assessee under any provision of this Act in computing the income of the nature referred to in sections 68, 69, 69A, 69B , 69C and 69D. There was no denial to 'set off of any loss' under sub-section (2) initially, until amendment was brought by the Finance Act, 2016 w.e.f. 1-4-2017 when the words "or set off of any loss" were added. Issue arises is as to whether words added by Finance Act, 2016 are prospective or should be interpreted to be curative in nature & thus have retrospective effect. Though there are judicial decisions in favour of its prospective application but it cannot be ignored that the sub section (2) of section 115BBE is negatively worded & that too with non obstante clause preceding. Such negative wording of this sub-section shows & emphasises that legislature was quite certain, vocal & emphatic to deny the claim of any deduction against such deemed income. When Explanatory Memorandum is read it appears that legislature omitted to mention the denial of 'set off of loss' initially when this sub-section was introduced and when legislature found that omission not in accord with the intention, it supplied that omission by bringing the explicit amendment. When legislature denied deduction in respect of expenditure or allowance, there was no reason that set off of loss was contemplated to be allowed. Legislature intended to tax the deemed income at a particular rate and thus there was no reason for leaving the 'set off of loss' outside the scope of denial. Explanatory Memorandum emphasised & denied extending the benefit of even basic exemption limit against such deemed income. That shows that no deduction or set-off of whatever nature was ever intended by the legislature. Similarly, Explanatory Memorandum of Finance Act, 2016 while adding the words stated that currently, there was uncertainty on the issue of set-off of losses against income referred in section 115BBE of the Act & the matter has been carried to judicial forums and courts in some cases has taken a view that losses shall not be allowed to be set-off against income referred to in section 115BBE. However, Memorandum further reads that, the current language of section 115BBE of the Act does not convey the 'desired intention'.

In that sense such amendment having been brought in the background as aforesaid, even that omission seems to have been bridged by the legislature and in that sense, such amendment may be read as curative and thus retrospective. Counter arguments can be given to this line of thinking as given by the decisions of several benches of the Tribunal but retrospective effect of such amendment is an issue which would keep on prodding the judges unless the final word comes from the highest court of the land.

Controversy as to retroactivity of 60% tax rate in some cases & its confiscatory nature

There is one more important facet of section 115 BBE and that is the tax rate. Taxation Laws (Second Amendment) Act, 2016 made the tax rate from 30% to 60% effective from 1st April 2017, which means that any amount in the nature of income under sections 68, 69 69A etc., would suffer the tax rate of 60%, for and from assessment year 2017-18. It is important to submit that the Taxation Laws (Second Amendment) Act, 2016 was though passed by Parliament on 15th December, 2016 but was made effective from 1st April 2017 i.e. from A.Y. 2017-18. Necessary implication of such amendment is that any income covered by these sections, even if, relating to the period after 1-4-2016 but prior to the enactment of Taxation Laws (Second Amendment) Act, 2016 would also attract tax rate of 60%. In many survey proceedings, conducted during the period between 1st April 2016 till the date of enactment of Taxation

Laws (Second Amendment) Act, 2016 assessees did make declaration of income covered by these sections under the ostensible and apparent belief that income which they have surrendered would attract tax rate of 30% as per the then applicable tax rate. But with the enactment of Taxation Laws (Second Amendment) Act, 2016, rules of the game underwent change & such already declared income was also hit by the enhanced rate of 60%.

It is quite strange and surprising that in the first place all such deemed income suffer flat rate of tax without set off of any loss etc., and on the other hand even that rate of 30% was increased to 60% with 25% surcharge thereon, thus making it an aggregate to 75% & that too from 1-4-2017 i.e., from A.Y. 2017-18. It means that an assessee who has agreed to surrender income under the aforesaid sections in survey taken place prior to 15-12-2016 on the premise and belief that the tax rate is 30% would end up paying 60% +25% surcharge as a result of the subsequent amendment, which operated in a retroactive manner.

In case of search taking place on or after 15-12-2016 penalty too has been prescribed under section 271AAB (1A), according to which penalty @ 30% to 60% of the undisclosed income may also be imposed, which means that impact of tax and penalty in respect of such incomes found as a result of search which took place after 15-12-2016 would be 105% to 135% (ignoring the effect of education and other cess). Does it mean that income-tax rates besides being atrocious, has assumed confiscatory proportions. Such high rate of tax with respect to declared income where assessee is not able to explain nature & source of such income earned, will discourage the assessees to make declaration of undisclosed income during search and survey proceedings so as to settle the issue and debar the department from early collection of taxes. Such situation will lead to more litigation.

Some further thoughts in relation to deemed income

Therefore everybody looks forward making declaration of income, if at all he has to so declare, during survey or otherwise under such head of income so that the rigour of high tax rate of 60%, as prescribed in section 115BBE can be avoided. There cannot be any clear cut answer or blanket proposition in this regard as it depends upon the facts and circumstances of each case. Attempt however remains to avoid applicability of sections 68, 69, 69A, 69B, 69C & 69D.

Section 41(1) provides *inter alia* that a trading liability in respect of which deduction has been made & allowed and such liability ceases to exist or is remitted by the creditor, such ceased/remitted trading liability shall be deemed to be the Profit & Gains of the business. It has been experienced that several trading liabilities appearing in the books of account may no longer be payable and yet continue to appear in the books of account over the years. If such liabilities are written back, such amount is liable to be taxed u/s. 41(1) under the head "Business Income". Similarly receipts from the discontinued business after the discontinuance is deemed to be income of the business and charged to tax in the year of receipt in the same manner as if such amount had been received before such discontinuance. Therefore, such an income so received would also partake the character of "Business Income". Gross Profit/Net Profit of the business may also fluctuate from year-to-year and any surrender on this score would also be assessed as "Business Income". Any recovery of the bad debts which have been previously allowed as a deduction while computing business income shall be assessed as business income under section 41(4). Excess stocks found are prone to be assessed as unexplained investment but short stocks may lead to the inference of its sale outside the books of account thus leading to addition to the business income. Suppressed sales, undisclosed scrap sales & debtors for goods found would also lead to the addition to the business income. Addition account of bogus purchases of the goods dealt & inflation of business expenses may also lead to the inflation of the business profits.

Controversies are closely associated with the deemed incomes and provide useful fodder for thoughtful interaction.

❍❑❍

CA Reepal G. Tralshawala

Cash Credits – Fundamental Principles

Introduction

1.1 Section 68 of the Income-tax Act is a deeming provision i.e., it presumes the receipt of or credit of any sum in the books of account as income of the assessee unless otherwise proved. This provision was brought into statute in order to plug loopholes of introducing unaccounted income in the books of account of the assessee by any means such as taking loans/deposits from third party or by way of capital or by way of gifts (prior to insertion of section 56(v)/56(vi)) or any other mode.

1.2 As per section 68 of the Act the burden of proof is on the assessee in whose books of account the credit is found for discharging the nature and source of such credit and failure to give proper and reasonable explanation for such credit, the income tax authority can fasten him with liability to tax on account of unexplained credit and treating it as taxable income.

2. Analysis of section 68

2.1 The Supreme Court in the case of *CIT vs. P. Mohanakala [2007] 291 ITR 278 (SC)* has interpreted the provisions of sec.68 of the Act wherein certain principles and guidelines are laid down as to the nature and scope of sec.68 of the Act. In para 14 of the decision, it lays down the following guiding principles-

"The question is what is the true nature and scope of section 68 of the Act? When and in what circumstances section 68 of the Act would come into play? That a bare reading of section 68 suggests that there has to be credit of amounts in the books maintained by an assessee; such credit has to be of a sum during the previous year; and the assessee offers no explanation about the nature and source of such credit found in the books; or the explanation offered by the assessee in the opinion of the Assessing Officer is not satisfactory, it is only then the sum so credited may be charged to income-tax as the income of the assessee of that previous year. The expression "the assessee offers no explanation" means where the assessee offers no proper, reasonable and acceptable explanation as regards the sums found credited in the books maintained by the assessee. It is true the opinion of the Assessing Officer for not accepting the explanation offered by the assessee as not satisfactory is required to be based on proper appreciation of material and other attending circumstances available on record. The opinion of the Assessing Officer is required to be formed objectively with reference to the material available on record. Application of mind is the sine qua non for forming the opinion."

2.2 The principles laid down can be summarised thus-

a) credit has to be there in the books of account of assessee;

b) such credit has to be of sum during the previous year;

c) no explanation about the nature and source of such credit found in the books of account is given by assessee; or

d) the explanation offered is not satisfactory in the opinion of AO.

2.3 In para 21 of the decision, the Supreme Court concludes as under-

"It is true that even after rejecting the explanation given by the assessee if found unacceptable, the crucial aspect whether on the facts and circumstances of the case it should be inferred the sums credited in the books of the assessee constituted income of the previous year must receive the consideration of the authorities provided the assessee rebut the evidence and the inference drawn to reject the explanation offered as unsatisfactory. We are required to notice that section 68 of the Act itself provides, where any sum is found credited in the books of the assessee for any previous year the same may be charged to income-tax as the income of the assessee of the previous year if the explanation offered by the assessee about the nature and source of such sums found credited in the books of the assessee is in the opinion of the Assessing Officer not satisfactory. Such opinion found itself constitutes a prima facie evidence against the assessee, viz., the receipt of money, and if the assessee fails to rebut the said evidence the same can be used against the assessee by holding that it was a receipt of an income nature. In the case in hand the authorities concurrently found the explanation offered by the assessee unacceptable. The authorities upheld the opinion formed by the Assessing Officer that the explanation offered was not satisfactory. The assessee did not take the plea that even if the explanation is not acceptable the material and attending circumstances available on record do not justify the sum found credited in the books to be treated as a receipt of an income nature. The burden in this regard was on the assessee. No such attempt has been made before any authority. All the decisions cited and referred to hereinabove are required to be appreciated and understood in the light of the law declared by this Court in Sumati Dayal's case (supra)."

2.4 The conclusion in para 21 of the Supreme Court decision suggests the following course of action before taxing the sum credited in books of account of assessee as its income-

i) find whether any sum is credited in the books of account of assessee;

ii) if (i) is yes, then call for explanation and evidences from the assessee and evaluate the same; and

iii) even if for any reason, the explanation given by assessee is found to be not satisfactory, evaluate further whether the same represents income of the assessee – this last evaluation only if assessee discharges burden to prove that the attending circumstances does not justify the credit in the books of account to be of income nature.

2.5 It is important to note here that sec.68 of the Act nowhere states that – identity, genuineness and creditworthiness is to be proved. Sec.68 only refers to nature and source of credit to be explained. In order to discharge the burden cast on the assessee to prove the credit in the books of account, the 3 ingredients i.e., identity of the creditor, genuineness of the transaction and creditworthiness of the creditor – are the guiding principles laid down by Courts. However, these ingredients are only guidance for the assessee for discharging the burden of proving credits in the books of account and nowhere the proposition is laid down that if these 3 ingredients are proved then no addition can be made or *vice versa*. For e.g., in the case of *Sumati Dayal vs. CIT (1995) 214 ITR 801 (SC),* the assessee therein gave explanation regarding the credit in books of account and evidence in support of the same in terms of the 3 ingredients stated above. However, the Supreme Court held at pages 808-809-

"This, in our opinion, is a superficial approach to the problem. The matter has to be considered in the light of human probabilities. The Chairman of the Settlement Commission has emphasised that the appellant did possess the winning ticket which was surrendered to the Race Club and in return a crossed cheque was obtained. It is, in our view, a neutral circumstance; because if the appellant had purchased the winning ticket after the event she would be having the winning ticket with her which she could surrender to the Race Club. The observation by the Chairman of the Settlement Commission that "fraudulent sale of winning ticket is not an usual practice but is very much of an unusual practice" ignores the prevalent malpractice that was noticed by the District Taxes Enquiry Committee and the recommendations made by the said Committee which led to the amendment of the Act by the Finance Act, 1972 whereby the exemption from tax that was available in respect of winning from lotteries, crossword puzzles, races, etc., was withdrawn. Similarly the observation by the Chairman that if it is alleged that these tickets were obtained through fraudulent means, it is upon alleger to prove that it is so, ignores the reality. The transaction about purchase of winning ticket takes place in secret and direct evidence about such purchase would be rarely available. An inference about such a purchase has to be drawn on the basis of the circumstances available on the record. Having regard to the conduct of the appellant as disclosed in her sworn statement as well as other material on the record an inference could reasonably be drawn that the winning tickets were purchased by the appellant after the event. We are, therefore, unable to agree with the view of the Chairman in his dissenting opinion. In our opinion, the majority opinion after considering surrounding circumstances and applying the test of human probabilities has rightly concluded that the appellant's claim about the amount being her winning from races is not genuine. It cannot be said that the explanation offered by the appellant in respect of the said amount has been rejected unreasonably and that the finding that the said amounts are income of the appellant from other sources is not based on evidence."

In *CIT vs. Noorjehan (Smt. P.K.) (1999) 237 ITR 570 (SC)* the Supreme Court, though in the context of section 69 of the Act, held that the word employed in sec. 69 is 'may' and not 'shall' and therefore even if the explanation offered by assessee is found to be not satisfactory, does not and need not in every case, automatically, result in deeming the value of the investment to be the income of the assessee. That is still a matter within the discretion of the officer, and therefore the Tribunal. In sec. 68 of the Act, the word employed is also 'may' and therefore, even if all the 3 ingredients are not established, however if the facts and the circumstances prove otherwise, then the AO or other authority at its discretion can still hold that the amount credited in the books of account is not the income of the assessee.

2.6 Any sum found credited in the books of an assessee maintained by him:

Credits in cash or credits generally

Even though the heading of section 68 of the Act refers to 'Cash Credit', the body of the section refers to any sum found credited and thus, the section is not confined merely to credits in actual 'cash'. Other credits by way of liabilities also require explanation as stipulated under section 68 so that when they are not satisfactorily explained, they are bound to be added – *VISP (P) Ltd. vs. CIT (2004) 265 ITR 202 (MP).*

Books of account

The expression books of assessee referred in section 68 refers to the assessee whose books show the credit entry meaning thereby that the books have to be the books of the assessee himself and not any other assessee – *Anand Ram Raitani vs. CIT (1997) 223 ITR 544 (Gau).*

Bank pass book – whether assessee's book

The Bombay High Court in *CIT vs. Bhaichand H. Gandhi (1983) 141 ITR 67 (Bom.)* has held that the pass book supplied by a bank to an assessee-constituent could not be regarded as a book of the assessee which expression means a book maintained by the assessee or under his instructions. It was so ruled on the principle that when moneys are deposited in a bank the relationship that is constituted between the bankers and the customers is one of debtor and creditor and not that of trustee and beneficiary. The pass book supplied is merely the copy of the constituent's account in the books maintained by the bank.

Rough books – also books for section 68

In was so held in *Haji Nazir Hussain vs. ITO (2004) 271 ITR (AT) 14 (Del.)* that where cash credits are recorded in the rough cash book of the assessee and there is no proper explanation, section 68 will apply and the credit amount can be assessed as income of the assessee.

Loose sheets are not books

The Hon'ble Supreme Court in *Mohd. Yusuf & Anr. vs. D & Anr. AIR 1968 Bom. 112* has observed that the content contained in document is hearsay evidence unless the writer thereof is examined before the Court. The piece of paper seized during search if considered in light of section 32 of the Indian Evidence Act and General Clauses Act defining the word 'document', the piece of paper contains jottings of certain figures and does not described or express the substance of any transaction and therefore the said paper does not come within the compass of definition of the word 'document' to be used as evidence. It further held that the piece of paper did not represent books of account for the reason that as per Black's Law Dictionary, books of account means: *"A detailed statement, in the nature of debits and credits between persons; an account or record of debits and credits kept in a book; a book in which a detailed history of business transaction is entered; a record of goods sold or services rendered; statement in detail of the transactions between the parties."* The SC in *CBI vs. V.C. Shukla (1998) 3 SCC 410* has held that the piece of paper seized in search not been proved to be written by the assessee relating to various business transactions in the normal course of business and therefore the said paper does not fall within the campus of the meaning of the books of account having credibility of its acceptance without support of corroborative evidence. Following the said decision, it was held in *Goyal (S.P.) vs. DCIT (2004) 269 ITR (AT) 59 (Bom.)* that what are found in loose sheets will not attract application of section 68, because they are not books of account, so as to attract section 68.

2.7 Offers no explanation about the source of credit or the explanation is not satisfactory

The explanation given by the assessee should be considered objectively before the officer takes a decision to accept it or reject it. As explained by the Supreme Court in *Sreelekha Banerjee vs. CIT (1963) 49 ITR 112 (SC)* if the explanation given by the assessee shows that the receipt is not of income nature, the department cannot "convert good proof into no proof" or otherwise act unreasonably and reject it. Thus, the explanation furnished by the assessee needs to be considered objectively and the explanation given cannot be rejected arbitrarily or capriciously, without sufficient grounds, on suspicion or on imaginary or irrelevant grounds – *Sona Electric Co vs. CIT (1985) 152 ITR 507 (Del.); Roshan Di Hatti vs. CIT (1977) 107 ITR 938 (SC)*. The explanation also cannot be rejected merely on the ground that the department is unable to verify its correctness – *Hastimal (S) vs. CIT (1963) 49 ITR 273 (Mad.).* On the other hand, if the explanation is unconvincing, the same may be rejected and an inference drawn that the amount represents undisclosed income either from a disclosed or an undisclosed source – *Vimalchand Bhimsen vs. CIT (1986) 159 ITR 941 (MP) – SLP dismissed (1990) 186 ITR (St.) 74.* In cases where the assessee furnishes full details regarding the creditors, it is up to the department to pursue the matter further to trace these and examine their creditworthiness – *CIT vs. Orissa Corporation (P) Ltd. (1986) 159 ITR 78 (SC); CIT vs. Shree Barkha Synthetics Ltd. (2004) 270 ITR 477 (Raj.)*. Once an explanation is given, it is for the Assessing Officer to accept it or reject it but he cannot accept the explanation in part and reject it in part – *Mehta Parikh & Co. vs. CIT (1956) 30 ITR 288 (SC); Lal Chand Bhagat Ambica Ram vs. CIT (1959) 37 ITR 288 (SC).* The department cannot draw inferences and assume that there has been some illegality in the assessee's transaction in the absence of any material in its possession – *Sivan Pillai (AS) vs. CIT (1958) 34 ITR 328 (Mad.); C.Ag. IT vs. Cherian (MJ) (1979) 117 ITR 371 (Ker).* It is not open to the department while rejecting the explanation of the assessee to make presumption that the witness have come forward to give false evidence to oblige the assessee – *Sheo Narain Duli Chand vs. CIT (1969) 72 ITR 766 (All.).*

3. Onus to prove & onus when shifts

It is well established that the onus of proving the source of any money received by the assessee is upon him. If liability to pay tax is disputed, it is the responsibility of the assessee to show that the receipt was either not income or income exempt from tax – *Kale Khan Mohammad Hanif vs. CIT (1963) 50 ITR 1 (SC); Govindarajulu Mudaliar (A) vs. CIT (1958) 34 ITR 807 (SC); CIT vs. Devi Prasad Vishwanath Prasad (1969) 72 ITR 194 (SC).* The provision of section 68 of the Act places responsibility on the assessee to prove what is best known to him, since the facts relating to him are in his custody and it is therefore for the assessee to establish the facts relating to the claim, whether a particular receipt or investment has income character. In *Sreelekha Banerjee vs. CIT (1963) 49 ITR 112 (SC)* it is held, that the assessee has legal obligation to explain the nature and source of entries in his books.

Onus when discharged

Once the assessee establishes the nature and source of credit in its books of account and proves (a) identity of the third party; (b) the ability of the third party to advance moneys; and (c) *prima facie* that the transaction is genuine one, it would be for the department to disprove the same – *CIT vs. Baishnab Charan Mohanty (1995) 212 ITR 199 (Ori.).* In *CIT vs. Orissa Corporation P. Ltd. (1986) 159 ITR 78 (SC)* it was held that when assessee has given names and addresses of creditors and the said creditors are income tax assessee whose index numbers are with the revenue, the initial burden lay on the assessee gets discharged. Where an assessee gives the correct name and address of the alleged creditors, their PAN numbers, it could be said that he has discharged his onus to prove the genuineness of credits in his accounts and unless the revenue authority issues notice to test the genuineness of the transaction or the capacity of the creditor to pay, the amount cannot be assessed in the hands of the assessee – *CIT (Addl.) vs. Hanuman Agarwal (1985) 151 ITR 150 (Pat.); Jalan Timbers vs. CIT (1997) 223 ITR 11 (Gau).* Where the assessee has proved the identity of creditors and the amounts were received by account payee cheques, the initial burden on the assessee is discharged. The finding of the Tribunal that cash credits should be treated as proved in absence of any further material to discredit the same has to be upheld – *DCIT vs. Rohini Builders (2002) 256 ITR 360 (Guj) [SLP dismissed (2002) 254 ITR 276].*

However, the *prima facie* evidences as suggested above needs to be ordinarily treated as discharge of onus, but the correct understanding is that the burden gets shifted to the department. It gets discharged only when the Assessing Officer accepts the explanation. Nothing prevents the department from probing the matter further and making necessary investigation in the matter.

Assessee not to prove source of source (except in certain cases as per proviso)

While discharging the onus cast upon the assessee, it is not the requirement of law that the assessee also needs to prove source of source i.e., once the assessee is able to establish the money received from the third party, he cannot be burdened with a further onus of establishing the source from which such third party has been able to obtain the money. [Refer - *Sarogi Credit Corpn. vs. CIT (1976) 103 ITR 344 (Pat.); DCIT vs. Rohini Builders (2002) 256 ITR 360 (Guj) [SLP dismissed (2002) 254 ITR 276]* – followed the decision of *Orient Trading Co. Ltd. vs. CIT (1963) 49 ITR 723 (Bom.)]; (2008) 8 DTR 199 (Raj.) Aravali Trading Co. vs. ITO.*

The Hon'ble Supreme Court in *CIT vs. Daulat Ram Rawatmall (1973) 87 ITR 349 (SC)* held that the onus to prove that the apparent is not the real is on the party who claims it to be so. As it was the department which claimed that the amount of FD belonged to the assessee even though the receipt had been issued in the name of third party, the burden lay on the department to prove that the assessee was the owner of the amount despite the fact that the receipt was in the name of third party. A simple way of discharging the onus and resolving the controversy was to trace the source and origin of the amount and find out its ultimate destination. So far as the source is concerned, there is no material on the record to show that the amount came from the coffers of the assessee or that it was tendered in the bank on behalf of the assessee. As regards, the destination of the amount it has already been mentioned that there is nothing to show that it went to the coffers of the assessee. On the contrary there is positive evidence that the amount was received by the third party and would thus follow that both as regards the source as well as the destination of the amount, the material on the record gives no support to the claim of the department.

4. Duty of AO to enforce attendance

It is the duty of the Assessing Officer to enforce attendance of a witness if his evidence is material, irrespective of whether request is from assessee. However, if assessee is asked to produce the creditor and is unable to do so, it would be for the assessee to request the AO to enforce the attendance of the creditor. Thus, if the AO does not exercise his powers to call the witness and examine him, he cannot treat the deposits in the name of the witness as suppressed income of the assessee – *Nathu Ram Premchand vs. CIT (1963) 49 ITR 561 (All); Munnalal Murlidhar vs. CIT (1971) 79 ITR 540 (All).* It has been held in *Cf. Food Corporation of India vs. Provident Fund Commissioner (1990) 1 SCC 68, 71 (SC)* that it is the legal duty of the officer concerned who is vested under section 131 with certain powers in respect of certain matters. It would be failure to exercise the jurisdiction particularly when a party to the proceedings requests for summoning evidence from a particular person. However, for seeking assistance of the Assessing Officer to enforce attendance of a witness, the assessee must furnish the complete address of such person and in case of failure to provide the correct and complete address, there is no duty on the Assessing Officer to issue summons – *Sri Jagdish Saran Shukla v. CIT (1988) 171 ITR 694, 697-98 (All).* Similar view is taken in *Ram Kumar Jalan vs. CIT (1976) 105 ITR 331 (Bom)* wherein the summons issued to the creditor was returned with postal remark 'not known' and the request of assessee to issue second summon on the same address was declined and addition made, it was held that the addition could not be treated as unjustified because the postal endorsement indicated that the addressee could not be traced. A fresh summon could be issued only if the address given in the first summons sent was erroneous.

5. Year of charge

The section provides that the sum so credited may be charged to income tax as the income of the assessee of that previous year. The chargeability to tax in respect of unexplained credits would be only in the year in which the credit first appears in the books of account of the assessee. In *CIT vs. Prameshwar Bohra (2008) 301 ITR 404 (Raj)* the High Court upheld the view of the Tribunal that since the credits did not relate to the impugned year in which the addition was made, the same was liable to be deleted only on this ground.

6. Peak Credit Theory

One of the defences taken by the assessee in respect of unexplained cash credit is that only the "peak" of the credits should be treated as unexplained. This defence is taken when number of credits appear in the books of account of any assessee side by side with a number of debits and so arranged in the serial number of dates of credit and debit so that the credit following a debit entry should be treated as referable to the latter to the extent possible and that not the aggregate but only the "peak" of the credits be treated as unexplained credits. Such a plea is generally accepted as it is logical and acceptable (irrespective of whether the creditor is genuine or not, since once AO is not satisfied with the explanation, alternative plea of applying peak theory may be raised) provided that the record show that a particular withdrawal/repayment is available on the date of subsequent credit. In *ACIT vs. Tritan Happy Home (P.) Ltd. (2005) 94 TTJ 628 (Ctk.)* it was held that the Commissioner (A) had rightly considered the entries in the cash book and instead of adding each and every entry, he had rightly considered peak credits for making the addition.

This proposition is not a proposition of law but normal probabilities, which can be displaced by any material that may indicate to the contrary.

7. Telescoping benefit

In *CIT vs. Tyaryamal Balchand (1987) 165 ITR 453 (Raj)* additions were made to the trading results as also amounts representing cash credits were added as income from undisclosed sources. The Tribunal found that the additions in trading results would cover the amount of cash credits as also substantial additions had been made in earlier years, it was held that the Tribunal was justified in deleting the addition on account of cash credits. Similar view is taken in *CIT vs. K.S.M. Guruswamy Nadar & Sons (1984) 149 ITR 127 (Mad); CIT vs. Jawanmal Gemaji Gandhi 151 ITR 353 (Bom).* However, again this is not a proposition of law and therefore it is for the assessee to show that the credits represents / is covered from the intangible additions so made. In *Kale Khan Mohammad Hanif vs. CIT (1963) 50 ITR 1 (SC)* it was held that there is nothing in law which prevents the Assessing Officer in an appropriate case in taxing both the cash credit, the source and nature of which is not satisfactorily explained, and the business income estimated by him after rejecting the books of account of the assessee as unreliable.

8. Partner & Firm

Section 68 of the Act provides for charging to tax the sum of amount in the hands of the assessee in whose books of account the amount is credited on the failure of the assessee to explain the source and nature of the credit. This would thus mean that the credit in the firm's books should be explained by the firm and that in the absence of a satisfactory explanation, it is the firm, which should be liable to tax – *Shanta Devi vs. CIT (1988) 171 ITR 532 (P&H).* However, there could be exception to such cases for example where the funds clearly emanate from the partners and the same is proved beyond doubt, in such cases, the burden of proof and assessability would be considered only in the hands of the partners. In *CIT vs. Jaiswal Motor Finance (1983) 141 ITR 706 (All)* it was held that where the cash advance from the partner is proved it could not be assessed in the hands of the firm. Similarly, in *CIT vs. Taj Borewells (2007) 291 ITR 232 (Mad)* it was held that once the firm has offered an explanation and established that the capital was contributed by the partners, the same could not be assessable in the hands of the firm unless there are contradictions and inconsistencies in the statement of the partners. In *CIT vs. Metal and Metals of India (2007) 208 CTR 457 (P&H)* it was held that where the credit in question belonged to partner who allegedly made it out of gift received from NRI, even if claim of gift received by partner was not accepted, addition was justified in the hands of partner and not in hands of assessee firm.

Other such instance would be a case where the partners introduce capital in the firm on the very first day of the firm coming into existence and in such a case, the cash credits could not be treated as income of the firm since the credits appeared in the books even before the firm had started its business – *India Rice Mills vs. CIT (1996) 218 ITR 508 (All); Surendra Mohan Sheth vs. CIT (1996) 221 ITR 239 (All);* contrary view taken in *CIT vs. Anupam Udyog (1983) 142 ITR 133 (Pat).* After elaborate review of the earlier case laws, it was decided in *Jagmohan Ram Ram Chandra vs. CIT (2005) 274 ITR 405 (All)* that there is no hard and fast rule that such amounts have to be added only in partner's cases or that it is liable to be taxed only in the firm's case. The inference will depend upon the facts of each case. It could not be the income of both the firm and partners.

9. Share Application money

Proviso is inserted to sec. 68 of the Act effective from AY 2013-14 whereby in case of a closely held company, any amount credited in books of account of the company towards share application money, share capital, share premium or any such amount, the AO may reject explanation unless that the person, being resident, in whose name the credit is recorded, also offers explanation about the nature and source of such sum credited. In other words, if any share application money or share capital or share premium or any such amount is credited in the name of any resident person, then source of source is also required to be explained for discharging the onus cast u/s. 68 of the Act. However, this source of source explanation is applicable only if the amount towards share application, etc., is received from resident person. Hence, if case of other than resident person, only the main provision of sec. 68 applies.

Prior to the insertion of proviso to sec. 68 of the Act, there are numerous decisions [– both favourable and contrary] – depending upon facts of each case, wherein sec. 68 of the Act is made applicable. In the latest decisions of the Bombay High Court in *CIT vs. M/s. Gagandeep Infrastructure P. Ltd. (Bom) 394 ITR 680,* it is held relying upon the decision of Hon'ble Supreme Court in *CIT vs. M/s. Lovely Exports (P) Ltd. 317 ITR 218 (SC)* that where the Revenue urges that the amount of share application money has been received from bogus shareholders then it is for the Income Tax Officer to proceed by reopening the assessment of such shareholders and assessing them to tax in accordance with law. It does not entitle the Revenue to add the same to the assessee's income as unexplained cash credit (para e). In the context of proving the source of source of the investment made by the subscribers, the Bombay High Court held that the amendment brought out by the FA 2012 w.e.f. AY 2013-14 is prospective and not retrospective. Similar view is taken in *CIT vs. Orchid Industries P. Ltd. 396 ITR 136 (Bom).*

Conclusion

Application of the provisions of section 68 of the Act would basically depend on the facts of each and every case. It is said that 'you take care of your facts and the law will take care of you' appropriately fits in cases of applicability of section 68 of the Act. The deeming provisions have become very stringent in recent past whereby the rate of tax is levied u/s. 115BBE of the Act, which at present is 60% of the amount added under deeming provision and no set off of loss is also allowed.

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> Truth can be stated in a thousand different ways, yet each one can be true.
>
> — *Swami Vivekananda*

Dharan V. Gandhi, *Advocate*

Implications of Provisos to Section 68

Introduction

The most effective and lethal weapon used by the Income-tax Department ('Department') against evasive tactics used by the assessees, to convert their unaccounted money to accounted one, is section 68 of the Income-tax Act, 1961 ('Act'). However, sometimes the same weapon is also used by them as a tool to ensure achievement of their internal targets.

Applicability of section 68 of the Act on share capital, share premium and share application money has become a very contentious issue these days, since the Department has issued many notices in past few years questioning the source of share capital. In this article, we shall be dealing with the impact of the new provisos to section 68 of the Act.

Background of section 68

Section 68 does not need any introduction. To summarise, it taxes any credit appearing in the books of an assessee, where the assessee is not able to or not satisfactorily able to explain the nature and source of such credit. It is a deeming fiction, which taxes a credit as income on unsatisfactory explanation about nature and source thereof and such fiction is applicable whether or not the credit is otherwise income chargeable to tax or not.

Initial onus is on the assessee to demonstrate the "nature and source" of the credit and when the same is discharged, the burden shifts onto the Department to prove that the credit is income chargeable to tax. Many judgments have held that the term "explain the nature and source of a sum found credited" would require an assessee to explain three things (ingredients) viz. (a) Identity of the creditor (b) capacity of the creditor to advance money and (c) genuineness of the transaction.

Also, various courts have held that, there is no need to explain the source of source or origin of origin[1].

Position in respect of share capital, share application etc. prior to 1-4-2012

The term 'any sum found credited' also takes under its sweep any sum credited as share capital, share premium or share application

1 49 ITR 723 (Bom.) Orient Trading Co. Ltd. vs. CIT; 59 ITR 632 (Ass) Tolara Daga vs. CIT

money or any such amount by whatever name called[2].

In so far as the burden of proof in respect of such credit is concerned, there are divergent views. The Hon'ble Supreme Court in case of *CIT vs. Lovely Exports P. Ltd.*[3], has held that *'if the share application money is received by the assessee company from alleged bogus shareholders, whose names are given to the AO, then the Department is free to proceed to reopen their individual assessments in accordance with law.'* Thus, the said judgment has reduced the rigours of section 68 insofar as, share capital etc. is concerned, in as much as, the Court has held that the onus is discharged on giving names and PAN of the investor. It further held that, if at all, the Department would like to assess any income, the same can be done in the hands of the investor. Thus, it can be deduced that, unlike other credits, wherein one has to explain three ingredients as stated above, the onus on the assessee company is limited while explaining share capital etc.

Following the said judgment, many courts[4] had earlier taken a view that where the identity has been established and PAN has been furnished, no addition can be made u/s. 68 of the Act and that the Department can take necessary action against the investors.

However, many courts have of late, deviated from the said ratio. From the judgments[5] referred to in footnote, it can be seen that the Delhi High Court and the Calcutta High Court have distinguished the judgment in case of Lovely Exports. They have distinguished mainly on the factual matrix of the said case and the case before them. Though, some courts[6], are still following the said judgment of the Apex Court.

In light of the various judgments which have come of late, one may say that the ratio of the judgment of the Apex Court in case of Lovely Exports (supra) has been diluted to a long extent. In fact, even the assessees are making a point to demonstrate the three ingredients even in case of credit in the nature of share capital etc. instead of merely submitting the name and PAN. Nonetheless, there still does not exist any requirement to explain the source of source or origin of origin in case of credit in the nature of share capital etc.

Position after 31-3-2012

By Finance Act, 2012, substantial amendments have been brought in section 68 of the Act by way of insertion of first and second proviso to section 68, as a result of which, additional burden has been saddled upon the assessees to prove the nature and source of share capital, share application money, share premium or any such sum by whatever name called.

First proviso to section 68 requires the shareholders or the person in whose name the credit appears, being a resident, to satisfactorily explain the nature and source of such sum so credited. Thus, by inserting the said proviso, additional onus of explaining the source of source has been laid down. Second proviso to section 68 provides for certain exceptions from application of first proviso.

The Explanatory Memorandum to the Finance Bill, 2012, specified the following reason for the proposed amendment, which is self-explanatory:

2 205 ITR 98 (Del.) Sophia Finance Ltd; 263 ITR 300 (Cal.) CIT vs. Ruby Traders and Exporters Ltd.; 299 ITR 268 (Del.) - CIT vs. Divine leasing and Finance Pvt. Ltd.

3 216 CTR 195(SC)

4 196 Taxman 441 (Del.) CIT vs. Siri Ram Syal Hydro Power (P) Ltd.; 325 ITR 25(P&H) CIT vs. GP International Ltd.; 330 ITR 298 (Del.) CIT vs. Dwarkadhish Investment (P) Ltd.; 333 ITR 100 (Bom.) CIT vs. Creative World Telefilms Ltd.

5 350 ITR 407 (Del.) CIT vs. Nipun Builders and Developers P. Ltd.; 342 ITR 169 (Del.) CIT vs. Nova Promoters and Finlease (P) Ltd.; 333 ITR 119 (Del.) CIT vs. Oasis Hospitalities Pvt. Ltd.; 386 ITR 162 (Cal.). Rajmandir Estates Private Limited vs. PCIT

6 403 ITR 415 (Bom.) PCIT vs. Veedhata Tower Pvt. Ltd.; 397 ITR 148 (Bom.) PCIT vs. Apeak Infotech; 394 ITR 680 (Bom.) CIT vs. Gagandeep Infrastructure (P.) Ltd.

"In the case of closely held companies, investments are made by known persons. Therefore, a higher onus is required to be placed on such companies besides the general onus to establish identity and credit worthiness of creditor and genuineness of transaction. This additional onus, needs to be placed on such companies to also prove the source of money in the hands of such shareholder or persons making payment towards issue of shares before such sum is accepted as genuine credit."

Having the requisite background of introduction of the provisos, we may now deal in detail with the impact of the said provisos.

Prospective/ retrospective

Firstly, the first proviso is held by numerous decisions of the Bombay High Court[7] to be prospective in nature and applicable w.e.f. AY 2013-14. Even the Delhi High Court[8] has held that the said proviso would not apply to AY 2004-05, thereby impliedly negating the retrospective application. Though, the Kolkata Bench of the ITAT in the case of *Subhlakshmi Vanijya (P.) Ltd. vs. CIT*[9], has held the proviso to be retrospective in nature, the Calcutta High Court[10] has refused to go into the issue of retrospectivity. Thus, in so far as retrospective application of the first proviso is concerned, the High Courts are in favour of prospectivity and therefore, would prevail over the ITAT judgment.

Onus under main section still subsists

The applicability of proviso would not mean that the onus laid down in the main part of section 68 has been done away with. The assessee company would have to explain the nature and source of the credit in its books of account which would require satisfaction of the three ingredients viz., identity, genuineness and creditworthiness. Only if the AO is satisfied with the same, he would go further to the proviso and would want himself to be satisfied on the additional burden as well.

Company in which public are not substantially interested

The proviso is applicable only to companies in which public are not substantially interested. Section 2(18) defines companies in which public are substantially interested. Barring those companies, these provisos would apply to all companies. All private companies would come within the net of the provisos. Even the explanatory memorandum, as brought out above, stated that in case of closely held companies, the investors, generally are known parties and therefore, the additional burden.

Credit in the nature of share capital, share premium etc.

These provisos are applicable only in respect of credit in the nature of share capital, share application money or share premium or any such sum by whatever name called. Any other credits like unsecured loans would not be subject to this additional burden. Share capital would also include preference share capital, as there is no express exclusion for preference share capital or premium on preference share capital. Further, it would also include share warrants. Debentures should be outside the ambit of the proviso whether convertible or not, though one may argue that compulsory convertible debentures are nothing but share capital only and therefore, should be covered by the residuary part of the proviso.

Who should provide the additional information of source of source?

The additional burden imposed by the proviso is that the shareholder or the person in whose name such credit stands in the books of the company, has to offer an explanation about the nature and source of such sum. Would this require only the investor to reply directly to the

7 394 ITR 680 (Bom.) CIT vs. Gagandeep Infrastructure (P.) Ltd; 397 ITR 148 (Bom.) PCIT vs. Apeak Infotech Ltd.; 403 ITR 415 (Bom.) PCIT vs. Veedhata Tower Pvt. Ltd.

8 375 ITR 0373 (Del.) CIT vs. Jansampark Advertising and Marketing (P) Ltd.

9 155 ITD 171

10 386 ITR 162 (Cal.). Rajmandir Estates Private Limited vs. PCIT; 393 ITR 0037 (Cal.) Success Tours and Travels Pvt. Ltd. and Anr. vs. ITO

AO or would the explanation tendered on behalf of such investor by the company would suffice? The purposive construction of the proviso would suggest that the AO has to be satisfied with the source of the investor, whether the same is furnished by the investor himself or by the assessee company.

Another angle to the above-mentioned issue is that what if the investor refuses to divulge the information to the assessee directly. Can the assessee company state that the investors are not replying to them or not divulging their confidential details to them and that the AO should use his powers u/s. 131(1) or 133(6) of the Act to get the information directly from the shareholders? Technically speaking, the onus is on the assessee to explain the nature and source of the investor and therefore, on non-compliance of the same, the AO can make the addition. The purpose behind insertion, as given in the explanatory memorandum, was the very fact that in case of closely held companies, investors are known persons and therefore, higher burden is placed. However, it is also true that the AO cannot merely wash off his hands on the incapability of the assessee to establish the source of source, in spite of making the requisite efforts. Sometimes *bona fide* difficulties may crop up like relationship going kaput. Earlier also, when a person was required to establish the creditworthiness of a party, which would mostly require furnishing of return of income and balance sheet of the party, the Courts have taken a view that when a person informs about his incapability to produce the requisite documents, he can request the AO to directly make inquiries, and no addition can be sustained when the AO does nothing[11]. Same rationale may be applied here, subject to the fact that the same is not made the norm and is used as an exception on showing *bona fide* cause.

In case, if the AO issues summons to the investors to explain the nature and source of their investment and if the investors fail to reply, then the AO would not be required to wait for anything and can straightaway make the addition u/s. 68 of the Act. This is because, the first proviso clearly states that additional burden if not fulfilled then the explanation of the assessee would be deemed to be not satisfactory.

Resident investor

This additional burden would apply only in case where the investor is a resident person. Thus, where share capital is introduced by residents as well as non-residents, the company would be required to demonstrate the identity, genuineness and creditworthiness in case of non-resident shareholders whereas it would be required to demonstrate the nature and source of the investor also, in case of resident shareholders. The term 'resident' has not been defined in the section and therefore, it should take meaning from section 6 of the Act. This may lead to another controversy. There may be dispute about the residential status of the investor and the Company may be required to demonstrate that the investor is non-resident, in case the company claims so. Such dispute may also stretch to the extent of determination of POEM. Of course, the assessment of such investor as non-resident, if available, would put the matter to rest.

Nature and source of such credit

The additional burden is to explain the 'nature and source' of such sum by the investor. Source would mean the source of investment of the investor. The investor would be required to demonstrate the money available with him from where the investment is made and nature of such money which may be a sale receipt in normal course of business, other revenue receipts, loans or share capital received by such investor. This may necessitate the production of the bank statement of the investor to show availability of the funds and the relevant part of the books of such investor along with any documentary evidence which shows the

11 366 ITR 232(P&H) CIT vs. Varinder Rawlley; 54 SOT 141(Del)(UO) Chiranjiv Charitable Trust vs. DCIT

nature of such available funds like the sale invoice, or share allotment details as well as the confirmation from the party wherefrom the investor received funds for further investment.

In so far as the requirement to explain the 'nature of such sum' is concerned, the same seems repetitive. 'Nature' as defined in Merriam Webster dictionary means 'the inherent character or basic constitution of a person or thing'. Thus, the investor is required to explain the character of the sum credited in the books of the company which would be nothing but investment in the form of share capital, share allotment or share premium etc. This would already be explained by the assessee company and in all probability, same explanation would be tendered by the investor to show the nature of such sum. Ideally, therefore, no addition can be made for not explaining the nature of such sum by the investor.

Another interpretation of the term 'nature and source' is by taking a cue from the same term used in main part of section 68. The said term is used in the main section as well as in the first proviso. The courts have interpreted the term 'nature and source' as appearing in the main part of section 68, to mean three ingredients viz. identity, genuineness and creditworthiness. The Department can seek to apply the same logic while interpreting the term 'nature and source' in the first proviso. However, the distinction in the main section and in the proviso is that, while the main section requires to explain the nature and source of a <u>credit</u> in the books of the recipient, first proviso requires a person to explain the nature and source of an <u>investment</u>. Accordingly, if we apply the three ingredients test for the first proviso, then identity would be of the recipient company, which would already be available with the AO. Further, genuineness of the investment transaction would already be explained by the Company. All that is required to be explained would be the creditworthiness of the investor to invest. Such explanation about the creditworthiness would include the explanation about the source as already explained in the earlier para.

If we take an example: if the source of the investment in share capital etc., is loan from a party, then the investor can demonstrate that the investment was in the nature of share capital of the company. Further, he would furnish his bank statement to show that the investment is through banking channel and that funds were available at the time of making the investment. He would then be required to explain the source of such investment which would be loan from a third party. He may bring the confirmation from the said party and relevant extract of his books to show the loan transaction. This would be sufficient to discharge the requirements of first proviso. Can the AO ask the investor to demonstrate the identity, genuineness and creditworthiness of such lender? He cannot ask, as the investor is not required to explain the 'nature and source' of the source but nature and source of the investment. The AO cannot go a step further to require the investor to explain the source of his source, though nothing stops him from making his independent inquiry about the source of the investor's source.

Quantum of premium and section 56(2)(viib)

Can the AO say that the 'nature' of the investment as given under first proviso to section 68 would require an investor to explain the quantum of premium charged? Quantum of premium is something which the parties have to decide mutually, amongst themselves. It is not a subject matter of scrutiny, in so far as section 68 is concerned. The Courts[12] have held that the revenue should not justifiably claim to put itself in the armchair of a businessman or in the position of the Board of Directors and assume the role of ascertaining how much is a reasonable premium having regard to the circumstances of the case.

In this regard, it would be pertinent to understand section 56(2)(viib), which was

12 98 taxmann.com 47 (MP) PCIT vs. Chain House International (P.) Ltd; 62 taxmann.com 192 (Del.) CIT vs. Anshika Consultants (P.) Ltd.; 392 ITR 7 (Bom.) CIT vs. Green Infra Ltd.

introduced to tackle such type of cases (inserted by the same Finance Act, 2012). This section taxes excess of premium over the fair market value of the shares issued (such fair market value has to be computed in accordance with the rules prescribed). Thus, section 56(2)(viib) is a deeming fiction and a step ahead of section 68 as it directly taxes the excess of share premium over the fair market value, without waiting for any explanation from the company; whereas section 68 taxes the amount of share capital or premium where the genuineness and source is not explained satisfactorily. Further, section 56(2)(viib) cannot tax the basic amount of share capital, which can be taxed u/s. 68 on fulfilment of the conditions. Thus, both the sections operate in different fields and have different conditions to be fulfilled, merely because requirement of the one of the section is fulfilled one cannot say that the transaction is free from the other section also.

Explanation has to be satisfactory
First proviso does not merely require an explanation about the source and nature from the investor but it also requires that such explanation should be satisfactory in the opinion of the AO.

In case the AO of the company is not satisfied with the explanation of the investor about the source of his investment, but he is satisfied with the explanation of the company regarding the three ingredients, can the company ask the AO to make addition in the hands of the investor and not in its hands? In the below noted case[13], the ITAT had held that where the AO had suspicion about the source of source, then same could be added in the source's assessments by reopening the same but same could not be assessed in hand of assessee. However, it may be difficult to apply the same logic here. This is because, the purpose behind insertion of the first proviso, makes it clear that if the source of the investor is not explained then it shall be deemed that explanation of the assessee company is not satisfactory and consequently, would lead to addition in the hands of the company.

The next issue here would be, can the same information be used by the AO of the investor to make addition in his hands? No addition can be made in the hands of the investor, if addition is/has been made in the hands of the company, since section 68 presumes that such unexplained credit is nothing but the unaccounted money belonging to the company, though nowhere such presumption is coming in black and white. Also, there is no section under which such investment recorded in the books can be added on unsatisfactory explanation of the source.

Not applicable to venture capital company etc.
Apart from the inherent exclusions like company in which public are substantially interested or non-resident investors, a specific exclusion is provided in the second proviso to section 68 which states that the first proviso is not applicable in case of investor being venture capital fund or venture capital company referred to in section 10(23FB) of the Act. The reasoning behind their exclusion is because such entities are well regulated and registered with SEBI.

The above section would also have certain implications under the Benami Transaction Prohibition Act, 1988. The same is covered elsewhere.

Conclusion
The Legislature introduced a slew of measures *vide* Finance Act, 2012, to tackle the menace of unaccounted money being made accounted one by way of share capital etc. The proviso in question, is a very strong measure wherein a company is required to even explain the source of the investor, which presupposes the fact that the company would be able to get those evidences easily as the investor would be a known party. Further, now, after the amendment of section 115BBE of the Act, the amount, if any, added u/s. 68 is subject to very exorbitant rate of tax viz., 60%. This makes the first proviso to section 68 more tyrannical especially, when the same is abused for achieving internal targets, as stated earlier.

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13 35 ITR (Trib.) 71 (Chan.) Jawahar Lal vs. ITO

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Benefit of Telescoping

This article deals with the theory of telescoping as applied in the Income-tax Law, the manner of its application and as to how and under what circumstances the benefit of telescoping could be claimed / availed by an assessee. Though the said theory has general applicability across the taxability of a wide range of items, usually the items of income on which the said theory is applied are those covered by sections 68 to 69D of the Income-tax Act, 1961 ["the Act" for short]. The said theory is also applied in cases where block assessments are framed.

1. Brief background of Telescoping

'Telescoping', is a word extensively used but scarcely defined under the Income-tax Law. No specific definition has been accorded to the term 'telescoping' either under the Income-tax Act, 1961 ["the Act"] or even the Judicial Law. So, what is 'telescoping' or what is the Theory of Telescoping as used in the Income-tax Law? In simple words and as applied in the tax law, telescoping means identifying an income and its application, so that ultimately tax is levied either only on the income or only on its application. In other words, in case where an assessee has certain undisclosed income and also certain undisclosed investments, then it could be reasonably presumed that the undisclosed investments have been sourced out of the undisclosed income, so that only the income may be taxed or only the investment may be taxed and not both, in the hands of the assessee under the provisions of the Act. The said theory which is judicially accepted[1] is in effect, a theory of probability or inference[2] which is applied in order to avoid taxing the same income twice – once on earning and then on utilizing / expending it. The theory of telescoping is applied keeping in view the well-established canon of taxation that the same income cannot be taxed twice.

2. Manner of application of the theory of telescoping

The theory of telescoping has been applied in the Tax Law ever since the Income-tax Act, 1922 was in operation. There are various judgments of the

1 Anantharam Veerasinghaiah & Co. vs. CIT – (1980) 123 ITR 457 (SC),

2 CIT vs. S. Nelliappan – (1967) 66 ITR 722 (SC)

Hon'ble Supreme Court and the various Hon'ble High Courts who have applied the theory of telescoping in dealing with income tax issues before them. The entire theory of telescoping rests on certain well accepted, fundamental principles of taxation that the same income cannot be taxed twice in the hands of the same person[3] or the income taxed in one year be not taxed in another year[4] or the same cannot be taxed under two different heads[5]. A brief look through on the manner of application of the theory of telescoping is discussed in the succeeding paragraphs.

(a) Peak Credit Theory

The most widely used and applied theory of telescoping is the theory of peak credit. The theory of peak credit has been aptly explained in the Commentary on Income Tax titled the Law of Income Tax which has been relied on by the Hon'ble Allahabad High Court[6]. It has been succinctly explained in the said Commentary that where a single credit or number of credits appear in the books of account of any particular person side by side with a number of debits, they should all be arranged in serial order; that a credit following a debit entry should be treated as referable to the latter to the extent possible and not the aggregate but only the "peak" of the credit should be treated as own for the purpose of tax. This is a generally accepted position as it is logical and acceptable (whether the creditor is a genuine party or not), provided there is nothing in the material on record to show that a particular withdrawal/repayment could not have been available on the date of the subsequent credit. The said theory may apply even where the credits are not appearing in the name of the same person but also in the names of other persons. However, this is only an inference and not a proposition of law and could very well be displaced by producing any evidence or material on record that the said withdrawals were not available for subsequent re-deposit. The theory of peak credit has been applied in various judgements[7]. However, it needs to be mentioned that the said theory could be applied only when the assessee owns all the credits and the factual foundation for the application of the said theory has to be laid by him, as held by various judicial precedents[8].

(b) Income taxed in earlier year telescoped to subsequent year

As stated earlier, another aspect of the theory of telescoping is whereby an income is taxed / addition is made to taxable income in an earlier year. In such cases, the assessee may claim that the income arising in subsequent year / subsequent period is sourced out of the income taxed earlier. It has been held by the Hon'ble High Court in the case of *Addl. CIT vs. Dharamdas Agarwal*[9], it was held if in a subsequent year cash credits are sought to be treated as income from undisclosed sources, the assessee can take alternative contention that the cash credits were out of undisclosed income taxed in earlier years and the assessee is entitled to raise such alternative plea for the first time even before the Appellate Assistant Commissioner. Similar proposition has been upheld by the Hon'ble High Court in the case of *CIT vs. Tyaryamal Balchand*[10] where again it was held that where the assessee was taxed

3 Bachulal Kapoor – (1966) 60ITR 74 (SC), Laxmipat Singhania – (1969) 71 ITR 291 (SC)

4 CIT vs. Ramshankar – 45 Taxman 282

5 CIT vs. Surat Cotton and Spinning – (1993) 202 ITR 932 (Bom.)

6 CIT vs. Fertlizer Traders – (2014) 222 Taxman 162 (Allahabad) (Mag.) reproducing from Law of Income Tax by A. C. Sampath Iyengar

7 CIT vs. Purushottam Jhawar, Fertlizer Traders (supra), et al.

8 Bhaiyalal Shyam Bihari vs. CIT - (2005) 276 ITR 38 (All.), CIT vs. Vijay Agricultural Industries – (2007) 294 ITR 610, CIT vs. D K Garg- ITA 115 of 2005 Delhi High Court

9 CIT vs. Dharamdas Agarwal – (1983) 144 ITR 143 (MP)

10 CIT vs. Tyaryamal Balchand – (1987) 165 ITR 453 (Raj)

on substantial undisclosed income in the past years, the same could be treated as income available with the assessee and an addition as undisclosed income in the subsequent year could be telescoped in the undisclosed income taxed earlier. Interestingly, in one of the cases the Hon'ble High Court[11] has gone a step further and held that even peak credit taxed in the earlier year is available for telescoping against peak credit worked out in the subsequent year and therefore not taxable. In fact, quite somewhat similar view is expressed by the Central Board of Direct Taxes ["the CBDT" for short] itself on income disclosed and declared under the Income Disclosure Scheme of 2016 in its Circular No. 29 of 2016 dated 18-8-2016.

(c) One type of income already taxed could be telescoped into another

In certain cases[12], it has been held that when two separate additions are made, one on account of suppression of profit and another on account of cash credit, it is open to the assessee to explain that the suppressed profits had been brought in as cash credits and one has to be telescoped into the other resulting only in one addition. In fact in one of the cases[13] it has been held that when the Revenue Authority levied a huge tax on the company on the basis that the books of the assessee company were unreliable and that the bulk of the company's profits had been kept outside its books as secret profits, then, those secret profits less the income-tax paid would be available with the company for distribution as dividends. Once the secret profits had been assessed to tax, it would have been open to the company to bring those profits into the books and distribute them, or what remained after payment of tax, as dividends. In yet another case[14], the Hon'ble Supreme Court held that even in the absence of direct evidence of any connection between the cash credit entries and the income withheld from the books of account by the assessees if the Tribunal inferred that there was a connection between the profits withheld from the books and the cash credit entries, then the said conclusion must be upheld and it cannot be said that the conclusion is based upon speculation.

(d) Telescoping – Income to investment and income to expenditure

The theory of telescoping could also be applied in cases where additions in respect of unexplained money / unexplained investment are sought to be made in the hands of the assessee. For example, if there is an addition in respect of undisclosed income or unexplained cash credits and also certain addition in respect of unexplained investments, then it could very well be pleaded by the assessee that the unexplained investment is sourced out of the income already taxed as unexplained cash credits[15]. Likewise, it has been held[16] that where an addition in respect of undisclosed income is made, the assessee could very well plead that there should be no separate addition in respect of unexplained expenditure from the said income since it would amount to double taxation.

(e) Can income of one person be telescoped in the hands of another ?

Another important facet of the theory of telescoping is whether when income is disclosed or taxed in the hands of one person, could another person claim a set-off of the said income against his / its undisclosed income. In this regard, there are a few judicial precedents wherein it has been held that when the search operation was carried out on a group as a whole, income taxed in the hands of one person of the group could be telescoped and set-off against income from another person

11 CIT vs. Sharraf Trading – (2015) 376 ITR 534 (Allahabad)

12 CIT v. K.S.M. Guruswamy Nadar & Sons – (1984) 149 ITR 127 (Mad.)

13 Lagadapati Subba Ramaiah vs. CIT – (1956) 30 ITR 593 (AP)

14 CIT vs. S. Nelliappan (supra)

15 CIT vs. Jawanmal Gemaji Gandhi – (1983) 15 Taxman 487 (Bom.)

16 CIT vs. Golani Brothers – (2018) 300 CTR 245 (Bombay)

in the same group. It has been held by the ITAT in one of the cases[17] that where the manager of the assessee, an educational society, was in a position to collect money from students who were admitted in assessee's college and he used his position to collect amount in excess of prescribed fee from students and while passing assessment order same was treated as undisclosed income in his hands, the said unaccounted receipts could not again be taxed in hands of the assessee as well. Again, while granting the benefit of telescoping in the hands of the partner in respect of amounts offered and taxed in the hands of the firm, the Tribunal[18] held that once an estimated addition on account of household expenses, investment in land, investment on foreign travel are being made and the source of such expenditure is stated to be flowing from the firm which has suffered tax as undisclosed income, then, telescopic benefit should be given to the total amount flowing from the firm as a share of profit coming to the assessee from the firm. In effect, it was held by the Tribunal that the quantum of the amounts available for the benefit of telescoping should not be restricted only to the specific amounts disclosed by the assessee as unexplained expenditure, etc., but the entire share of profits which would have been available to the assessee as a partner of the firm which has already suffered tax on its undisclosed profits. In view of the above precedents, it is quite clear that it is possible to claim the benefit of telescoping in respect of undisclosed income offered by one person in the hands of another person.

III. Power / discretion of the appellate authorities to allow telescoping in cases where some connection can be inferred

The Hon'ble High Court has held[19] that an assessee is entitled to raise an alternative plea of non-taxability of certain income on the ground of telescoping for the first time even before the First Appellate Authority. In fact, in a case[20] before the Hon'ble Supreme Court, the ground relating to telescoping of additions was urged only in the second round of proceedings before the Tribunal. Revenue's contention before the Hon'ble Supreme Court was that the Tribunal was not competent to allow the assessee's appeal on a ground not raised in the memorandum of appeal. The said contention was rejected by the Hon'ble Supreme Court.

The above article merely summarises the various facets of the benefits of telescoping which are by no means exhaustive. However, I believe the above article would help the readers in taking an appropriate decision considering the utility of the theory of telescoping in determining the taxability of undisclosed income. Since the applicability of the theory of telescoping is vitally dependent on the fair and correct exercise of discretion by various authorities I would like to conclude this article with the following words of the Hon'ble Chief Justice of India, Shri H. R. Khanna (as he then was) in the case of *CIT vs. Simon Carves Ltd.*[21] *"The taxing authorities exercise quasi-judicial powers and in doing so they must act in a fair and not a partisan manner. Although it is part of their duty to ensure that no tax which is legitimately due from an assessee should remain unrecovered, they must also at the same time not act in a manner as might indicate that scales are weighted against the assessee. We are wholly unable to subscribe to the view that unless those authorities exercise the power in a manner most beneficial to the revenue and consequently most adverse to the assessee, they should be deemed not to have exercised it in a proper and judicious manner.*

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17 J. B. Education Society vs. ACIT – (2013) 28 ITR (Trib) 284 (Hyderabad)

18 Rajni M. Patel vs. DCIT – (2015) 43 ITR (Trib) 628 (Ahemedabad)

19 Addl. CIT vs. Dharamdas Agarwal – (1983) 144 ITR 143 (MP)

20 CIT vs. S. Nelliappan – (1967) 66 ITR 722 (SC)

21 CIT vs. Simon Carves Ltd. – (1976) 105 ITR 212 (SC)

CA Vinay Kawdia

Sections 69, 69A & 69B - Unexplained Investments, Money etc.

Introduction

Chapter VI of the Income-tax Act, 1961 ("the Act") titled "Aggregation of Income" *inter alia* covers sections 68, 69, 69A, 69B, 69C and 69D. Sections 69, 69A and 69B deal with charging to income-tax on "deemed" basis –

Section 69 – Unexplained Investments: Amount of investments made by the assessee, which are not recorded in the books of account, and source whereof is not satisfactorily explained.

Section 69A – Unexplained Money: Money and the value of the bullion, jewellery or other valuable article of which assessee is found to be the owner and which is not recorded in his/her books of account and the assessee offers no explanation about the nature and source of such money, bullion, jewellery or other valuable article or the explanation offered by the assessee is not in the opinion of the AO satisfactory.

Section 69B - Amount of investments, etc., not fully disclosed in books of account: Amount of investments, bullion, jewellery or other valuable article not fully recorded in the books of account.

Section 69 – Unexplained Investments

Where in the financial year immediately preceding the assessment year the assessee has made investments which are not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of the investments or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the value of the investments may be deemed to be the income of the assessee of such financial year.

Ingredients of S. 69

Conditions precedent referred to in section 69 that must be satisfied before its application are:

i) Investment must have been made **<u>in</u>** the financial year relevant to assessment year in question;

ii) Investment must not have been recorded in the books of account, if any; ***<u>and</u>***

iii) Assessee offers no explanation about the nature and source of the investments or the explanation offered by him is not satisfactory.

Upon all the above conditions being cumulatively satisfied, the value of investments may be deemed to be the income of the assessee of such previous year.

The initial burden of proving the nature or source of investment not recorded in the books of account is on the assessee, which the assessee must discharge by providing a credible explanation. However, it is for the revenue to establish first that the said investments have actually been made. *[Pirani vs. ACIT 250 ITR 467, Vasanthi vs. ACIT 257 ITR 94, Surendra Khandhar vs. ACIT 321 ITR 254 (Bom.) Jagjit Pal Singh Anand vs. CIT 320 ITR 106 (Del.), Etc.]*

Section 69A – Unexplained Money etc.

Where in any financial year the assessee is found to be the owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or valuable article is not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the money and the value of the bullion, jewellery or other valuable article may be deemed to be the income of the assessee for such financial year.

Ingredients of S. 69A

i) in the financial year immediately preceding the assessment year (i.e. previous year) the assessee is found to be the owner of any money, bullion, jewellery or other valuable article

ii) such money, bullion, jewellery or other valuable article is not recorded in the books of account, if any, maintained by the assessee

iii) assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article; OR the explanation offered by the assessee is not, in the opinion of the AO, satisfactory,

Upon all the abovementioned conditions being cumulatively satisfied, the money and the value of the bullion jewellery or other valuable article may be deemed to be the income of the assessee for such previous year.

Once a person is found in possession, custody and control of money, bullion or other valuable article or thing, burden to prove that he is not the owner shifts on him. If he fails to give satisfactory explanation and discharge the burden, value can be added as income under section 69A of the Act.

The *Madhya Pradesh High Court in Chuhadmal Takanmal vs. CIT [1987] 166 ITR 12* held that in view of provisions of section 110 of the Evidence Act, since the assessee was found in the possession of the watches he was presumed to be the owner of them until the ownership of some other person was proved. [This view stands affirmed by the Supreme Court in *Chuhadmal Takanmal vs. CIT, 38 Taxman 19 (SC).*]

Section 69B – Amount of investments, etc., not fully disclosed in books of account

Where in any financial year the assessee has made investments or is found to be the owner of any bullion, jewellery or other valuable article, and the AO finds that the amount expended on making such investments or in acquiring such bullion, jewellery or other valuable article exceeds the amount recorded in this behalf in the books of account maintained by the assessee for any source of income, and the assessee offers no explanation about such excess amount or the explanation offered by him is not, in the opinion of the AO, satisfactory, the excess amount may be deemed to be the income of the assessee for such financial year.

Ingredients of section 69B

i) the assessee maintains books of account

ii) in the financial year – the assessee has made investments OR the assessee is found to be the owner of any bullion, jewellery or other valuable article

iii) the AO finds that the amount expended – on making such investment OR in acquiring such bullion, jewellery or other valuable article exceeds the amount recorded in this behalf in the books of account; and

iv) the assessee offers no explanation about such excess OR the explanation offered by him is not, in the opinion of the AO, satisfactory.

Upon satisfaction of all the abovementioned conditions, the excess amount may be deemed to be the income of the assessee for such financial year.

The burden to prove that real investment exceeds the investments shown in the books of account of the assessee is on the department and no addition can be made under this section merely on the basis of fair market value. This section is not applicable if there is no evidence of understatement of purchase price. *[Amar Kumari vs. CIT 226 ITR 344, CIT vs. Naresh 261 ITR 664, CIT vs. Dinesh Jain (HUF) 352 ITR 629, CIT vs. Sadhna Gupta 352 ITR 595].*

Addition u/s. 69/69B solely on the basis report of the departmental valuation officer/stamp valuation rates is not justifiable unless positive evidence for understatement is there. *[CIT vs. Shakuntala Devi 224 CTR 79 (Delhi), etc.]*

General Principles

– As per the scheme of S. 69, S. 69A, etc. before any action can be taken pursuant to the said sections the relevant condition precedent referred to in such section has to be first complied with. *[J. S. Parkar vs. V.B. Palekar [94 ITR 616 (Bom.)]*

– Even if presumption u/s. 132(4A) is raised against the assessee, the ingredients by way of prerequisite conditions of section 69 have to be satisfied and cannot be presumed to have been established on the basis of section 132(4A) of the Act simpliciter. *[Ushakant N. Patel vs. CIT [2006] 282 ITR 553 (Guj.)].*

– Merely because the assessee's explanation regarding certain investments made by his wife and sons is not acceptable, the revenue cannot treat the investments as the undisclosed income of the assessee. The revenue should bring on record material from which it could be concluded that the investments were in fact made by the assessee. If this was not done, no amount could be added as the undisclosed income of the assessee. *[CIT vs. Daya Chand Jain Vaidya [1975] 98 ITR 280 (All.)]*

– The word `may' has been used in all of these sections, thereby giving the discretion to the assessing officer to treat a particular sum as income or not; therefore, even if the assessee does not provide an explanation, or provides one that is unsatisfactory, it is not necessary in all cases for the amount to be treated as the assessee's taxable income *[CIT vs. Noorjahan 237 ITR 570 (SC); CIT vs. Moghul Durbar 216 ITR 301 (AP) etc.]*

– The provisions of sections 69, 69A, 69B and 69C treat unexplained investments, unexplained money bullion etc. and unexplained expenditure as deemed income where the nature and money, bullion, etc., and unexplained expenditure as deemed income where the nature and source of investment, acquisition or expenditure, as the case may be, have not been satisfactorily explained. In these cases, the source not being known, such deemed income will not fall even under the head `Income from Other Sources' and the deductions that are applicable to the incomes under any of the heads will not be attracted – *[Fakir Mohmed v. CIT 247*

ITR 290 (Guj.), CIT v. Ramkant 252 ITR 210 (Cal.), Bijjala v. CIT 253 ITR 105 (AP), etc.]

– **Intangible additions cannot protect assessee** – The funds comprising the intangible additions made in earlier year would not help an assessee to presume that the said fund was always available to cover the unexplained income of the succeeding years. It is for the assessee to establish that he has not earned any secret profits during the relevant year and that the investment flowed from the intangible additions made in the preceding years – *[CIT vs. M.A. Unnerikutty [1985] 154 ITR 844 (Ker.)]*

– **It is not necessary that books of account are to be rejected** – For applying sections 69 and 69B, it is not necessary that the books of account are to be rejected. The onus of proving the source of a sum of money is on the assessee. If he disputes the liability for tax, it is for him to show that the receipt was not income or that it was exempted from taxation under the law. In the absence of any proof, the Assessing Officer is entitled to charge it as taxable income. It is not necessary that the books of account have to be rejected expressly or that it is to be, in express terms, recorded that the books of account are not reliable or the explanation is not satisfactory – *[Unit Construction Co. Ltd. vs. Jt. CIT [2003] 260 ITR 189 (Cal.)]*

– Whether S. 69 can be applied in the hands of legal heirs to seek explanation on source of funds being invested by deceased – Held No. *[ITAT Pune in Rajbai Kadam – 83 ITD 229, Cochin ITAT in C. Selvakumar – 6 SOT 646]*

Burden placed u/s. 69 & 69A *vis-à-vis* the same as placed u/s. 69B

Two findings are required to be given by the AO before invoking deeming fiction under sections 69 and 69A. One is that assessee is found to have made investment or to be the owner of money, bullion, jewellery or other valuable article in the current financial year and the other is that they are not at all recorded in the books of account maintained by the assessee. The deeming fiction then permits the AO to treat the 'value' of such money, bullion, jewellery or other valuable article as assessee's income.

Whereas, the findings to be given for invoking S. 69B are –

(i) there is an investment or acquisition of money, bullion, jewellery or other valuable article recorded in the books, **and**

(ii) actual amount spent on investment or in acquisition is more than the amount recorded in the books.

The deeming fiction thereafter permits the AO to treat the excess over what is recorded in the books as the assessee's income for that financial year.

Addition u/ss. 69, 69A etc. – Tax applicable

Up to A.Y. 2012-13, the additions u/ss. 68/69/69A/69B/69C/69D ('Specified Sections') were part of total income of the assessee and were taxable at the normal rate / rate applicable to the total income so computed. However, upon introduction of S. 115BBE w.e.f. A.Y. 2013-14, this position has been changed with introduction of special rate of tax applicable to income of the nature specified in S. 68 to S. 69D.

Section 115BBE has since its introduction by the FA, 2012 w.e.f. AY 2013-14, been amended thrice. Once by F.A. 2016 w. e. f. A.Y. 2017-18 when sub section (2) was amended to prohibit setting off of any loss against income of the nature referred to in specified sections and second time, by the Taxation Laws (Second Amendment) Act, 2016 (passed on 15-12-2016) w.e.f. 1-4-2017 to increase the applicable rate of tax from 30% to 60% in respect of the income of the nature specified in

S. 68 to S. 69D and to make the section applicable to voluntary income offered by assessee as well income determined by AO under the above specified sections.

Finally sub-section (2) was amended by F.A. 2018 so as to also include income referred to in clause (b) of sub-section (1).

The said amendment seems to rectify the inadvertent non-reference to clause 1(b) in sub-section (2). Also, as the revised Section 115BBE was substituted from A.Y. 2017-18 and hence the insertion of reference to clause 1(b) is also made effective retrospectively from A.Y. 2017-18.

Section 115BBE as applicable w.e.f. 1-4-2017 [i.e. A.Y. 2017-18]

115BBE. *(1) Where the total income of an assessee,—*

(a) includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D and reflected in the return of income furnished under section 139; or

(b) determined by the Assessing Officer includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, if such income is not covered under clause (a),

the income-tax payable shall be the aggregate of—

(i) the amount of income-tax calculated on the income referred to in clause (a) and clause (b), at the rate of sixty per cent; and

(ii) the amount of income-tax with which the assessee would have been chargeable had his total income been reduced by the amount of income referred to in clause (i).

(2) Notwithstanding anything contained in this Act, no deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee under any provision of this Act in computing his income referred to in clause (a) and clause (b) of sub-section (1).

Salient feaures of section 115BBE

– The section applies to all assessees.

– The section applies irrespective of the minimum threshold.

– Items which could have been taxed by the AO under the provisions of sections 68 to section 69D can also be offered for taxation by the assessee voluntarily in his return of income by paying tax, on or before the end of the previous year, at the rates mentioned in section 115BBE.

– As per sub-section (2) of section 115BBE no deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee under any provision of this Act in computing his income under S. 115BBE(1).

– No basic exemption is allowed while calculating tax at special rate under section 115BBE

– It is debatable issue as to whether deductions under Chapter VI-A are allowable against income computed u/s 115BBE.

– Income referred to in Section 68, 69, 69A, 69B, 69C or 69D is taxable @ 60% u/s. 115BBE of the Act.

– **The total incidence of tax in respect of income of the nature referred to above is 77.25%. [(60 + 3%) + 25% surcharge].**

Addition u/ss. 69, 69A etc. – Penal consequences

Legal fiction is only for a definite purpose. They have to be strictly construed and they are limited to the purpose for which they are created and should not be extended beyond their legitimate field. There cannot be fiction upon fiction. It assumes significance in the context of penalty provisions. Since deeming provisions are created by a fiction, there can be no fiction upon fiction and, therefore, the deemed income cannot be *ipso facto* liable for penalties. In other words, though the addition was made under deeming provisions of S. 69, 69A etc., during the course of penalty proceedings u/s. 271(1)(c), it is incumbent upon the AO to establish that in fact the amount so added was income and that too of the assessment year under consideration.

– The fiction created under sections 68, 69, 69A, 69 B and 69C cannot, by itself, be extended to penalty proceedings to raise a presumption of concealment of income – *[CIT vs. Baroda Tin 221 ITR 661 followed in Vinod K. Bafna vs. ITO (ITA No. 935/PUNE/2014 dt. 18-1-2017), Patel Engineering vs. ITO [31 TTJ 154 (ITAT Ahd.)]*

Penalty u/s. 271AAC

– In a case where the income determined includes any income referred to in section 68, 69, 69A, 69B, 69C or 69D for any previous year, the assessee shall also be liable for penalty, in addition to tax payable under section 115BBE, a sum @ 10% of the tax payable under clause (i) of sub-section (1) of section 115BBE.

– **However**, no penalty shall be levied in respect of income referred to above, to the extent such income has been included by the assessee in the ROI furnished under S. 139 and the tax in accordance with the provisions of section 115BBE (1)(i) has been paid on or before the end of the relevant previous year.

– **Thus, if penalty under section 271AAC is also levied then the incidence of tax works to 83.25% u/s. 115BBE r.w.s. 271AAC [77.25% + 6%].**

Income declared during the course of survey/search

Generally, whatever excess stock, cash, unrecorded debtors etc., gets unearthed during serach/survey action are generated only out of assessee's regular business activity. It represents nothing but assessee's hard earned regular business income, though represented by some unrecorded purchases/sales etc. If assessee doesn't have any other secret business activity/ other secret source of income, other than that disclosed in his returns of income from time to time, provisions of section 69 etc. and thereby s. 115BBE can't be made applicable.

– If It was not the case at the time of search/ survey proceedings that declarant was doing some other secret activities in which such income was earned and alleged to have been invested in unrecorded stock, etc. as declared, the additional income can be said to have generated out of assessee's regular business activity, and accordingly, in author's opinion, there is no scope for application of section 69, 69A etc. and thereby S. 115BBE of the Act. *[See: Daulatram Rawatmal 64 ITR 593(Cal.); Annamalai Reddier 53 ITR 601 (Ker); CIT vs. Margret's Hope Tea Co. Ltd. (201 ITR 747)]*

– *Hon'ble Rajasthan HC in Pr. CIT vs. Bajargan Traders C/o. Kalani & Co. [ITA No. 258/2017]* held that the tribunal was legally justified in treating the investment in excess stock for ₹ 70,04,814 found during the course of survey as 'business income' instead of 'Income from Other Sources under section 69.

– Income disclosed at time of survey in the nature of excess stock was includible in business income and therefore eligible for computation of deduction under section 40(b), in respect of remuneration to partners – *M/s. Silver Palace vs. DCIT – ITA No. 893/PUNE/2016 dt. 29-6-2018. ITO vs. Jamnadas Muljibhai (99 TTJ 197), M/s Dev Raj Hi-Tech Machines vs. DCIT (ITA No, 326 of 2014 dt. 7-10-2015 (Amritsar), etc.]*

However, the above proposition can't be taken as general rule and treatment of additional income unearthed during the course of survey / search proceedings as regular business income or otherwise shall depend on facts and circumstances of each case, manner and nature of declaration given and incriminating documents found during survey / search proceedings.

Conclusion

In the past, revenue authorities had no reason to apply deeming provisions u/s. 68 to 69D on voluntarily income returned by assessee under various heads. Such cases are likely to increase in view of the power available under the provisions of section 115BBE to tax disclosed income under deeming provisions at special rates. Therefore, assessees can take benefit of section 115BBE (1)(a) by voluntarily offering the income of the nature specified in S. 68 to S. 69D in the return of income filed u/s. 139 and by paying tax, on or before the end of the previous year, at the rates mentioned in section 115BBE. This willl save the assessee from penal consequences u/s. 271AAC. This acquires more significance in search cases as summarised in following chart:

Tax/Penalty in respect of undisclosed income declared /found during search

(AFTER 15-12-2016)

Sr. No.	Tax Payable u/s. 115BBE? (Income u/s. 68,69, etc.)	Undisclosed income Voluntarily offered in ROI and taxes paid before end of previous year?	Specified Previous Year?	Penalty - S. 271AAC	Penalty - S. 271AAB (1A) (applicable for specified P.Y. only)		Penalty -S. 270A	Total Tax + Penalty
					Clause (a)	Clause (b)		
1	Y	Y/N	Y	N	Y	N	N	107.25%
2	Y	Y/N	Y	N	N	Y	N	137.25%
3	Y	N	N	Y	N		N	83.25%
4	Y	Y	N	N	N		N	77.25%
5	N	Y/N	Y	N	Y	N	N	Tax + 30%
6	N	Y/N	Y	N	N	Y	N	Tax + 60%
7	N	Y/N	N	N	N		Y - UR	Tax + (50% of Tax)
8	N	Y/N	N	N	N		Y - MR	Tax + (200% of Tax)

Notes:
- All the percentages are in relation to amount of undisclosed income found during search.
- Penalty u/s. 270A is 50% of tax payable on undisclosed income in case of under reporting. **(UR)**
- Penalty u/s. 270A is 200% of tax payable on undisclosed income if under-reporting is due to misreporting. **(MR)**
- Specified previous means the previous year-

which has ended before the date of search, but the date of furnishing the return of income under sub-section 139(1) for such year has not expired before the date of search and the assessee has not furnished the return of income for the previous year before the date of search; OR the year in which search was conducted. [S. 271AAB(3)(b)]

Further, as specified u/s. 271AAC(2), no penalty u/s. 270A (applicable w.e.f. A.Y. 2017-18) shall be imposed upon the assessee in respect of the income referred to in S. 68/69/69A/69B/69C/69D of the Act.

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Harsh Kothari, *Advocate*

Section 69C – Unexplained Expenditure

Section 69C was introduced by the Taxation Laws (Amendment) Act, 1975 to deem as income of the assessee any expenditure incurred in any financial year where the assessee offers no explanation about the source of such expenditure or any part thereof or where an explanation has been offered, the same is not satisfactory in the opinion of the assessing officer.

While explaining the scope of section 69C, the Delhi High Court in the case of *Yadu Hari Dalmia vs. CIT (1980) 126 ITR 48* observed that where an assessee has, in fact, incurred certain expenditure and is not able to account for the same satisfactorily, an inference can be drawn that the expenditure or the unaccounted part thereof must have been met out of the undisclosed income of the previous year. The Court further observed that section 69C was only clarificatory and that even otherwise an addition could be made to the total income in respect of amounts of expenditure which the assessee is found to have actually incurred but not satisfactorily explained.

Incurrence of expenditure

The first test laid down in section 69C is that an assessee must have incurred some expenditure. Addition on account of a mere inference is not sustainable. In the case of *CIT vs. Lubtec India Ltd. (2009) 311 ITR 175 (Del.),* two sheets of paper were recovered from the assessee's premises which showed a noting of certain items like dinner, gift, projector, advertisements in newspapers, magazines and hoardings, etc. The assessing officer held that the assessee had incurred expenditure mentioned in those sheets of paper and added the same as income of the assessee under section 69C. High Court observed that (i) section 69C postulates that expenses must have been incurred by the assessee and thereafter any explanation given about the source of such expenditure is not satisfactory in the opinion of the assessing officer; (ii) the addition under section 69C cannot be sustained as there was nothing to show that expenses were in fact incurred by the assessee; and (iii) the assessee had contended that it did not have that kind of money to incur such expenditure and that the assessing officer did not take any action to find out whether such expenses were actually incurred or not.

A connected issue which arises is as to whether an addition can be made under section 69C in the absence of a direct proof of incurrence of expenditure though the surrounding circumstances may clearly show that the assessee must have incurred some expenditure.

Delhi High Court in the case of *Yadu Hari Dalmia vs. CIT (supra)* held that there cannot be any difference between (i) a case where there is a direct proof of unexplained expenditure and (ii) a case where the circumstances clearly justify an inference that the assessee must have incurred excess expenditure but the quantum of such expenditure requires estimation for want of direct evidence. Therefore, even where there is no direct proof that unexplained expenditure has been incurred (say, for example a diary containing details of expenses incurred seized during the search) an addition can be made under section 69C. The Delhi High Court, however, observed that in a case where an estimate has to be made, it should not be done purely on guess-work and on the basis of broad probabilities but by conducting exhaustive or detailed enquiries, survey or investigation and gathering some tangible material for the estimate.

Expenditure incurred and recorded in the books of account

The provisions of section 69C cover within its ambit such expenditure which is incurred by the assessee but not recorded in the books of account. In the case of *CIT vs. Suryadeep Salt Refinery & Chemical Works Ltd. (2013) 219 Taxman 251 (Guj.),* incorrect figures were shown in the balance sheet filed along with the return of income. However, during the course of the assessment proceedings, the discrepancies in the balance sheet were duly explained and rectified and the capital work-in-progress was also accounted in the books of accounts. Gujarat High Court held that once an amount had already been recorded in the books of account of the assessee, the same cannot be said to be falling under section 69C.

Similar was the view taken by the Delhi High Court in *CIT vs. Radhika Creation (2011) 10 taxmann.com 138 (Delhi).* In this case, the assessing officer examined the details of certain expenditure and found that the same were not authenticated by any vouchers and consequently, added the same as unexplained expenditure under section 69C. High Court noted that the Tribunal had deleted the addition under section 69C on the ground that as the expenditure was accounted in the regular books of account, the source of the same was clearly explained. High Court upheld the findings of the Tribunal and observed that the action of the assessing officer in going into the authenticity of the expenditure was outside the purview of section 69C.

Explanation about the source

The second condition which, if fulfilled, attracts section 69C is that the assessee offers no explanation about the source of the expenditure incurred or a part thereof, or even when an explanation is offered by him, the same is not satisfactory in the opinion of the Assessing Officer. The Courts have laid down that the assessing officer while considering the explanation of the assessee must act reasonably and he should reach a conclusion as to whether the explanation of the assessee is satisfactory or not based on relevant factors and after conducting a just and fair inquiry. *(Sreelekha Banerjee vs. CIT (1963) 49 ITR 112 (SC), Sumati Dayal vs. CIT (1995) 214 ITR 801 (SC), Khandelwal Constructions vs. CIT (1997) 227 ITR 900 (Gau.), Hindusthan Tea Trading Co. Ltd. vs. CIT (2003) 263 ITR 289 (Cal.))*

It may be noted that the section requires an assessee to explain the source of expenditure and not its reasonableness. In other words, once the assessing officer is satisfied about the source of the expenditure, an addition cannot be made under section 69C merely because he feels that the expenditure incurred by the assessee is excessive and unreasonable.

Expenditure 'may' be deemed to be the income

If the above two tests are met, the amount covered by such expenditure or part thereof may be deemed to be the income of the assessee for such financial year. The legislature has used the words 'may' and not 'shall'. Supreme Court in *CIT vs. Smt. P. K. Noorjahan (1999) 237 ITR 570 (SC)* in the context of section 69 held that the assessing officer is conferred a discretion regarding treating any investment which has not been satisfactorily explained as the income of the assessee. The assessing officer is not obliged to treat such source of investment as income of the assessee in every case where the explanation offered by the assessee is not found to be satisfactory. Supreme Court observed that the question whether a particular source of investment should be treated as income or not under section 69 has to be considered in the light of the facts of each case.

Following the Supreme decision in P. K. Noorjahan, the Allahabad High Court in *Pr. CIT vs. Rama Shankar Yadav (2017) 85 taxmann.com 173 (All.)* held that the provisions of section 69C are *pari materia* to section 69A and that it is not mandatory to make an addition under the same inasmuch as the legislature has used the word "may" in the provision. Allahabad High Court concluded that the assessing officer has full discretion to add or not to add any expenditure or any part thereof in the income of the assessee even if no explanation has been offered or if offered is not found to be satisfactory provided such discretion is exercised in a judicious manner.

Proviso to section 69C

The Finance (No. 2) Act, 1998 inserted a proviso in section 69C w.e.f. 1st April 1999 providing that unexplained expenditure which is deemed to be the income of the assessee shall not be allowed as a deduction under any head of income notwithstanding anything contained in any other provision of this Act.

Circular No. 772 dated 23rd December 1998 while explaining the amendments brought by the Finance (No. 2) Act, 1998 stated that the introduction of the proviso to section 69C was necessitated because while the unexplained expenditure was deemed to be the income of the assessee, there was no corresponding provision for disallowance of such expenditure. Consequently, the assessees who were subjected to tax under section 69C would claim such expenditure as a deduction under section 37 thereby defeating the object of section 69C.

Gujarat High Court in the case of *Krishna Textiles vs. CIT (2009) 310 ITR 227 (Guj.)* observed that the proviso to section 69C did not have retrospective application. Similar view was taken by the Andhra Pradesh High Court in the case of *P. Ram Gopal Varma vs. DCIT (2013) 357 ITR 493 (AP)* where the Court observed that the proviso to section 69C creates a new liability or at least impairs an existing right of claiming a deduction of the unexplained expenditure which the assessee had prior to the insertion of the proviso in the statute. High Court held that the proviso does not have a retrospective operation as it changes the existing legal position and creates a new obligation on the assessee. Further, there is nothing in the language of the proviso or in the notes to clauses and the CBDT Circular No. 772 explaining the rationale behind insertion of the proviso which suggests a retrospective application.

Section 115BBE – Rate of tax

Section 115BBE was inserted by the Finance Act, 2012 w.e.f. 1st April 2013 to provide for the rate of tax at which income referred to in, *inter-alia*, section 69C would be charged.

Prior to the introduction of section 115BBE, the unexplained expenditure deemed as income under section 69C was subject to tax as per the tax rate applicable to the assessee. Consequently, in the case of assessees who paid tax based on the slab rates, no tax was charged in respect of income not exceeding the basic exemption limit and in respect of income exceeding the basic exemption limit, the same was chargeable as per the slab rates. The intent behind introducing this section as stated in the Explanatory Memorandum to the Finance Bill, 2012 was to remove taxation of deemed income as per the slab rates so as to curb the practice of laundering of unaccounted money by taking advantage of the basic exemption limit.

At the time of introduction, section 115BBE provided that the income referred to in section 69C would be chargeable at the rate of 30% without allowing any deduction from such income in respect of any expenditure or allowance under any provision of the Act.

Section 115BBE was thereafter amended by the Taxation Laws (Second Amendment) Act, 2016 w.e.f. 1st April 2017 to provide that any income referred to in section 69C whether reflected by the assessee himself in his return of income or whether determined by the assessing officer during the assessment shall be taxed at the rate of 60%. Statement of objects and reasons annexed to the Taxation Laws (Second Amendment) Bill, 2016 state that the amendment was necessitated as concerns were raised post demonetisation of currency that some of the existing provisions of the Income-tax Act, 1961 could possibly be used for concealing black money.

Section 115BBE(2) was amended by the Finance Act, 2016 w.e.f. 1st April 2017 to provide that in addition to the existing provision denying deduction in respect of any expenditure or allowance; set off of any loss shall also not be allowed to the assessee under any provision of this Act in computing his income referred to in section 69C.

Jaipur Bench of the Income-tax Appellate Tribunal in the case of *ACIT vs. Sanjay Bairathi Gems Ltd. (2017) 166 ITD 445 (Jaipur - Trib.)* held that the insertion of the above words 'set off of any loss' in section 115BBE(2) were prospective in nature. Consequently, the Tribunal held that there was no bar for set off of current year's business loss under section 71 against income arising under section 69B brought to tax under the head "income from other sources". This decision was relied upon and followed in *Pitamber Commodity Futures (P) Ltd. vs. ACIT (ITA No. 863/Jp/2017).*

Section 271AAC – Levy of penalty

Section 271AAC was inserted in the statute by the Taxation Laws (Second Amendment) Act, 2016 w.e.f. 1st April 2017. The said section provides that the assessing officer may, in a case where the income of the assessee includes any income referred to in section 69C, direct the assessee to pay in addition to the tax payable under section 115BBE(1)(i), a penalty at the rate of 10% of the tax payable under section 115BBE(1)(i).

Proviso to section 271AAC states that no penalty shall be levied in respect of income referred to in section 69C to the extent such income has been included by the assessee in his return of income furnished under section 139 and the assessee has paid tax in accordance with section 115BBE(1)(i) on or before the end of the relevant previous year.

Section 271AAC(2) clarifies that no penalty shall be imposed upon the assessee under the provisions of section 270A in respect of the income referred to in sub-section (1). Section 271AAC(3) states that the procedure laid down in section 274 and the time limit prescribed in section 275 shall apply.

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> Renunciation and spirituality are the two great ideas of India.
>
> — *Swami Vivekananda*

Rahul Hakani, *Advocate*

Taxation of Unexplained Incomes up to A.Y. 2012-2013

Introduction

Presently, provisions of Section 115BBE deal with the taxation of income referred to in Section 68, section 69, 69A,69B, 69C or Section 69D. Section 115BBE was inserted by the Finance Act, 2012 w.e.f 1-4-2013. Section 115BBE provided for a flat rate of tax @ 30% on the amounts deemed as income u/s. 68 to section 69D. Thus, benefit of slab rate of tax on income taxed u/s. 68 to 69D was withdrawn

Further, sub-section (2) of Section 115BBE provided that no deduction in respect of any expenditure or allowance shall be allowed to the assessee while computing the deemed income u/ss. 68 to 68D.

By Finance Act, 2016 w.e.f 1-4-2017 sub-section (2) was further amended by inserting that no set-off of any loss will be allowed while computing deemed income u/s. 115BBE.

Thus the introduction of Section 115BBE and the subsequent amendments throw some light on the law prevailing before the introduction of Section 115BBE which the legislature desired to overturn by specifically legislating on those points.

The conundrum of a headless income

In cases of survey/search, very often declaration is made pursuant to excess stock detected. Such declaration is included in the Return of Income and is adjusted against business expenses / losses by the assessee. However, the assessing officer treats such declaration as deemed income u/s. 69 and disallows any deduction against such income.

Thus, the primary issue is the head under which deemed income u/ss. 68 to 69D are taxable. Once this issue is decided the other issues are consequential. Also, where assessee is able to explain the nature and source satisfactorily, the corresponding income will not be taxed u/s. 68 to 69D but will be taxed under a particular head of Income.

Under the scheme of the IT Act 1961 computation of income is made as per provisions of Chapter IV which covers section 14 to section 59. Various heads of income have been defined in sec 14. The nature of income to be classified under different heads and procedure of its computation is specified under different sub-chapters from A to F of Chapter IV. The next Chapter V covering sec 60 to 65 deal with income of other persons included in total income which is not relevant for present discussion. Thereafter it is Chapter VI which covers sections 66 to 80 which is relevant. It has two parts, one dealing with aggregation of income (from sec 66 to 69D) and other with carry forward & set off of losses (from sec 70 to 80). Thus, strictly speaking deemed income u/ss. 68 to 69D do not have any head of Income. But whether such an interpretation is correct? In *Addl. CIT vs. Ghai Lime Stone Co (1983) 144 ITR 140(MP)(HC)* it is held that S.68 does not debar an assessee from offering alternate explanations.

The Gujarat High Court in *Fakir Mohmed Haji Hasan vs. CIT [2001] 247 ITR 290 (Guj) (HC)*, was dealing with a case where value of gold confiscated by the Customs department was treated as demmed income u/s. 69A. The assessee claimed that the gold confiscated was a trading loss and same should be allowed as a deduction from deemed income u/s. 69A. The Gujarat High Court held as under:

> "6. Under section 4 of the Act, income-tax is to be charged in accordance with the provisions of the Act in respect of the total income of the previous year of every person. As provided by section 5 of the Act, total income of any previous year of a person would, *inter alia*, include all income from whatever source derived which is received or is deemed to be received by such person, subject to the provisions of the Act. It will be seen from section 69A that where the bullion, jewellery or other valuable article is not recorded in the books of account and there is no explanation about the nature and source of its acquisition, or the explanation is not satisfactory, the value thereof may be deemed to be the income of the assessee of the financial year immediately preceding the assessment year in which the assessee is found to be the owner of such bullion, etc.
>
> 6.1 The scheme of sections 69, 69A, 69B and 69C of the Act would show that in cases where the nature and source of investments made by the assessee or the nature and source of acquisition of money, bullion, etc., owned by the assessee or the source of expenditure incurred by the assessee are not explained at all, or not satisfactorily explained, then the value of such investments and money, or value of articles not recorded in the books of account or the unexplained expenditure may be deemed to be the income of such assessee. It follows that the moment a satisfactory explanation is given about such nature and source by the assessee, then the source would stand disclosed and will, therefore, be known and the income would be treated under the appropriate head of income for assessment as per the provisions of the Act. However, when these provisions apply because no source is disclosed at all on the basis of which the income can be classified under one of the heads of income under section 14 of the Act, it would not be possible to classify such deemd income under any of these heads including "Income from other sources" which have to be sources known or explained. When the income cannot be so classified under any one of the heads of income under section 14, it follows that the question of giving any deductions under the provisions which correspond to such heads of income will not arise. If it is possible to peg the income under any one of those heads by virtue of a satisfactory explanation being given, then these provisions of sections 69, 69A, 69B and 69C will not apply, in which event the provisions regarding deductions, etc., applicable to the relevant head of income under which such income falls will automatically be attracted.
>
> 6.2 The opening words of section 14 'Save as otherwise provided by this Act' clearly leave scope for 'deemed income' of the nature covered under the scheme of sections 69, 69A, 69B and 69C being treated separately, because such deemed income is not income from salary, house property, profits and gains of business or profession, or capital gains, nor is it income from 'other sources' because the provisions of sections 69, 69A, 69B, and 69C treat unexplained investments, unexplained money, bullion, etc., and unexplained expenditure as deemed income where the nature and source of investment, acquisition or expenditure, as the case may be, have not been explained or satisfactorily explained. Therefore, in these cases, the source not being known, such deemed income will

not fall even under the head, 'Income from other sources'. Therefore, the corresponding deductions, which are applicable to the incomes under any of these various heads, will not be attracted in case of deemed incomes which are covered under the provisions of sections 69, 69A, 69B and 69C in view of the scheme of those provisions.

7. It is, therefore, clear that when the investment in or acquisition of gold, which was recovered from the assessee was not recorded in the books of account and the assessee offered no explanation about the nature and source of such investment or acquisition and the value of such gold was not recorded in the books of account, nor the nature and source of its acquisition explained, there could arise no question of treating the value of such gold, which was deemed to be the income of the assessee, as a deductible trading loss on its confiscation, because such deemed income did not fall under the head of income 'Profits and gains of business or profession'."

Thus, in a nutshell, according to the Gujarat High Court, once income is taxed u/ss. 68 to 69D it will be a headless income and thereby it will not be eligible for any allowance, deduction or set-off of loss.

The decision in *Fakir Mohmed Haji Hasan (supra)* was subsequently considered in the case of *Krishna Textiles vs. CIT [2009] 310 ITR 227 (Guj) (HC).* In this case the Assessing Officer compared the copy of account of the assessee-company as appearing in the books of the Gujarat Mineral Development Corporation (GMDC) with the books of account of the assessee and found that certain drafts allegedly sent to the GMDC by the assessee had not been accounted for in its books, but the entries in respect thereof appeared in the account of the assessee in the books of the GMDC. Accordingly addition was made. The Tribunal sustained the addition. The Tribunal had also rejected the alternative contention raised by the assessee that corresponding deduction should be given inasmuch as the payments were made for purchases of raw materials like coal etc. The Tribunal held that in absence of any evidence, it cannot be presumed that the payments were made for business purposes. The High Court on the alternative contention held that if addition is made u/s. 69C then deduction of expenditure u/s. 37 has to be allowed. The High Court held as under :

"Since it was an admitted position that the assessee was carrying on the business of coal and lignite and purchases were made from time-to-time from the GMDC, in that case, even if any addition was required to be made under section 69C, the entire expenditure towards it had to be allowed as a deduction under section 37(1). If the argument canvassed by the revenue, that if an addition on account of unexplained expenditure was made under section 69C, then the fact that deduction could not be allowed under section 37(1) was obvious and automatic, was accepted, then there was no need of amending section 69C by adding the proviso which has come into force with effect from 1-4-1999, and is relevant to the assessment year 1999-2000 onwards and has not been made retrospective in operation. The assessment year under consideration was, admittedly, 1987-88 to which the effect of this amendment would not be applicable. Thus, taking into consideration the totality of the facts and circumstances of the case, the revenue authorities were not justified in making and/or confirming the disputed addition inasmuch as even if the assessee did incur expenditure for purchasing coal, lignite, etc., from the GMDC, the equivalent debit in the profit and loss account would neutralise each other and no addition could be made."

In the above decision a difference was carved out between addition u/s. 69 to 69D and 69C and thereby it was held that the decision in *Fakir Mohmed Haji Hasan (supra)* was not applicable. However, the Court did not dwell into the question of head of income where income is taxed u/s. 68 to 69D.

Thereafter in *DCIT vs. Radhe Developers India Ltd. [2010] 329 ITR 1 (Guj.)(HC)* the Assessing Officer, therefore, worked out the investment at a sum of ₹ 25,10,80,000 as being unexplained investment and added the same under section 69B of the Act. According to the Assessing Officer, the aforesaid amount would include a sum of ₹ 12,80,00,000 disclosed as receipt of on-money by Shri Ashish Patel as per the statement dated May 1, 1996. Simultaneously, the claim made by the assessee that a sum of ₹ 12,80,00,000 was paid for acquiring the development rights of 7 lakh sq. yds. of the land was not believed by the Assessing Officer and the claim of deduction denied. The Tribunal for the reasons stated in its impugned order, came to the conclusion that the addition for the undisclosed receipt had to be sustained only to the extent of ₹ 12,80,00,000 as accepted by the assessee and there was no basis for making addition to the tune of ₹ 20,55,86,000 as the assessee had acquired the development rights only in relation to 7 lakh sq. yds. of land and not 11.11 lakh sq. yds. of land. At the same time, the Tribunal also recorded that the amount of ₹ 12,80,00,000 paid by the assessee for acquisition of development rights had to be treated as allowable deduction under section 37 of the Act. The High Court held as under :

> "The decisions of this court in the case of *Fakir Mohmed Haji Hasan [2001] 247 ITR 290 (Guj.)* and *Krishna Textiles [2009] 310 ITR 227 (Guj.)* are neither relevant nor germane to the issue considering the fact that in none of the decisions the legislative scheme emanating from the conjoint reading of the provisions of sections 14 and 56 of the Act have been considered. The Apex Court in the case of *D.P. Sandu Bros. Chembur P. Ltd. [2005] 273 ITR 1* has dealt with this very issue while deciding the treatment to be given to a transaction of surrender of tenancy right. The earlier decisions of the Apex Court commencing from the case of *United Commercial Bank Ltd. vs. CIT [1957] 32 ITR 688 (SC)* have been considered by the Apex Court and, hence, it is not necessary to repeat the same. <u>Suffice it to state that the Act does not envisage taxing any income under any head not specified in section 14 of the Act</u>. In the circumstances, there is no question of trying to read any conflict in the two judgments of this court as submitted by the learned counsel for the Revenue."

Thus, as per the above decision the deemed income u/ss. 68 to 69D were not headless income and they have to be taxed under some head of income.

In *CIT vs. Chensing Ventures [2007] 291 ITR 258/163 Taxman 175 (Mad.)* the assessee during the course of survey could not explain the source for the payment of ₹ 28.50 lakh. It was surrendered voluntarily as income for taxation. The assessee filed a return admitting business loss of ₹ 11.95 lakh and set off the same against the income of ₹ 28.50 lakh admitted at the time of survey as income from undisclosed sources. The Assessing Officer did not allow set off of business loss against income from undisclosed sources. The Court held that once the business loss was determined the same had to be set-off against the income determined under any other head of income. A loss after set off against the income under the same head was eligible for set off against other heads of income, unless the law prohibited or banned such set off. The Court, accordingly, held that the income offered during the course of survey had to be scaled down by the business loss of the assessee.

In *Commissioner of Income-tax – II vs. Shilpa Dyeing & Printing Mills (P.) Ltd. [2013] 39 taxmann.com 3 (Gujarat)* was dealing with the issue of eligibility of set-off of loss against income declared during survey on account of excess stock and such declaration included in the Return of Income. In this case assessee is a company engaged in the business of dyeing and printing. During the course of scrutiny for the assessment year 2008-09, the Assessing Officer noticed that in a survey action conducted at the business premises of the assessee, it had declared a sum of ₹ 100.98 lakh (rounded off) on account of excess stock. In the return, the assessee had suggested current year's loss against such income. Assessing Officer holding a belief that income from unlisted source would not fall under any of the heads of the income, the same has to be taxed separately, the current losses were not allowed to be set-off against such income.

The High Court following the decision of *CIT vs. Chensing Ventures [2007] 291 ITR 258(Mad.)(HC)* and *Dy. CIT vs. Radhe Developers India Ltd. [2010] 329 ITR 1(Guj.)(HC)* held that as per Section 71 loss of current year was to be set-off against income declared during survey.

In *CIT vs. Babulal K. Daga [2016] 387 ITR 114 (Guj.) (HC)* in the context of Section 69C relating to disclosure during survey and included in Return of Income it was held that if assessee can point out that even on unaccounted receipts, expenditure was incurred for purpose of business, it would be only reasonable profit on such receipts which should be taxed. However one may note that this decision was in the course of revision proceedings u/s. 263.

In *Commissioner of Income Tax, Trichur vs. Kerala Sponge Iron Ltd.)[2016] 285 CTR 198 (Ker)(HC)* it was held that cash credit u/s. 68 was a headless income and hence not eligible for set-off current year year and brought forward business loss. Reliance was placed on *Fakir Mohmed Haji Hasan (Supra).* However, subsequent decision of Gujarat High Court in *Dy. CIT vs. Radhe Developers India Ltd. (Supra)* was not considered.

In *Kim Pharma (P.) Ltd. vs. Commissioner of Income-tax [2013] 258 CTR 454 (P&H)(HC)* it was held that unexplained money surrendered during search was not reflected in books of account and no source from where it was derived was declared by assessee, was assessable as deemed income of assessee under section 69A and not business income and further set off of loss was not allowed. Reliance was placed on *Fakir Mohmed Haji Hasan (Supra)*. However, subsequent decision of Gujarat High Court in *Dy. CIT vs. Radhe Developers India Ltd. (Supra)* was not considered.

After considering above decision in *Kim Pharma (P.) Ltd. vs. CIT (Supra)* the Chandigarh Tribunal in *Liberty Plywoods (P.) Ltd. vs. Asstt. CIT [2013] 140 ITD 490 (Chd.)(Trib.)* held that business loss cannot be set-off against income declared during survey but unabsorbed depreciation can be set-off against said income.

Further in *Gaurish Steels P Ltd. vs. ACIT [2015] 43 ITR(T) 414 (Chd.)(Trib.)* it was held that where assessee was engaged in business of construction of building, surrender made by assessee on account of discrepancy in cost of construction of building, stock and advances and receivables would be considered as business income and consequently business losses incurred by assessee during year could be set off against such income surrendered.

The Agra Tribunal in *Satish Kumar Goyal vs. JCIT [2016] 159 ITD 393 (Agra)(Trib.)* held that addition u/s. 68 of cash receipts was to be assessed as income from other sources and eligible for set-off against current year losses u/s. 71. This decision was rendered after considering the decision of *Kim Pharma (P.) Ltd. vs. CIT (Supra) Fakir Mohmed Hazi Hasan vs. CIT (Supra)* and *Dy. CIT vs. Radhey Developers India Ltd. (Supra).*

Conclusion

From the above analysis, the legal position which emanates can be concluded as under :

1) Deemed income u/ss. 68 to 69D is not a headless income. However, an assessee in Punjab & Haryana or Kerala may have to point out that decisions in *Kim Pharma (P.) Ltd. vs. Commissioner of Income-tax (Supra) & Commissioner of Income Tax, Trichur vs. Kerala Sponge Iron Ltd. (Supra*) cannot be relied upon as said decisions have not considered the Supreme Court decision in *D. P. Sandu Bros. Chembur P. Ltd. [2005] 273 ITR 1(SC).*

2) The deemed income will be taxed as Income from Other Sources unless assessee is able to explain nature and source and establish that deemed income is business income. If it is assessed as Income from other sources, it can claim set-off of loss as per Section 71 but will not be able to claim set-off of loss u/s. 72. Assessee will be able to claim set-off of unabsorbed depreciation.

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CA Kalpesh Katira & CA Prathmesh Pokharankar

Taxation of Unexplained Incomes from AY 2013-14

Background

To begin with, unexplained income simply means any income for which assessee does not have valid explanation about the nature and / or source or the assessing officer is not satisfied with the explanation provided by the assessee.

Under the provisions of Income-tax Act, 1961 ("the Act") broadly, the term 'unexplained income' is dealt within sections 68, 69, 69A, 69B, 69C and 69D as under.

Section	Section deals with
68	Cash Credits
69	Unexplained investments
69A	Unexplained money, etc.
69B	Amount of investments, etc., not fully disclosed in books of account
69C	Unexplained expenditure, etc.
69D	Amount borrowed or repaid on hundi

As per the aforesaid sections, these amounts of unexplained income are by a fiction of law to be charged to income-tax as income of the assessee of the previous year in which the credit is reflected, investment is made or expenditure incurred. Accordingly, one could take a position that these amounts would be part of total income of the assessee and would be taxed at the rate applicable to the taxpayer or depending on its legal status. As a consequence, in case of individuals, HUF, etc., no tax was levied up to the basic exemption limit and even if such income was higher than basic exemption limit, it was getting taxed at the lower slab rate. Also, that expenditure incurred, if any, would be deductible and the losses for the year would be set off against such income.

The "White Paper on Black Money" presented in the Parliament on 16th May 2012 was, *inter alia*, concerned with the laundering of unaccounted money by taking advantage of basic exemption limit. Hence in order to curb this escape, section 115BBE has been introduced.

Object and purpose

The above stated position of taxing income of the nature referred to in the specified sections at the normal rate / applicable rate of income-tax on the total income of the assessee has been changed with effect from Assessment Year (AY) 2013-14. The Finance Minister in his budget speech, while introducing the Finance Bill, 2012 on 16th March 2012, said as under:

> "I propose a series of measures to deter the generation and use of unaccounted money. To this end, I propose ....Taxation of unexplained money, credits, investments, expenditures, etc., at the highest rate of 30 per cent irrespective of the slab of income."

Further, the reason and purpose of the provision of section 115BBE was explained by the Memorandum to the Finance Bill, 2012 as under:

> *"1) Under the existing provisions of the Income-tax Act, certain unexplained amounts are deemed as income under section 68, section 69, section 69A, section 69B, section 69C and section 69D of the Act and are subject to tax as per the tax rate applicable to the assessee. In case of individuals, HUF, etc., no tax is levied up to the basic exemption limit. Therefore, in these cases, no tax can be levied on these deemed income if the amount of such deemed income is less than the amount of basic exemption limit and even if it is higher, it is levied at the lower slab rate.*
>
> *2) In order to curb the practice of laundering of unaccounted money by taking advantage of basic exemption limit, it is proposed to tax the unexplained credits, money, investment, expenditure, etc., which has been deemed as income under section 68, section 69, section 69A, section 69B, section 69C or section 69D, at the rate of 30% (plus surcharge and cess as applicable). It is also proposed to provide that no deduction in respect of any expenditure or allowance shall be allowed to the assessee under any provision of the Act in computing deemed income under the said sections. This amendment will take effect from 1st April, 2013 and will, accordingly, apply in relation to the assessment year 2013-14 and subsequent assessment years."*

Thus, section 115BBE is designed to impose greater tax burden on the assessees who fail to explain the "nature and source" of their income, investments, expenses, etc. However, the substantive law dealing with provisions of sections 68, 69, 69A, 69B, 69C and 69D is unchanged and only the taxation mechanism on such unexplained income has been changed.

Accordingly, the Finance Act, 2012 has introduced the new section 115BBE to provide for the special rate of tax which will be applicable to income of the nature referred to in sections 68, 69, 69A, 69B, 69C and 69D.

The section has since its introduction by the Finance Act, 2012 w.e.f. AY 2013-14 been amended three times. The common point is that all three amendments are introduced at different point in times but all three amendments are applicable from AY 2017-18 onwards. Accordingly, the taxability as provided by section 115BBE gets divided in two parts as under.

- Taxability of undisclosed income from AY 2013-14 to AY 2016-17; and
- Taxability of undisclosed income from AY 2017-18 onwards.

Taxability of undisclosed income from AY 2013-14 to AY 2016-17

Let us first understand the taxability of undisclosed income from AY 2013-14 to AY 2016-17 which provides as under.

- Clause (a) of sub-section (1) of section 115BBE provides for tax at the rate of 30% on such undisclosed income covered by sections 68 to 69D (surcharge and cess are also applicable);
- Clause (b) of sub-section (1) of section 115BBE provides that while calculating income-tax, an assessee's total income would be reduced by the income taxed under clause (a) and tax will be calculated on balance of income at the applicable tax rates depending on the legal status of taxpayer. The total tax liability will be the addition of tax calculated under clause (a) and clause (b).

The provisions of section 115BBE stated that the deemed income under section 68 to 69D is to be taxed at the rate of 30% (plus surcharge and cess as applicable). Therefore, from AY 2013-14 onwards, all the undisclosed income is taxed @ 30% (plus applicable surcharge and education cess) irrespective of the legal status of taxpayer viz. individual, company, firm, etc. In addition to tax @ 30%, surcharge and cess as is applicable is also required to be paid. Surcharge depends upon the legal status of the person and his total income e.g., Finance Act, 2016 provides that in case of an individual surcharge is payable @ 12% if his total income exceeds ₹ 10 crore and not otherwise. In case of domestic companies, surcharge is payable @ 7% where total income exceeds ₹ 1 crore but does not exceed ₹ 10 crore and in case of domestic companies whose total income exceeds ₹ 10 crore surcharge is payable @ 12%. Corresponding rates for foreign companies are 2% and 5%. Education Cess is payable @ 3%[1]. Thus, the tax incidence, for AY 2016-17, on the income of the nature referred to in specified sections was ranging from 30.90% to 34.608%.

Thus, section 115BBE is designed to impose greater tax burden on the assessees who fail to explain the "nature and source" of their income, investments, expenses, etc. The real purpose of introducing this provision was to charge higher tax at the maximum marginal rate in respect of income / expenditure / investment on the assessee who fails to explain the nature and source of said income/expenditure/investment.

Sub-section (2) provides that notwithstanding anything contained in the Act, no deduction in respect of any expenditure or allowance shall be allowed to the assessee under any provisions of the Act in computing his income referred to in clause (a) of sub-section (1). Up to AY 2016-17 there is no prohibition on set off of loss although deduction in respect of any expenditure or allowance is not allowed. Further, the claim of deduction under Chapter VI-A is debatable and is not specifically restricted by sub-section (2) of section 115BBE of the Act.

Thus, the provisions of section 115BBE applies to all assessees –

- irrespective of the legal status i.e., it applies to individuals, HUFs, firms, LLP, co-operative society, AOP, BOI, political party, etc.;
- irrespective of their residential status i.e., it applies to residents as well as non-residents
- including those covered by presumptive taxation under sections 44AD / 44ADA / 44AE
- it does not provide for minimum threshold limit i.e., it is applicable even to the smallest of amount of unexplained income if the amount is chargeable under the specified sections.

Taxability of undisclosed income from AY 2017-18 onwards

As mentioned above, there are three amendments applicable from AY 2017-18 onwards and all three amendments are made at different points in time. Let us analyse the three amendments in their respective order.

The 1st amendment is by the Finance Act, 2016 with effect from AY 2017-18. In the said amendment, the Finance Act, 2016 has amended sub-section (2) to prohibit setting off of any loss against income of the nature referred to in specified sections 68 to 69D. Before this amendment, the deduction of any expenditure or allowance was not allowed against the undisclosed income forming part of sections 68 to 69D. Consequently, from AY 2017-18 onwards, current year and brought forward losses are also not allowed to be set-off against the undisclosed income covered within the ambit of section 115BBE of the Act. However, it may be noted that the said restriction of setting of losses does not apply to years prior to AY 2017-18.

The 2nd amendment is by the Taxation Laws (Second Amendment) Act, 2016 w.e.f. 1-4-2017

1. From AY 2019-20 onwards, Health & Education Cess is payable @ 4% as against 3% up to AY 2018-19

i.e., AY 2017-18 onwards. The amendments made by the Taxation Laws (Second Amendment) Act, 2016 are drastic and has far reaching implications going forward.

Subsequent to demonetisation announced on 8th November 2016, there were views expressed by professionals / peers that the undisclosed income held in the form of demonetised currency can be deposited in the bank and the said amount can be offered for taxation under specified sections. Consequently, tax on the said income may be paid under section 115BBE @ 30% plus applicable surcharge and cess and in which case, the person may not be subject to penalty.

It was with a view to prevent such practice and to overcome the views expressed, the amendments has been made to section 115BBE of the Act.

Chapter II of the Taxation Laws (Second Amendment) Act, 2016 amends existing provisions of sections 115BBE and also introduces a new section 271AAC in the Act.

The Statement of Objects & Reasons appended to the Taxation Laws (Second Amendment) Act, 2016, *inter alia* states the object and purpose of introducing PMGKY as under –

> "1. Evasion of taxes deprives the nation of critical resources which could enable the Government to undertake anti-poverty and development programmes. It also puts a disproportionate burden on the honest taxpayers who have to bear the brunt of higher taxes to make up for the revenue leakage. As a step forward to curb black money, bank notes of existing series of denomination of the value of five hundred rupees and one thousand rupees (hereinafter referred to as specified bank notes) issued by the Reserve Bank of India have been ceased to be legal tender with effect from 9th November, 2016.
>
> 2. ***Concerns have been raised that some of the existing provisions of the Income tax Act, 1961 could possibly be used for concealing black money.*** It is, therefore, important that the Government amends the Act to plug these loopholes as early as possible so as to prevent misuse of the provisions. The Taxation Laws (Second Amendment) Bill, 2016, proposes to make some changes in the Act to ensure that defaulting assessees are subjected to tax at a higher rate and stringent penalty provision."

The President has given assent to the Taxation Laws (Second Amendment) Act, 2016 on 16 December 2016. Chapter III of the Taxation Laws (Second Amendment) Act, 2016 has amended the provisions of Finance Act, 2016 so as to provide the higher rate of surcharge on the tax amount relating to undisclosed income.

The original sub-section (1) as it stood for AY 2013-14 to AY 2016-17 and the amended sub-section (1) applicable with effect from AY 2017-18 are stated as under.

From AY 2013-14 to AY 2016-17

> "Section 115BBE(1): Where the total income of an assessee includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, the income-tax payable shall be the aggregate of
>
> (a) the amount of income-tax calculated on income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D , at the rate of thirty per cent; and
>
> (b) the amount of income-tax with which the assessee would have been chargeable had his total income been reduced by the amount of income referred to in clause (a)."

From AY 2017-18 onwards

> "Section 115BBE(1): Where the total income of an assessee,—
>
> (a) includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D *and reflected in the return of income furnished under section 139;* or

(b) *determined by the Assessing Officer includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, if such income is not covered under clause (a)*,

the income-tax payable shall be the aggregate of-

(i) the amount of income-tax calculated on the income referred to in clause (a) and clause (b), at the rate of sixty per cent; and

(ii) the amount of income-tax with which the assessee would have been chargeable had his total income been reduced by the amount of income referred to in clause (i)."

The significant amendments made by the Taxation Laws (Second Amendment) Act, 2016 are as under.

- Earlier there was no bifurcation between the income declared by the assessee in its return of income and income determined by the Assessing Officer. However, the new section 115BBE(1) covers both the situation of income declared by the assessee in its return of income under clause (a) and income determined by the Assessing Officer under clause (b).
- Further, the rate of tax applicable on the income covered under clause (a) and clause (b) will be @ 60% (plus applicable surcharge and education cess) as against the earlier rate of 30% (plus applicable surcharge and education cess).
- The rate of surcharge in the pre-amended provisions was as applicable to the legal status of the assessee as mentioned aforesaid. However, Chapter III of the Taxation Laws (Second Amendment) Act, 2016, has amended the provisions of Finance Act, 2016 to provide for the surcharge of 25% on the tax amount i.e., 25% of tax rate of 60% being 15%.

The aforesaid amendments are effective from AY 2017-18 onwards. Accordingly, the income under specified sections for earlier years will continue to be governed by the pre-amended provisions irrespective of the fact that the assessments of such years are completed after the AY 2017-18. In this connection, one can rely upon the decisions of Jaipur Tribunal in the case of *ACIT vs. Sanjay Bairathi Gems Ltd - [2017] 84 taxmann.com 138* and *ACIT vs. Satish Kumar Agarwal - [2018] 96 taxmann.com 373.*

Prior to the enactment of the Taxation Laws (Amendment Act), 2016 there could have been a question as to whether an assessee, on his own, could offer certain amounts for taxation under the provisions of sections 68, 69, 69A, 69B, 69C and 69D. It is now clear that items which could have been taxed by the provisions of sections 68 to 69D can also be offered for taxation by the assessee in his return of income by paying tax, on or before the end of the previous year, at the rates mentioned in section 115BBE.

Thus, the total incidence of tax in respect of income of the nature referred to in specified sections of 68 to 69D is 77.25% (60% + 15% surcharge + 2.25% education cess).

Since the amendment to section 115BBE made by the Taxation Laws (Second Amendment) Act, 2016 is effective from 1st April 2017, a question arises as to whether it is retroactive since it covers cases where income of the nature referred to in specified sections pertains to the period from 1st April 2016 to 8th November 2016. In other words, is the section applicable to acts done before its enactment.

A statute is retrospective when it takes away or impairs any vested right acquired under the existing laws, or creates a new obligation, or imposes a new duty, or attaches a new liability in respect of transactions or considerations already past. A substantive law determines the rights and liabilities of the parties concerned, whereas procedural laws govern the manner in which such rights or obligations are to be enforced or realized. A law applicable to the assessment is the law as it stands in the year of assessment and not that during the year in which the income was earned.

In this matter, the reference may be made to the Supreme Court decision in the case of *CIT vs. Scindia Steam Navigation Co. Ltd. [1961] 42 ITR 589* wherein it was held that total income has to be computed in accordance with the law existing as on 1st day of the assessment year.

The rate of tax on income subjected to tax under section 115BBE of the Act is specified in the Act itself and not in the annual Finance Act. The Taxation Laws (Second Amendment) Act, 2016, inter alia, amended the provisions of section 115BBE of the Act so as to enhance the rate of tax from 30% to 60% and the same is effective from 1st April 2017 i.e., AY 2017-18 onwards and accordingly, it will apply to AY 2017-18 onwards.

Subsequently, section 115BBE of the Act is amended 3rd time by the Finance Act, 2018 with retrospective effect from 1st April 2017.

Sub-section (2) of section 115BBE begins with a non-obstante clause and provides that no deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee under any provision of this Act in computing his income referred to in clause (a) of sub-section (1). Thus, before the above amendment sub-section (2) by the Finance Act, 2018, it provided that no deduction in respect of any expenditure or allowance or set-off of any loss shall be allowed to the assessee under any provision of the Act in computing his income referred to in clause (a) of sub-section (1) which deals with unexplained income reflected in the return of income furnished under section 139.

In order to rationalise the provisions of section 115BBE, the amendment has been made in the said sub-section (2). Thereby, the provisions of sub-section (2) which restricts the deduction for any expenditure, allowance or set off of any loss are now applicable to the entire sub-section (1) i.e. whether undisclosed income is offered by the assessee in its return of income under clause (a) or determined by the Assessing Officer under clause (b).

Some of the other important points in section 115BBE are as under.

- It was debatable and continues to be a debatable question as to whether deductions under Chapter VI-A are allowable against such income.
- Clause (a) covers income referred to in specified sections which has been reflected in return of income furnished under section 139. Such income reflected in a belated return under section 139(4) or in a revised return furnished under section 139(5) would certainly be covered by clause (a).
- Pre-requisite for revising a return of income is "discovery" of omission or any wrong statement in the return of income filed by the assessee. Consequently, income covered by specified sections which is reflected in revised return after issue of notice by the AO may not be regarded being covered by clause (a).
- Return furnished under section 153A of the Act is regarded as if it is a return filed under section 139 of the Act and therefore it appears to be arguable proposition that a disclosure in the return filed under section 153A would be regarded as covered by clause (a). It could be debated as to whether a return filed under section 153C could be regarded as being covered by clause (a).
- However, income referred to in specified sections which has been reflected in returns furnished under section 148 will not be covered by clause (a) as the same is not furnished under section 139.

Penalty provisions under section 271AAC

The Taxation Laws (Second Amendment) Act, 2016 has inserted the provisions of section

271AAC to provide for the levy of penalty on the undisclosed income taxed in accordance with the provisions of section 115BBE of the Act.

Irrespective of whether the case of the assessee falls under clause (a) or clause (b) of section 115BBE(1), the rate of tax is 60% plus surcharge plus cess. However, the levy of penalty depends on whether the case of an assessee falls under clause (a) or clause (b) of 115BE(1).

The section 271AAC provides that penalty can be levied if the income assessed includes income of the nature referred to in specified sections and if the assessee has not included such income in his return of income or having included it in the return of income has failed to pay tax on such income before 31st March of the previous year. In other words, the penalty may not be levied under section 271AAC if the undisclosed income referred to in sections 68 to 69D are offered to tax in the return of income by the assessee *suo-motu* and the tax liability as provided in section 115BBE is paid on or before the end of the relevant previous year. Therefore, if 100% of the tax liability is not paid before 31st March of the previous year, the penalty may be applicable as provided in section 271AAC. However, there is no immunity from penalty if the undisclosed income is determined by the Assessing Officer.

The penalty is payable @ 10% on the basic tax rate of 60% (excluding surcharge and education cess). Accordingly, the penalty payable will be 6% under section 271AAC of the Act. If penalty under section 271AAC is also levied then the incidence of tax would be increased to 83.25% (60% + 15% surcharge + 2.25% education cess + 6% penalty).

Further, section 271AAC also provides that no penalty under the provisions of section 270A (Penalty for under-reporting and misreporting of income) shall be imposed upon the assessee. Also, section 271AAC further states that the provisions of sections 274 and 275 i.e., for Procedures and Bar of limitation for imposing penalties, respectively, shall as far as may be, apply in relation to the penalty referred to in this section.

The other important points to be taken care if income relating to undisclosed income is offered to tax in the return of income by the assessee on its own are as under.

- Assessee will be liable to pay interest under section 234C of the Act, if assessee in his return of income declares income under specified sections but does not pay advance tax in accordance with the provisions of the Act.
- Belated returns will be subject to payment of interest under section 234A and default in payment of advance tax will trigger interest under section 234B.
- In a case where advance tax paid is more than 90% of the tax payable but less than 100% of the tax payable, interest under section 234B may not be leviable but the assessee will not be entitled to claim immunity from penalty.

Conclusion

To conclude, the unexplained income referred to in section 68 to 69D was taxed @30% plus applicable surcharge and cess under section 115BBE from AY 2013-14 to AY 2016-17. Thereafter, from AY 2017-18 onwards, the aforesaid income has been charged to tax @ 60% plus surcharge @25% plus education cess @ 3%, the effective tax rate comes to 77.25%. Also, the penalty under section 271AAC may be levied @ 10% of the basic tax amount chargeable under section 115BBE which would be 6% leading to effective tax rate of 83.25%. In order to avail benefit of immunity from penalty, the assesse may disclose the unexplained income referred to in aforesaid sections in his return of income and pay the full amount of tax under section 115BBE on or before end of the relevant previous year.

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CA Priti Shah & CA Rohit Katariya

Relevance of Black Money Act

1. Introduction

The saying – "The nation should have a tax system that looks like someone designed it on purpose" by William Simon fits perfectly in today's era of globalisation. The Gordian Knot of tax evasion and generation of black money, which results into huge tax revenue losses to governments, have awakened all countries to design a legislation for such menace.

In India as well, the problem of tax evasion and generation of black money is not new-fangled and it primarily ensues through two sources. The first source being activities which are not permitted by law, such as crime, drug trade terrorism, and corruption. The second includes legally permissible activities, not accounted for and / or reported to revenue authorities, which may result in tax evasion. To impede the first source, the Government of India has introduced various laws like the Benami Transactions (Prohibition) Act, 1988, the Prevention of Corruption Act, 1988, the Prevention of Money Laundering Act, 2002 ("PMLA"), etc., over the years. However, for the latter source, no detailed and distinct regime was framed by the Government for the long run except steps in the form of demonetisation in the year 1946 and 2016; Voluntary Disclosure Scheme in the year 1951 and in the year 1997-98 and other measures in the form of amendments to the Income-tax Act, 1961 ("ITA") etc. Also, the disclosure of foreign assets in the return of income was introduced in 2012. Further, an extended period of 16 years (in place of 6 years) for issuance of reassessment notice in cases involving foreign assets was also prescribed w.e.f. 1st July 2012. Even such measures were not as effective as envisaged to achieve the objective of unearthing undisclosed money. Therefore, there was a need to recognise serious and habitual tax evasion as a crime and implement a harsh distinct tax regime of fiscal and penal consequences to provide effective deterrence against tax evasion.

With this backdrop, the Government enacted a new law in 2015, called the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 ("BMA"). This has put India right ahead on the world map as it becomes one of the most aggressively legislating country and maybe the first ever country to frame a statute specifically on the subject of black money. The BMA aims at implementing a separate regime for taxation of any undisclosed foreign income and assets with severe penal consequences against the tax evaders in respect of their undisclosed money stashed abroad.

2. Purpose of BMA

Before dealing with the provisions of BMA, it would be necessary to know what triggered its origination. Given below are some illegal sources leading to generation of red money and legal sources generating black money. For tax laws purposes, the treatment of red money and black money is alike.

(a) Corruption

Corruption is by and large, a major source of black money. For petty consideration, large tax evasion is ignored, which is never detected. Even stringent measures, such as search and seizures or surveys, adopted by the department have proven to be least effective in detecting any *mala fide* cases of tax evasion due to rent seeking tendencies.

(b) Hawala Transactions

Another major source of black money is 'hawala' transactions. The 'hawala' system of illegal money transfer is also directly linked to terrorist financing.

(c) Drug Trafficking

Drug trafficking is a global black market dedicated to the cultivation, manufacture, distribution and sale of drugs, the funding for which primarily comes from black money.

(d) Tax Havens

The tendency of countries to levy high taxes has led to the birth of tax havens, offshore jurisdictions or mid-shore jurisdictions. This has pumped up the amounts of black money in such tax havens.

(e) Banking Secrecy Norms

The banking secrecy norms in tax havens have further supported tax evasion as they refuse to share any information of bank accounts held by any person to anyone which means lack of transparency.

With this insight, let us now delve into the provisions of BMA.

3. Whom does BMA apply to?

The provisions of BMA do not apply to all persons. Hence, before applying BMA, it is fundamental to analyse whether one is covered under BMA. Section 2(2) of BMA defines the term "assessee" to mean a person –

a) Being a resident other than not ordinarily resident in India in terms of section 6(6) of the ITA;

b) By whom tax or any other sum of money is payable under BMA; and

c) Every person who is deemed to be an assessee in default under BMA.

The term person includes individual, HUF, company, firm, AOP, BOI, local authority and every artificial juridical person not covered above. Therefore, the term "assessee" hereunder is wide enough to cover every resident person barring individuals, HUFs and Trusts who are not ordinarily resident in terms of section 6(6) of the ITA. The provisions of BMA are not applicable to non-residents as they are taxed only in respect of their Indian sourced income. In the recent ruling of the Hon'ble Mumbai Tribunal[1], it was held that the provisions of BMA are applicable only to residents and are not applicable to non-resident assessees.

It would be interesting to determine whether a person who is a dual resident would be considered as an "assessee" under BMA. The BMA and the ITA are in *pari materia* and must be read together. Thus, where the residential status of a person under the ITA is determined pursuant to the application of tie breaker rule under a duly negotiated Double Taxation Avoidance

1 Hemant Mansukhlal Pandya TS-670-ITAT-2018(Mum) dated 16th November 2018

Agreement ("DTAA"), the provisions of DTAA should also be taken into consideration while determining his residential status under BMA. Therefore, if a person is considered as a non-resident in India under the ITA, by virtue of the tie breaker rule, then such person shall also be considered as a non-resident under BMA. Hence, BMA shall not apply to such person. This is clarified by the CBDT in Question No. 6 of FAQs issued *vide* Circular No. 15 of 2015 dated 3rd September 2015.

Further, the liability to pay tax alone is not a *sine qua non* for a person to be regarded as an assessee under BMA. Even if a person is liable to pay any other sum under BMA (such as penalty) he shall be considered to be an assessee for the purpose of BMA.

The term "assessee in default" is also not defined under BMA but the persons covered under this term have been referred to in section 30(4), 30(5) and 32(14). While section 30(4) and section 30(5) deal with an assessee who fails to pay tax arrears or installments respectively, section 32(14) deals with the failure of a debtor of the assessee to pay the sum due to him towards recovery of his arrears under BMA.

4. Which income or assets does BMA cover?

This comprehensive new law is to specifically deal with income and assets which are parked outside India by residents and which have escaped tax in India. Section 3(1) provides that every assessee shall be taxed in respect of his total undisclosed foreign income and assets. Section 2(12) defines the term "undisclosed foreign income and asset" to comprise of two elements –

a) the total amount of undisclosed income of an assessee from a source located outside India, referred to in section 4 and computed in the manner laid down in section 5 and

b) the value of an undisclosed asset located outside India, referred to in section 4 and computed in manner laid down in section 5.

The expression "undisclosed foreign income" has not been defined under BMA and hence, recourse is taken from the definition of "income" as provided u/s. 2(24) of the ITA. There could be issues where the foreign source countries characterize and tax the income in a different manner than the ITA. The term "undisclosed asset located outside India" is defined u/s. 2(11) to mean an asset (including financial interest in any entity) –

a) located outside India;

b) is held by assessee in his name or as a beneficial owner; and

c) assessee offers no explanation about the source of investment or the explanation given by him is in the opinion of the Assessing Officer ("AO") unsatisfactory.

To interpret the term "financial interest", reference may be drawn to instructions for filing income-tax return issued by the CBDT. Since the term is not defined under BMA and the ITA, this is the only proximate source of information for interpreting the said term, it would have persuasive value.

Further, the term "beneficial owner" is not defined under BMA but is defined under Explanation 4 to section 139 of the ITA. In many instances, the foreign assets are held by residents, underneath the mask of non-residents, by means of a nominee agreement. By virtue of such an agreement, whether the resident person shall be treated as a beneficial owner under BMA?

The crux of the aforementioned provision lies in the requirement that the assessee, being the legal or beneficial owner of an asset located outside India, has to offer a satisfactory explanation regarding the source of investment in the asset. Where the explanations offered are adequate, the provisions of BMA shall not apply even though the asset has not been disclosed in the return of income. While the provisions of the ITA, such as Section 68, Section 69, already cover such instances relating to foreign assets acquired from income from unexplained sources, it is important to note that the consequences under BMA are much more stringent.

Further section 3(1) empowers the AO to assess undisclosed foreign asset as and when it comes to the knowledge of the AO, irrespective of the year to which it pertains. Therefore, the provisions of BMA can be triggered even if the asset was acquired by a person prior to previous year 2015-16, in the year when he was resident.

Section 4(1) of BMA provides that foreign income is considered undisclosed if the income is from a source located outside India and if -

a) the same is not disclosed in the return of income for the relevant year filed u/s. 139(1)/(4)/(5) of the ITA; or

b) in respect of which return of income was required to be furnished but not furnished within the time specified u/s. 139(1)/(4)/(5) of the ITA.

Therefore, as per section 2(11) r.w. section 4, action under BMA can be initiated only if foreign income is not disclosed in the original / revised / belated return. In the recent ruling of Hon'ble Madras High Court in the case of *Srinidhi Karti Chidambaram*[2], the proceedings under BMA were quashed as the assessee had filed a revised return u/s. 139(5) and disclosed the details of foreign assets.

5. Onus on whom?

BMA presumes that the accused has the required culpable mental state for an offence under the Act i.e., he had the intention, motive or knowledge of a fact or belief in, or reason to believe, a fact to commit an act considered an offence under BMA. The onus to prove non-culpability beyond reasonable doubt is shifted to the accused. Considering that penal consequences are being imposed, it is a cause of concern that legislators have sought to shift the burden of proof onto the accused. Even as per section 114(g) the Indian Evidence Act, 1872, Courts can presume existence of certain facts if the person liable to produce evidence which could be and is not produced, which if produced would have been unfavourable to the person who withholds it. Therefore, when a person liable to disclose his foreign assets fails to do so, the onus to prove he is non-guilty shall be on the assessee and not on the department. This is a major shift that BMA has introduced compared to the ITA; where in certain instances, onus of proof is also on the department.

6. What are the consequences under BMA?

The consequences on undisclosed income and assets under BMA and the ITA are tabulated hereunder:

	BMA	**ITA**
Tax	30%	78%[3]
Penalty	Three times of tax i.e., 90%	10% of tax i.e., 7.8%
Total liability	120%	85.8%

Note that while computing the above total amount of undisclosed foreign income and assets under BMA and ITA, no deduction in respect of any expenditure or allowance or set off of any loss shall be allowed. Therefore, it is evident that the consequences under BMA are much harsh as compared to the ITA, since the total liability under the former exceeds the value of undisclosed income and assets.

Further, BMA contains no provision for foreign tax credit for taxes paid outside India as juxtaposed to the ITA. This will lead to double taxation of incomes and the assessee will have to pay 120% of the undisclosed income or asset even after paying taxes outside India.

2 TS-658-HC-2018 (Mad.) dated 2nd November 2018

3 Including Surcharge @ 25% and cess @4%

As per section 49 and 50 of BMA, in case of wilful failure to furnish return of income in relation to foreign income and assets before the expiry of the relevant assessment year or having filed the return of income, there is a wilful failure to furnish details relating to foreign income and assets in the same, the defaulting person shall be punishable with rigorous imprisonment for a term ranging from 6 months to 7 years in addition to penalty of ₹ 10 lakh. Even as per the ITA, the imprisonment term is the same for wilful failure to furnish return of income if the tax sought to be evaded exceeds ₹ 25 lakh and in any other case a rigorous imprisonment for a term ranging from 3 months to 2 years.

7. Impact of BMA

As explained above, the ITA lays down a wider scope to deal with worldwide unexplained income and assets of residents and Indian sourced income and assets of non-residents, whereas the provisions of BMA are largely restricted to deal with undisclosed foreign income and assets of residents. This would still make one ponder - why BMA is enacted as a separate legislation? In the following paragraphs, an attempt is made to analyse the reason behind enacting this draconian law:

Predicate offence

The White Paper on Black Money, 2012 has clarified that black money not only includes wealth earned from illegal means but also from legal sources. Owing to this, tax evaded is treated at parity with proceeds of crime under the provisions of BMA.

Section 88 of BMA amends the Schedule of PMLA to include "offence of wilful attempt to evade any tax, penalty or interest referred to in section 51 of BMA" as a scheduled offence. Under PMLA, all offences listed in the Schedule are considered as predicate offence[4] and the occurrence of the same is a pre-requisite for initiating investigations into the offence of money laundering. The term "predicate offence" has been defined under Article 2(h) of the United Nations Convention Against Corruption which means any offence as a result of which proceeds have been generated that may become the subject of an offence as laundering of proceeds from crime.

Accordingly, the income-tax evasion by the assessee apropos foreign income and assets has been brought within the scope of money laundering. The upshot of this landmark change by the Government (i.e., by introduction of BMA r. w. PMLA) would be that investigation against the assessee can be carried out by both, the income-tax authorities and Enforcement Directorate, which may lead to simultaneous prosecution under the respective laws. Now, a question arises as to how the objective of the Government to bring back the black money stashed abroad by Indian citizens can be achieved by treating an offence under BMA as a predicate offence?

Many countries treat tax evasion as a civil offence and therefore, whenever the Indian authorities sought information from foreign counterparts with respect to Indian residents, having foreign bank accounts or assets, the same was turned down on the ground of confidentiality obligations either on the account of bank secrecy laws or skewed provisions of the DTAAs. To outstrip this drawback, the amendment in the Schedule to PMLA is mooted through the route of BMA thereby making tax evasion a criminal offence and opening a new recourse for the Indian tax authorities to gather vital information from their foreign counterparts. Following options are now possibly available to the Indian tax authorities to counter black money –

(a) Financial Action Task Force ("FATF")

The FATF was founded with the objective to set standards and promote effective implementation of legal, regulatory and operational measures for combating *inter*

4 Q13 FAQs on PMLA dated 1st May 2013

alia money laundering[5]. India was granted a full-fledged membership in June 2010. This is where BMA acts as a facilitating agent. Since an offence under BMA is included as a scheduled offence under PMLA, prosecution proceedings could be triggered not only under BMA, but also under PMLA. Hence, once PMLA gets triggered, India would be in a position to co-ordinate and to seek co-operation from FATF member nations for the reason that money laundering is a criminal offence for each member of the FATF.

(b) United Nations Convention against Corruption ("UNCAC")

In 2011, India became the 152nd country to ratify the UNCAC. One of the purposes of this Convention is to promote, facilitate, and support international co-operation and technical assistance in the prevention of and fight against corruption including in asset recovery.

The Convention requires the States to criminalise laundering of proceeds of crime, obstruction of justice, and illicit enrichment. Further, it requires countries to have mechanisms for freezing, seizure, and confiscation of the proceeds of crime and cooperate in criminal matters by extradition and mutual legal assistance to the greatest possible extent. One of the fundamental objectives of the Convention is the return of assets for which member countries shall provide full cooperation and assistance.

As per the aforesaid explanation, BMA treats tax evasion as money laundering and proceedings under PMLA can be initiated. Under PMLA, property or records of the person involved in money laundering can be attached, frozen or seized. Thus, India now has a legislature which provides a mechanism for freezing, seizing and confiscation of the property outside India. Therefore, being a member of UNCAC, India can avail the cooperation of the member nations for establishing title of property or income belonging to any resident assessee.

8. Sources of Information

The above procedure can be smoothly carried out only when Indian authorities have information about the tax evaders. Section 10 of BMA provides that assessment can be initiated under BMA on receipt of information from an Income-tax authority under the ITA, from an authority under any law for the time being in force (FEMA, Customs, etc.) or any information coming to the notice of the AO.

Under the ITA, for assessment u/s. 147 or 153A, the AO should be in possession of information on basis of which he has a reason to believe that income was not taxed. Also, it is essential that the information so possessed by the AO should be duly authenticated and verified by him. The Hon'ble Mumbai Tribunal, in the recent case of *Hemant Mansukhalal Pandya*[6], held that no addition can be made on the basis of an unauthenticated and unverified document. While the powers of the AO are quite narrow in scope under the ITA, the AO has been given unfettered powers under BMA. Under the latter, there is no requirement for the AO to have a reason to believe and this makes BMA a lethal law. Further, in exercise of the powers conferred upon him, the AO can serve a notice under BMA on the basis of a report published in a newspaper or on the basis of any unauthentic and unofficial information made available through any website / blog. Further, the AO can also rely on stolen or leaked data to initiate the proceedings under BMA. Thus, information regarding offshore investments made by residents obtained by the AO through the various information leaks such as the Swiss leak, the Panama papers, the Paradise papers etc. can be used for initiation of assessment under BMA.

5 http://www.fatf-gafi.org/about/

6 TS-670-ITAT-2018(Mum) dated 16th November 2018

India has negotiated DTAAs with other countries over the years to insert Articles for Exchange of Information by way of Protocol. Further, India has been proactively engaging with foreign governments, for exchange of information under other agreements such as Tax Information Exchange Agreements ("TIEAs"), Multilateral Convention on Mutual Administrative Assistance in Tax Matters ("MAC") and South Asian Association for Regional Co-operation ("SAARC") Multilateral Agreement. These steps have enabled India to receive information from foreign countries of financial information through Automatic Exchange of Information ("AEOI"). The information under the AEOI will include information of controlling persons (beneficial owners) of the asset. Similarly, India has also entered into information sharing agreement with the USA under the Foreign Account Tax Compliance Act. Apart from the above, there can be other sources of information such as the Schedule FA that has been incorporated as a part of the ITR Form *vide* Finance Act, 2012.

With respect to Switzerland, India has proactively amended the India-Switzerland DTAA through a Protocol in the year 2011 for exchange of information on a request basis concerning taxes covered by the Agreement. In addition to the above, India and Switzerland are also signatories to the MAC and the Multilateral Competent Authority Agreement ("MCAA"). Pursuant to the same, AEOI is activated between the two countries for sharing financial account information, effective from 1st January 2018, with first transmission in September 2019. Accordingly, India will receive information of financial accounts held by Indian residents in Switzerland for 2018 and subsequent years, on an automatic basis.

It is pertinent to note that all the information obtained regarding the foreign bank accounts or assets shall not automatically mean that they represent black money stashed abroad. There may be a case where the account belongs to an NRI or has already been disclosed and therefore, only after proper assessment any tax or / and penalties shall be levied. This is in accordance with the intent of the Government to not tax *bona fide* cases.

9. Conclusion

The baptism of new parallel legislation by the Government in the form of BMA effectuates severe consequences in the form of penalty of three times of the tax payable as juxtaposed to penalty embodied in the ITA of either 10%[7] or 50% / 200%[8] of the tax payable. Correspondingly, BMA also comprehends more stringent legislation which exposes the offender to PMLA by characterising the offence as a predicate offence.

Before we conclude, this article would be incomplete if no mention is made about the income derived by NRIs from sources in India which are undisclosed in the foreign country where they now reside. It should be noted that the shift in the legislature to deal with black money is not only prevalent in India, but even other countries are taking such initiatives. Like India, UK, in its Finance Act, 2017, introduced 'Requirement to correct' legislation which required disclosure of undeclared offshore tax liabilities in respect of foreign income and assets by 30th September 2018. In the absence of any disclosures, it shall tantamount to 'failure to correct' and will attract higher penalties. Australia also has established Black Economy Taskforce in 2016 to combat black money in Australia and their recommendations are soon going to be effective from 1st July 2019.

Therefore, with rampant change in each country's domestic laws, advancement of technology and with effective mechanism in place for exchange of information between countries all over the world, circumventing the provisions of BMA, by way of any mask, to stash money in any jurisdiction without paying taxes, may no longer be possible. Thus, BMA, being a draconian law, may help the Government to end the era of the black money economy in the future.

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7 Under section 271AAC

8 Under section 270A

SS-III-53

Ashwani Taneja, *Advocate*

Relevance of Benami Act

How far shall the menace of additions under sections 68 and 69 to 69D of Income-tax Act, 1961 haunt under the regime of new Benami Law

Fundamental Theme

The most complex question which most of us face now-a-days, is if any assets such as share capital, loans, gifts, gold/jewellery, cash, immovable property or an investment/ expenditure in any other form is discovered by any investigative agency; then would the same be subject to provisions under section 68 to 69D of the Income-tax Act or would these be attached as benami property by the authorities under the Benami law? Further questions arise such as whether action can be taken only in any one of the legislations or there can be simultaneous action under both the Acts? Thus the question arising here is "what is going to be the interplay between these species of legislations? Are they **mutually exclusive or cumulative?"**

It is quite often seen that there are various types of transactions which are roped in by the Assessing Officers under sections 68 to 69D of the Income-tax Act, 1961. Let us analyse a few such transactions by taking real life situations which have been faced by certain taxpayers after introduction of the new Benami Law, as contained in Prohibition of Benami Property Transactions Act, 1988 (in short referred to as **PBPT**).

Chronicles of Benami Transactions

Bogus Share Capital

Situation I

A search operation by the Income Tax Department takes place upon the premises of R Ltd. During the course of search, Mr. R (director-cum-shareholder of R Ltd.) is required to surrender some undisclosed income on the insistence of search officials. Accordingly, Mr. R makes aggregate surrender of ₹ 100 crore and also deposits the amount of tax payable thereon. The break-up of the amount so surrendered contains amongst other disclosures, share capital amounting to ₹ 20 crore received by R Ltd. from B Ltd. During the course of search operation, the statement of Mr. R was recorded wherein he explained as to how the said share capital was routed. It was explained by him that cash of equivalent amount was provided by him to B Ltd., who in turn issued the cheque of equivalent amount to R Ltd. and accordingly R Ltd. issued shares to B Ltd. In the light of such disclosures the search operation was concluded.

Subsequently, notices are issued by the Initiating Officer (hereafter referred to as 'IO') under section 24(1) of PBPT Act to all of the aforesaid three parties namely B Ltd, R Ltd. and Mr. R, wherein it was alleged that aforesaid transaction of share capital is a benami transaction. A Provisional Attachment Order (PAO) is also passed by IO under section 24(3) by making attachment of sum of ₹ 20 crore in the bank account of R Ltd., for the following alleged reasons:-

1) Ltd is not the real owner of the share certificates.

2) Consideration was provided by Mr. R and not by B Ltd. for subscribing into share capital.

3) Mr. R is the real owner of the share certificates and thus beneficial owner under PBPT Act.

4) R Ltd. is benamidar of the aforesaid share capital as per PBPT Act.

5) A sum of ₹ 20 crores lying in the bank account of R Ltd. is benami property liable to be confiscated under PBPT Act.

Now in the aforesaid given situation, we need to evaluate as to what extent and in what manner can the reasoning and action of the IO be justified under the provisions of PBPT Act.

Let us analyse the transaction and the reasoning of IO in a 'step by step' manner:-

a) In this case the admitted position is that cash was paid by Mr. R to B Ltd. And B Ltd. in turn paid the sum via cheque to R Ltd. towards subscription of share capital. Therefore, admittedly the consideration has not been provided by B Ltd. Hence, the IO can strongly assert that first condition of section 2(9)(A) is satisfied.

b) The share certificates are issued by R Ltd. in the name of B Ltd.:

   Because of the admission of Mr. R, it can be *prima facie* alleged by the IO that B Ltd. does not enjoy the true ownership rights of the share certificates. Thus, it can be strongly asserted that B Ltd. does not hold the impugned asset (i.e., share certificates) for its own benefit, but for the benefit of Mr. R who provided the consideration. Accordingly, in the given facts he can at the best hold B Ltd. as Benamidar but NOT R Ltd. as has been done by him, as per provisions of PBPT Act, 1988.

c) The IO's action of treating the amount of ₹ 20 crore lying in the bank account of R Ltd. as benami property:

   In my view, the IO's action is not in accordance with law because in this transaction what can be best described as benami property, if at all, are the share certificates issued to B Ltd. in its name on account of the consideration provided by Mr. R and thus what could be matter of attachment is the share certificates only, and not the amount deposited in the bank.

However, there could be some debate on this issue because one may also contend that the amount received by way of cheque by R Ltd. is also benami property in as much as the amount received by R Ltd. from B Ltd. actually belongs to Mr. R.

However, this reasoning would not be sound as when R Ltd. received the cheque, it issued its share certificates to B Ltd. in lieu of the cheque so received and thus the transaction stood squared off in the books of R Ltd.

The next important thing left to be determined here would be the nature and characteristics of share certificates issued by R Ltd. in favour of B Ltd. in the context of PBPT Act.

In my view, in the aforesaid peculiar facts, the IO can very well contend that the real ownership of these share certificates and control is not with B Ltd. but with Mr. R and thus these are benami property of which B Ltd. is benamidar and Mr. R is beneficial owner in terms of corresponding provisions of PBPT.

Situation II

Now let's twist the facts here to explore another situation. In the aforesaid facts if cash is paid directly by R Ltd. to B Ltd. then the question may arise as to whether there will be any change in identification and characterisation of the alleged benami property.

The reasonable contention in the light of the changed facts would be that in lieu of cash, B Ltd. issued cheque to R Ltd. and thus transaction stood squared off in the books of B Ltd. Similarly, R Ltd. issued share certificate in lieu of cheque received by it. Therefore the transactions also got squared off in the books of R Ltd. Hence, the moot point is about determination of nature and characteristics of share certificates issued and registered in the name of B Ltd.

In the given situation, one may very well contend that the share certificates registered in the name of B Ltd. are actually beneficially owned by R Ltd. and not by B Ltd. and thus B Ltd. is simply a benamidar and R Ltd. the beneficial owner as per provisions of PBPT Act.

Situation III

Let us examine a third situation where B Ltd. gives cheque to R Ltd. (in lieu of cash received by B Ltd. from Mr. R) on account of **'loan'** (and NOT on account of share capital) on which interest is payable by R Ltd. say at the rate of 12% per annum.

In my view, in this scenario also the inference shall remain the same to the extent that the first transaction has gotten squared off in the books of B Ltd. and when R Ltd. issued acknowledgement of the same which is then shown as a 'loan asset' by B Ltd. in its balance sheet. What is to be evaluated and determined is the nature and characteristic of said 'loan asset' shown by B Ltd. in its books of account. Here also, the Initiating Officer may very well assert and allege that the loan asset is not owned by B Ltd. but Mr. R and B Ltd. is merely benamidar of said asset as per the provisions of PBPT Act.

In my view, it is very important to observe that in all the above three situations if any property could be held to be benami, it could only be the share certificates / loan assets held in the name of B Ltd. and **NOT** the amount of cheque issued by B Ltd. from its bank accounts. The said cheque amount cannot be even termed as proceeds from sale of a benami property. Thus by no stretch of imagination, the said amount can be made a subject matter of attachment under section 24(3) or 24(4) of PBPT Act. Any such action done by the IO would be illegal per se.

The opponents of the above view may also contend that there would not be any benami property in any of the aforesaid three situations in as much as there is no actual asset in existence here. The argument made by them here is that the share certificates or the loan assets are dummy assets and that dummy assets cannot be treated as benami property.

Though, the argument looks to be quite logical, it is flawed in as much as the admitted facts here show that the impugned assets very much exist on paper and are duly registered and held in the name of B Ltd. Thus, the authorities implementing the benami law would strongly contend that one of the objectives to bring out benami law is also to capture such kinds of benami assets which are actually parked in the name of some benamidar and its enjoyment is done by the beneficial owners. The asset may be created in physical form, on papers or in any dummy form, however so long as its beneficial interest is hidden or lies somewhere else it has to be identified as benami property. This is imperative so as to dig out all the benami properties and prosecute real offenders and to clean the economy of such transitions / assets. The arguments are quite strong from both the sides, but the law available before us is vague and incomplete. All such issues would finally be settled through suitable legislative amendments under the law and/or judgments of higher courts.

Further, all said and done, whatever may be the final position as interpreted by the courts with respect to determination and attachment of benami property, one thing is clear that the consequences of making a surrender (whether forced or voluntary) during the course of search and survey carried out during the income tax proceedings are now far more disastrous than what these used to be until new PBPT Act had not spread its tentacles.

Legal position where no 'admission' or 'surrender' is made

In the three situations dealt above it was presumed that there was a clear admission that cash was originally paid by Mr. R or R Ltd., and that B Ltd. did not have any beneficial interest. However the question arises that, if there is no admission from any party and additions are made by Assessing Officer under section 68 of Income-tax Act 1961, by treating the amount of share capital / loan received by the company as unsubstantiated, then whether on the basis of such additions can the IO under PBPT Act treat such share certificate / loan assets as benami property and such shareholders / loan creditors as benamidar and such assessee (or alleged payer) as beneficial owner?

On properly breaking down the legal provisions, I am of the well thought out view that though the undiluted principles might remain same, there would a material change on account of huge distinctions in the parameters of onus of proof as stipulated in the two pieces of legislation i.e., Income-tax Act 1961 and PBPT Act. It is a well accepted fact that the fabric of Income tax law is woven in such a fashion that various additions and disallowances are made by the Assessing Officer also on a deemed basis since the income tax law permits the Assessing Officer to do so, e.g., addition on account of deemed dividend under section 2(22)(e) and additions under sections 68 to 69D of the Act and so forth and so on.

However, the fabric of Benami Law is totally different in this regard. The perusal of provisions of the PBPT Act, 1988 show that under this law no deeming actions are permitted to be done on the part of IO. Even otherwise, it is well settled position of law coming from various courts including the Hon'ble Supreme Court that the burden to prove a property as benami property is upon the person who asserts it so. Ready reference can be made to the landmark judgment of the Supreme Court in the case of *Jaydayal Poddar vs. Bibi Hazra, [(1974) 1 SCC 3].*

There would therefore be heavy burden cast upon the Initiating Officer to lay down concrete initial proof that the aforesaid share certificates / loan assets are benami property and to do so the IO could be duty bound under the law to bring out positive evidences on record to demonstrate that cash came from the coffers of Mr. R or R Ltd. and that B Ltd. does not have any beneficial control and interest over such assets. Merely because an Assessing Officer under the income tax proceedings deemed the said asset as unexplained and accordingly deemed it as the unexplained income of R Ltd, it would not *ipso facto* give powers and jurisdiction to the IO under the PBPT Act to presume a state of fact and then treat it as benami property and hold B Ltd. as benamidar and R Ltd. or Mr. R as beneficial owner on a deemed basis.

Let us analyse a few more transactions which may be hit under sections 68, 69 to 69D of the Income-tax Act 1961.

Unexplained expenditure/investment

Apart from the issues arising under section 68 of the Income-tax Act we quite often face transactions which are treated as unexplained expenditure/investment by the Assessing Officer. One of the most pertinent question here would also be as to if any item/ transaction is covered by the Assessing officer under section 69 to 69D of the Income tax law whether the same would still be liable to be covered under PBPT Act? Let's try to analyse on the basis of some real life examples as discussed under:

Cash Catch

A car going from Delhi to Chandigarh is intercepted by the Police and a huge sum of cash is recovered which is handed over to the Income Tax department. There were 2 passengers in the car namely Mr. A and Mr. B and when the interrogation is done by the Income tax department it is informed by Mr. B that cash was delivered to him by Mr. Y, with the instructions to deliver it further to Mr. Z. Then interrogation is done of Mr. Z who denies any knowledge of Mr B and the cash. Thereafter inquiry is done from Mr. Y who claims that cash was handed over to him by Mr. X for onward delivery to Mr. B.

In a nut shell, the real source and ownership of the cash is not explained by any person. Thus, under these circumstances the investigation wing of the Income tax department hands over the matter and all the statements recorded of all these persons to the Benami Prohibitions Unit (BPU).

Thereafter the BPU makes requisite enquiry from Mr. B and treats the amount of cash as benami property and Mr. B as benamidar and holds that the identity of the beneficial owner is not known. Under these circumstances let us analyse whether action of the IO is justified. The first question to be decided here is whether the impugned amount of cash is liable to be dealt with under section 69 of the Income-tax Act or under benami law or it can be covered under both?

In my considered view, the scope and object of new Benami Law is to deal with the assets held in the name of a person, whose real owner is someone else. So the first question that would arise here is that whether 'cash' can be said to be held in the 'name' of any person, because cash is not registered or titled in the name of any person. The ostensible ownership of cash is always considered by way of its possession. As per my thoughts and analysis, if the ownership of the cash is admitted and accepted in hands of the possessor, then the operation of Benami Law would be ousted and in that case it would be liable to be examined under section 69 of the Income Tax Act only. On the other hand, if the person in whose possession cash is found denies it's ownership, then it would be difficult for an Assessing Officer to make its assessment under section 69 of the Income-tax Act, 1961 in the hands of such person. That is where the real role of Benami Law comes into play. In the given scenario, since Mr. B denied any kind of ownership of impugned amount of cash, the benami law officer got an occasion to examine it under the provisions of PBPT Act.

If we analyse provisions of Section 2(9) of the PBPT Act which defines benami transaction we find that its clause (D) may be relevant here and therefore reproduced hereunder for ready reference

2. In this Act, unless the context otherwise requires,—

(9) "benami transaction" means,—

(D) a transaction or an arrangement in respect of a property where the person providing the consideration is not traceable or is fictitious.

A reading of clause (D) suggests that the IO may very well contend that the cash (property) is held by Mr. B as a result of a transaction/ arrangement where the person providing the consideration is not traceable or fictitious and therefore impugned amount of cash recovered falls under the purview of benami transactions and is a benami property under section 2(8), being subject matter of benami transactions and the benamidar is Mr. B and beneficial owner is not known.

It may be quite interesting to note that the definition of beneficial owner which as per section 2(12) means ***a person, whether his identity is known or not, for whose benefit the benami property is held by a benamidar.***

Thus, as per law it is not mandatory for the IO to identify the beneficial owner before declaring a property to be a benami property. However, a word of caution to be kept in mind here is that though it may not be necessary to identify the beneficial owner, it is essential for the IO to demonstrate and accordingly give a finding that the beneficial owner of the alleged beneficial property is someone other than the alleged benamidar. I would not hesitate in mentioning that the aforesaid views are highly debatable and subject to various 'ifs and buts'. The law contained in PBPT Act is highly vague especially in absence of any statements of subjects, explanatory notes to the clauses or any other background material. Therefore a better picture would emerge when lot of churning is done before the courts and accordingly views are expressed by the courts.

Jewellery Tale

The position with regards to gold, diamond or jewellery being movable property and not being capable of being registered in the name of a particular person would be similar. However, the attempt to explain the ownership of the same may be made by a person in whose possession it is found with the help of supporting bills/ invoices. The underlying principles for its treatment under sections 69-69D of the Income-tax Act *vis-a-vis* section 2(9) of the PBPT Act would broadly remain the same as discussed above in the case of cash. Undoubtedly there would be some variation in the practical approach of various officers depending upon situations and mode and manner of recovery of such assets.

Anecdote of Shares

Let us now analyse the possibility of treatment of shares held by a person as benami property. The shares are registered and held in the name of a particular person. Hence the approach to be followed by officers would be slightly different as compared to the other movable assets as discussed above for choosing the proper course of action for making assessment under sections 68 to 69D, or covering the same under the net of Benami Law. If the shares are found to be registered in the name of say Mr. B, but it is found by the concerned officers that consideration for its acquisition was say provided by Mr. R and it is also found that there shares are beneficially enjoyed by Mr. R and not Mr. B, then it would be a simple and straight case of shares being benami property where Mr. B would be benamidar and Mr. R would be beneficial owner.

On the other hand, if it is found by the officer that the shares are registered in the name of Mr. B and held by Mr. B but he is neither able to explain the source for providing the consideration for its acquisition nor is he able to prove that its consideration is provided from disclosed sources and there is nothing in the possession of the IO to suggest that the shares are not beneficially held by Mr. B, then the IO has no jurisdiction to treat the same as benami property. However, the Assessing Officer would be very much within his rights to make an addition under section 69B in the hands of Mr. B. Similar principles can be followed for treatment of all such properties which are or capable of being legally registered in the name of a particular person e.g. debentures, bonds, FDRs, immovable properties and so forth and so on.

Corporate veil : How far it survives under Benami Law

It is quite often seen that many companies are found struggling with the issue raised by the Assessing Officer in the assessment proceedings for substantiation of amount of cash credits in the form of share capital/loans received by them. If the assessing officer finds that the assessee company is not able to discharge its onus as stipulated under section 68 of Income-tax Act 1961 to explain the nature of source of any such sum, then the same may be deemed to be income of assessee and added as such under section 68 of Income Tax Act, 1961. However, the next question that arises under such cases is that under the PBPT Act proceedings, up to what extent can the IO go in making attachment of the properties of any such company where the addition has been made under section 68 of Income-tax Act, 1961. In other words, under such cases where addition has been made under section 68, whether the Initiating Officer can make attachment of the amount or also the properties acquired by the company from such amount or both or none. This is one of the most frequent questions which is being analysed on both sides i.e., Benami Law officers on the one side and professionals and their clients who are affected under this law on the other side.

Before proceeding further on this issue, it is relevant here to recapitulate that company duly incorporated under law of the land is treated as separate legal juristic person under the eyes of law which is different from its shareholders. The shareholders may have beneficial interest in the assets of the company through their shareholding in the company but they are never deemed to be owner themselves of the assets/ properties of the company. The principles in this regard were laid down way back in the case of *Mrs. Bacha F.Guzdar vs. CIT [SC (1955) 27 ITR 0001]/ Salomon vs. Salomon & Co Ltd [UKHL 1, AC 22 (1897)],* wherein it was clearly laid down that there is a **corporate veil** between the shareholder and the company which cannot be lifted except through the due process of law.

Thus, coming back to the issue before us, the amount treated as unexplained income in the hands of the company may be unexplained income of that company or shareholder or any other person, however once the said amount comes in domain and control of the company and the company becomes its rightful owner then it cannot be categorised as a benami property.

Further, in any case, the assets / properties acquired by the said company from such amounts are assets of the company acquired in its own right and control and shown as such in its balance sheet. Thus, under these circumstances the company would be its legal as well as it's beneficial owner and therefore benami law would have no application. If the IO alleges otherwise, then it will be his primary obligation to prove it so and that too with the help of positive and cogent evidences to prove and demonstrate that the said assets / properties are beneficially enjoyed by certain other person(s) and NOT by the said company and that the said company is holding it only for the name sake purposes. Thus, it will be an altogether different exercise to be done by IO within the framework of provisions of the PBPT Act and read with relevant provisions of the Indian Evidence Act, 1872 and other applicable allied laws. In any case, the IO does not have the power or justification to treat such assets/ properties as benami on deemed basis merely for the reason that the original amount of share capital or loan received by it was not found to be properly substantiated in the opinion of the IO or the Assessing Officer during income tax proceedings.

Buying benami property for loved ones

It is like a ritual in our country for an individual to buy property in the name of loved ones viz spouse, children, parents, brothers or sisters. Fortunately, the PBPT Act, 1988 excludes such transactions from the definition of benami transaction as contained in section 2(9)(A). However, there is a serious rider to claim the benefit of such exclusion. The Act stipulates that the consideration for such property has been provided or paid out of **'known sources'** of the individual who has bought such property.

However, if the IO finds that the consideration is not paid or provided out of **'known sources'** of the individual, then he may refuse to give the benefit of exclusion and may thus treat such property as benami property and such individual as beneficial owner and the other person as benamidar of such property.

The story does not end here. The assessing officer may also require such an individual to explain and substantiate source for acquisition of such property in terms of section 69S to 69 D of the Income-tax Act, 1961 and in case he is not satisfied with the explanation, he may make addition to the taxable income of such individual on account of consideration paid or provided for buying such property. Thus, there would be parallel action under both the laws.

However, next question that arises here is that what is meaning of the expression **'known sources'**. It may be noted that usually the expressions used so far in other legislations have been like "disclosed sources…" or "declared sources….." or "out of the sources on which tax has been paid…"etc. However, this kind of expression 'known sources' has been used for the first time to my knowledge. Thus, how it will be different from 'disclosed/declared sources' is matter of interpretation and debate. The PBPT Act, 1988 has not defined the meaning of the expression 'known sources', therefore everyone will make its own guess to find out contextual meaning of this expression as has been used by the legislature. One thought that comes here is that expression 'known sources' is wider than the expression 'disclosed/declared sources'. Thus, something which can be described and has proper identity should fall within the scope of the said expression. It can be something disclosed/declared and also something though not disclosed/declared but otherwise known or identified which can be described. But to be covered within the meaning of 'disclosed/declared' the nature of the amount should be the one which has been disclosed/declared to Income Tax or other authority.

Further, the other important aspect to be noticed here is that the legislature has not used the expression **"known sources of income**". It is because of the fact that a person may make borrowings also from where consideration may be paid. Thus with a view to take care of such a situation, the word 'income' has been removed on the recommendation made by the **Standing Committee on Finance** of the Parliament in its 28th Report presented before Parliament on 28th April, 2016.

Beware of the 'catch'

In addition to the aforesaid rider, in order to claim the benefit of exclusion of the property purchased in the name of brother, sister, parents, lineal ascendant or descendant, there is one more requirement as per the law that there should be **joint ownership** of the person providing the consideration along with the person in whose name property is purchased. If the property is not in joint ownership, then it may fall in the definition of Benami Transaction and may be treated as Benami Property and then all the consequences as provided under the law may follow.

Interplay with other laws:

Before concluding our discussion on the topic, I would like to draw the attention of the readers upon two very significant provisions of PBPT Act, 1988:

Section 60 of PBPT, 1988 provides that the application of other laws is not barred. It states that the provisions of this Act shall be in addition to, and not, save as hereinafter expressly provided, in derogation of any other law for the time being in force.

Similarly, **Section 67** provides that this Act shall have overriding effect. It states that the provisions of this Act shall have effect, notwithstanding anything inconsistent therewith contained in any other law for the time being in force.

From combined reading of aforesaid two provisions, following distinctive features of this new law can be noted:-

1) The provisions of PBPT Act, 1988 operate in addition to the provisions of any other law. In other words, it is quite possible that in any given situation, Benami Law, Income-tax Act, Prevention of Money Laundering Act, 2002 as well as any other law can be applied simultaneously if requisite conditions of application of any such law exist. Thus, in other words the application of Benami Law is not mutually exclusive to application of any other law and *vice-versa*. A person may have been given clean chit under Income Tax provisions, but it would not mean that he would be automatically given clean chit under Benami Law also. Thus, it would purely depend upon the facts and the circumstances of the case leading to the violation in concerned laws. Thus, Benami Law may have a multiplier effect also.

2) **PBPT Act, 1988** has overriding effects on the provisions contained in any other law. However, in many cases it is noted that few Initiating Officers in their orders (i.e., Statement of Case) have missed out one important point that PBPT Act's provisions shall have overriding effect only where there is a provision in any other law which is inconsistent with the provisions of PBPT Act. Thus, if there are no inconsistent provisions in Benami Law applicable to a particular scenario, the effect of the provisions of other laws are not barred or nullified. For example, Section 91 and Section 92 of "Indian Evidence Act" provide that where documentary evidence and oral evidence are compared, then documentary evidence shall have precedence over the oral evidence. As there is no contrary provision in this regard in "The PBPT Act", any authority under Benami Law cannot simply disregard the provisions of Section 91 and Section 92 of Indian Evidence Act by simply taking shelter of Section 67 of "The Prohibition of Benami Property Transactions Act", 1988.

Conclusion

It is to be carefully noted that the fabric of benami law is structured in a unique manner. Adequate care needs to be taken now by the citizens of this country to ensure that no benami transaction is done by them, either knowingly or otherwise. Further, there is a heavy onus placed upon the professionals to ensure that all the replies/clarifications under Income-tax or any other law should not be filed in any careless or casual manner as this could lead to pushing his clients into the deep well of Benami Law. Further, the replies to notices and submissions under the benami law need to be submitted, right from the stage of Initiating Officer, after properly appreciating the fine principles of this law. Any incorrect or wrong information may put his client as well as concerned professional into difficulty.

All said and done, this is a new law and mostly vague so far. It is yet to evolve with the help of court judgments and suitable amendments or clarifications from the legislature. Thus, views expressed herein are personal views based upon my thinking, observations and experiences gained from day-to-day handling of the proceedings before the Initiating Officers, the Adjudicating Authority and the Appellate Tribunal. I hope I shall be pardoned by the readers for something stated herein inadvertently which is felt to be inaccurate or imperfect.

(The author is a former member of Income Tax Appellate Tribunal and is presently practising as lawyer as partner of the law firm M/s. RRA TaxIndia, Advisors and Advocates, New Delhi appearing before Benami Law authorities as well as before High Courts and Supreme Court. He can be reached at ashwani@taxindia.net)

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CA Dinesh Tejwani

TECHnovation

2018 : Technology Trends in Audit, Tax and Accounting

As the year 2018 comes to an end, it is time to look back and see evolving technology trends in audit, tax and accounting domain. While several startups in this area received substantial venture funding, few privately owned companies too demonstrated innovation.

Accounting

New technologies are bringing innovation to accounting systems e.g., artificial intelligence. At the same time startups are coming up with unique marketing ideas to get millions of subscribers.

One such example is Wave accounting. This Canadian startup has only one pricing model: Free. This Toronto based company with total funding of 82 million dollars has been offering its cloud-based accounting software free since 2009. Today it boasts of a user base of 3.5 million! It started with an advertisement driven revenue model. The practice of showing advertisement on its pages was discontinued in Jan 2017. Currently, the company has three revenue models. These modules are payment processing, payroll and lending.

In Japan, online accounting software Freee raised 60 M$ Series E funding, taking its total funding to 143 M$. Started in 2013, this company claims to have captured 38% of cloud-based accounting market share with 1 million business users and 5,000 certified advisors

It will be in place to talk about Xero: the poster child of tech startups in New Zealand. The company which started in 2007 to re-imagine accounting today boasts of over 1 million users across 180 countries. The company is listed on Australian Securities Exchange and has a market capitalisation of 4.15 B$ (As on 29-11-2018). The tagline of the company was "Beautiful Accounting Software" and now changed to "Beautiful Business".

Back in India, Tally continues to be the market leader with 1.5 million licensed customers, and it is believed that there is a market of 5 million pirated software users. However, cloud-based accounting companies like QuickBooks and Zoho are taking full advantage of digital technologies in their solutions and are appealing to millennials and a new breed of entrepreneurs.

Zoho Corporation, the company operating in seven countries with its headquarters at Chennai, launched Zoho Books in 2017. It offers easy integration with other Zoho applications, business workflow automation, fetches bank transactions, offers document tagging with accounting entries among other innovative features.

Accounts Payable and Receivable

This is one area, which seems to has seen major funding activity in the USA. Most of these startups are targeted towards small and medium businesses and are trying to bring automation in order-to-cash and procure-to-pay processes. The aim is to reduce time and cost of processing bills and collect payments.

For making the procure-to-pay process easy, these startups provide various features like

- Received bills by e-mail
- Dragging bills to the app
- Get requisite approvals from team members
- Pay electronically or get cheques printed and mailed
- Automated entries of purchase and payment in accounting systems

For order-to-cash, various innovative features provided include

- Speedy invoicing *via* mobile apps
- Reminders to customers for payment
- Multiple payment options for electronic payment
- Auto update of accounting entries

Few prominent startups with major funding this segment are AxidXchange with 574 M$, Bill.com with 222 M$ and BillTrust with 104 M$. All the three companies are US based.

AvidXchange is integrated with over 100 accounting systems and offers ACH (Automated Clearing House) bank-to-bank payments.

Talking about India, Tally and Zoho have initiated e-payment features but are limited to only one bank at the moment. Zoho recently launched integration with ICICI bank wherein one can directly receive payment from customers and make payment to vendors from within the accounting system. Tally has integration with DBS Bank for making direct payment to vendors.

Asset Management

For asset-heavy industries like oil and gas, electricity etc., drones are increasingly being used for asset inspection. Not only these drones reach areas where sending humans may be difficult, but they are also being enhanced with artificial intelligence to analyse visual images to generate useful data. Example: detection of a crack in a railway track. Drone inspection by IBM Maximo is one such application used in asset maintenance.

Ernst and Young too is working on a project to use drones for inventory counting as part of digital audit capabilities. The tool is being tested for inventory count at factories as well as retail outlets.

Tax

Tax filing automation continues to draw more startups and funding by VCs. Let us begin by the story of Indian startup ClearTax. This October, ClearTax raised 50 M$ in Series B taking its total funding to 65 M$.

The company started by offering income-tax filing solutions to taxpayers and added GST and TDS filing solutions for businesses and tax professionals.

Later it added investment in mutual funds to its platform, which it believes goes well with its objective of tax filing and tax saving easier for taxpayers, especially millennials. According to the company's website, 2.1 million tax returns (against 1 million in 2016) were filed on its platform during 2018 and over 80,000 businesses used its GST filing platform

TaxFyle: This US-based startup recently received Series A funding of 4 M$. It offers easy to use tax filing platform for individuals and small businesses and is used by about 40,000 taxpayers. It offers 40% cost savings as compared to the filing by retail tax shops

Audit

The audit is fast moving towards cloud-based, paperless and interactive project management platforms. Now artificial intelligence and blockchain technologies are further changing the shape of the audit.

One example of excellent use of artificial intelligence is AppZen. This Silicon Valley startup has received funding of 53 M$. It uses its patented AI technology to audit 100% of expenses reports, invoices and contracts to flag high-risk policy violations, inconsistencies. This helps to accelerate the employee reimbursement process. The tools automatically detect duplicate expense claims, out of policy spend, travel and booking violations, weekend and holiday spend and corrupt practices. The analytics by the tool is then able to flag top violators. The app claims to be far more productive and effective than even a large team of auditors.

For business contracts, the tool is able to find out discount term violations, non-applied rates, duplicate invoices, duplicate charges, pricing violations, payment terms violations and vendor frauds.

Another US-based company AuditBoard has raised 44 M$ so far. It aims to streamline the audit universe by offering a fully integrated platform for SOX, operational audit, Compliance and Enterprise Risk Management.

Practice Management Software

For tax practitioners, practice management tools too are getting good investor interest

Canopy is one such suite which has received funding of 72 M$. It provides a suite of application for practice management, tax resolution, notices and transcripts. It aims to provide a more modern and convenient experience to clients and at the same time bringing efficiency to the tax practitioners office.

Future of our profession

These developments leave us with several questions and doubts about the future of audit, tax and accounting. Let us examine three scenarios:

Will accountants be replaced by robots?

There are discussions that technologies like robotic process automation (RPA), artificial intelligence will make accountants redundant. Today a lot of work involves working across diverse systems, collecting and inputting data. RPA is a technology where a software or robot is configured to process a transaction automatically. This processing may involve capturing data from an existing application, interpreting an manipulating it to communicate with another digital system.

Will Audit profession be dead in 10 years?

Professor David Yermack, a Professor of Finance and Business Transformation at Stern school of business presented this gloomy view in a roundtable discussion at New York University. The primary reason for this observation was emerging distributed ledger technology of blockchain will reduce the need of audit by 97%.

Will ChatBots help you file tax returns?

TaxBot, an Australian chatbot is making an effort to file simple tax returns by chatting with taxpayers like a human, gathering information in the process, analysing it with its artificial intelligence and then complete the tax return in less than 5 minutes!

H&R and IBM are working to train IBM the language of taxes. This technology is being applied to tax preparation interviews with tax pros. The end result is that Watson (the AI tool from IBM) is able to understand the context of queries, interpret responses and then suggest credits or available deductions.

Conclusion

While there is no 100% answer to the above questions, one thing is very clear: the way we work is definitely changing and will change more in times to come. In the last 30 years we have moved from manual books of account to computerised accounting, from paper-based filings to eFilings. During this process, we needed to reskill ourselves.

Secondly, these technologies are still at an early stage and far from being perfect. Cost of adoption and mindset of businesses is also a challenge these technologies will face.

But these technologies will sure change our work profile. While accountants may no longer work on business processes, they will still be required to configure the "robots" that will do automatic processing. While blockchain may do away with the need to do a major part of the routine audit, auditors will still be required to apply judgment on accounting standards for true and fair presentation of financial data. For tax laws, advisory by human will never be replaced by AI-powered chatbots.

It makes sense to keep oneself abreast of these developments and learn new skills.

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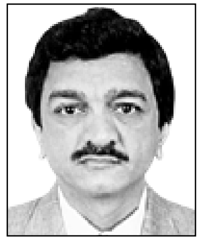

B. V. Jhaveri, *Advocate*

DIRECT TAXES

Supreme Court

Disallowance u/s. 14A to be restricted to the amount of exempt income only and not at a higher figure

PCIT vs. State Bank of Patiala, Supreme Court [(2018) 99 taxmann.com 286 (SC)]

The Department had filed Special Leave Petition in the Supreme Court against the judgment of the High Court of Punjab & Haryana in the case of *Pr. CIT vs. State Bank of Patiala reported in 99 taxmann.com 285 (for A.Y. 2010-11)* wherein the Punjab & Haryana High Court followed its earlier decision in the case of *Pr. CIT vs. State Bank of Patiala reported in 393 ITR 476 (for A.Y. 2009-10)* decided on 27th February, 2017 wherein their Lordships of the Punjab & Haryana High Court held as under:

> "After hearing learned counsel for the parties, we notice that the issue on merits has been decided in favour of the assessee in State Bank of Patiala's case *[(2017) 391 ITR 218] (for A.Y. 2008-09).* The amount of disallowance under section 14A was restricted to the amount of exempt income only and not at a higher figure. Once that was so, we do not consider it appropriate to discuss the scope of Section 263 of the Act as the same has been rendered academic in view of the issue being answered in favour of the assessee on merits. Thus, no substantial question of law arises. Consequently, the appeal stands dismissed."

Their Lordships of Punjab & Haryana High Court also relied upon their earlier decision in ITA No. 193 of 2017 dated 22nd May, 2017 (for A.Y. 2010-11) in the case of *Pr. CIT vs. State Bank of Patiala.*

Against the aforesaid order of their Lordships of the Punjab & Haryana High Court dated 14th November, 2017 in the case of *Pr. CIT vs. State Bank of Patiala*, the SLP was filed before the Supreme Court. The said SLP was dismissed both on the ground of delay as well as on merit.

In view of the aforesaid dismissal of the Special Leave Petition of the Department on merit against the order of the Punjab & Haryana High Court dated 14th November, 2017, the Hon'ble Supreme Court has approved the conclusion of the Punjab & Haryana High Court to the effect that the amount of disallowance u/s. 14A is to be restricted to the amount of exempt income only and not at a higher figure.

Paras S. Savla, Jitendra Singh, Nishit Gandhi, *Advocates*

DIRECT TAXES
High Court

1. Reassessment – Section 147 of Income-tax Act, 1961 – Reopening on the ground that the assessee had not filed Return of Income whereas the same was filed – Possibility of application of section 50C mentioned in the affidavit – in reply but not in reasons recorded – Though the AO may be correct about applicability of section 50C notice issued under section 148 is bad in law [A.Y. 2010-11]

Mumtaz Haji Mohmad Memon vs. ITO [2018] 408 ITR 268 (Guj.)

The assessee before the Hon'ble Gujarat High Court was an individual. During the year 2009, the assessee, along with two other co-owners, sold an immovable property for a declared sale consideration of ₹ 50 lakh. In the return filed for the relevant assessment year 2010-11, the assessee disclosed the sale and after adjusting the cost of improvement and indexed cost of acquisition, offered a sum of ₹ 2,45,900/- by way of capital gains. The return filed by the assessee was not taken for scrutiny assessment. The AO issued notice under section 148 of the Act on the ground that the assessee has not filed return of income for the year under consideration i.e., 2010-11 and had not offered the capital gains that arose out of sale consideration to tax. The assessee filed his objections wherein he has brought factual matrix of his case that he has filed return of income for the year under consideration and also declared the capital gains on such sale consideration. The AO rejected the objections raised by the assessee. In such order, he recorded that the co-owner had declared the total sale consideration of the property at ₹ 1,18,95,000/-. Further, the report received from the Sub-Registrar, Surat, would show that the market value of the said property was determined at ₹ 1,18,95,000. He was therefore of the opinion that the assessee should have shown his share of the sale consideration at ₹ 39,65,000/-, in spite of which, he declared the sum at ₹ 16,66,667/-. Primarily on these grounds, the objections were rejected. Notably, the Assessing Officer did not make any comment on the assessee's contention that return of income was filed. Being aggrieved by the order passed by the AO rejecting the objections the assessee filed a writ petition before Hon'ble Gujarat High Court. Hon'ble High Court observed that the reasons proceeded on two fundamental grounds. One, that the property in question was sold for a sum of ₹ 1,18,95,000/- ; and two, that the assessee had not filed the return and that therefore his 1/3rd share out of the sale proceeds was not offered to tax. The High Court held that both these factual grounds are totally incorrect as it was admitted by the Revenue. It was undisputed that the assessee had actually filed the return of income for the said assessment year and also offered his share of income of the declared sale consideration to tax as capital gains. The High Court observed that the Assessing Officer may have dispute with respect to computation of such capital gains, he cannot simply dispute the fact that the assessee did file the return. Importantly, even the second factual assertion of the Assessing Officer in the reasons recorded was totally incorrect, as he referred to said sum of ₹ 1,18,95,000/- as a sale price of the property. The High Court held that the Assessing Officer may be correct in pointing out that when the sale consideration as per the sale deed is ₹ 50 lakh but the registering authority has valued the property on the date of sale at ₹ 1,18,95,000/- for stamp duty calculation, section 50C of the Act would apply, of course, subject to the riders contained therein. However, this was not the cited reason for reopening the assessment. The reasons cited are that the assessee filed no return and that 1/3rd share of the assessee from the actual sale consideration of ₹ 1,18,95,000 therefore, was not brought to tax. These reasons were interconnected and interwoven. In fact, even if these reasons are seen as separate and severable grounds, both being factually incorrect, the Revenue simply could not have hoped to salvage the impugned notice. The court further held that through the affidavit-in-reply a faint attempt has been made to entirely shift the centre of the reasons to a completely new theory, viz., the possible applicability of section 50C of the Act. However, the reasons recorded nowhere mentioned this possibility. Reasons recorded, ignored the fact that the sale consideration as per the sale deed was ₹ 50 lakh and that the assessee had by filing the return offered his share of such proceeds by way of capital gains. The court thus quashed notice issued u/s. 148.

2. Appeal to Appellate Tribunal – section 253 of the Income-tax Act, 1961 – Scope of Rule 27 of Income-tax (Appellate Tribunal) Rules – Assessee entitled to defend order of the Commissioner of Income Tax (Appeals) on all grounds including on grounds held against it without filing a cross-objection. [A.Y. 2001-02, 2002-03]

PCIT vs. Sun Pharmaceutical Industries Ltd. [2018] 408 ITR 517 (Guj.)

The assessee before the Hon'ble Gujarat High Court was a company engaged in various businesses including manufacturing pharmaceuticals. For relevant assessment years, the assessee had filed the return of income computing income in terms of section 115JB. The AO issued notice under section 148 for the both the assessment years and finalised the assessment making various additions and disallowances. On appeal, CIT(A) allowed the appeals of the assessee by accepting the assessee's grounds against the additions made by the AO. However, on the question of validity of reopening of the assessments, the learned CIT(A) held against the assessee. The department being aggrieved preferred to appeal before the Tribunal. Since the assessee was not aggrieved by the order passed by the learned CIT(A), it had not preferred any appeal. It did not even file a cross-objection against the departmental appeal. Later on, relying on Rule 27 of the Income-tax Appellate Tribunal's Rules (Rules), the assessee challenged the validity of the re-assessments before the Tribunal. Despite objections from the revenue, the Tribunal permitted the assessee to raise such contentions and ultimately held that the notices for reopening of assessments in both the years were bad in law and declared them as invalid. The department challenged the

Tribunal order before the Hon'ble Gujarat High Court under section 260A of the Act. Hon'ble High Court observed that rule 27 of the rules makes it clear that the respondent in appeal before the Tribunal even without filing an appeal can support the order appealed against on any of the grounds decided against him. It can be easily appreciated that all prayers in the appeal may be allowed by the Commissioner (Appeals), however, some of the contentions of the appellant may not have appealed to the Commissioner. When such an order of the Commissioner is at large before the Tribunal, the respondent before the Tribunal would be entitled to defend the order of the Commissioner on all grounds including on grounds held against him by the Commissioner without filing an independent appeal or cross-objection. The High Court observed that Rule 27 of the Rules is akin to rule 22, Order XLI of the Civil Procedure Code. Sub-rule (1) provides that any respondent, though he may not have appealed from any part of the decree, may not only support the decree but may also state that the finding against him in the court below in respect of any issue ought to have been decided in his favour. The High Court decided the question against the Revenue and in favour of the Assessee.

3. Capital Gains – Section 50 of the Income-tax Act, 1961 – Sale of land along with building for development purposes – consideration received only for land – Section 50 is not applicable [A.Y. 2004-05]

Jaidayal Prannath Kapur vs. ITO [2018] 408 ITR 315 (Mad.)

The assessee, a partnership firm, was dealing in purchase and sale of paper. The assessee filed its return of income for the year under consideration 2004-05 showing a loss of ₹ 40,486/-. The AO finalised the assessment of the assessee by determining total income at ₹ 1,36,22,800/- by applying the provisions of Section 50 of the Act to compute the capital gains arising from the transfer of property owned by the assessee situated in Chennai on the ground that the assessee failed to furnish any concrete proof to show that only the building has been subjected to depreciation all along, and that the land was not a part of the schedule for fixed asset at any point of time. AO further contended that land was shown separately elsewhere in the balance sheet under asset projections. The AO held that the assessee had not given any satisfactory reply supported by documentary evidence and that the provisions of Section 50 of the Act are squarely applicable to the assessee's case. On further appeal, the CIT(A) as well as the Appellate Tribunal upheld the action of the AO. The assessee being aggrieved filed an appeal before the Hon'ble Madras High Court. The Court observed that land is not a depreciable asset. Section 50 of the Act deals only with transfer of depreciable assets. Once the land forms part of the assets of the undertaking and the transfer is of the entire undertaking as a whole, it is not possible to bifurcate the sale consideration to a particular asset. Section 50 of the Act applies only when depreciable assets alone are transferred. The Court observe that the assessee, *vide* letter dated December 21, 2006, had specifically stated that no depreciation was claimed on the building after March 31, 1998, and that land with the abandoned building was handed over to the developer for development, and the building was demolished. The assessee further stated that they never claimed any depreciation on the land and in the depreciation statement also, the description given was with reference to a building only. The assessee further contended that in the depreciation schedule, nowhere a land is shown as asset eligible for depreciation and that there is no rate prescribed for allowing depreciation on land. Further, the development agreement clearly stated that the land alone had been the subject of development and that the building in the land had been demolished. The Court thus held that the Assessing Officer is not correct in stating that the land sold is a short-term capital asset, on which, depreciation had been claimed.

4. Duties of the Tribunal – Tribunal confirmed the CIT(A) order by merely recording that it accepts the view of the (CIT) Appeals – Non-speaking order – Appeal restored to the Tribunal for fresh consideration [A.Ys. 2003-04 and 2004-05]

Cheryl J. Patel vs. ACIT – [ITXA Nos. 643 & 424 of 2016, Hon'ble Bombay High Court]

The Tribunal had passed its order simply affirming the order of the CIT(A) without giving any independent reasons for the same. The said order was challenged before the Hon'ble High Court. The Hon'ble High Court while remanding the appeals back to the Tribunal held that the Tribunal has not given any independent reasons showing consideration of the submissions made on behalf of the assessee. It was further held that though an appellate order which affirms the order of the lower authority need not be a very detailed order, nevertheless, there should be some indication in the order passed by the appellate authority, of due application of mind to the contentions raised by the asseseee in the context of findings of the lower authority which were the subject matter of the challenge before it. In view of above, the appeals were restored to the Tribunal for fresh consideration keeping all contentions open.

5. Assessment u/s. 153A r.w.s. 153D – Prior approval u/s. 153D – Application of mind necessary – Mechanical approval vitiates entire process – Order bad in law [A.Y. 2007-08]

PCIT vs. Smt. Shreelekha Damani – (ITXA No. 668 of 2016, Hon'ble Bombay High Court)

The question that was posed before the Hon'ble High Court was whether the mandatory approval of the Joint Commissioner of Income Tax required to be granted u/s. 153D of the Income-tax Act, 1961 ["the Act"] in respect of assessment orders passed u/s. 153A / 153C has to be judicious with due application of mind or is it a mere procedural aspect and it could be merely mechanical. The question of legality of the approval was raised by the assessee for the first time before the Tribunal. This was not a case where no approval was granted at all. The Tribunal had in this case quashed the assessment order u/s. 153A on the ground that despite the existence of approval from Additional CIT in this case, the same was without any application of mind and therefore not a valid approval as contemplated u/s. 153D of the Act. While affirming the order of the Tribunal, the Hon'ble High Court observed that the Addl. CIT recorded that he sought draft order on or before 24th December, 2010. However, the draft order for approval under Section 153D of the Act was submitted only on 31st December, 2010. Hence, there was not enough time left to analyse the issues of draft order on merit. Therefore, the order was approved as it was submitted. Clearly, therefore, the Addl. CIT for want of time could not examine the issues arising out of the draft order. His action of granting the approval was thus, a mere mechanical exercise accepting the draft order as it is without any independent application of mind on his part. The Court thus held that the Tribunal was, therefore, perfectly justified in coming to the conclusion that the approval was invalid in the eyes of law. It was further held that though the statute does not provide for any format in which the approval must be granted or the approval granted must be recorded. Nevertheless, when the Addl. CIT while granting the approval recorded that he did not have enough time to analyse the issues arising out of the draft order, clearly this was a case in which the higher Authority had granted the approval without consideration of relevant issues. Question of validity of the approval goes to the root of the matter and could have been raised at any time. As such the appeal was dismissed.

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Neelam Jadhav, Neha Paranjpe & Tanmay Phadke, *Advocates*

DIRECT TAXES
Tribunal

Unreported Decisions

1. Capital gGains – Section 2(42A) r.w.s 45 & 48 – ESOP Options provide valuable right to the Assessee to exercise and have allotment of shares. It is a capital asset. If the assessee transfers the option itself, the Capital Gains will have to be assessed as long-term Capital Gains if the options have been held for more than three years

N.R. Ravikrishnan vs. ACIT (ITA No.: 2348/Ban/2018)[Assessment Year: 2007-08], order dated 31-10-2018

Facts

The Assessee is an individual and the assessment year under consideration is A.Y. 2007-08. The Assessee filed his return of income for the impugned assessment year on 29-7-20017 declaring total income at ₹ 25,03,015/-. During the year under consideration, the Assessee did not purchase the shares for himself but transferred his "ESOP" option to Infosys Technologies Ltd and computed long term capital gains at ₹ 20,41,672/- on the contention that it was held for more than 36 months. Further the Assessee invested the said capital gains in the investment prescribed u/s. 54EC of the Act and claimed the benefit of Sec 54EC for the year under consideration. The said return was selected for the scrutiny assessment. The learned AO rejected the contention of the Assessee and taxed the same as STCG and passed an order u/s. 143(3) of the Act. The Assessee contested the said order and the matter travelled up to Hon'ble ITAT. Hon'ble ITAT set aside the order of the learned AO on the observation that the said order was passed after seeking directions of Add. AO u/s. 144A and no opportunity was given to the Assessee at that time. Thereafter, the learned AO passed a fresh assessment order u/s. 143(3) r.w.s. 254 of the Act continuing with his previous stand. Aggrieved by the same, the Assessee preferred an appeal before learned CIT(A) but did not find any success. Thereafter, the Assessee filed an appeal before Hon'ble ITAT. During the course of hearing, the learned AR submitted that since the option was held by the Assessee for more than 36 months, it was a long-term capital asset and gains arose from the said transfer were long term in nature. Whereas on the contrary, the learned DR vehemently opposed the submission of the Assessee and submitted that as prior to the vesting date, the assessee himself could not have exercised any such right and therefore, it is to be treated as STCG. After hearing both the parties, Hon'ble ITAT held as under:

Held

Hon'ble ITAT observed that both the lower authorities failed to appreciate the facts in right perspective. Hon'ble ITAT observed that the Assessee himself did not exercise his right and did not acquire any shares pursuant to the same. The Assessee simply transferred his option which was there with him for a period of more than 36 months. If ESOP options had been exercised, and the shares allotted thereby would have been sold after their allotment, then undisputedly the gains arising therefrom would have to be treated as STCG. However, in the facts under consideration, no shares were allotted to the Assessee and it is a case of buy back of ESOP options by Infosys Technologies Ltd., with Infosys BPO Ltd., the assessee's employer, as a confirming party. Hon'ble ITAT considered the case laws relied upon by the Assessee and came to the conclusion that the "ESOP" held by the Assessee for more than 36 months is a long-term capital asset. Subsequently, Sec 54EC deduction of the Assessee was confirmed by Hon'ble ITAT. Finally, the issue was decided in favour of the Assessee and against the revenue.

2. Capital Receipt vs. Revenue receipt – Section 2(24) and Section 4 – Compensation received for loss of source of income impairing its profit-making structure or sterilisation of profit making apparatus is a capital receipt not chargeable to tax

DCIT. vs. Rishabh Infrastructure Pvt. Ltd. (ITA 157/RPR/2014) [Assessment Year: 2011-12] order dated 23-10-2018

Facts

The Assessee is a private limited company and the Assessment Year is 2011-12. During the year under consideration, the Assessee received an amount of ₹ 3,01,47,107/- that was claimed as a capital receipt in the return of income and was not offered to tax. During the course of the scrutiny assessment proceedings, the learned A.O. asked the detailed explanation of the said amount. In pursuance to the same, the Assessee submitted that it had entered into a memorandum of understanding ("MOU") with another company namely "Lafarge India Pvt. Ltd." ("LIPL") for carrying out certain work. However due to the reasons beyond control, only work relating to acquisition of land, that to partly, could be undertaken by it and other activities as per the "MOU" could not be carried out at all between both the parties and they entered into another "MOU" wherein compensation was determined for termination of earlier "MOU". Further it was submitted before the learned A.O. that the aforesaid compensation was determined and received on closure/termination of its business activity resulting into "loss of source of income" impairing its profit-making structure or sterilisation of profit making apparatus and thus, it is a capital receipt not chargeable to tax. Further the Assessee had showed the said amount under the head "Reserve and surplus". The Assessee relied upon various case laws. However, the learned AO did not agree with the said explanation of the Assessee and concluded that although nomenclature used is "compensation" but the same is actually a business receipt which is revenue in nature and added the same to the returned income of the Assessee. Aggrieved by the same, the Assessee preferred an appeal before the learned CIT(A) and the said appeal was allowed in favour of the Assessee and against the revenue. Against the said order, the revenue filed an appeal before Hon'ble ITAT. Both the parties argued at length, made exhaustive submissions and relied upon various case laws. After hearing both the parties, Hon'ble ITAT held as under:

Held

Hon'ble ITAT perused the records carefully and observed that the Assessee was incorporated with the sole objective of undertaking the infrastructure development activity of construction of railway track and siding on behalf of "LIPL" which is not at all disputed by the Revenue. Further the Assessee had acquired a part of lands required for the said railway track and siding which were subsequently transferred to "LIPL" and income from the same was shown and offered as business income. Hon'ble ITAT noted that the entire work of construction of the railway track and siding was its sole business and the isolated activity of acquisition of land for such railway siding cannot be visualised. It was observed that since "LIPL" continued to remain indecisive as to execution of the entire work by the Assessee and also unresponsive to problems faced by them, the execution of work was stalled by the Assessee. Hon'ble ITAT thereafter referred to various case laws and decided the issue in favour of the Assessee and against the revenue.

Reported Decisions

3. Stay of penalty proceedings – Penalty proceedings initiated by the department u/s. 271C are stayed by ITAT when the quantum proceedings are pending before it and application of section itself is challenged in the appeal

Uber India Systems (P) Ltd. vs. JCIT (ITA 436 & 437/Mum/2018) [Assessment Year: 2016-17 and Assessment Year 2017-18] order dated 28-9-2018, [2018] 98 taxmann.com 199 (Mumbai - Trib.)

Facts

The assessee is a company incorporated under the provisions of Companies Act 1956 and is engaged in the business of providing marketing and support services to Uber B.V. incorporated under the laws of Netherlands and is a tax resident of Netherlands. The assessment years are 2016-17 and 2017-18. For both the assessment years, Uber B.V. engaged the Appellant to provide various services under Inter company service agreement. On 12-1-2018 a survey was conducted u/s. 133 (2A) of the Act at the registered office of the assessee. During the course of survey, it was observed that the assessee had made various payments to driver-partners and no tax was deducted u/s. 194C of the Act on the aforesaid payments. The department was of the view that the said section has applicability to the facts under consideration and the Assessee ought to have deducted the tax u/s. 194C of the Act. Accordingly, an order was passed which is ultimately challenged by the assessee before Hon'ble ITAT and is pending for adjudication. Meanwhile, the learned AO initiated the penalty proceedings u/s. 271C of the Act. Pursuant to the action of the learned AO, the Assessee filed a stay application before Hon'ble ITAT and requested it to stay the same. During the course of hearing, the Assessee *prima facie* established the merits of the said appeal and further contended that the applicability of sec 194C is itself in challenge in the present appeal. Further the learned AR, relying on various decisions, submitted that Hon'ble ITAT has power to stay penalty proceedings when the quantum proceedings are pending before it. On the contrary, the learned DR vehemently opposed the submission of the Assessee. After hearing both the parties, Hon'ble ITAT held as under:

Held

Hon'ble ITAT observed that the Assessee has made out a *prima facie* case in favour of the assessee proving that the outcome of the appeal before Hon'ble ITAT will directly impact the proceedings which are hurriedly being finalised by the learned A.O., which may entail huge liability by way of penalty on the assessee. Hon'ble ITAT further held that since the appeal is pending before it, the Revenue authorities should be restrained from passing any order imposing penalty on the assessee u/s. 271C of the Act however the proceedings may continue. While coming to the said conclusion, it relied upon the decisions of Hon'ble Courts in the case of *"ACIT v. GE India Industrial (P) Ltd" [2013] 358 ITR 410 (Guj.)* and *"CIT vs. Wander (P.) Ltd." [2013] 358 ITR 408 (Bom.)*. Finally, Hon'ble ITAT directed the Addl. CIT (TDS)/revenue authorities not to pass orders imposing penalty for a period of six months from the date of this order or disposal of appeal by the Tribunal whichever is earlier.

4. House property – Sec 22 – Income of the assessee from letting out space on terrace for installation of mobile tower/antenna is taxable as 'income from house property' and, therefore, deduction under section 24(a) is available

Kohinoor Industrial Premises Co-operative Society Ltd. vs. ITO, Ward-31(2)(2), Mumbai (ITA 670/Mum/2018) [Assessment Year: 2013-14] order dated 5-10-2018, [2018] 98 taxmann.com 365 (Mumbai - Trib.)

Facts

The assessee is a co-operative society and the Assessment year under consideration is 2013-14. For the year under consideration, the Assessee while filing its return of income offered its income from letting out some space on terrace for installation of mobile towers/antenna under the head "Income from house property" and accordingly claimed a deduction u/s. 24(a) of the Act. The return was selected for the scrutiny assessment. During the course of the assessment proceedings, the learned AO observed that the terrace could not be termed as house property as it was the common amenity for members. Further the assessee could not be considered to be owner of the premises since as per the tax audit report, conveyance was still not executed in favour of the society. Finally, the learned A.O. in his assessment order assessed the said income under the head income from other sources. Bring aggrieved by the same, the Assessee preferred an appeal before the learned Commissioner of Income Tax (A) but did not find any success. Thereafter, the Appeal was filed before Hon'ble ITAT. Both the parties put forth their submissions before Hon'ble ITAT. After hearing both the parties and perusing records, Hon'ble ITAT held as under:

Held

Hon'ble ITAT observed that undisputedly, the assessee has derived rental income from letting out space in the terrace of the building to mobile companies for installing their mobile tower/antenna and the terrace of the building cannot be considered as distinct and separate but certainly is a part of the house property. Hon'ble ITAT further noticed the Departmental Authorities have failed to bring on record any material to demonstrate that in addition to letting-out space on the terrace for installation and operation of antenna, the Assessee has provided any other service or facilities to the cellular operators. Thus, from the material on record, it is evident that the income received by the Assessee from the cellular operators/mobile companies is on account of letting out space on the terrace for installation and operation of antennas and nothing else. Further it noticed the fact that in no other assessment year, Assessee's claim of such income as house property has been disturbed by the learned A.O. It referred to the decisions cited by the learned AR and finally applying the rule of consistency held in favour of the Assessee and against the revenue.

5. Medical relief – Sec 11 and proviso to sec 2(15) – Charitable purpose: Where nursing school is located within hospital's premises and students of nursing school get training in hospital, both the activities are intricately connected with each other and does not hit by proviso to sec 2(15) of the Act. The Assessee trust is entitled for Sec 11 exemption

MAJ Hospital vs. DCIT- Exemption, Kochi (ITA 499/Coch/2017) [Assessment Year: 2011-12] order dated 12-11-2018, [2018] 100 taxmann.com 1 (Mumbai - Trib.)

Facts

The assessee is a charitable trust registered u/s. 12A of the Act. The Assessment year under consideration is 2011-12. The Assessee filed its return of income declaring Nil income after claiming exemption u/s. 11 of the Act. During the course of assessment proceedings, the learned A.O. treated the income received from running a hospital and nursing school as business activity and denied the exemption claimed by the Appellant. Being aggrieved, the Assessee filed an appeal before the learned CIT(A) but did not find any success. The learned CIT(A) following an earlier order in the appellant's own case observed that Assessee is entitled to exemption u/s.11 only in respect of the income received from hospital. However, with regard to the income from nursing school, the benefit of exemption u/s. 11 was denied. Being aggrieved by the same, the Assessee preferred an appeal before Hon'ble ITAT. After hearing both the sides, Hon'ble ITAT held as under:

Held

While deciding the issue, Hon'ble ITAT observed that the school of nursing run by the Trust was located in the same premises where the assessee runs the hospital. Further, the students of the nursing school get training in the said hospital. After perusing the facts, Hon'ble ITAT came to the conclusion that the hospital and nursing schools are intricately connected and dependent on each other and in fact are part of one inseparable activity. Further Hon'ble ITAT noticed that the Circular No.11/2008 dated 19-12-2008 enunciates that the activities with regard to education and medical relief are not hit by the restrictive provisions contained in the proviso to s.2(15). On the abovementioned observations, Hon'ble ITAT held in favour of the Assessee and against the revenue.

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CA Tarunkumar Singhal & Sunil Moti Lala, *Advocate*

INTERNATIONAL TAXATION
Case Law Update

A. SUPREME COURT

1. Revenue's SLP dismissed against High Court order holding that TDS was not deductible u/s. 195 on payment towards reimbursement of expenses as the assessee had no privity of contract with the service provider

Pr. CIT vs. Organizing Committee Hero Honda FIH World Cup – [TS-660-SC-2018] - Special Leave Petition (Civil) Diary No. 37870/2018

Facts

(i) The assessee organisation entered into a contractual relationship with the Federation of International Hockey (FIH) for organising / sponsoring the Men's Hockey World Cup in the financial year 2009-10.

(ii) Under the arrangements the FIH was to act as the facilitator, receiving the amounts and arranging for provisional services connected with the event (services primarily concerned with the travel, hospitality and provision of food etc.) and claimed reimbursements of payouts from the assessee, being the event organiser / sponsor.

(iii) The AO was of the opinion that the payment made to FIH by the assessee of the aforesaid reimbursements was liable for deduction of tax under section 195 of the Act, opining that the payouts also included commission which was per se taxable.

(iv) The assessee claimed that the payments were only reimbursement of the expenses, which were duly supported by documentary evidence.

(v) The CIT(A) accepted the assessee's explanation noting that the reimbursements were such that the assessee could not hold an independent inquiry into each transaction and the assessee had no privity of contract with the service providers. The Tribunal affirmed the CIT(A)'s order.

(vi) The Delhi High Court held that the findings of fact were conclusive since the lower appellate authorities, after considering the submissions and record, had held that the assessee had no privity of contract with the service provider and thus there was no substantial question of law arising in this regard.

Held

(i) The Court dismissed the SLP filed by the Revenue holding that there was no reason to interfere in the matter.

B. HIGH COURT

2. Representative assessee of foreign resident is liable for not only an income

which is deemed to have accrued in India, through a business connection, but also that which has directly arisen or accrued in India

DIT(IT) vs. Board of Control for Cricket in Sri Lanka - [2018] 97 taxmann.com 600 (Calcutta) – ITA Nos. 242 & 279 of 2008

Facts

(i) A joint management committee of India, Pakistan and Sri Lanka, [PAK-INDO-LANKA joint management committee (PILCOM)] was formed to co-host/ conduct the world cup 1996 tournament. Bank accounts were opened by PILCOM in London to be operated jointly by India and Pakistan cricket boards. In this account, moneys from sponsorships, TV rights etc., were deposited.

(ii) PILCOM paid certain amounts to eleven non-resident cricket associations for allowing to host the tournament which included certain amount paid as guarantee money. ITO(TDS) made an order under section 201(1)/194E against PILCOM demanding certain amount as tax which ought to have been deducted by it.

(iii) The Tribunal held that only that proportion of the total fund received by the cricket association of any country from PILCOM which was equal to the ratio of the number of matches played by such country in India to the total number of matches played by that country in the tournament should be considered to be income arising or accruing to the cricket association of that particular country. Tax should be deducted at source in respect of this portion of the payment made by it to a particular association.

(iv) On appeal against the above order of the Tribunal, the High Court dismissed the appeal *vide* its decision in *PILCOM vs. CIT [2011] 335 ITR 147 (Cal.),* with the observation that the order of the Tribunal did not call for any inference.

(v) The non-resident cricket associations filed return showing their income as Nil. Notice under section 148 was issued and order was passed under section 147 for all the cricket boards. The AO made an assessment of income of each assessee through PILCOM (i.e. representative assessee).

(vi) On further appeals, the Tribunal held that a representative assessee / agent is liable to tax in India on behalf of the non-resident assessee only with respect to its income which is 'deemed to have accrued in India' under section 9, whereas in the present case, as decided in its earlier order (discussed above) the income had accrued in India and not 'deemed to have accrued in India'. Therefore, it held that PILCOM could not be liable as agent under section 163.

(vii) Aggrieved, the Revenue filed an appeal to the High Court against the order of the Tribunal.

Held

(i) The Court held that section 5 divides the income in two categories viz., one which is received in India and one which arises or accrues or deemed to arise or accrue in India but may be received in India or elsewhere and section 9 merely tries to classify the income which is deemed to accrue or arise in India by saying that it should *inter alia* arise from business connection of the non-resident in India.

(ii) The Court held that only because of use of the short title to section 9, i.e. Income deemed to accrue or arise in India, does not absolve the representative assessee of the duty to account for any income which has directly arisen to the non-resident in India.

(iii) Thus, it held that the Tribunal misunderstood the law in holding that since the income earned by the non-resident cricket boards were held to have directly arisen in India, this income could not be deemed to have arisen or accrued to the non-resident in India and the responsibility of the representative assessee was confined to only accounting for income which was deemed to have arisen in India.

(iv) The Court held that section 160 makes it abundantly plain that a representative assessee would represent a non-resident assessee in respect of his income specified in section 9 and thus the representative assessee not only represents an income which has directly arisen or accrued in India but also that which has indirectly arisen or accrued in this country, through a business connection.

(v) Accordingly, the Court affirmed the orders of the AO and the CIT(A) and set aside the Tribunal's order, stating that points left open by the Tribunal may be decided by it in accordance with law.

C) Tribunal Decisions

3. Conversion of CCPS into equity shares is not a taxable transfer – Conversion does not involve an 'exchange' as the preference shares cease to exist – Sale of the resulting equity shares on conversion will be a taxable transfer – Gains on sale to be calculated on the basis of cost of the original preference shares

Periar Trading Company Private Limited vs. ITO [TS-659-ITAT-2018(Mum.)] Assessment Year 2012-13

Facts

(i) Periar Trading Company Private Limited (the "Assessee") participated in a rights issue of Trent Limited ("the Company") and subscribed to 1,634 compulsorily convertible preference shares ("CCPS") of the Company at INR 550 per share for a total consideration of INR 2,83,98,700 (approx. USD 400,000). The CCPS were automatically convertible into equity shares of the Company in ratio of 1:1.

(ii) The Assessing Officer ("AO") treated the conversion as a taxable transfer and taxed INR 2,85,01,968 (approx. USD 400,000), being the difference between the fair market value of resulting equity shares of the Company and cost of acquisition of the CCPS, as long-term capital gains.

(iii) CIT(A) relying on rulings of the Bombay High Court in *CIT v. Santosh L. Chowgule [1998] 234 ITR 787* and the *Andhra Pradesh High Court in ACIT vs. Trustees of H.E.H. The Nizam's Second Supplementary Family Trust (1976) (102 ITR 248)*, rejected the Assessee's appeal and held that the conversion of the CCPS was nothing but a transfer by way of 'exchange' under section 2(47) of the Income-tax Act, 1961 ("ITA") taxable under section 45 of the ITA.

On appeal by the Assessee, the Tribunal held in its favour as under:

Decision

(i) The Tribunal followed its earlier decision in the case of *ITO vs. Vijay M. Merchant [1986] 19 ITD 510* where, on the basis of a Circular dated May 12, 1984 *vide* F. No. 12/1/64-IT(A) (the "Circular") issued by the Central Board of Direct Taxes ("CBDT") explaining the rationale behind the introduction of section 55(2)(b)(v), the Tribunal had ruled that conversion of preference shares into equity shares would not be a taxable transfer. The Circular provides that:

> "... Section 14 of the Finance Act, 1964, introduces a new clause (v) in sub-section (2) of section 55 of the Income-tax Act, 1961, laying down the method for determining the cost of acquisition of a new share which becomes the property of the assessee on conversion of one type of share into another type of share. A question has been raised whether the transaction of conversion of one type of share into another attracts the capital gains tax under Section 45(1) .... The position in this regard is as follows: (1) Where one type of share is converted into another type of share (including conversion of debentures into equity shares), there is, in fact, no "transfer" of a capital asset within the meaning of section 2(47) of the Income-tax Act, 1961. Hence, any profits derived from such conversion are not liable to capital gains tax under section 45(1) of the Income-tax Act. However, when such

newly converted share is actually transferred at a later date, the cost of acquisition of such share for the purposes of computing the capital gains shall be calculated with reference to the cost of acquisition of the original share of stock from which it is derived."

(ii) The Tribunal acknowledged that treating the conversion as a taxable transfer by way of an exchange would give rise to undesirable double taxation – because section 55(2)(b)(v) would have the effect of denying the assessee a step-up in basis, and that the conversion did not constitute an exchange since, on conversion, the CCPS ceased to exist.

(iii) The Tribunal distinguished the cases relied on by the tax authorities in support of their argument on the ground that neither case had considered neither section 55(2)(b)(v) of the ITA nor the Circular.

(iv) The Tribunal also relied on a Supreme Court ruling in *Gillanders Arbuthnot & Co. 66 ITR 622* and a Bombay High Court ruling in *Texspin Engg. & Mfg. Works 263 ITR 345* to hold that section 48 of the ITA did not allow for the market value of the resulting equity shares to be treated as the 'full value of consideration' for the purpose of determining capital gains, and therefore the conversion was not a taxable transfer. In Texspin, the Bombay High Court, following the landmark Supreme Court ruling in *BC Srinivasa Setty (1981) 128 ITR 294 (SC),* held that in the absence of a prescribed method to determine the 'full value of consideration' for the purpose of computing capital gains, a transaction (in Texspin, it was a conversion of a partnership firm into a private limited company) could not be regarded as having been intended to fall within the scope of the charging provision i.e., section 45.

Comment

The Finance Act, 2017 amended Section 47 of the ITA (Transaction not regarded as Transfer) with effect from April 1, 2018 to insert clause (xb) which provides that the conversion of direct preference share into equity shares will not be regarded as a taxable transfer. Further amendments were introduced to provide that the holding period of the resulting equity shares would commence from the date of acquisition of the original preference shares, and that the cost basis of the resulting equity shares would be that of the original preference shares.

The amendments were welcomed by the private equity and venture capital investor community (who frequently structure investments through the use of CCPS), and are a strong step in the direction of introducing certainty to India's tax laws. The Tribunal's ruling will likewise be welcomed, especially by investors who undertook conversions prior to April 1, 2018 and took the position that the conversion was not a taxable transfer.

4. Payments for web-hosting services are in the nature of business income – Payments do not constitute royalties for "use of industrial, commercial or scientific equipment" – No withholding tax applicable u/s. 195.

EPRSS Prepaid Recharge Services India P. Ltd. vs. ITO [TS-623-ITAT-2018(Pun.)] Assessment Year : 2011-12

Facts

(i) The payee, Amazon Web Services LLC ("AWS") is a company incorporated in the USA and is a subsidiary of Seattle headquartered Amazon.com Inc. It provides on-demand cloud computing services to individuals, companies and governments, on a paid subscription basis. The payer, EPRSS Prepaid Recharge Services India Private Limited ("ESIPL" or the "Assessee") is a company incorporated in India and is a distributor of online recharge solutions for mobile phones, dish-to-home connections etc.

(ii) ESIPL uses servers to provide its online recharge solutions. Due to the prohibitive costs of purchase/maintenance of servers on its own account, ESIPL entered into an agreement (the "Agreement") with AWS for the provision of the Services (involving the use of AWS' servers). Believing that the Payments for the Services constituted neither royalties nor fees for technical services ("FTS"), ESIPL did not withhold tax.

(iii) On the basis that the Agreement granted ESIPL a limited licence to use and access the Services, the AO concluded that the Payments were for the "use or right to use any industrial, commercial or scientific equipment ("ICS Equipment") i.e., AWS' servers, constituted royalties under Explanation 2 ("Explanation 2") to section 9(1)(vi) of the Income-tax Act, 1961 ("ITA"), were taxable in India, and ESIPL should therefore have withheld on the Payments. The AO relied on Explanation 5 ("Explanation 5") to section 9(1)(vi) of the ITA to depart from established precedents requiring use of ICS Equipment to involve control, possession or physical access to the ICS Equipment.

(iv) Due to ESIPL's failure to withhold tax, the Payments were disallowed (under section 40(a)(i) of the ITA) as deductions from the Assessee's taxable income. On appeal by the Assessee, the Commissioner of Income Tax (Appeals) upheld the order of AO.

Decision

Upon appeal by the assessee, the Tribunal held in its favour as under:

- The Tribunal held that payments for web-hosting services would not amount to payments for "use of ICS Equipment". The Tribunal interpreted the phrase "use of ICS Equipment" as used in the US Treaty definition of royalty to mean that possession and control of the equipment (in this case, AWS servers) should vest with the payer (in this case, ESIPL). On that interpretation ESIPL could not be said to have paid royalties to AWS since it did not possess or control AWS' servers, and consequently, the Payments would not be taxable.
- The Tribunal rejected the tax department's argument on retrospective applicability of Explanation 5. Relying on a ruling of the Bombay High Court in NGC Networks ITA No. 397/2015, judgment dated January 29, 2018, the Tribunal observed that the law cannot compel a person to do something which he cannot possibly perform and held that the insertion of Explanation 5 with retrospective effect could not impose a withholding tax obligation on the Assessee for payments made in years that had already elapsed prior to the insertion.
- The Tribunal held, relying on a ruling of the Delhi High Court in New Skies Satelite BV ITA No. 473, 474 & 500 of 2012 & 244 OF 2014; judgment dated February 8, 2016, the meaning of royalty (as clarified retrospectively by Explanation 5 would not override the definition of royalties in the US Treaty.
- The fact that under Clause 5.1 of the Agreement, the Payments could fluctuate on a monthly basis, also aided the Tribunal in arriving at its conclusion. In the Tribunal's view, payments in the nature of royalty would need to be fixed (at least to some extent).

Based on the above conclusions, the Tribunal concluded that tax was not required to be withheld on the Payments, since they did not constitute royalties. Consequently, disallowance was not warranted.

Comments

The reader may also refer to the following judicial pronouncements on the subject:

Favourable decisions:

(i) Kotak Mahindra, [2007] 11 SOT 578

(ii) Savvis Communication Corporation, [2016] 158 ITD 750

(iii) Atos Origin IT Services Singapore Pte. Ltd., [2011] 46 SOT 52

(iv) Standard Chartered Bank, [2011] 47 SOT 191

(v) Dell International Services Private Limited., In re (305 ITR 37 (AAR))

(vi) Bharati Axa General Insurance Co Ltd., In re, [2010] 194 TAXMAN 1

Unfavorable decisions

(i) Cargo Community Network Pte. Ltd. 289 ITR 355 (AAR)

(ii) IMT Labs, 287 ITR 450 (AAR) and

(iii) Poompuhar Shipping Corporation Ltd., [2014] 360 ITR 257

5. No TDS obligation on royalty towards 'bundled software' until license key activation

Sophos Technologies Private Limited [TS-676-ITAT-2018(Ahd.)] Assessment Year 2012-13

Facts

(i) Sophos Technologies Private Limited (assessee) during AY 2012-13 procured anti-virus software from Russia and anti-spam software from Israel and bundled these softwares with assessee's own Unified Threat Management Software.

(ii) The bundled product was ultimately sold to end customers. The royalty in respect of anti-virus and anti-spam software was paid only when the end customer activated the licence key. However assessee recognised the revenue from the sale of its software at the point of sale to the distributor and made a provision for the royalty that it may have to pay upon activation of key in respect of the outsourced component which is part of the bundled product. Thus, the actual liability to pay for this product crystallized at a much later time when the product was eventually activated by the end customers and that was also the point of time when tax withholding obligations are discharged.

(iii) AO contended that the provision for the liability in respect of royalty payable for the bundled product was not admissible as a deduction because the assessee had failed to deduct the tax at source. AO accordingly held that the assessee was liable to deduct tax at source u/s 195 and thus disallowed expense u/s 40(a)(i). On appeal, CIT(A) upheld AO's order.

Decision

On appeal by the Assessee, the Tribunal held in its favour as under:

(i) The Tribunal observed that taxability of royalty income in terms of the provision in respect of treaties i.e., India-Russia DTAA and India-Israel DTAA arose only at the point of time when the royalties were paid to the resident of the other Contracting State. Thus ITAT stated that by purview of Article 12(1) the trigger for tax liability under the treaty was the point of time when the royalty income was paid to the resident of the other Contracting State. In view of the above ITAT relied on *Saira Asia Interiors (P.) Ltd*.

(ii) The Tribunal stated that the liability to deduct tax at source arose only when the income embedded in the relevant payment was exigible to tax. Thus ITAT clarified that the sale of bundled software to the distributor was not a point of time when the royalty in respect of the bundled product became payable but the point was when the end product is activated. ITAT remarked that, "…the Assessing Officer's approach of treating the entire provision as income exigible to tax in the hands of the supplier of the anti-virus/anti-spam product is fallacious."

(iii) ITAT observed that it was evident from records that the tax withholding liability had been discharged by the assessee as and when the activation of key had taken place. Thus ITAT remarked that "This approach is legally correct because activation of the end product is the trigger to royalty accruing to the vendors and as such to the income in the hands, if taxable, being brought to tax in India. The approach of the assessee thus cannot be faulted with. "

The Tribunal thus ruled in favour of assessee and deleted disallowance u/s. 40(a)(i).

6. Reimbursement of Seconded employees salary does not constitute FIS / FTS – Not liable for TDS – Distinguishes Centrica ruling

AT&T Communication Services (India) P. Ltd. [TS-644-ITAT-2018 (Del.)] Assessment Years: 2011-12 and 2012-13

Facts

(i) AT&T Communication Services India P. Ltd., assessee, is a wholly owned subsidiary of AT&T Communication Services International Inc., USA which is engaged in following services:- i) Provision of market research, administrative support and liaison services; ii) Provision of network outsourcing services - solutions business; and iii) Provision of network support services - network monitoring and support.

(ii) The assessee entered into master service agreement with AT&T USA for provision of market research, administrative support and liaison services and other support services. AWPS is a company incorporated in the US and is engaged in provision of manpower recruitment services. During subject AY 2011-12, the assessee required personnel for facilitating its business operations in India. Accordingly, certain employees having different work profiles and job responsibilities were seconded by AWPS to assessee in India. Accordingly, the international assignees were released from all obligations towards AWPS and would function solely under the control, direction and supervision of the assessee. Pursuant to the secondment agreement, the assessee reimbursed a sum of ₹ 4,17,56,851/- to AWPS for the salary and other cost paid by AWPS to such expatriates outside India for and on behalf of the assessee.

(iii) The AO was of the firm belief that the assessee ought to have deducted tax at source u/s. 40a(i) of the Act and for failure disallowed ₹ 4,17,56,851/-.

(iv) The AO was of the opinion that the said amount remitted to AWPS constituted Fees for Included Services (FIS)/Fee for Technical Services (FTS) in terms of Indo-US DTAA as well as u/s. 9(1)(vii) of the Act and relied upon the decision of Delhi HC in case of *Centrica India Offshore Pvt. Ltd. DRP* further confirmed AO's order.

Decision

The Tribunal held in favour of the assessee, as follows:

(i) Considering the facts on record, ITAT held that "it can be reasonably concluded that the employees seconded to the assessee company are working as the employees of the assessee company, their salary is subject to TDS u/s. 192 of the Act and, therefore, provisions of section 195 are not applicable on the facts of the case in hand."

(ii) With respect to Revenue's reliance on Delhi HC ruling in *Centrica*, ITAT remarked that Revenue's reliance was totally misplaced inasmuch as the seconded employees of AWPS were not taking forward the business of AWPS in India, but, were effectively working under the control and supervision of the assessee company. ITAT stated that by no means can they be said to be rendering services on behalf of AWPS. ITAT noted that in the case of *Centrica (supra)*, it was established only to provide services to the overseas entity to ensure that the services to be rendered to the overseas entities by the Indian vendor are properly co-ordinated.

(iii) ITAT concluded that reimbursement made by the appellant company cannot be classified as FTS/FIS under the provisions of the Act and Indo-US DTAA. ITAT stated that total tax deducted by the assessee u/s. 192 of the Act is ₹ 1,97,36,176/- which was much higher than the withholding tax sought to be levied by the AO which comes to 10% of ₹ 4,17,56,851/-.

(iv) Considering the facts in totality, ITAT directed AO to delete the Sec. 40(a)(i) addition.

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INDIRECT TAXES
GST Gyan

Negative List under Input Tax Credit – Section 17 – Before and after 2018 Amendment

Goods and Services Tax is a value added tax and consequently it provides for set off of input tax paid against the output tax liabilities. However, the law does not envisage granting set off of each and every inward supply. We all know that, the inward supplies in respect of which the ITC is not permitted to be availed are separately provided for in section 17(5) of the CGST Act. Section 17(5) is therefore commonly referred to as "Negative List" supplies. The Central Goods & Services Tax Amendment Act 2018, received assent of the President on 29th August 2018 and it was published in Official Gazette on 30th August 2018. **The provisions contained in the said Amendment Act would come into force from such date as the Central Government may notify.** However, as the law has made certain amendments to section 17, it is necessary to compare the provisions of section 17 prior to Amendment Act of 2018 and after amendments thereto. This article tries to analyse the same.

1. Amendment to section 17(3)

Section 17(2) requires that where the inward supplies are used partly for effecting taxable supplies (including zero-rated supplies) and partly for effecting exempt supplies, the amount of credit shall be restricted to so much of the input tax as is attributable to the said taxable supplies (including zero-rated supplies). The ITC pertaining to value of exempt supplies is therefore not eligible. Section 17(3) provides that in such cases value of exempt supplies shall also include sale of land and, subject to clause (b) of paragraph 5 of Schedule II, sale of building. (i.e. Sr. No. 5 of Schedule III of the CGST Act).

An explanation has been inserted in section 17(3) to clarify that the expression ''value of exempt supply'' shall not include the value of activities or transactions specified in Schedule III, except those specified in paragraph 5 of the said Schedule. It appears that the said amendment does not lay down any new law, but merely clarifies the position.

Besides, following additional activities and transactions are added in Schedule III by the Amendment Act, 2018

- Supply of goods from a place in the non-taxable territory to another place in the non-taxable territory without such goods entering into India.

- Supply of goods by the consignee to any other person, by endorsement of documents of title to the goods, after the goods have been dispatched from the port of origin located outside India but before clearance for home consumption.

- Supply of warehoused goods to any person before clearance for home consumption [By *Explanation 2*, it is clarified that the expression "warehoused goods" shall have the same meaning as assigned to it in the Customs Act, 1962].

It would therefore mean that in all the aforesaid cases, there will be no reversal of ITC u/s. 17(2) of the CGST Act. Whether the said amendments in Schedule III would take effect from 1st July 2017 or it would be prospective in nature, would be clear once the said provision is notified by the Government.

2. Amendment in section 17(5)(a)

Section 17(5)(a) deals with restrictions on ITC in respect of inward supplies of motor vehicles and other conveyances (i.e., vessels and aircrafts). ITC was permissible only if such motor vehicles or other conveyances are used for the following purposes ("specified purposes"):

- For making further taxable supply of vehicles and conveyances.

- Taxable supply of imparting training on driving, flying, navigating such vehicles and conveyances.

- Taxable supply of transportation of passengers.

- Transportation of goods.

In all other cases, ITC was not permissible.

As the entry dealt with input tax on supply of vehicles and conveyances only, any other input supplies relating to such vehicles and conveyances (ex: repair services, insurance services, purchase of vehicle parts etc.) were eligible for ITC.

Amended Act has increased the list of negative list supplies relatable to vehicles and conveyances. At the same time, it also excludes certain inward supplies from negative list which were earlier not eligible for ITC. The amendments are explained below:

- Set off in respect of motor vehicles for transportation of persons having approved seating capacity of more than thirteen persons (including driver) will be allowed under the amending provisions, whether or not they are used for specified purposes mentioned above. [It may be noted that, "motor vehicle" has been defined in the Act to have the same meaning as assigned to it in clause (28) of section 2 of the Motor Vehicles Act, 1988].

- Set off in respect of other motor vehicles, vessels or aircrafts would not be eligible unless they are used for specified purposes as mentioned above. Similarly, services of general insurance, servicing, repair and maintenance relating to such other motor vehicles, vessels or aircrafts would also be not eligible as ITC, unless they are used for specified purposes or the receiver is engaged in the manufacture of such motor vehicles, vessels or aircraft; or is in the supply of general insurance services in respect of such motor vehicles, vessels or aircraft insured by him.

  As the words "other conveyances" used in the earlier law has been replaced by 'aircrafts and vessels only", all other forms of conveyances which are not "aircrafts" or "vessels" or "motor vehicle" like a vehicle running upon fixed rails or a vehicle of a special type adapted for use only in a factory or in any other enclosed premises or a vehicle having less than four wheels fitted with engine capacity of not exceeding twenty-five cubic centimetres, would be eligible for ITC.

3. Amendment in section 17(5)(b)

Section 17(5)(b) was divided into four categories of supplies. viz. (i) inward supplies of food and beverages, outdoor catering, beauty treatment, health services, cosmetic and plastic surgery services, (ii) membership of a club, health and fitness centre, (iii) rent-a-cab, life insurance and health insurance services and (iv) travel benefits extended to employees on vacation such as leave or home travel concession. As regards category (i), the ITC was denied even if, it was obligatory for an employer to provide to its employees under any law for the time being in force. Besides, the expression 'rent-a-cab' was not defined, hence created difficulties. As regards 'renting' and 'hiring' of vehicles under the pre-GST scenario, conflicting judgments were passed:

In *Commissioner of Service Tax vs. Vijay Travels 2014 (36) STR 513 (Guj.)* & *Anil Kumar Agnihotri vs. CCEx 2018 (10) GSTL 288 (All.),* it was held that there is no distinction between activity of 'renting of vehicle' and 'hiring of vehicle' and both are used synonymously.

Whereas, in *CC & C Ex vs. Sachin Malhotra 2015 (37) STR 684 (Uttarakhand)* it was held that there is a distinction between activity of 'renting of vehicle' and 'hiring of vehicle' and unless the control of the vehicle is made over to the hirer and he is given possession for howsoever short a period, which the contract contemplates, to deal with the vehicle, no doubt subject to the other terms of the contract; there would be no renting.

Elaborating on the distinction between hiring and renting of vehicle, the Court observed that under the rent-a-cab scheme, the hirer is endowed with the freedom to take the vehicle wherever he wishes, and he is only obliged to keep the holder of the licence informed of his movements from time to time. When a person chooses to hire a car, which is offered on the strength of a permit issued by the Motor Vehicles Department, then the owner of the vehicle, who may or may not be the driver, will offer his service while retaining the control and possession of the vehicle with himself. The customer is merely enabled to make use of the vehicle by travelling in the vehicle. In the case of a passenger, he is expected to pay the metered charges, which is usually collected on the basis of the number of kilometers travelled. Unlike the said scenario, in the case of a rent-a-cab scheme, as is clear from the very fundamental principle underlying the scheme, it is to give the hirer the freedom to use the vehicle as he pleases, which, undoubtedly, implies that he must have possession and control over the vehicle. The court therefore made distinction between hiring and renting of vehicle in the context of rent-a-cab operator scheme.

The matter is now before Supreme Court in the case of *Vijay Travels vs. Commissioner 2015 (38) STR J245 (SC).*

In the amended Act, categories (i) and (iii) have been merged and services where ITC was ineligible under 'rent-a-cab services' category has been restricted.

Consequently, ITC is denied in respect of following supplies:

(i) Food and beverages, outdoor catering, beauty treatment, health services, cosmetic and plastic surgery services, life insurance and health insurance services.

(ii) ITC is also not allowed where input supplies are in the nature of renting or hiring of such motor vehicles, vessels or aircrafts falling under section 17(5)(a)/(aa) unless they are used for the purposes specified therein. Therefore, while denying the ITC, the law does not make any distinction between renting or hiring.

In both the cases mentioned above, ITC is allowed, where an inward supply of such goods or services or both is used by a registered person for making an outward taxable supply of the same category of goods or services or both or as an element of a taxable composite or mixed supply;

As regards, membership of a club, health and fitness centre & travel benefits extended to employees on vacation such as leave or home travel concession; the restriction contained in the pre-amended law continues. However proviso has been inserted below, to clarify that, ITC in respect of such goods or services or both shall be available, where it is obligatory for an employer to provide the same to its employees under any law for the time being in force. It therefore appears that, where the supplies mentioned in section 17(5)(b) which are otherwise ineligible for credit, are provided to employees under statutory obligations, the ITC would be eligible.

The readers may note that the amended provisions of 2018 Act would become operational only from the notified date/s. No such date/s have been notified yet.

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Go on bravely. Do not expect success in a day or a year. Always hold on to the highest. Be steady. Avoid jealousy and selfishness. Be obedient and eternally faithful to the cause of truth, humanity, and your country, and you will move to the world

— *Swami Vivekananda*

CA Rajkamal Shah & CA Bharat Vasani

INDIRECT TAXES
GST – Legal Update

NOTIFICATIONS

13th Amendment to CGST Rules (CGST Notification No. 60/2018 dt. 30-10-2018)

- Rule 83A inserted to provide for procedure of Examination of GST Practitioners.
- Rule 109A – Clause 1(b) amended to provide that appeal may be made to any officer not below the rank of Joint Commissioner (Appeals) where decision or order is passed by the Deputy or Assistant Commissioner or Superintendent.
- Rule 109A – Clause 2(a) amended to provide that appeal may be made to any officer not below the rank of Joint Commissioner (Appeals) where such decision or order is passed by the Additional or Joint Commissioner.
- Rule 142A inserted to provide for procedure of recovery of dues under existing laws. Format of FORM GST REG-16 (Application of Cancellation of Registration) amended to include situation of change in constitution leading to change in PAN. Also, in case of death of sole proprietor, application shall be made by the legal heir/successor before the concerned tax authorities. In such case, as an alternate to filing return for the tax period in which effective date of surrender of registration falls, an application may be filed with proper officer to the effect that no taxable supplies have been made during the intervening period.
- Form GSTR-4: Details in Serial No. 4A in Table 4 in respect of Inward Supplies from Registered Supplier not to be furnished.
- Format of Part II (other than return related liabilities) of GST PMT-01 (Electronic Liability Ledger) amended.

Non-applicability of TDS provisions on PSU (CGST Notification No. 61/2018 dt. 5-11-2018)

(These amendments are effective from 1-10-2018)

Proviso to Section 51 inserted to exempt supply of goods or services or both by a public sector undertaking to another public sector undertaking, whether or not a distinct person from the provisions of TDS.

Extension of due date of filing returns (CGST Notification No. 62, 63, 64, 65/2018 dt. 29-11-2018)

Principal Place of Business	Return Form	Return Period	Due Date
Srikakulam district in the State of Andhra Pradesh	GSTR-3B	September, 2018 and October, 2018	30-11-2018
	GSTR-1 (Monthly)	September, 2018 and October, 2018	30-11-2018
	GSTR-1 (Quarterly)	July-September, 2018	30-11-2018
	GSTR-4	July-September, 2018	30-11-2018

Principal Place of Business	Return Form	Return Period	Due Date
Cuddalore, Thiruvarur, Puddukotai, Dindigul, Nagapatinam, Thenai, Thanjavur, Sivagangai, Tiruchirappalli, Karur, Ramanathpuram in the State of Tamil Nadu	GSTR-3B	October, 2018	20-12-2018
	GSTR-1 (Monthly)	October, 2018	20-12-2018

Extension of due date of GSTR-7 (CGST Notification No. 66/2018 dt. 29-11-2018)

Due date for filing of TDS return in Form GSTR-7 for the months of October, 2018 to December, 2018 is extended up to 31-1-2019.

CIRCULARS

Scope of del credere agent (DCA) within Principal-Agent relationship under Schedule I of CGST Act, 2017 (Circular No. 73/2018-CGST dt. 05-11-2018)

In commercial trade parlance, a DCA is a selling agent who is engaged by a principal to assist in supply of goods or services by contacting potential buyers on behalf of the principal and who guarantees the payment to the supplier.

- *When DCA does not falls within the ambit of "agent" as per Schedule I*
  - i) In case where the invoice for supply of goods is issued by the supplier to the customer, either himself or through DCA.
  - ii) The temporary short-term transaction based loan being provided by DCA to the buyer is a supply of service by the DCA to the recipient on Principal-to -Principal basis and is an independent supply.
  - iii) Accordingly, interest charged by DCA to buyer on loan is exempt as per S. No. 27 of Notification No. 12/2017 dt. 28-6-2017.
- *When DCA falls within the ambit of "agent" as per Schedule I*
  - i) In case where the invoice for supply of goods is issued by the DCA in his own name.
  - ii) In such case, the temporary short-term transaction based credit being provided by DCA to the buyer no longer retains its character of an independent supply and is subsumed in the supply of the goods by the DCA to the recipient.
  - iii) The value of the interest charged for such credit would be required to be included in the value of supply of goods by DCA to the recipient as per Sec 15(2)(d) of the CGST Act.

Collection of tax at source by Tea Board of India (Circular No. 74/2018-CGST dt. 5-11-2018)

Tea Board of India being the operator of the electronic auction system for trading of tea across the country including for collection and settlement of payments, falls under the category of electronic commerce operator liable to collect TCS u/s. 52 of CGST Act.

It is clarified that TCS shall be collected by Tea Board from the –

(i) sellers (i.e., tea producers) on the net value of supply of goods i.e., tea; and

(ii) auctioneers on the net value of supply of services (i.e., brokerage).

PRESS RELEASE

Advisory to UIN entities claiming GST refunds dt. 9-11-2018

Many UIN entities while filing invoice data in FORM GSTR-11 are reporting Place of Supply as the state in which they are registered. This may lead to delay in processing / rejection of refund claims.

It is hereby clarified that the Place of Supply should be reported as mentioned in the invoice.

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CA Naresh Sheth & CA Jinesh Shah

INDIRECT TAXES

GST – Recent Judgments and Advance Rulings

A. Writs and Special Leave Petitions

1. Saji S., Ranjith R. vs. Commissioner – State GST Department, Asst. State Tax Officer – Kerala High Court (2018-TIOL-162-Hc-Kerala-GST)

Facts, Issues involved and Contentions of the Petitioner

The petitioner is a registered dealer. He purchased certain goods from Chennai and then transported it to Kerala. While the goods were in transit, the Assistant State Tax Officer (ASTO) detained the goods and issued Ext. P3 notice of detention under Section 129 of CGST Act.

Based on the demand raised in Ext. P3 notice, the consignor paid the tax and penalty under the ASTO's directions. However, he erroneously paid the tax and penalty under the wrong head of SGST/CGST instead of IGST. Therefore, the authorities refused to release the goods.

Aggrieved by the above, the petitioner had filed this writ petition.

The petitioner's counsel drew attention to Section 77 of the GST Act and also to Rule 92(1) of the CGST Rules, 2017, especially the proviso appended to the Rule. To hammer home his contentions that even if the remittance were to treated as a mistake on the consignor's part, the statute empowers the authorities to transfer the deposit from one head to another: from SGST to IGST.

The Government Pleader, on the other hand, submitted that the petitioner could as well pay the amount under 'IGST' and then claim a refund from the head 'SGST'. According to her, if the authorities have to go for an adjustment, it will take more than a couple of months' time.

Held

Section 77 - Tax wrongfully collected and paid to Central Government or State Government

(1) *A registered person who has paid the Central tax and State tax or, as the case may be, the Central tax and the Union territory tax on a transaction considered by him to be an intra-State supply, but which is subsequently held to be an inter-State supply, shall be refunded the amount of taxes so paid in such manner and subject to such conditions as maybe prescribed.*

(2) *A registered person who has paid integrated tax on a transaction considered by him to be an inter-State supply, but which is subsequently held to be an intra-State supply, shall not be required to pay any interest on the*

amount of Central tax and State tax or, as the case may be, the Central tax and the Union territory tax payable.

Rule 92(1) of the CGST Rules, 2017 reads as:

(1) Where, upon examination of the application, the proper officer is satisfied that a refund under sub-section (5) of section 54 is due and payable to the applicant, he shall make an order in FORM GST RFD-06, sanctioning the amount of refund to which the applicant is entitled, mentioning therein the amount, if any, refunded to him on a provisional basis under sub-section (6) of section 54, amount adjusted against any outstanding demand under the Act or under any existing law and the balance amount refundable:

PROVIDED that in cases where the amount of refund is completely adjusted against any outstanding demand under the Act or under any existing law, an order giving details of the adjustment shall be issued in Part A of FORM GST RFD-07.

Section 77 provides for the refund of the tax paid mistakenly under one head instead of another. However, Rule 92 speaks of adjustment. If the amount of refund is adjusted against any outstanding demand under the Act, an order giving details of the adjustment is to be issued in Part A of FORM GST RFD-07.

The petitioner's counsel lays stress on this process of adjustment and asserts that the amount remitted under one head can be adjusted under another head, for the demand of any amount under the Act.

Under these circumstances, the Court found no difficulty for the respondent officials to allow the petitioner's request and get the amount transferred from the head 'SGST' to 'IGST'. It may take some time, as the Government Pleader has contended, but it is inequitable for the authorities to let the petitioner suffer on that count.

The court held that the 2nd respondent will release the goods forthwith along with the vehicle and, then, ensure that the tax and penalty already stood remitted under the 'SGST' is transferred to the head 'IGST'.

The writ petition was disposed of accordingly.

B. Rulings by Authority of Advance Ruling

2. M/s. Spaceage Syntex Pvt. Ltd. – AAR Maharashtra (2018-TIOL-269-AAR-GST)

Facts, Issues involved and Query of Applicant

Applicant is engaged in trading of export entitlement licences such as Duty Free Import Authorisation (DFIA), Duty Free Replenishment Certificate (DFRC), etc. Applicant has purchased said licences from exporters and sold them to manufacturers to avail benefit of entitlement of duty free imported goods.

Duty credit scripts are used for payment of basic customs duty, anti-dumping duty, etc. W.e.f. 13-10-2017, Government *vide* notification no. 35/2017 – Central tax (rate) dated 13-10-2017 has prescribed NIL rate of tax on duty credit scripts classified under HSN code 4907.

Applicant seeks an advance ruling as to whether *GST is applicable on Sale and / or Purchase of DFIA licenses.*

Therefore the basic issue to be decided in the application is whether DFIA will be covered under 'Duty Credit Scrips' and attract NIL rate of tax.

Department was of the view that DFIA is different from Duty credit scrips on the following grounds:

- Duty Credit Scrips are issued under MEIS and SEIS schemes and are freely transferable.

- Duty credit scrips are used for payment of specified duties of customs on imported goods.
- DFIA is an exemption scheme and not a duty credit scheme.
- DFIA entitles the holder to import goods duty free.
- Duty credit scrips can be used to import any Open General License (OGL) items whereas under DFIA only items specified in particular authorisation can be imported.

Applicant's submissions were as under:

- Though MEIS and DFIA are under different chapters, it makes no difference as rationale behind both the scrips need to be taken into consideration.
- Essence of the benefits under MEIS and DFIA is reward in duty payment.
- Rationale behind both the scrips need to be taken into consideration. Press release issued by GST council explains this. FTP policy enumerates both MEIS and DFIA as export incentives.
- Main objective of exempting duty credit scrip was to take all possible measures to support the exporter earning valuable foreign exchange and providing significant employment.
- Discriminating exporter having MEIS and DFIA licence is against natural justice.
- Letter issued by GST council clarifies that DFIA licence is like MEIS / SEIS and exempt from GST. This clarification is given by GST council and not superintendent.
- It is incorrect to ignore the intention of the legislature.
- Duty credit scrips referred in entry no. 4907 is inclusive concept which includes all duty credit scrips where duty saving / non-payment is involved.

Applicant thereby requested the AAR not to interpret the words Duty credit scrips in narrow sense but to interpret in the broader sense keeping in view the legislative intent.

Discussions by and observations of AAR

The basic issue is whether DFIA licence is a 'Duty Credit Scrip' as defined under GST laws.

<u>DFIA:</u>

DFIA are paper authorisation that allow holder to import inputs that go into manufacture of products to be exported. Under DFIA, only items specified in annexure can be imported. DFIA is issued only after the goods are exported and all the export obligations are completed. DFIA, under GST laws, is covered under HSN 4907. DFIA are quantity based.

<u>Duty Credit Scrips</u>:

Duty Credit Scrips are issued under MEIS and SEIS scheme and can be used to pay specified duties of customs to central government. Duty credit scrips are value based. Duty credit scrips are freely transferable.

Difference between DFIA and duty scrips includes the following:

- Duty credit scrips can be used for payment of specified duties of customs whereas DFIA does not give any credit of duty.
- Duty Credit scrips are covered under MEIS and SEIS whereas DFIA is not covered.
- DFIA enables duty free import of inputs whereas duty credit scrips are issued to reward the exporters to offset infrastructural inefficiencies and
- Validity of DFIA is 12 months whereas the validity of Duty credit scrips is 24 months.

Applicant has submitted that GST council had observed that duty credit scrips such as MEIS were losing its value due to reduced usability as it could no longer be used to pay IGST / GST. Hence, it clearly appears that only duty credit scrips was losing its value and not DFIA as DFIA does not envisage payment of duty at all. DFIA is connected with duty free imports.

DFIA and Duty credit scrips are not one and same or similar at all. They are different incentives given to exporters with different conditions. Even though both are incentive to promote export, both schemes are used in different circumstances and in different manner. When FTP itself has segregated the two different chapters, it will not be proper to consider the two schemes as one and the same.

Hence, DFIA is distinguishable from Duty credit scrips and cannot be considered as duty credit scrips even though it falls under HSN 4907. GST exemption is only in respect of duty credit scrips.

Applicant has submitted the letter received from GST council, which clarified that advance authorisation, are to be included in duty credit scrips. However, it appears that Government has not issued any circular, notification, etc. in this regard.

Ruling of AAR

Sale and / or purchase of DFIA licence is liable to GST.

3. M/s. Kundan Misthan Bhandar – AAR Uttarakhand (2018-TIOL-276-AAR-GST)

Facts, Issue involved and Query of Applicant

Applicant has a sweetshop on ground floor from where they supply food items such as sweetmeats, namkeen, cold drinks and other edible items. They also run a restaurant on the first floor in the same building.

Applicant has sought advance ruling for the following questions:

1. *Whether supply of pure food items such as sweetmeats, namkeens, cold drinks and other edible items from sweetshop that also runs a restaurant is a transaction of supply of goods or services?*
2. *What is the nature and rate of tax applicable to the following items supplied from the ground floor of a sweetshop and wherein restaurant is also located on the first floor and whether applicant is entitled to claim benefit of input tax credit with respect to the same:*
   a. *Sweetmeats, namkeen, dhokla, etc. commonly known as snacks, cold drinks, ice cream and other edible items.*
   b. *Ready to eat (partially or fully pre-cooked / packed) items supplied from live counters such as jalebi, chole bhature and other edible items*
   c. *Takeaway order of sweetmeats or namkeen by a person sitting in the restaurant of a sweetshop when such products are not consumed within the premise of applicant but are takeaway.*

Discussions by and observations of AAR

In the present case, the applicant has a sweetshop on the ground floor and a restaurant on the first floor of the same building. It was noticed that very often than not, two or more goods or a combination of goods and services was supplied together.

The question before the AAR was whether the transactions undertaken by applicant will constitute supply of goods or supply of services.

Under GST law, supplies that are bundled, with two or more supplies of goods or services or a combination thereof can be classified either as composite supply or as mixed supply.

Composite supply is defined u/s. 2(30) of CGST Act to mean *a supply made by a taxable person to a recipient consisting of two or more taxable supplies of goods or services or both, or any combination* *thereof, which are naturally bundled and supplied in conjunction with each other in the ordinary course of business, one of which is a principal supply.*

Mixed supply is defined u/s. 2(74) of CGST Act to mean *two or more individual supplies of goods or services, or any combination thereof, made in conjunction with each other by a taxable person for a single price where such supply does not constitute a composite supply.*

For a supply to be considered as a mixed supply, the first requisite is to rule out that supply is composite supply.

In order to constitute a composite supply, the goods or services or both are to be supplied together, in a natural bundle and in normal course of business, provided one of them has to be a principal supply.

In the instant case, the nature of restaurant services is such that it may be treated as the main supply and the other supplies combined with such main supply are in the nature of incidental or ancillary services. Thus, restaurant services get the character of predominant supply over other supplies.

Therefore, in the present case, supply shall be treated as supply of service and the sweetshop shall be treated as extension of the restaurant in as much as the said activity covered under clause 6(b) of Schedule II of the Act which is as under:

The following composite supplies shall be treated as a supply of services, namely:—

(b) supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (other than alcoholic liquor for human consumption), where such supply or service is for cash, deferred payment or other valuable consideration.

Since the supply of restaurant service is treated as principal supply therefore the rate applicable on such composite supply shall be rate attributable to the restaurant service i.e. 5% [HSN- 9963] subject to condition that input tax credit will not be availed on the provision of such service.

Ruling of AAR

In respect of question (1), supply shall be treated as supply of service and sweet shop shall be treated as extension of restaurant services.

In respect of question (2), rate of GST on aforesaid activity and takeaway items shall be 5% with the condition that no ITC can be claimed in respect of goods and services used for supplying such services.

4. M/s. Nash Industries (I) Pvt. Ltd. – AAR Karnataka (2018-TIOL-260-AAR-GST)

Facts, Issue involved and Query of Applicant

Applicant is in the business of manufacturing sheet metal pressed components and caters to various industries, ATM, printers etc., and is having multi-locational facilities in and around Bangalore. Such components are manufactured by the applicant based on the drawings provided by the customer.

To manufacture such components, applicant had designed and manufactured certain tools. Such manufactured tools were billed to the customer and were retained by the applicant for manufacturing the sheet metal pressed components.

Applicant stated that the erstwhile Central Excise Valuation Rules provided that the amortised cost of tool is to be added to the value of the goods removed for the purpose of payment of Excise duty.

Applicant was of the view CGST Act and Rules have similar valuation provisions and hence cost of amortisation is to be added to the value of goods supplied for the purpose of payment of GST.

Applicant drew analogy that had he procured such tool from outside then the cost of tool would have formed part of the value of supply of component. As per section 15(2)(b) if the tool is provided free of cost to the supplier, the amortised cost of tool would have formed part of the taxable supply.

However, applicant's customers were of the view that cost of amortisation is not to be included in valuation of goods for the purpose of payment of GST.

In absence of clarity on the matter, the applicant has sought an advance ruling on the following question:

1. *Whether amortised cost of the tool is to be added to arrive at the value of goods supplied for the purpose of GST under Section 15 of the CGST Act read with Rule 27 of CGST Rules?*

Discussions by and Observations of AAR

AAR observed that there were two supplies involved in the entire activity.

Applicant, once he gets the order for the specialised components, manufactures the tools specifically required for the job and invoices it to the recipients. The applicant needs to collect the applicable tax on the tools and the recipient becomes the owner of such tools.

Later the recipient gives the tool free of cost to the applicant and the applicant uses the same for the manufacture of the components. Section 7(1) of the CGST Act 2017 stipulates that 'Supply' shall be made for a consideration. Therefore, consideration is an essential element in supply. However, Section 7(1)(c) specifies that the activities described in Schedule I shall be considered as 'Supply' even if there is no consideration involved. One such activity covered in Schedule I is permanent disposal of business assets. As the tools are supplied by the recipient to the applicant for the limited purpose of manufacture / supply of components, the activity does not amount to permanent transfer of business asset of the recipient. Therefore, the activity of free supply of tools by the recipient to the applicant does not amount to supply as defined in Section 7 of the CSGT Act 2017.

AAR examined the provisions of Section 15 of the CGST Act 2017 in order to address the question raised by the applicant.

Section 15(1) of the CGST Act provides as under:

"The value of a supply of goods or services or both shall be transaction value, which is the price actually paid or payable for the said supply of goods or services or both when the supplier and the recipient of the supply are not related and the price is the sole consideration for the supply"

Therefore, the transaction value carried out at arm's length, constitutes the value of supply.

AAR considered Section 15(2)(b) of CGST Act 2017 relevant to the facts of this case and analysed the same.

Section 15(2) (b) of the CGST Act 2017 reads as follows:

"Any amount that the supplier is liable to pay in relation to such supply but which has been incurred by the recipient of the supply and not included in the price actually paid or payable for the goods or services or both."

Either the tools could be manufactured by the applicant himself **or** they could get it manufactured by someone else **or** the recipient could supply them free of cost.

In case the applicant procures the tools from the third party, then they would incur the cost and such cost would be included in the value of taxable supply to the recipient.

However, when the first or third situation prevails, then the applicant has not spent any amount in respect of the tools. Here the cost of the tool is borne by the recipient of the supply whereas the same should have been borne by the applicant, as evident from the situation discussed above.

Therefore the facts and circumstances of the transaction as put forth by the applicant attract Section 15(2)(b) of the CGST Act 2017.

Ruling of AAR

The amortised cost of tools re-supplied back to the applicant free of cost shall be added to the value of the components while calculating the value of the components under Section 15 of the CGST Act 2017.

5. M/s. Synthite Industries Limited – AAR Andhra Pradesh (2018-TIOL-255-AAR-GST)

Facts, Issue involved and Query of Applicant

The applicant (Job worker) is engaged in job work of removing "Caffeine" from tea powder imported from foreign company viz., HTH Hamburger Teehandel Gmbh Im. & Export, Hamburg, Germany (Principal) and then subsequently exporting the decaffeinated tea to his Principal.

Applicant undertakes "super critical fluid extraction" process. The raw material is being supplied by applicant's principal foreign customer free of cost and the processed output is exported back to the principal. The tea powder contain caffeine which is removed by the applicant-job worker through extraction process.

In backdrop of above facts, applicant has sought advance ruling on the following questions:

1. *Whether the process of providing job work service to foreign customer as explained above is taxable under GST. Does such transaction attract GST?*
2. *If GST is applicable, whether they have to pay IGST or SGST+CGST?*
3. *Is the job work service provided by them is exempted from service tax under Mega exemption list as per notification No. 25/2012 dated 20-6-2012 and not chargeable to GST?*

Discussions by and observations of AAR

Job work is defined u/s. 2(68) of CGST Act to mean *any treatment or process undertaken by a person on goods belonging to another registered person.* The one who does the said job work is termed as job worker. The ownership of goods does not transfer to the job worker. He is only required to carry out processes as specified by the principal.

There is no doubt that the applicant is squarely covered under definition of job work as defined u/s. 2(68) of CGST Act.

Process of providing job work service by the applicant to the foreign principal shall be classified under the **HSN Code services heading 9988,** which reads as under:

"9988 – Manufacturing services on physical inputs owned by others. The services included under Heading 9988 are performed on physical inputs owned by units other than the units providing the service. As such, they are characterised as outsourced portions of a manufacturing process or a complete outsourced manufacturing process. Since this heading covers manufacturing services, the output is not owned by the unit providing this service. Therefore, the value of the services in this Heading is based on the service fee paid, not the value of the goods manufactured."

Therefore, in light of the above, the aforesaid services are covered by Entry No. 26 (HSN Code 9988) and **liable to tax @18%**.

As regards to IGST liability, Section 13(3) of IGST Act reads as under:

(3) The place of supply of the following services shall be the location where the services are actually performed, namely:—

(a) ***Services supplied in respect of goods which are required to be made physically available by the recipient of services to the supplier of services, or to a person acting on behalf of the supplier of services in order to provide the services:***

Provided that when such services are provided from a remote location by way of electronic means, the place of supply shall be the location where goods are situated at the time of supply of services:

Provided further that nothing contained in this clause shall apply in the case of services supplied in respect of goods which are temporarily imported into India for repairs and are exported after repairs without being put to any other use in India, than that which is required for such repairs.

Transaction undertaken by applicant squarely falls under clause (a) of Section 13(3) of IGST Act, 2017. Hence, the place of supply for the aforesaid transaction is the location where services are actually performed i.e., State of Andhra Pradesh. Hence, the tax liability under SGST Act/ CGST Act will apply.

Ruling of AAR

In respect of question (1), the process of providing job work service to foreign principal, in the premises of the applicant, is taxable under APGST Act, 2017 / CGST Act, 2017 as per Entry 26 (HSN Code 9988) Proviso (iv), and liable to tax @ 18%.

In respect to question (2), the place of supply for this transaction is the location of supplier of service as per Section 13(3)(a) of IGST Act, 2017. Hence, the tax liability under APGST Act, 2017 / CGST Act, 2017 will apply.

In respect of question (3), as the Service tax Act itself is subsumed under Goods and Services Act, the Notification No. 25/2012 – ST dated 20-6-2012 is no more applicable.

6. Vservglobal Private Limited – AAR Maharashtra (2018-TIOL-263-AAR-GST)

Facts, Issue involved and Query of Applicant:

Applicant is incorporated in India and is engaged in providing back office support services to overseas companies (hereinafter referred to as 'Clients') engaged in trading of chemicals and other products. Applicant comes into picture only after finalisation of purchase/ sale order by the client. Applicant intends to undertake following activities:

1. *Get SDF (Sales Detail Form) & PDF (Purchase Detail Form) from concerned party*
2. *Generate order No. in VOSS*
3. *Create PO (Purchase Order) & SC (Sales Contract) in VOSS*
4. *Liase with supplier for cargo readiness*
5. *Process payment request in VOSS*
6. *Various other back-office functions.*

Apart from above, the applicant will also maintain record of employees of clients, their payroll processing etc. All the payments to third parties like supplier, employees, etc., will be done directly by clients and the applicant will maintain accounting for the same. Applicant will be compensated on fixed monthly basis or as per the volume of transactions, on mutually agreed terms, in convertible foreign exchange.

In light of above, applicant has sought advance ruling on the following question:

1. *Whether the aforesaid services proposed to be rendered by the applicant will qualify as "zero rated supply" in terms of s.16 of the IGST Act, 2017 or not.*

Applicant's submissions

As per legal understanding of the applicant, the aforesaid services qualify as "zero rated supply" in terms of Section 16 of IGST Act, 2017.

As per Section 16(1)(a) of the Act, export of goods or services or both is a zero rated supply.

The phrase 'Export of Service' is defined in Section 2(6) of the Act which reads as under:

"export of services" means the supply of any service when, -

i. The supplier of service is located in India;

ii. The recipient of service is located outside India;

iii. The place of supply of service is outside India'

iv. The payment for such service has been received by the supplier of service in convertible foreign exchange; and

v. The supplier of service and the recipient of service are not merely establishments of a distinct person in accordance with Explanation 1 in section 8.

Applicant is providing services to overseas offices of recipients. Aforesaid services are not specified under any sub-section from (3) to (13) of Section 13 of IGST Act and hence place of supply will be the location of service recipient as per Section 13(2) of the IGST Act. Payment for services will be received in convertible foreign exchange. Further, the applicant and its clients are separate incorporated companies and therefore, they are not merely establishment of distinct person in terms of statutory provisions. Thus, it is clear that the services proposed to be rendered by the applicant satisfy all the condition of "Export of Services" and therefore, covered under the definition of "Zero Rated Supply".

Personal Hearing

During the course of personal hearing, a question was posed as to how the services rendered by applicant is not covered under the definition of 'Intermediary Services' as defined under Section 2(13) of the IGST Act which is reproduced below:

"(13) "intermediary" means a broker, an agent or any other person, by whatever name called, who arranges or facilitates the supply of goods or services or both, or securities, between two or more persons, but does not include a person who supplies such goods or services or both or securities on his own account."

Applicant's additional submissions

CBEC in the Educational Guide released by it had explained the concept of 'Intermediary' and its exclusion clause in para 5.9.6 which reads as under:

*"Similarly, persons such as call centres, who provide services to their clients by dealing with customers of the client on client's behalf, but actually provided these services on their own account", **will not be categorised as intermediaries."***

An identical issue to the case in hand came before the Hon'ble Authority for Advance Ruling In Re: GoDaddy India Web Service Private Ltd., reported as 2016 (46) S.T.R. 806 (AAR).

The above definition contains an exclusion as per which the person who supplies goods or services on his own account is not included. In the instant case, the applicant proposes to supply "Business Support Service" comprising of "Back office support" and "Accounting" which is its principal supply. The said "Business Support Service" would be provided by applicant to its client would be on Principal to Principal basis. Therefore, the instant case is covered by exclusion clause in definition of 'Intermediary'.

Department's contention

Proper officer argued that application submitted by the applicant is not maintainable. Since the question pertains to "Zero Rated Supply", it means it relates to place of supply and question pertains to place of supply cannot sought before Hon. Advance Ruling Authority.

Further, if Hon. Advance Ruling Authority has accepted the application, alternative argument is made that in the instant case main issue is the place of supply is outside India or inside India. The proper officer analysed the Section 12 and Section 2(14) of IGST Act and applied it to the instant case.

On the website of Vikudha Overseas Corporation Limited (Hong Kong based client) it is learnt that company has operated throughout the world and operated his business in India. The Vikudha Overseas Corporation Limited has operated in India through its branch whatever name called Group Company, sister concern, etc. M/s Vikudha India Trading Limited, having registered office Dhantak Plaza, 201, Opp.

Waman Centre, Makwana Road, Marol, Andheri East, Mumbai, MH 400059 IN (As per website of ministry of commerce) and the director of company are Mr. Deapkumar Balkishan Adukia and Seema Sanjau Enand.

The applicant will provide services specified in agreement to M/s. Vikudha India Trading Limited, which operates in India and represents M/s. Vikudha Overseas Corporation Limited.

This means that the applicant will provides services to M/s. Vikudha India Trading Limited and therefore the location of recipient of service is in India at 201, Dhantak Plaza, Opp. Waman Centre, Makwana Road, Andheri (E), Mumbai. Therefore, place of supply of service is not outside India. Only mere agreement by foreign company with Indian company is not sufficient to determine Exports of services.

It is also seen from bank account of M/s Vservglobal Pvt. Ltd., that payment for such services has not been received by the supplier in convertible foreign exchange.

From the aforesaid fact and related provision under the statute, the above transaction does not qualify export of services, hence, not qualified under "Zero Rated Supply".

Discussions by and Observations of AAR

Applicant is registered person under GST who is supplier of services incorporated in India.

On basis of service agreement, applicant submits that services proposed to be rendered by them such as back office administrative and accounting support services, payroll processing services and maintenance of records of employees satisfy all the conditions of export of services and should qualify as zero rated supply of services.

In the course of final hearing, a reasonable doubt was raised by the members whether the applicant is an 'intermediary' as defined under the Act.

Section 2(13) of IGST Act defines intermediary as under:

"intermediary" means a broker, an agent or any other person, by whatever name called, who arranges or facilitates the supply of goods or services or both, or securities, between two or more persons, but does not include a person who supplies such goods or services or both or securities on his own account;

In the context of definition of 'Intermediary' as mentioned above, the service agreement was examined as a whole to ascertain whether the applicant is an Intermediary or not. It is necessary to decide whether place of supply is outside India.

Important clauses of service agreement are reproduced as under:

1. Applicant commits to provide back office administrative and accounting services.
2. Clients will provide software VOSS to the applicant for accounting purpose.
3. Applicant will obtain SDF and PDF from concerned party.
4. Generate order no. in VOSS.
5. Create PO and Sales order.
6. Liaise with suppliers, inspection authorities and customers.
7. Various other functions on behalf of clients.

A sum of all the above activities indicate that applicant as a person arranges or facilitates supply of goods or services between the overseas client and customer of the overseas client and is therefore clearly covered in the definition of an ***intermediary***.

As the applicant is held as an intermediary, the provisions pertaining to place of supply in case of intermediary services provided in Section 13(8) are relevant. Therefore, place of supply would be the location of supplier of services which is located in State of Maharashtra, India.

It is seen that the condition (iii) of Section 2(6) of the IGST Act is not satisfied and hence without examining condition (v) of the said section as to distinct person, it is held that the services proposed to be rendered by the applicant do not qualify as 'export of services' as defined under Section 2(6) of IGST Act and thus not a 'Zero Rated Supply' as per Section 16(1) of IGST Act.

Ruling of AAR
The Hon. Advance Ruling Authority decided that aforesaid services proposed to be rendered by the applicant do not qualify as 'Zero Rated Supply' in terms of Section 16 of IGST Act.

7. Bajaj Finance Limited – AAR Maharashtra (2018-TIOL-264-AAR-GST)

Facts, Issues involved and Query of Applicant
Applicant is engaged in providing various types of interest bearing loans to customers. EMI payable by the customer is used to pay-off both interest and principal amount. In case of delay in repayment of EMI, the applicant collects penal interest for the number of days of delay in terms of the agreements executed by the customers. The per cent of penal interest ranges between 2% to 4% per month depending on the product.

The relevant extract of clauses of sample auto loan agreement in respect of penal interest is reproduced below:

"1. DEFINITIONS AND ABBREVIATIONS

I. "Penal charges" shall mean and include overdue charges on non-payment of installment on the due date. ……

II. TERMS OF THE LOAN:

3. The borrower agrees and confirms that:

(iv) BFL is entitled to levy penalty as follows on default

(a) for continuing non-payment of amount due, a penalty not exceeding 3% per month on the amount due calculated on pro rata basis from due date till actually paid as per clause B of the schedule.

Applicant is of the view that penal interest collected is in the nature of additional interest, therefore, it is not subject to GST levy.

In light of above, the applicant has sought advance ruling on the following:

1. *Whether the penal interest is to be treated as interest for the purpose of exemption under Sr. No. 27 of Notification No. 12/2017-Central Tax (Rate) dated 28-6-2017?*

2. *If the answer to the above is negative, whether the activity of collecting penal interest by the applicant would amount to a taxable supply under the GST regime?*

Applicant submitted that penal interest represents the time value of money for the period of delay in making payment of installment. It is nothing but additional interest on loan. Therefore, the penal interest shall be given similar treatment as that of the principal interest which is factored in EMI / Installment amount, and, hence, shall also be covered under definition of interest as defined under Notification no. 12/2017 – Central tax (rate):

*"(zk) **"interest" means interest payable in any manner in respect of any moneys borrowed or debt incurred** (including a deposit, claim or other similar right or obligation) but does not include any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised."*

Applicant submitted that services of providing loans is exempt under the GST regime, in so far consideration is represented by way of interest. Therefore, penal interest would be exempt from GST levy.

It is further submitted that the expression agreeing to tolerate an act used in Entry 5(e) of Schedule II, should be understood to cover instances where the consideration is being charged by the person in order to allow another person to undertake any particular activity.

Contrary to the above, the penal interest is collected on happening of any event of default by the customers in making the payment of loan installments. It is submitted that Intention of the parties entering into loan agreement is to grant / avail the loan and not to tolerate non-payment of loan dues. Therefore, merely because of existence of the clause of penal interest in the contract for breach of the performance of the contract, it does not mean that the parties have entered into the contract for the penal interest. Therefore, the collection of penal interest does not even fall under the ambit of deemed supply under clause 5(e) of Schedule II of CGST Act.

However, contention of the proper officer was based on the ground of clause 5(e) of Schedule II of CGST Act and according to him, bounce / penal charges on non-performance of a contract is an activity or transaction which is treated as a supply of service and the applicant is receiving consideration in form of charges, liquidated damages and is accordingly required to pay tax on such amount.

Discussions by and observations of AAR

The applicant has agreed to do an act (the act of tolerating of delayed payment of EMIs by their customers) and such act, by the applicant, squarely falls under clause 5(e) of Schedule II of CGST Act and therefore, amount received by the applicant for having agreed to do such an act, would attract tax liability under GST laws.

Further applicant stated that penal interest is part of interest and therefore, eligible for exemption. However, penal interest is received by the applicant only because their customer/s have defaulted in repaying the due EMIs. This amount is over and above the interest amount received on account of extending deposits, loans, etc.

Further, assumption by applicant that EMI is nothing but a new loan amount is not only fallacious but also devoid of merit because from the agreements it is seen that rate of interest on loan advanced and rate of penal charges are collected on so called new loan amount (i.e. defaulted EMI) are also different. Further, as per facts of the case, the rate of penal interest ranges between 2% to 4% i.e. not fixed as in case of interest on loan.

Thus, it is very clear that in case of default of EMI by the customer, the applicant would tolerate such act of default or situation and the defaulting party was required to compensate the applicant by way of payment of extra amounts in addition to the principal and interest.

Ruling of AAR

In respect of question (1), penal interest is not to be treated as interest for the purpose of exemption.

In respect of question (2), the aforesaid activity squarely falls under clause 5(e) ofSchedule II of the CGST Act and, therefore, construes as "supply" and would attract tax liability under GST.

❍❑❍

Truth is infinitely more weighty than untruth; so is goodness.

— *Swami Vivekananda*

 

CA Rajiv Luthia & CA Keval Shah

INDIRECT TAXES
Service Tax – Case Law Update

Citation: 2018-TIOL-2432-HC-DEL-ST

Case: National Building Construction Company Ltd vs. Union of India and Ors.

Background facts of the case

The petitioner has filed the present writ petition under Article 226 of the Constitution of India challenging the letter dated 3rd December, 2015 from the DGCEI informing them about the permission accorded authorising the Additional Director General, DGCEI, Lucknow Zonal Unit to investigate service tax evasion cases of all branches of the petitioner. The petitioner also prays for quashing of notices/summons issued for production of documents and details issued by Asst. Director, DGCEI, Regional Meerut Unit on the ground that they are unwarranted and arbitrary.

The petitioner is primarily engaged in carrying out civil work and construction for various departments of government and public sector undertakings all over India. The petitioner has not opted for centralized registration for service tax. The petitioner has 88 service tax registrations in different Commissionerates and consequently files and submits separate service tax returns based on registrations.

Petitioner's unit in Greater Noida was subjected to audit by Additional Commissioner (Audit), Central Excise, Noida for the period April, 2010 to March, 2013. The main audit objection is on the petitioner's alleged failure to pay service tax on the Project Management Consultancy Charge.

Similarly, the CCE, Patna has issued SCN dated 13th March, 2015 for recovery of Service Tax on payments received by the petitioner for rendering service in the nature of advice and consultancy for technical assistance under the heading "Consultancy Engineer" service @ 10% of the total project executed under the Pradhan Mantri Gram Sadak Yojana.

As per the respondents the issue and question of service tax liability on PMC charge is almost a universal issue that would arise across most registrations. Consequently, file F.No. DGCEI/LNZU/NBCC/190/2015 was moved and *vide* impugned letter dated 3rd December, 2015, the Assistant Director (Investigation), DGCEI has conveyed and authorised the Additional Director General, Lucknow to investigate the case of service tax evasion by all branches of the petitioner. The investigation and enquiry are specific to the PMC charge. The respondents submit that centralised investigation is necessary and justified as multiple investigations all over the country on the same issue and question would result in inconvenience, harassment and wastage of time and resources.

As per petitioner, Finance Act does not permit centralised enquiry and investigation except where search has been conducted or arrest has been made u/s. 90 of the Act. Section 14 of the CE Act, 1944 states that summons could be issued by an officer making an enquiry. Therefore, summons cannot be issued by an officer not permitted to conduct enquiry or where no enquiry is pending. Any authorised officer u/s. 73 of the Finance Act during the course of pending proceedings is entitled to ask a person to produce accounts, documents etc. Accordingly, summons/notices u/s. 14 of CE Act issued by the Office of Assistant Director, DGCEI, Regional Unit, Meerut asking for details and documents on all India basis are invalid and contrary to law.

As per the petitioner, the following legal issues arise for consideration in the present writ petition:

"a. In the absence of any provision under the Finance Act, 1994, whether the DGCEI is empowered to conduct inquiry/ investigation and if so what is the scope and safeguard for the tax payers?

b. Whether the issuance of summons u/s.14 Central Excise Act, 1944 has to be preceded by an inquiry, if so, said inquiry should be under specific provision of law or not?

c. Whether DG, DGCEI direction to investigate against petitioner on all India basis by formation of an opinion that "service tax evasion by all branches of NBCC" in impugned letter dated 3-12-2015 is based on any materials and sustainable in law?

d. Whether the Finance Act has provision for reassessment/reinvestigation for the same very period for which investigation/ audit/issuance of SCN/Adjudication of SCNs have already been done, if so what is the scope and parameter of the same in the absence of any provisions in law?

e. Whether the officers of DGCEI are permitted to proceed on the change of opinion, if so what are the parameter in the absence of any review power under the law?

f. Whether in the facts and circumstances, the DGCEI investigation and issuance of summons is arbitrary, malicious and motivated?"

Observations of the High Court

a) Service tax does not have a separate enactment like the CE Act, Customs Act or the Income-tax Act. Section 65B of the Act which deals with interpretation. *Vide* clause 55 it is stated that the words and expressions used in Chapter V of the Finance Act relating to service tax but not defined in the Chapter and are defined in the CE Act or the rules made thereunder, shall so far as may be, apply in relation of service tax. Sections 12E & 14 in addition to other provisions of the CE Act have been made applicable to service tax in view of section 83 of the Act. Conspicuously provisions of the Income-tax Act have not been made applicable to service tax. We have made this observation as some of the arguments by the petitioner proceed are predicated on the procedure and principles applicable to the income tax proceeding, notwithstanding the difference in the statutory scheme and procedure prescribed under the Finance Act read with and as per CE Act. In the Income-tax Act each assessment year is separate and self-contained period which is assessed to tax. Income-tax Act is return centric and assessment is made year wise. Differences between procedure and principles applicable under the Finance Act read with CE Act & the Income-tax Act are manifold and need not be elaborated in entirety for the present judgment. However, we would encounter diametric difficulties if we apply the procedure & principles applicable to income tax proceedings to the procedure applicable to service tax as per the Finance Act.

b) Section 73 of the Finance Act prescribes the procedure and is the complete code for recovery of service tax non or short levied or paid or erroneously refunded to a person. The SCN envisaged and as per the statutory mandate of Section 73(1) must particularise and specify with factual and legal assertions why recovery of the amount quantified should not be made on account of non or short levy, payment or erroneous refund. Necessarily, these details and particulars should have been previously ascertained, as they would constitute the basis and foundation of the notice u/s. 73(1). **Assessment in terms of Section 73(1) is clearly period specific and not return specific. The period may or may not coincide with the assessment year or even one return. At the same time it may relate to several returns or a case where no return has been filed.** Further, section 73(1B) of the Act clarifies that where the assessee/person has not paid self-assessment tax as per the return in full or in part, the deficient amount can be recovered along with interest without service of notice under sub-section 1 to section 73 of the Finance Act. Recovery of tax not paid in terms of the return does not require issue of notice u/s. 73(1) of the Act. Thus, as per section 73, unless payment is made in terms of sub-sections 3 & 4 thereof, the starting point for proceedings for adjudicatory assessment is the issue of SCN u/s. 73(1) of the Act. It is not the service tax return *per se*, but the SCN which is adjudicated and decided. This requirement and mandate of Section 73(1) has to be kept in mind when we examine the procedural provisions and power vested with the CEO to conduct enquiry and investigate to ascertain details and facts. Issue of SCN is a condition precedent to raising an enforceable demand is the principle laid down in and *Gokak Patel Volkart Limited vs. CCE, Belgaum (1987) 2 SCC 93.*

c) The heading of Section 72 empowers and authorises the CEO to make and pass an order known as "best judgment assessment". In terms, the CEO can make an assessment of the value of the taxable service to the "best of the judgment" and determine the sum payable by an assessee or refundable to the assessee on the basis of such assessment. It is a type of assessment authorised by law in the absence of full and complete details and material. "Best judgment assessment" need not be exact and precise, albeit an objective and fair assessment of the taxable amount based upon the material and evidence available and gathered. This provision cannot be equated with and read as a provision prescribing and authorising a separate and alternative procedure for adjudication u/s. 73. Section 72 does not authorise CEO to take up returns for service tax for scrutiny assessment and pass an adjudicatory order, except possibly in cases where refund is claimed. Section 72 does not prescribe a procedure for taking up the returns for assessments, except when refund of tax is due as per the return and has to be adjudicated.

d) Provisions of Chapter V, section 73(1) in particular, and the Rules are also clear pointers that section 72 is a provision which authorises and empowers the CEO to make "best judgment assessment" in proceedings for recovery under and in terms of section 73. Neither section

72 nor Rules postulate passing of an assessment order for recovery of service tax independent of and without following the procedure u/s. 73(1). Section 72 only authorises and states "best judgment assessment" order can be passed when the circumstances so warrant. In view of the above discussion and ratio, we would in a given case accept that there could be more than one SCN overlapping the same period of time for distinct issues and subject matters. The Finance Act does not bar and prohibit different SCN on different issues, facts and subject matter. Each SCN being independent has to be adjudicated and decided. However, repeated or multiple SCN u/s. 73(1) can result in harassment and inconvenience and also reflect on the governance and administration of the Finance Act. Every attempt should be made to issue consolidated SCN even on divergent issues and subject matters.

e) Section 14, empowers the CEO to issue summons to any person to give evidence and produce documents. The summons can be issued to any person whose attendance the officer considers necessary. The power can be exercised to collect evidence or a document or any other thing in any inquiry which the officer is making for any purposes under the Act. Use of the words "any inquiry" and "for any purposes under the Act" are significant and important when we examine the contention of the petitioner that the word "inquiry" used in Section 14 would mean enquiry post the issue of SCN u/s. 73(1) and not before issue of a notice under said section. The statutory requirement is that the enquiry which the officer is making should be for any of the purposes of the Finance Act. The expression "any of the purposes of this Act" used in section 14 though a wide and broad expression is also a restriction. When read in this manner, we would not restrict the scope and power to collect evidence, documents etc., to cases where SCN u/s. 73(1) has been issued or any other specific proceeding is pending. Summons u/s. 14 can be issued to ascertain and verify details and ask for relevant evidence and material or the purpose of the Finance Act. This would be the right way to interpret section 14 for the procedure prescribed and followed both in CE Act and Finance Act is that the SCN is issued post and after information, evidence and documents have been collected and facts are ascertained. We are therefore not inclined to accept the contention giving a restricted meaning to the term "inquiry" in section 14 as confined to post notice enquiry after issue of notice u/s. 73(1). However, we should not be understood as accepting or stating that notice or summons u/s. 14 of the CE Act can be issued without any cause, reason or justification. Any power given cannot be abused and exercised in an arbitrary manner or for ulterior motives. Motivated and capricious deviations in exercise of power u/s. 14 of the CE Act can always be checked by the Court.

f) It would be now relevant to deal with the contention of the petitioner that the respondents have the power to conduct Special Audit u/s. 72A and access and visit the premises registered with the Service Tax Department under Rule 5A of the Rules. The petitioner referring to Rule 5A had stated that they would have no objection to an authorised officer from the Commissionerate having access to the premises registered under the Rules for the purpose of carrying out scrutiny, verification and check. Respondents on the other hand submit that Rule 5A is for periodical checks by the officers and notwithstanding the said power, the Board can issue a notification vesting all-India power with the particular CEO in view of Rule 2(b) of the CE Act. Rule 5A no doubt vests and authorises the CEOs with power to access registered premises of a person for scrutiny, verification and check but this would not show that the CEO does not have power and cannot take recourse to investigation and issue summons for collection of evidence and documents u/s. 14. The power conferred in the form of section 14 like conduct of Special Audit u/s. 72A or access to the registered premises under Rule 5A(1) have the same object and purpose i.e. empower the CEO to ascertain facts and also collect material and evidence. These arguments have to be rejected as power u/s. 14 and other powers relating to investigation and enquiries cohabit and exist together and are also independent. It may not be appropriate to exercise power under Rule 5A, when direction to produce documents and furnish information would be appropriate and suffice.

g) Exercise of discretionary power relating to procedure can be challenged on limited number of grounds, like patent and gross misuse, *ex facie* grave disproportionate hardship and inconvenience to the person when a more convenient and acceptable mode for compliance is available, or *mala fides* in exercise of power etc. Courts would, however, not interfere merely because the authority has exercised discretion that is not acceptable to the assessee. The choice whether or not to exercise power of special audit, summons etc., is for the respondents to decide and exercise, and not for the petitioner to direct.

h) Rule 3 of the CE Rules state that the Board may appoint such CEO as they think fit for exercising the powers under Chapter V of the Finance Act. Rule thus empowers and authorises the Board to appoint CEO to exercise power relating to service tax. Thus investigation/inquiry functions and adjudicatory functions can be demarcated and divided between/amongst different CEOs. While dividing and demarcating the functions, the Board for the said purpose can fix local limits within which the CEO would exercise power and also specify the taxable service in relation to which such power can be exercised. Thus, the Finance Act or the Rules i.e., Chapter V of the Finance Act, 1994 or Service Tax Rules,1994, do not refer to and specify territorial or pecuniary jurisdiction to the CEO in relation to powers to be exercised under the Finance Act. This is left to the Board to decide and confer power on the CEOs. We would observe that Rule 3 of the Rules confers very wide discretion to the Board without any restriction and limitation to confer jurisdiction on the CEOs to exercise powers under the Finance Act and the Rules. The Board is empowered to assign, withhold, and confer jurisdiction amongst different officers and for this purpose demarcate and divide the functions to be performed. Rule 3 of the Rules, no doubt, refers to local limits i.e., the area or the "Venue". However, taxation laws recognise difference and distinction between "jurisdiction" and "venue". The term "venue" refers to place of assessment i.e., location at which the party may request the case to be tried. The question of "jurisdiction" relates to the subject matter i.e., jurisdiction of an officer to exercise power. <u>A person who is not the CEO, lacks subject matter jurisdiction and consequently any action, act or order would suffer from lack of "jurisdiction" in a sense that it cannot be waived. Lack of jurisdiction by way of subject matter can be challenged at any time, even in the execution proceedings and cannot be waived by consent. Lack of jurisdiction</u>

<u>by "venue" can be waived by consent or when not raised within reasonable time by applying principle of estoppel. No assessee has a vested right to be assessed at a particular location and "venue"</u>.

i) It follows and we hold that the Board has wide discretion in power while fixing the local limit assigned to a CEO. Local limit can be PAN or all India. Argument and contention that use of the expression "local limit" impliedly excludes all India jurisdiction is without foundation and fallacious. The provision permits and allows the Board to fix "local limits" and does not bar and prevent the Board from conferring all India jurisdictions. The Board is equally empowered to authorise centralised or pan India investigations to be undertaken by the CEOs. This may indeed be desirable and necessary to curtail delay, facilitate complete and detailed investigation at one location rather than multiple investigations and enquiries which would be overlapping. Multiple enquiries would be inconvenient and cause harassment to many assessees especially when similar or identical issues are involved. A pragmatic and practical approach is required in matters of procedure.

j) In terms of the said Rule, the Board has issued Notification Nos. 20/2014 and 22/2014 both dated 16th September, 2014. Notification No. 20/2014 (the first notification) is a master notification which defines territorial jurisdiction (local limits) of the field formations on geographical basis. It specifies territorial jurisdiction for exercise of powers by officers in service tax matters. Notification No. 22/2014 (the second notification) specifies jurisdiction of officers of DGCEI throughout territory of India and empowers them with all powers under Chapter V of the Finance Act. The second notification clearly answers the contention raised. Validity of this notification is not challenged in the writ petition. Learned counsel for the petitioner in the written submission had questioned validity of the second notification, but in the absence of pleadings and prayer in the writ petition the contention cannot be examined and adjudicated.

k) We do not agree with the petitioner's assertion that centralisation of investigation would lead to harassment and inconvenience. Normally, it would be desirable that investigations are centralised when identical and similar issues in case of an assessee arise for consideration in different Commissionerates. Even if the information sought is not available and has to be collected from the different locations, this can be done and with a request to the respondents to grant reasonable time

l) In view of the aforesaid discussion, it is held as under:

(i) ***CEOs of DGCEI have all India jurisdictions and can issue notices and enquire into the matters relating to service-tax against any assessee/ person even if the said person or assessee is registered with one or multiple Commissionerates.***

(ii) ***Notice u/s. 14 of the CE Act i.e. Central Excise Act can be issued even if proceedings u/s. 73 of the Finance Act, 1994 are not pending. However the notice should relate to matters and issues relating to provisions of services and imposition of service tax.***

(iii) ***The petitioner should comply with the notices issued or would be issued by the CEOs, DGCEI to furnish evidence and documents pertaining to the PMC charge in respect of Commissionerate/***

registration except those subject matter of SCN dated 13th March, 2015 issued by the Commissionerate of Central Excise and Service Tax, Patna.

(iv) Interim orders are accordingly, vacated except and limited to evidence and documents, subject matter of demand cum-SCN dated 13th March, 2015 issued by the Patna Commissionerate.

(v) Period between 10th February, 2016 when the stay order was passed till the pronouncement of the judgment would be excluded for purpose of computing limitation period specified for issue of show cause notice u/s. 73(1) of the Finance Act.

Citation: 2018-TIOL-3296-CESTAT-MUM

Case: Tahnee Heights Co-operative Housing Society vs. Commissioner of CGST, Mumbai South

Background facts of the case

Appellant is a co-operative housing society registered under Maharashtra Co-operative Societies Act, 1960. The appellant is the owner of the building, known as "Tahnee Heights", in which members of the society own their residential flats. The members of the appellant's society contribute towards maintenance and up-keep of the building and common expenses, as per the bye-laws adopted by the society under the Act of 1960. For the period July, 2015 to January, 2017, appellant had paid service tax amount of ₹ 20,77,586/- under protest under the category of "Club or Association service", in respect of the contributions received from its members.

Later, the appellant had filed six nos. of refund applications on the ground that there are no distinct persons viz, service provider and service receiver and since the person contributing and benefiting are the same, as per the principles of mutuality, the activities should not be subject to levy of service tax. It was further contended that the appellant not being a body corporate, its case will not be governed by *explanation 3(a)* appended to section 65B (44) of the Finance Act, 1944 (effective from 1-7-2012)

The revenue / CCE (Appeals) rejected refund application *inter alia*, on the ground that in the light of *explanation 3(a)* to section 65B(44) ibid, the appellant and its members are to be treated as distinct entities and therefore, the appellant has correctly paid service tax. Hence, the present appeal.

Arguments put forth

The appellants submitted as under:

a) There is no involvement of any consideration in as much as the appellant only recovers contribution from the members and its apportionment is pre-decided in accordance with the bye-laws of the society. It was submitted that due to the principle of mutuality, there are no distinct persons and the transaction does not fall within the ambit of first part of the definition of "service".

b) It was further submitted that due to the incorporated status of the appellant, *explanation 3 (a)* of section 65B(44) of the Finance Act, 1994 does not apply for levy of service tax.

The respondents submitted as under:

a) As per the concept of "negative list" of services defined u/s. 66D (w.e.f. 1-7-2012), any service if not categorised there under or specifically exempted under any notification, shall be considered as a taxable service, for the purpose of levy of service tax.

Decision

a) There is not much of difference for recognition of the taxable service in dispute, for levy of service tax, under both the unamended i.e., Section 65(25aa) & 65(105) (zzze) and amended provisions section 65B(44) of the service tax statute. In order to be categorised as a "taxable service", there must be existence of two parties i.e., the service provider and the service receiver. As far as the relationship between an incorporated society or club and its members is concerned, it is an undisputed fact that such incorporated association is a distinct legal entity. However, since the association was formed or constituted and existed for the exclusive purpose of catering/meeting to the requirements of its members, as per the laid down policy in the bye law, it cannot be said that here is involvement of two persons, one to be termed as the service provider and the other as the service receiver. Thus, the incorporated association and its member being one and the same, the activities undertaken or the services provided by the former will not be considered as a service, exigible to service tax under the principle of mutuality.

b) Considering various judgments delivered by Hon'ble SC and the Hon'ble HC on the issue of principle of mutuality *vis-a-vis* leviability of tax on the club or association service, this Tribunal in the case of Federation of Indian Chambers of Commerce & Industry (supra) has held that on application of the principle of mutuality, services provided by clubs/ associations to their respective members would not fall within the ambit of the taxable "club or association" service. Though the said decisions were rendered under the unamended definition of taxable service (up to 30-6-2012), but the ratio laid down therein is squarely applicable to the post amended definition of "service' contained in the negative list regime (w.e.f. 1-7-2012), in as much as, in absence of presence of both service provider and service receiver, the transaction cannot be statutorily terms as taxable service and will not be exigible to service tax

c) As regards the issue of ascertaining the status of the appellant, whether an incorporated body or otherwise, for the purpose of consideration of applicability of *explanation 3(a)* appended to section 65B of the Act. It is observed that the statutory provisions Maharashtra Co-operative Act, 1960, of reveals that upon registration of the society, the same is legally accepted as a body corporate and thereafter, its function and operation are strictly guided as per the laid down bye-laws, provided for the purpose. In this case, it is no doubt, a fact that the appellant is a co-operative society and is duly incorporated under the Act of 1960. The appellant also does not provide any service to its members, who pay the amount towards their share of contribution, for occupation of the units in their respective possession. Further, the fact is also not under dispute that the appellant does not provide any facilities or advantages for subscription or any other amount paid. Thus, under such circumstances, the appellant cannot be termed as an unincorporated association or a body of persons, for the purpose of consideration as a 'distinct person'. Accordingly, the *explanation* furnished under clause 3(a) in section 65B of the Act will not designate the appellant as an entity, separate from its members.

d) It is concluded that the activities undertaken by the appellant should not fall within the scope and ambit of taxable service, for payment of service tax. Therefore, service tax amount paid by the appellant should be eligible for refund.

Citation: 2018-TIOL-2474-HC-MUMBAI-ST

Case: Bhushan Bal Kulkarni vs. Asst. Commissioner, Service Tax Division-I

Background facts of the case

The petitioner filed a declaration under VCES scheme in proper format on 23rd March 2013. The declaration covered the period from April, 2010 to December, 2012. For such period, the Petitioner made a declaration of unpaid tax of ₹ 4,73,527/-. Subsequently, the petitioner realised that such declaration of ₹ 4,73,527/- of unpaid tax included a sum of ₹ 1,32,842/- which the Petitioner had already paid in the past. According to the petitioner, therefore, his net tax dues were of ₹ 3,40,686/-. On the basis of such reduced tax liability, the petitioner also deposited with the Government the instalments as per the terms of the scheme of settlement.

On 27th December, 2013, petitioner addressed a letter to the department stating that he has already paid the tax dues of ₹ 3,02,841/-, which is an excess of the first instalment.

The Assistant Commissioner heard the petitioner on the question of grant of benefits of the scheme. The petitioner urged that the original declaration of tax dues of ₹ 4,73,527/- was inclusive of an amount of ₹ 1,32,841/- already paid by the Petitioner and that the petitioner's net tax liability was only ₹ 3,40,686/-. He further pointed out that according to such liability the petitioner had already deposited the instalments which would satisfy the requirements of the scheme.

The ACST rejected the petitioner's plea on the ground that petitioner himself had made a declaration of ₹ 4,73,527/-. The petitioner could have but had not asked for the amendment of the declaration. In absence of any such amendment the petitioner had to pay the instalments as per the declared tax dues of ₹ 4,73,527/-.

The petitioner has challenged the order of ACST rejecting the application for the benefit of under VCES.

Decision

a) The ACST does not dispute Petitioner's assertions that not the tax of ₹ 4,73,527/-, but sum of ₹ 3,40,686/- was outstanding. The declaration includes payment of ₹ 1,32,841/- previously made.

b) The ACST ought to have considered the correct figure of tax dues. He could not have enforced the petitioner's declaration which was factually erroneous. Even if the declaration required an amendment, the petitioner had under his letter dated 27th December, 2013 brought the correct facts to the notice of the Departmental Authorities. Such letter could have been treated as a request for amending the declaration. Nothing is brought to notice that such amendment application had to be filed in a particular format. Even if so, the same would be a purely procedural aspect.

c) Impugned order dated 23rd January, 2015 is set aside. No other defect is pointed out in the petitioner's application. The authority shall therefore grant the benefit of the VCES to the petitioner.

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> Practice truthfulness. Twelve years of absolute truthfulness in thought, word and deed gives a man what he wills.
>
> — *Swami Vivekananda*

Janak C. Pandya, *Company Secretary*

CORPORATE LAWS
Company Law Update

[Before the National Company Law Appellate Tribunal – New Delhi] Order dated 14th November, 2018.

1. Company Appeal (AT) (Insolvency) No. 82 of 2018

   Binani Industries Limited vs. Bank of Baroda & Anr.

2. Company Appeal (AT) (Insolvency) No. 123 of 2018

   Rajputana Properties Pvt Ltd. vs. Binani Industries Limited

3. Company Appeal (AT) (Insolvency) No. 188 of 2018

   Rajputana Properties Pvt Ltd. vs. Ultratech Cement Ltd. & Ors.

4. Company Appeal (AT) (Insolvency) No. 216 of 2018

   Binani Industries Limited vs. Binani Cements Limited & Anr.

5. Company Appeal (AT) (Insolvency) No. 234 of 2018

   Mr. Vijay Kumar Iyer Resolution Professional vs. Mr. Braj Bhusandas Binani & Ors.

The purpose of the Resolution Plan under the Insolvency and Bankruptcy Code is for maximisation of the value of assets of the Corporate Debtor and same is not a sale or auction or recovery or liquidation of the Corporate Debtor.

Brief

All the above appeals arise out of the order(s) passed by the Adjudicating Authority (National Company Law Tribunal), Kolkata Bench, Kolkata **("AANCLT")** All the above appeals were heard and are disposed-off by the common judgment.

The following points were noted from the order of the AANCLT.

1. The Corporate Insolvency Resolution Process **("CIRP")** was initiated against Binani Cements Limited.

2. Mr. Vijay Kumar Iyer, Resolution Professional **("RP")**, invited the "Resolution Plan" for the above.

3. M/s. Rajputana Properties Private Limited **("Rajputana")** and Ultratech Cement Limited ("Ultratech") have submitted their resolution plans.

4. The Committee of Creditors **("CC")** has approved the plan submitted by

Rajputana. However, 10.53% of the CC who were forced to vote in favour of the plan recorded a protest note alleging that they had not been dealt equally as compared to other financial creditors.

5. The resolution plan of Ultratech and its revised offer was not properly considered by the CC.

6. The AANCLT also observed that Rajputana's plan was discriminatory and contrary to the scheme of the IBC and directed the CC to consider the other plans including that of Ultratech.

Various applications were filed objecting to various findings / directions of the AANCLT as given below.

1. AANCLT order to referred back the Plan to RP and to consider in accordance with the rules and regulations of the IBC. The grievances of the appellant are that they should have been allowed to interact with and meet the bidders/Resolution Applicants, Financial creditors and other stake holders.

2. AANCLT has not allowed the proposal for the repayment of the dues of the "Financial Creditors" and close the "Corporate Insolvency Resolution Process" order due to absence of any jurisdiction.

3. CC has been granted liberty to consider the settlement plan proposed by Binani Industries Limited.

4. The plan of Rajputana has not been accepted for various reasons as mentioned in the order.

5. The adverse observations made against the RP.

The questions before the NCLAT is as follows.

1. Whether the "CC" discriminated between the eligible "Resolution Applicants" ("RA") while considering the plan of Rajputana? And

2. Whether Rajputana's plan is discriminatory.

Judgment

The NCLAT has dismissed all the applications, allowing the plan of Ultratech and directed the AANCLT to remove certain findings against the RP.

The NCLAT has made the following observations.

1. The objective of the IBC is to promote resolution over liquidation. Resolution is for the maximisation of value of assets of the Corporate debtor. The judgment in the case of *"Arcelor Mittal India Pvt Ltd., vs. Satish Kumar Gupta and Ors."* was referred. In the above case, the Supreme Court has observed that .... Corporate Debtor consist of several employees and workmen...... if there is a resolution applicant who can continue to run the Corporate Debtor as going concern, every effort must be made to try and make it possible…

2. On "Financial Creditors", as Members of the "Committee of Creditors and their Role," it has mentioned that it should have capability to assess viability and willing to modify terms of existing liabilities. Further, the liabilities of all creditors who are not part of the negotiation process must also be met.

3. IBC aims at promoting availability of credit and both "Financial Creditors" as well as "Operational Creditors" need to be on a level playing field.

4. Dues of "Operational Creditors" must get at least similar treatment as compared to the dues of "Financial Creditor".

5. Resolution plan is not a sale or buying the "Corporate Debtor" but it is resolution of the Corporate Debtor as a going concern. There is no need for CIRP, Interim Resolution Professional, Resolution Professional or regulated process for sale.

6. Resolution plan is not an auction. The viability of a "Resolution Plan" are not amenable to biding or auction. It requires application of mind by the "Financial Creditors" who understand the business well.

7. Resolution plan is not an individual effort by a creditor to recover its dues. IBC prohibits and discourages recovery in several ways.

8. It is also not a liquidation. IBC allows liquidation only on failure of "CIRP"

9. On Rajputana's Resolution plan, it has observed that (i) it discriminates between the two "Financial Creditors" who are similarly situated as guarantors. (ii) on Operational Debtor, for unrelated parties it has provided 35% of verified claim and no amount for related party. It has observed that IBC does not prescribe differential treatment between the similarly situated "Operational Creditors" or the "Financial Creditors" on one or other grounds.

10. Clauses (b) and (c) of Regulation 38(1) being inconsistent with the provisions of IBC. IBC Board by its Regulation cannot mandate that the Plan should provide liquidation value to the "Operational Creditors [Regulation 38(1)(b)] or liquidation value to the dissenting Financial Creditors [Regulation 38(1)(c)]. The said regulation being against Section 249(2) cannot be taken in to consideration. The judgment in case of "Central Bank of India vs. Resolution Professional of the Sirpur paper Mills Ltd. & Ors. Company Appeal (AT) (Insolvency) No. 526 of 2018 was referred.

11. CC has failed to safeguard the interest of the stakeholders of the "Corporate Debtor" but also ignored the revised plan by Ultratech, which has taken care of maximisation of the assets of the Corporate Debtor.

12. Section 25(2) (h) provides for invitation of "Resolution Plan" this also includes submission of revised offer in continuation of the plan already submitted and accepted by the RP.

Subsequently Rajputana filed an application before the Supreme Court against NCLAT order. The Hon'ble Supreme Court has upheld the NCLAT order by dismissing the appeal by Rajputana.

Sanjeev Shah & Abdullah Faikh

CORPORATE LAWS

Overview of Companies (Amendment) Ordinance, 2018 – An ever changing law!

Background

The Ministry of Corporate Affairs (MCA) had, in July 2018, constituted a committee (the Committee) under the Chairmanship of Mr. Injeti Srinivas, Secretary, MCA, to review the existing framework under the Companies Act, 2013 (2013 Act), dealing with offences and related matters and to make recommendations to improve the standards of corporate compliance.

The Committee submitted its report in August 2018. The Committee recommended that the existing rigour of the law should continue for serious offences, whereas for lapses that are essentially technical or procedural in nature, they may be shifted to an in-house adjudication process. The Committee observed that this would serve the twin purposes of promoting ease of doing business and better corporate compliance. It would also reduce the number of prosecutions filed in the Special Courts, which would, in turn, facilitate speedier disposal and bring serious offenders to book.

The Committee also recommended declogging the National Company Law Tribunal (NCLT) through significant reduction in compounding cases before the NCLT. Additionally, the report also touched upon certain essential elements related to corporate governance, such as declaration of commencement of business (reinstatement of the erstwhile section 11 of the 2013 Act), maintenance of a registered office, protection of depositors' interests, registration and management of charges, declaration of significant beneficial ownership and independence of independent directors.

In order to give effect to the above recommendations of the Committee, the Companies (Amendment) Ordinance, 2018 (the Ordinance) was promulgated on 2nd November 2018 amending various provisions of the 2013 Act.

This article contains salient features of the Ordinance.

I. Recategorisation of offences

Certain offences have been recategorised as defaults carrying civil liabilities to bring them under an in-house adjudication mechanism. This has been **done in a two-fold manner, i.e., by removal of imprisonment for certain procedural defaults on one hand, and replacing the provision of fine with a penalty,** on the other hand. Recategorisation of offences have been made in below mentioned provisions of the 2013 Act:

- Section 53(3) – Issue of shares at a discount
- Section 64(2) – Alteration of share capital
- Section 92(5) – Annual return
- Section 102(5) – Statement to be annexed to notice of general meeting
- Section 105(3) – Proxies
- Section 117(2) – Resolutions and Agreements to be filed with Registrar of Companies (ROC)
- Section 121(3) – Report on annual general meeting
- Section 137(3) – Filing of Financial statement with ROC
- Section 140(3) – Removal, resignation of auditor
- Section 157(2) – Company to inform Director Identification Number (DIN) to ROC
- Section 159 – Punishment for Contravention in respect of DIN
- Section 165(6) – Number of Directorships in a company
- Section 191(5) – Payment to Director for Loss of Office, etc., in connection with transfer of undertaking, property or shares
- 197(15) – Overall maximum managerial remuneration and managerial remuneration in case of absence or inadequacy of profits
- 203(5) – Appointment of Key Managerial Personnel (KMP)
- 238(3) – Registration of the offer of scheme involving transfer of shares

II. Ensuring regularisation of the default and prescribing stiffer penalties in case of repeated defaults

Towards this end, the Ordinance has amended section 454(3) and Section 454(8) of the 2013 Act and introduced a new section 454A as summarised below:

Sr. No.	Section of 2013 Act	Particulars	Ordinance amendment
1.	454(3) Adjudication of Penalties	Order of adjudicating officer	The adjudicating officer shall in addition to imposing the penalty on the company / the officer in default / any other person, also give the direction of making good the default.
2.	454(8) Adjudication of Penalties	Default in compliance of adjudicating officer's order	Default is deemed to occur not only when the company or the officer in default does not pay the penalty imposed by the order of the adjudicating officer or Regional Director (RD), but also in case of failure to comply with such order.
3.	454A	Penalty for repeated default	Where a penalty in relation to a default has been imposed on a company or any other person, and such company or person commits the same default again within a period of 3 years from the date of order imposing such penalty, passed by the adjudicating officer / RD as the case may be, such company or other person shall be liable for the second and every subsequent defaults for an amount equal to twice the amount provided for such default under the relevant provision of the 2013 Act.

III. Declogging the NCLT

This is sought to be achieved in the following manner:

a) **Vesting in the Central Government the power to approve change in the financial year**

Under section 2(41) of the 2013 Act, Indian companies / foreign companies registered in India are required to follow the period of April–March, as their financial year. However, an Indian company / body corporate which is a holding company or a subsidiary or associate company of a company incorporated outside India, and is required to follow a different financial year for consolidation of its accounts outside India, it is allowed to change the financial year (to a period other than April–March), with the approval of NCLT. The Ordinance has transferred the authority of giving approval from NCLT to the Central Government.

b) **Vesting in the Central Government the power to approve conversion of public companies into private companies**

In terms of Section 14(1), the power to approve conversion of a public company into a private limited company has been shifted from NCLT to the Central Government.

Pending applications with NCLT submitted prior to 2nd November 2018 in case of (a) and (b) above will be disposed by the NCLT.

c) **Enlarging the jurisdiction of RD by enhancing the pecuniary limits up to which they can compound offences**

RD can compound an offence which is punishable with maximum fine of up to ₹ 25,00,000 (earlier ₹ 5,00,000).

IV. Other reforms

The Ordinance also seeks to improve the standards of corporate governance and tackle the menace of shell companies. In this regard, the following amendments have been made:

Sr. No.	Section of the 2013 Act	Particulars	Ordinance amendment
1.	10A	Declaration for Commencement of business	A company incorporated after the commencement of the Ordinance and having share capital cannot commence any business (or) exercise any borrowing powers unless: a) A declaration is filed by a director with the Registrar of Companies (RoC) within 180 days from the date of incorporation with regard to the receipt of subscription money from each of the subscribers to the memorandum; b) The company has filed with the RoC within 30 days of incorporation, a verification of its registered office. If aforesaid declaration of receipt of subscription money is not filed within 180 days of incorporation and the RoC has reasonable cause to believe that the company is not carrying on any business or operations, the RoC is empowered to initiate action to remove the name of the company from the register of companies. The above provisions are applicable to all companies, whether private or public, having share capital.

Sr. No.	Section of the 2013 Act	Particulars	Ordinance amendment
			Above is a reintroduction of earlier section 11 which was omitted by the Companies (Amendment) Act, 2015 in different form.
2.	10A(3) and 12	Non-maintenance of registered office to be a ground for removal of the name of the company	If the RoC has reason to believe that a company is not carrying on any business or operations, it may physically verify the registered office address of the company and if any default is found in complying with the requirement of maintenance of registered office, it may initiate action for the removal of name of the company from the register of companies.
3.	77	Registration of charges	Maximum time for creation and modification of charge on or after the commencement of the Ordinance with RoC has been reduced from 300 days to 60 days from date of creation / modification. In case of delay beyond 60 days, RoC may allow registration within further period of 60 days on payment of ad valorem fees.
4.	90	Register of Significant Beneficial Owners (SBO) in a company	Considering the importance of the SBO disclosures, the punishment for non-compliance is enhanced to the effect that the contravention is punishable with fine or imprisonment (up to one year) or both, instead of being punishable with only a fine. Further, a limitation period of one year has been prescribed for a shareholder whose rights have been suspended by an order of NCLT for not providing SBO disclosure for making an application to it for relaxation or lifting of the restrictions placed on such shares by NCLT's order. In case no such application is made within 1 year of NCLT's order, then such shares shall be transferred to the Investor Education and Protection Fund (IEPF).
5.	164	Disqualification from appointment of director	A person will be disqualified as a director if he accepts directorships exceeding the maximum number of directorships permitted i.e., maximum of 20 directorships, out of which not more than 10 shall be in public companies.

Conclusion

The Ordinance has been promulgated to reduce the burden on the NCLT from procedural matters, improve the general compliance regime and also enhance the ease of doing business in India. It has helped to bring about rationalisation of offences under the 2013 Act.

After the promulgation of the Ordinance, the MCA has, on 5th November 2018, floated notice inviting public comments on a further slew of changes to the 2013 Act. Hence, more amendments are round the corner!

Source:

1. *Companies Act, 2013*
2. *Report of the Committee to review offences under the Companies Act, 2013 – August 2018*
3. *Companies (Amendment) Ordinance, 2018 as published in the Gazette of India dated 2nd November 2018*

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CA Mayur Nayak, CA Natwar Thakrar & CA Pankaj Bhuta

OTHER LAWS
FEMA Update and Analysis

In this article, we have discussed recent amendment to FEMA through updation of Master Direction, circulars and in addition to it we have discussed few compounding orders recently issued by RBI.

1. Updated through Master Direction

A. FED Master Direction No. 5/2015-16- Master Direction – External Commercial Borrowings, Trade Credit, Borrowing and Lending in Foreign Currency by Authorised Dealers and Person other than Authorised Dealers (Updated as on 22th November, 2018)

Para 2.5 (Hedging requirements) has been amended to incorporate changes made by AP Dir. Series Circular 11 dated 6th November, 2018 & AP Dir. Series Circular 15 dated 26th November, 2018

B. FED Master Direction No. 19/2015-16 – Master Direction – Miscellaneous (Updated as on November 12, 2018)

In Para 3 (Resident bank account maintained by residents in India – Joint holder – Liberalisation) and Para 4 (Meeting of Medical expenses of NRI close relatives by resident individuals) have been amended to provide reference to Section 2(77) of the Companies Act, 2013) Section 6 of the Companies Act, 1956 has been replaced with Section 2(77) of the new Companies Act, 2013)

C. FED Master Direction No.18/2015-16- Master Direction – Reporting under Foreign Exchange Management Act, 1999 (Updated as on November 20, 2018)

Since this Master Direction has been significantly amended, it has been replaced rather than showing the changes in track mode for reader convenience.

D. FED Master Direction No. 8/2015-16 – Master Direction – Other Remittance Facilities (Updated as on November 6, 2018)

Para 3.3 (Meeting of medical expenses of NRI close relatives by resident individuals) following has been amended to provide reference to Section 2(77) of the Companies Act, 2013) Section 6 of the Companies Act, 1956 has been replaced with Section 2(77) of the new Companies Act, 2013).

2. Updated through A.P. (DIR Series) Circulars (Pending)

1) External Commercial Borrowings (ECB) Policy – Review of Minimum Average Maturity and Hedging Provisions

a) **Amendments *vide* A.P. Dir. Series Circular No. 11 dated 6th November, 2018**

In terms of paragraphs 2.4.1, 2.4.2 and 2.5 of Master Direction No. 5 on "External Commercial Borrowings, Trade Credit, Borrowing and Lending in Foreign Currency by Authorised Dealers and Persons other than Authorised Dealers", dated January 1, 2016 as amended from time to time, certain eligible borrowers raising foreign currency denominated ECBs under Track I, having a minimum average maturity requirement of 5 years, are mandatorily required to hedge their ECB exposure fully.

Extant Guidelines provided under Para 2.4.2 and 2.5 of Master Direction No.5 on "ECB, Trade Credit, Borrowing and Lending in Foreign Currency by AD and Persons other than AD", are amended as under :-

- <u>Minimum Average Maturity</u>: Present minimum average maturity requirement for ECBs in the infrastructure space by **eligible borrowers** is 5 years.

  RBI has now reduced the same **to 3 years.**

- <u>Hedging Requirements</u>: RBI has reduced the average maturity requirement from extant 10 years to 5 years for exemption from mandatory hedging provision applicable to ECBs raised by above referred eligible borrowers. Accordingly, **the ECBs with minimum average maturity period of 3 to 5 years in the infrastructure space will have to meet 100% mandatory hedging requirement.**

Further, it is also clarified that ECBs falling under the aforesaid revised provision but raised prior to the date of this circular will not be required to mandatorily roll-over their existing hedges.

Accordingly para 2.5 of the Master Direction has been amended.

(Comments: The reduction in the average maturity period and mandatory hedging requirement period is a welcome move and will help borrowers to raise funds for short term period and reduce the hedging cost.)

b) **Amendments *vide* A.P. Dir. Series Circular No. 15 dated 26th November, 2018.**

On a further review of the extant provisions, RBI has **reduced the mandatory hedge coverage from 100 per cent to 70 per cent** for ECBs raised under Track I of the ECB framework by eligible borrowers given at paragraph 2.4.2(vi) of the aforesaid Master Direction for a maturity period between 3 and 5 years.

RBI further clarified that ECBs falling within the aforesaid scope but raised prior to the date of this circular will be required to mandatorily rollover their existing hedge(s) only to the extent of 70 per cent of outstanding ECB exposure.

The relevant paragraph of Master Direction has been updated.

(Comments: The reduction in the mandatory hedge cover from 100 per cent to 70 per cent is a welcome move and will help borrowers to reduce the hedging cost)

3. Analysis of some recent compounding orders issued by RBI:

A. Inbound Investment (FEMA 20/2000-RB)

1. Failure to obtain, specific and prior Government approval for issue of shares to person resident outside India against pre-operative / pre-incorporation expenses

Applicant	Elringklinger Automotive Components (India) Private Limited
Compounding Application number	C.A. No. 752/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under compounding order	₹ 35,28,759/-
Date of order	06th September, 2018
Facts of the case	Amongst other facts, the parent of the applicant Elringklinger AG, Germany, directly made a payment of ₹ 1,95,05,050/- on November 3, 2006, to M/s. Maharashtra Industrial Development Corporation ('MIDC') on behalf of the applicant to acquire land for setting up its manufacturing plant in Pune, Maharashtra as pre-operative/ pre-incorporation expenses. In turn, the applicant allotted 19,50,505 equity shares to M/s. Elringklinger AG, Germany. The shares of the applicant were allotted on February 27, 2007, to its parent company against pre-incorporation expenses of November, 2006. However, issue of equity shares in lieu of pre-incorporation expenses was made permissible by the Consolidated FDI Policy Circular which came into effect only from April 1, 2011; the applicant was required to obtain approval of the Foreign Investment Promotion Board (FIPB), Ministry of Finance. It was however denied the approval *vide* FIPB letter dated March 31, 2017, in which the company was also directed to unwind the said transaction by way of repatriation of the investment proceeds by the investee company to the foreign investor. In order to implement the said order the applicant unwound the transaction on December 29, 2017.
Selected Contravention	<u>Failure to obtain, specific and prior Government approval for issue of shares to person resident outside India against pre-operative / pre-incorporation expenses</u>: Paragraph 3 (e) of Schedule 1 of erstwhile Foreign Exchange Management (Transfer of issue of Security by a Person Resident outside India) Regulations, 2000 notified *vide* Notification No. 20/2000-RB stated as follows: "an Indian company intending to issue shares to a person resident outside India, in accordance with these Regulations directly against foreign inward remittance (or by debit to NRE account/ FCNR account) or against consideration other than inward remittance shall obtain prior approval of the Foreign Investment Promotion Board (FIPB) of.

	Government of India, if the Indian company : proposes to issue shares to a person resident outside India against pre-operative/ pre-incorporation expenses (including payments of rent etc.), subject to compliance with the conditions specified by the Government of India and the Reserve Bank from time to time
Comments	Though Foreign Exchange Management (Transfer or Issue of Security By a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations; Para 1(3)/1(4)/1(5) of Schedule 1 of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Para 3(e) of Schedule 1 of erstwhile FEMA 20/2000- RB dated May 3, 2000 which allow issue of shares against pre-incorporation/pre-operative expenses under automatic route subject to conditions. It is a point to ponder whether capital expenditure could at all be classified as pre-incorporation/pre-operative expenses?

2. Delay in filing Annual Return on Foreign Liabilities and Assets (FLA Returns)

Applicant	Acko Technology & Services Private Limited
Compounding Application Number	C.A. No. 756/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under compounding Order	₹ 10,000/-
Date of order	1st August, 2018
Facts of the case	The applicant had received foreign inward remittance in Financial Year 2016-17. The applicant had not filed the Annual Return on Foreign Liabilities and Assets (FLA return) to the Reserve Bank of India for the Financial Year 2016-17 on or before July 15.
Contravention	<u>Delay in filing Annual Return on Foreign Liabilities and Assets (FLA Returns)</u> : Paragraph 9(2) of Schedule 1 of erstwhile Foreign Exchange Management (Transfer of issue of Security by a Person Resident outside India) Regulations, 2000 notified *vide* Notification No.20/2000-RB read with A. P. (DIR Series) Circular No. 29 dated February 2, 2017 stated as follows: All Indian companies which have received Foreign Direct Investment in the previous year(s) including the current year, shall submit to the Reserve Bank of India, on or before the 15th day of July each year, a report titled 'Annual Return on Foreign Liabilities and Assets' as specified by the Reserve Bank from time to time.
Comments	Though Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations; Regulation 13(3) of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Para 9(2) of Schedule 1 of erstwhile FEMA 20/2000- RB dated May 3, 2000. Guidance on computation matrix for compounding of contravention relating to non-submission / delayed submission of FLA was introduced *vide* AP (DIR Series) Circular No. 29 dated February 02, 2017.

3. Delay in receipt of a part of the consideration for the partly-paid equity shares issued to a non-resident beyond the prescribed time limit.

Applicant	Hinduja National Power Corporation Limited (HNPCL)
Compounding Application Number	C.A. 4687/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under Compounding Order	₹ 62,81,097/-
Date of order	7th September, 2018
Facts of the case	In order to finance the cost escalations of its 1040 MW thermal power project at Vishakhapatnam, applicant issued partly paid-up equity shares under a rights issue to the existing resident and non-resident shareholders on June 12, 2015. The shares were accordingly allotted on June 29, 2015. The consideration amounting to ₹ 288,92,77,541/- was received from the non-resident investor i.e. HEL by HNPCL on various dates extending beyond a period of 12 months. The entire consideration towards issue of shares to the non-resident investor was required to be brought within a period of 12 months by the applicant. The applicant, however, brought only an amount of ₹ 1,72,67,24,823/- within a period of 12 months from the date of issue of shares. Further *vide* letter dated June 22, 2016 applicant requested the Reserve Bank for grant of extension of time for receipt of the balance consideration of ₹ 1,16,25,52,718/- beyond the prescribed time which was not acceded to by the RBI.
Selected Contravention	<u>Delay in receipt of a part of the consideration for the partly-paid equity shares issued to a non-resident beyond the prescribed time limit.</u>: Regulation 2(ii) of erstwhile Foreign Exchange Management (Transfer of Issue of Security by a Person Resident outside India) Regulations, 2000 notified *vide* Notification No. 20/2000-RB read with para 2(ii)(a) of AP DIR Circular No. 3 dated July 14, 2014 stated as follows: The entire consideration towards issue of shares to the non-resident investor was required to be brought within a period of 12 months by the applicant.
Comments	Though Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations; Regulation 2(v) Explanation (b) of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Regulation 2(ii) of erstwhile FEMA 20/2000- RB dated May 3, 2000 r.w. para 2(ii)(a) of AP DIR Circular No. 3 dated July 14, 2014.

4. Transfer of shares of an Indian company from non-resident Indian (NRI) to a non-resident entity without obtaining prior approval from the Reserve Bank.

Applicant	Muthukumar Ayarpadde
Compounding Application Number	C.A. 4650/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under Compounding Order	₹ 5,59,965/-
Date of order	27th August, 2018
Facts of the case	The applicant is an NRI, Mr. Muthukumar Ayarpadde, who purchased 499,500 equity shares of face value of ₹ 10/- each of Sathya Auto Private Limited (SAPL), an unlisted Indian company. Amongst other facts, Mr. Ayarpadde transferred all the shares (499,500 shares) to another non-resident entity vi. MK Auto Components Limited (MKAL) on June 06, 2008. MKAL was incorporated under the laws of Malaysia to act as the overseas holding company for making downstream investments into India.
Selected Contravention	<u>Transfer of shares of an Indian company from non-resident Indian (NRI) to a non-resident entity without obtaining prior approval from the Reserve Bank</u>: Regulation 9(2)(ii) of erstwhile Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000 notified *vide* Notification No.20/2000-RB stated as follows: A non-resident Indian may transfer by way of sale or gift, the shares or convertible debentures or warrants of an Indian company or units of an Investment Vehicle held by him or it to another non-resident Indian only.' Whereas the applicant transferred the shares of an Indian company to a non-resident entity without obtaining prior approval from the Reserve Bank thereby contravening the said FEMA provisions.
Comments	Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations and accordingly Regulation 10(2) of extant FEMA 20(R)/2017-RB dated 07/11/2017 replaces Regulation 9(2)(ii) of erstwhile FEMA 20/2000- RB dated May 3, 2000. Regulation 10(2) now allows NRI to transfer capital instruments acquired on repatriation basis to any NR under general permission route.

5. Receipt of foreign investment in a company engaged in brownfield pharmaceutical business, without prior approval of the then Foreign Investment Promotion Board (FIPB)

Applicant	Raks Pharma Private Limited
Compounding Application Number	CA No 4656 / 2018

Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under compounding order	₹ 3,08,686/-
Date of order	16th August, 2018
Facts of the case	The applicant is engaged in the pharmaceutical industry. Previously, in 2010, Amneal Pharma Investment Holding, Mauritius (incorporated on June 24, 2010), acquired the entire shareholding of the applicant company from third party resident investors. Thereafter, Amneal Pharma Investment Holding, Mauritius had infused funds through FDI in the applicant company under automatic route during the period between October 2011 to February 2013 However, pursuant to Notification No. FEMA 242/2012 – RB, dated October 19, 2012, foreign investment in brownfield pharmaceutical was brought under approval route with effect from October 19, 2012. This Notification was pursuant to Press Note 3 of 2011. Then FIPB had granted post-facto approval to the applicant vide letter dated October 30, 2017, subject to compounding by RBI from the date of the Press Note 3 of 2011. Remittances received prior to October 19, 2012 have not been considered for compounding by RBI on the premise that FEMA Notification (Notification No. FEMA 242/2012-RB) in this regard was issued only on October 19, 2012.
Contravention	<u>Receipt of foreign investment in a company engaged in brownfield pharmaceutical business, without prior approval of the then Foreign Investment Promotion Board (FIPB)</u> : Regulation 5(1) of Notification No. FEMA 20/2000-RB permits purchase of shares by certain persons resident outside India under Foreign Direct Investment Scheme, subject to terms and conditions specified in Schedule I. Further, Paragraph 25.2 which later renamed as Paragraph 17.2 of Annexure B of Schedule I of erstwhile Notification No. FEMA 20/2000-RB classifies the brownfield pharmaceuticals sector under the approval route category.
Comments	Though Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations; Regulation 5(1) of extant FEMA 20(R)/2017-RB dated 07/11/2017 r.w. Para 16.2 of Reg 16.B thereof corresponds to Regulation 5(1) of erstwhile FEMA 20/2000- RB dated May 3, 2000 r.w. Para 25.2/Para 17.2 of Annexure B of Schedule I thereof.

	It may be noted that while RBI has adopted 19-10-2012 for re-classification of brownfield pharmaceutical sector from automatic route to approval route in this case, whereas in contrast, it has adopted the date of issuance of Press note 3 of 2011 viz. 8-11-2011 in a compounding order containing identical facts (viz. M/s. Alphamed Formulations Private Limited - C.A. HYD 307).

*Corrigendum: In the previous issue, Notification No. FEMA/296/2014-RB dated 3-3-2014 w.e.f. 8-1-2014 should be read as Notification No. FEMA 242/2012-RB w.e.f. 19-10-2012 against Compounding order C.A. HYD 307 in case of M/s. Alphamed Formulations Private Limited.

6. Delay in reporting of downstream investment

Applicant	Jetair Private Limited
Compounding Application Number	C.A. 4714/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under compounding order	₹ 1,55,833/-
Date of order	28th August, 2018
Facts of the case	The applicant company is engaged in the business of acting as travel and tourist agents. The applicant company had not received any foreign direct investment (FDI). However, since it is a non-resident owned and/or controlled company, it was deemed to have received indirect FDI by virtue of its shareholding pattern. The applicant company made downstream investment in India into M/s. Jetair Tours Private Limited in May 2015. This downstream investment made by the applicant company, on account of the aforesaid indirect FDI, was required to be reported to the (then) Secretariat of Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP) and then Foreign Investment Promotion Board (FIPB) within 30 days of such investment. However, there was a delay in meeting the above mentioned reporting requirements, beyond the stipulated period of 30 days, resulting in a contravention.
Contravention	Delay in reporting of downstream investment: Regulation 14(6)(ii)(a) of erstwhile Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000 notified *vide* Notification No. 20/2000-RB stated as follows: Downstream investments by Indian companies will be subject to the following conditions: (a) such a company/LLP has to notify Secretariat for Industrial Assistance, DIPP and FIPB of its downstream investment in the form available at FIPB website within 30 days of such investment.

Comments	Though Foreign Exchange Management (Transfer or Issue of Security By a Person Resident Outside India) Regulations, 2000 has been replaced by revised regulations; Regulation 13.1 (11) of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Regulation 14(6)(ii)(a) of erstwhile FEMA 20/2000- RB dated May 3, 2000. Indian investing entities should periodically monitor its ownership and control to ascertain whether it is indeed owned and/or controlled by persons resident outside India at the time of making a downstream investment.

7. Repatriation of excess amount towards refund of share application money

Applicant	Technovaa Plastic Industries Pvt. Ltd.
Compounding Application Number	C.A.No. AHM- 56 /2015-16
Compounding Authority Name	Foreign Exchange Department, Ahmedabad
Amount imposed under Compounding Order	₹ 26,94,802/-
Date of order	29th June, 2016
Facts of the case	Amongst other facts, applicant had issued shares on 30/03/2015 for ₹ 85,09,34,000/- out of total consideration amount of ₹ 101,49,73,574/- received on 13/05/2014. However, applicant had actually refunded ₹ 16,57,41,669/-($27,45,431@ 60.37) as per dollar rate at the time of refund resulting in excess refund of ₹ 17,02,095/- ($27,45,431@0.62 exchange rate difference). Effectively, the company has borne the exchange rate fluctuation. RBI has not construed this as a contravention. Aforesaid refund transaction took place on 18-7-2014 through normal banking channel within 180 days from the date of receipt of the funds through AD bank under advice to RBI Ahmedabad.
Comments	In C.A. 789/2016 - M/s. PAR Formulations Pvt Ltd., RBI has justifiably taken contrary view and considered that the applicant has made a contravention on this count. Applicant therein on similar facts had repatriated excess INR since it had made remittance of INR equivalent of excess dollars received towards refund of extra share capital application money instead of making remittance of dollar equivalent of INR receipt.

B. Outbound Investment (FEMA 120/2004-RB)

1. Disinvestment of JV without submission of Annual Performance Report

Applicant	Shyam Metalics and Energy Ltd.
Compounding Application Number	CA No. 4658 / 2018

Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under Compounding Order	₹ 1,15,924/-
Date of order	6th September, 2018
Facts of the case	The applicant company set up a JV in Zimbabwe by name Shyam Minimet Africa Private Ltd. in August, 2011 under Automatic route with the object to purchase / acquire/ sell/ dispose and deal in mines and mining rights. However no activity could be undertaken due to lack of commercially feasible opportunities. The company had remitted funds totalling Euro 76,118/- (equivalent to INR 51,84,798/-) between August 2011 and October 2012. As no opportunities came their way, the applicant company decided to close the JV to save on recurring administrative expenses and write off the investment in August 2015. It submitted APRs for the years 2012 to 2015 in July 2015 and initiated process of filing for closure of the JV with the concerned authorities in Harare. The company finally filed for dissolution in January 2017 while the APR for the year 2016 was pending. Subsequently, the APR was filed in April 2017 only.
Contravention	Disinvestment from the JV without submission of the Annual Performance Report: Regulation 16(1)(v) of the Notification no. FEMA 120/2004-RB, dated 7-7-2004, states that an Indian party may transfer, by way of sale to another Indian party any share or security held by it in a JV or WOS outside India subject to the condition that the overseas concern has been in operation for at least one full year and the Annual Performance Report together with the audited accounts for that year has been submitted to the Reserve Bank. Also, as per paragraph 15(iii) of the notification ibid, "An Indian Party which has acquired foreign security in terms of the Regulation in Part I shall submit to the Reserve Bank, through the designated Authorized Dealer, every year on or before a specified date, an Annual performance Report (APR) in Part III of Form ODI in respect of each JV or WOS outside India".
Comments	On many occasions, there could be a time lag between commencement of closure proceedings and eventual dissolution of JV on account of fulfilment of regulatory procedures in the host country. Care must be taken in those situations to continually file Form APR in the intervening period.

2. Making remittances to overseas entity through banks other than the designated Authorized Dealer (AD) bank. Also, delay in reporting of the disinvestment of step-down subsidiary.

Applicant	Take Solutions Limited
Compounding Application Number	C.A. 4674/2018

Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under compounding order	₹ 68,50,414/-
Date of order	08th August, 2018
Facts of the case	A. Amongst other facts, the applicant had made outward remittances towards subscription to equity shares through its Authorized Dealer (AD) banks, viz., HSBC bank until March 2007 and through YES bank. In addition to the outward remittances towards equity in overseas WOS, the applicant further made remittances through CitiBank and DBS bank (i.e. banks other than the designated AD bank) for extending loan to its WOS. B. Amongst other facts, one of the step-down subsidiary (SDS) was merged with WOS on September 30, 2010. However, the disinvestment of the step-down subsidiary (SDS) was reported with delay on July 27, 2017.
Selected Contraventions	A. Making remittances to overseas entity through banks other than the designated Authorized Dealer (AD) bank: Regulation 6(2)(v) of FEMA 120/2004-RB, dated 7-7-2004, states that the Indian Party must route all transactions relating to the investment in a JV/ WOS through only one branch of an authorised dealer to be designated by it. B. Delay in reporting of the disinvestment of the step-down subsidiary: Regulation 13 of FEMA 120/2004-RB, dated 7-7-2004, states that a JV/WOS set up by the Indian party as per the Regulations may diversify its activities / set up step down subsidiary/ alter the shareholding pattern in the overseas entity Provided the Indian party reports to the Reserve Bank, the details of such decisions taken by the JV/WOS within 30 days of the approval of those decisions by the competent authority concerned of such JV/WOS in terms of local laws of the host country, and, include the same in the Annual Performance Report required to be forwarded annually to the Reserve Bank in terms of Regulation 15.
Comments	A. One must bear in mind that financial commitments in all forms including extending guarantee needs to be undertaken only through the designated AD. B. All minute changes including change in capital structure of SDS, disinvestment of SDS etc., needs to be reported under Section B of Part I of Form ODI.

3. Issuance of corporate guarantees by the applicant on behalf of its overseas step-down subsidiaries beyond the 1st level subsidiary.

Applicant	Wipro Limited
Compounding Application Number	C.A. 4710/2018
Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under compounding order	₹ 69,17,862/-
Date of order	10th August, 2018
Facts of the case	The applicant had incorporated multiple wholly owned subsidiaries (WOSs) abroad, out of which three WOS, namely, Wipro Holdings (Mauritius) Limited, Wipro Cyprus Private Limited and Wipro LLC (formerly known as Wipro Inc.) had further set-up subsidiaries under them. The applicant issued corporate guarantees in favor of step-down subsidiaries (SDSs) of these WOSs, beyond the 1st level, without prior approval of the Reserve Bank of India.
Contravention	Issuance of corporate guarantees by the applicant on behalf of its overseas step-down subsidiaries beyond the 1st level subsidiary: Regulation 6(4) of FEMA 120/2004-RB, Dated 7-7-2004, states that "An Indian Party may extend a loan or a guarantee to or on behalf of the Joint Venture/ Wholly Owned Subsidiary abroad, within the permissible financial commitment, provided that the Indian Party has made investment by way of contribution to the equity capital of the Joint Venture."
Comments	Indian Parties are permitted to issue corporate guarantees on behalf of their first level step down operating JV /WOS set up by their JV / WOS operating as either an operating unit or as a Special Purpose Vehicle (SPV) under the Automatic Route. However, issuance of corporate guarantee on behalf of second generation or subsequent level step down operating subsidiaries is covered under the Approval Route, provided the Indian Party indirectly holds 51 per cent or more stake in the overseas subsidiary for which such guarantee is intended to be issued.

C. Inbound Investment (FEMA 24/2004-RB)

1. Entering into partnership with a person resident outside India without obtaining prior approval

Applicant	Expedition Voyages
Compounding Application Number	CA No. 4661 / 2018
Compounding Authority Name	Foreign Exchange Department, Mumbai

Amount imposed under Compounding Order	₹ 73,108/-
Date of order	3rd September, 2018.
Facts of the case	Expedition Voyages, a Partnership Firm was formed vide a Deed of Partnership made on March 23, 2015 between Mr. Karl Espen Fjermeros a resident of New York and Mr. John Jayanta Ambat a resident of India. As per Deed of Partnership, the profit and loss of the business of the firm shall be shared between the partners in the ratio of 70% (Mr. Karl Espen Fjermeros) and 30% (Mr. John Jayanta Ambat). Mr. Karl Espen Fjermeros remitted total amount of ₹ 38,51,373.22 in five tranches between 15-07-2015 to 28-12-2015. The applicant subsequently reversed the transaction and remitted back the total amount of ₹ 38,51,373.22 on May 28, 2018 to Mr. Karl Espen Fjermeros.
Contravention	<u>Entry into partnership with a person resident outside India without obtaining prior approval</u>: Regulation 3 of the Notification no. FEMA 24/2004-RB, dated 3-5-2000, states that "Save as otherwise provided in the Act or rules or regulations made or directions or orders issued thereunder, no person resident outside India shall make any investment by way of contribution to the capital of a firm or a proprietary concern or any association of persons in India. Provided that the Reserve Bank may, on an application made to it, permit a person resident outside India subject to such terms and conditions as may be considered necessary to make an investment by way of contribution to the capital of a firm or a proprietary concern or any association of persons in India."
Comments	Though Foreign Exchange Management (Investment in Firm or Proprietary concern in India) Regulations, 2000 has been substituted by FEMA 20(R)/2017-RB dated 07.11.2017; Regulation 5(4) r.w. Schedule 4 of extant FEMA 20(R)/2017-RB dated 07/11/2017 corresponds to Regulation 3 of erstwhile FEMA 24/2000- RB dated May 3, 2000. Persons other than NRI/OCI are allowed to make investment in Indian partnership firm by way of contribution to the capital of a firm only after seeking prior permission from RBI.

D. Borrowing or Lending in Foreign Exchange (FEMA 3/2000-RB)

1. Raising loan from ineligible lender and for unpermitted end-use

Applicant	Aircom International India Private Limited
Compounding Application Number	CA No. 4720 / 2018

Compounding Authority Name	Foreign Exchange Department, Mumbai
Amount imposed under Compounding Order	₹ 5,05,935/-
Date of order	23rd August, 2018
Facts of the case	The applicant company raised foreign currency loan on February 7, 2001 from its parent company for general corporate expenses without obtaining LRN and adhering to reporting requirements. The lender was not a recognised lender at the time and became eligible only from June 2001. Further, the applicant company also raised foreign currency loans in 7 tranches from July 15, 2004 to May 15, 2006 from the parent company, for working capital purposes without obtaining LRN and adhering to reporting requirements. Working capital was permitted as end-use only with effect from September 4, 2013.
Selected Contraventions	In terms of Regulation 6 of Notification No. FEMA 3/2000-RB, "a person resident in India may raise in accordance with the provisions of the Automatic Route Scheme specified in Schedule I, foreign currency loans of the nature and for the purposes as specified in that Schedule''. Paragraph 1(iii) of Schedule I to FEMA Notification No. FEMA.3/2000-RB, provides that "The borrowings in foreign currency by way of issue of bonds, floating rate notes or other debt instruments by whatever name called may be made from – (a) International bank or export credit agency or international capital market, or (b) Multilateral financial institutions, namely, IFC, ADB, CDC etc., or (c) Foreign collaborator or foreign equity holder as specified by the Reserve Bank, or (d) Supplier of equipment provided the amount of loan raised does not exceed the total cost of the equipment being supplied by the lender, or (e) Any other eligible entity as prescribed by the Reserve bank in consultation with the Government of India." Paragraph 1(iv) of Schedule I to FEMA Notification No. FEMA.3/2000-RB provides the end-uses for which ECB is permitted. However, loan towards 'lease deposit for office premises' is not a permitted end-use.
Comments	Due to frequent policy changes under ECB regime, it is necessary to be abreast of updated regulations at the time of raising ECB. As on even date, ECB can be raised from direct equity holder for working capital purposes and general corporate purposes provided loan is for a minimum average maturity of five years.

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CA Gautam Shah

In Focus – Accounting and Auditing

Ind AS – Banks and NBFCs

Background

On 29th September 2015, RBI recommended a road map to MCA for implementation of Ind AS for Banks and NBFCs from 2018-19 onwards. Later, on 5th April 2018, RBI issued a circular deferring implementation of Ind AS for banks by one year. Hence currently roadmap for Ind AS for banks and NBFCs are as follows:

Banks

Mandatory for accounting periods beginning from 1 April 2019 onwards

NBFCs

Phase I – Mandatory for accounting periods beginning from 1st April 2018 onwards

– Listed or Unlisted NBFCs whose net worth is => Rupees 500 crore.

– Holding, subsidiary, joint venture or associate companies of the above class of companies

Phase II - Mandatory for accounting periods beginning from 1st April 2019 onwards

– Listed NBFCs whose net worth is =< Rupees 500 crore.

– Unlisted NBFCs having ₹ 250 crore = < Net Worth < ₹ 500 crore.

– Holding, subsidiary, joint venture or associate companies of the above class of companies

However, the following classes of entities were not covered in the roadmap:

– NBFCs having a net worth below 250 crore INR and not covered under the above provisions shall continue to apply Accounting Standards specified in Annexure to Companies (Accounting Standards) Rules, 2006.

– Urban Cooperative Banks (UCBs) and RRBs shall not be required to apply Ind AS and shall continue to comply with the existing Accounting Standards for the present.

Major impacts of adoption of Ind AS by Banks and NBFCs

Currently banks and NBFCs are following existing Accounting Standards issued by ICAI & RBI guidelines. Adoption of Ind AS will have major impact in many areas.

Key impacts are discussed below:

- **Classification and Measurement of Financial Instruments**

Most challenging standards in terms of practical application are the Financial Instruments Standards (Ind AS 109, Ind AS 32 & Ind AS 107). In case of NBFCs and banks, these standards will have major impact as the major balance sheet items of NBFCs and banks are financial Instruments only.

Banks - As per the current accounting practices in accordance with the AS and RBI guidelines, investments are classified into three categories namely:

– Available for Sale

– Held to Maturity

– Held for Trading

Investment in HTM is carried at cost and tested for impairment while investment in HFT & AFS are marked-to-market & resulting loss is recognised and gains are ignored.

NBFCs - AS 13 – 'Accounting for Investments' along with Schedule III (Division I) used to give guidance about classification of investment into Non-current & Current. However, Ind AS further introduces the concept of Financial Assets and Liabilities.

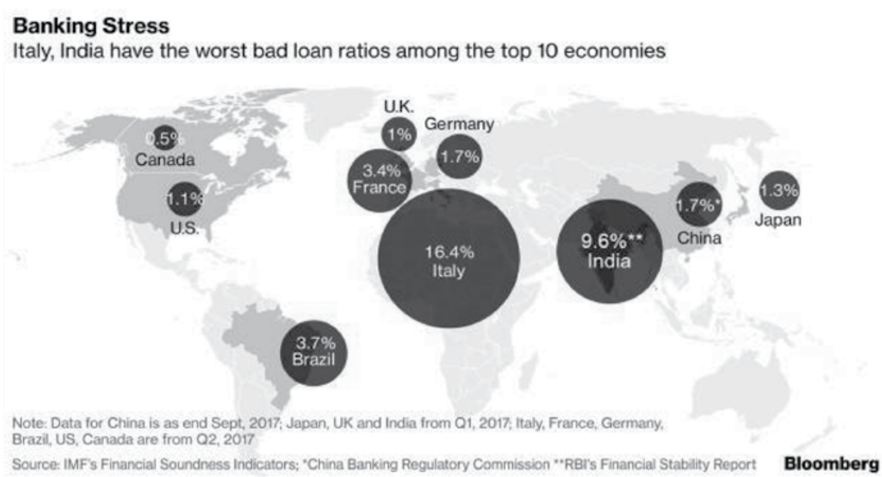
Previously applicable Accounting Standards followed the Historical Cost Convention and did not give emphasis to Fair Valuation of Assets and Liabilities.

As per Ind AS 109, all financial assets (Investments, loans, advances, trade receivables, deposits, etc.) will have to be classified at Amortized Costs, Fair Value through Other Comprehensive Income (FVOCI) or Fair Value through Profit and Loss (FVTPL). All the unrealised gains or losses on financial assets measured at FVOCI would be accounted in the Other Comprehensive Income (OCI) whereas all the unrealised gains or losses on financial assets measured at fair value through the profit and loss would be accounted in the Profit and Loss account.

Ind AS 9 requires financial asset classification to be based on contractual cash flow characteristics and the business model of the Bank. Judgment may be required in determining whether the SPPI criterion is met – whether interest reset satisfy SPPI needs assessment of each contract.

Since the accounting is driven by business model, it may impact terms of loan contract and business decisions like underwriting of loans or assignment of portfolio.

Provision for Advances (NPAs) and Other Financial Assets (Expected Credit Loss model)



As per current RBI guidelines, the provisioning is primarily based on ageing of assets (days pass due) and the security is available. This shows that provisioning is done after actual situation of NPA arises. Though RBI has also prescribed for provision on standard asset as a prudent measure, it still remains rule based provisioning without taking into consideration the actual macro & micro economic factors, business environment, past organisation specific history etc.

As per Ind AS 109 impairment provisioning is done based on "Expected Credit Loss" (ECL) model. It applies to financial assets that are not measured at FVTPL, including specified financial guarantees and loan commitments issued. The expected credit losses model will likely result in earlier recognition of credit losses because it will require the recognition of either a 12-month or lifetime expected credit loss allowance or provision that includes not only credit losses that have already occurred, but also losses that are expected in the future. The proposals may increase the credit loss allowance or provision recorded by many banking entities.

It is to be noted that preparation & setting up of an ECL model & its yearly revision will be a challenge faced by NBFCs and Banks as it has direct impact on profitability through provisions.

Quotes from Experts : "CLSA estimates that ECL will boost provisioning by $30 billion and consume more than $26 billion of capital at state-run banks and $4 billion for private lenders". "The new Indian Accounting Standards could result in sizable incremental bad debt provisioning requirements for Indian banks given their relatively low levels of provision coverage at present," said Nicholas Yap, a Hong Kong-based credit desk analyst at Nomura International (HK) Ltd. "This could pressure banks' capital levels."

- **Hedge Accounting**

Under Ind AS, hedge accounting is more closely aligned with risk management and is available for a broader range of hedging strategies. Ind AS 109 allows an entity to switch to a new hedge accounting model that is aligned more closely with risk management. The new model may allow additional hedging strategies; however, some current hedging strategies may be restricted. The new model is more principles-based and a more judgmental approach is required in the assessment of qualifying, rebalancing and discontinuing hedge accounting.

- **Income Recognition (Interest Income & Fee Income)**

Under Indian GAAP, loan processing, service charges, commission or such origination fees were either accounted upfront or amortised over the contractual term of the instrument.

Under Ind AS, these fees will be amortised over the life of loan through EIR (Effective Interest rate) model. This will result in a temporary deferral of revenue recognition. For NBFCs, it means a negative impact on its profits and hence, in its net worth. Profit and Loss account will get normalised over the term of the instrument.

- **Income recognition on NPA**

As per the guidelines issued by RBI, interest income on NPAs is recognised on receipt basis whereas in Ind AS, interest income is recognised on gross carrying amount less impairment in case asset is in stage 3 of ECL. Hence, ECL model will decide the recognition of income on NPA & its timing.

- **Securitisation**

Under Indian GAAP, the derecognition of assets was largely driven by the 'true sale' criteria.

The guidance on derecognition of assets under Ind AS is significantly different and focuses on whether significantly all the risks and rewards related to the asset have been transferred. A summary of the derecognition conditions set out by Ind AS 109:

– Transfer of all risks and returns – assets to be derecognised from the books

– Retention of all risks and returns – assets not to be derecognised

– Retention of some risks and returns – however, surrender of control – partial derecognition of financial assets

In the securitisation structures prevalent in India, the originators retain the entire excess spread. The originators also retained the subordinated class of PTCs issued by the securitisation trust, in order to comply with the MRR as also to provide the needed enhancement. Retention of the excess spread implies that the entire rewards also flow back to the originator.

Thus, under Ind AS, securitisation structures that are most commonly used in India would not qualify the derecognition criteria. They will continue to be recorded in the balance sheet, separately from other Financial Instruments, while the money received in the sale transaction will be classified as a liability, as Secured Borrowings. Gain will be recognised as per EIR method.

Ind AS 101 prescribes that grandfathering provisions will apply and previously derecognised assets will not be subsequently recognised as per Ind AS even if the transfer does not qualify for de-recognition as per Ind AS.

- **Direct Assignment**

Ind AS does not make a distinction between securitisation and direct assignment – hence, the requirements for de-recognition remain the same. The RBI guidelines in case of direct assignment prohibit any credit enhancement. Thus, while there is an MRR to the extent of at least 10%, however, that is by way of a vertical tranche of the pool, that is, a *pari passu* share in the receivables

Direct assignment is a case where qualifying for de-recognition for Ind AS's will be easiest – since, to the extent of the fully proportional share of principal and interest sold, there is no risk/reward retention by the originator. Thus, DA transactions can continue to be off balance sheet under Ind AS.

Currently, NBFCs have to amortise the gain on assignment over the period of loans. Under Ind AS, as loans would be derecognised from the assignee's book, it would lead to front-ending of gains in the income statement.

- **Special Purpose Vehicles**

Special Purpose Vehicles (SPV) set up for securitisation transactions are generally not consolidated based on the guidance in Accounting Standard (AS) 21, Consolidated Financial Statements (control is based on ownership of voting power).

However, under Ind AS 110, the evaluation of control is based on the following:

– power over the investee

– exposure, or rights, to variable returns from its involvement with the investee

– the ability to use its power over the investee to affect the amount of the investor's returns

Most SPVs fulfil this definition of control set out by Ind AS 110, and thus companies may have to consolidate the securitisaton SPVs.

Conclusion

Implementation of Ind AS comes with lots of challenges to the NBFCs and Banking sector as they will have to deal with certain non-rule based management estimates. It also poses challenges to other stakeholders of financial information like regulators, investors, analysts, credit rating agencies and lenders as they will have to analyse information, recreate models and take decisions based on the non-conventional reporting. Considering the volume of changes due to Ind AS implementation and onerous disclosure requirements, banks will need to reassess and upgrade their policies, processes and IT systems. Few other challenges:

- Provisions & Impairment – ECL as per Ind AS involves banks to make robust estimates and establish when significant changes in credit risk occur, increasing the level and complexity of judgment significantly. Volatility will also increase as external data, such as ratings, credit spreads and predictions about future conditions, will be assessed in the calculation of ECLs. Acceptability of this subjective provisioning as compared to current Rule based provisioning by Regulators?

- Current Mergers of banks will require assessment of Business Combination and Fair Valuation of Assets & consideration. Whether impact of same are considered in current mergers of PSU Banks?

- Implementation of Ind AS may need excess provisioning as per ECL, which will impact Tier I capital of banks. How the banks will be further capitalised to ensure required capital adequacy?

- Alignment of financial reporting as per Ind AS with regulatory requirement with reference to format of financial statements, disclosures?

If above challenges are addressed:

The adoption of Ind AS is a welcome change and it will play a key role in enhancing the corporate comparability of Financial Statements of Indian Companies with the global standards. It will improve the quality of Financial reporting and bring financial Statements closer to economic reality.

In the long run, moving to internationally acceptable accounting standards will help the Indian banking system in becoming more resilient and tapping international pools for their capital requirements.

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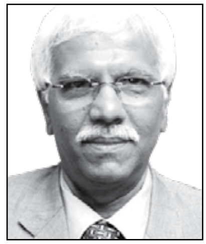
Be not afraid, for all great power throughout the history of humanity has been with the people. From out of their ranks have come all the greatest geniuses of the world and history can only repeat itself. Be not afraid of anything. You will do marvelous work.

— *Swami Vivekananda*



Kishor Vanjara, *Tax Consultant*

Tax Articles for Your Reference

Articles published in Taxmann, The Bombay Chartered Accountant Journal (BCAJ), The Chamber's Journal (CJ), The Chartered Accountant Journal (CAJ), All India Federation of Tax Practitioners Journal (AIFTPJ), Sales Tax Review(STR), Income Tax Report (ITR), SEBI & Corporate Laws (S & C Law), Times of India and Economic Times for the period October 2018 to November 2018 has been arranged and indexed topic-wise.

Topic	Author	Magazine	Volume	Page
A'				
Accounting and Auditing				
In Focus – Accounting and Auditing Critical Analysis of Report on Audit Quality Review for 2017-18	Khurshed Pastakia	C J	Vol.VII/No.1	128
Blockchain may lead to New Era of Accounting and Auditing Practices	Anand Prakash Jangid	CAJ	67/No.04	533
Standards on Auditing – Importance and Overview in Global Perspective	Abhihit Bandyopadhyay	CAJ	67/No.05	667
Review of Historical Financial Information	Gautam Shah & Mehul Mahajan	CAJ	67/No.05	681
Risk Assessment, Audit Conclusions and Reporting	Abhay V. Kamat	CAJ	67/No.05	694
Ind AS for NBFCs – Not Just an Accounting Challenge	Manoj Kumar Vijai and Prateek Mankad	CAJ	67/No.05	713
Ind AS 115 – New Rules for Revenue Recognition under Ind AS : An Analysis and Overview	Pravin Sethia	CAJ	67/No.05	717
Ind As vs. ICDS Differences	Dolphy D'Souza	BCAJ	50-B/Part 1	79
Ind AS/GAAP – Accounting of Financial Guarantees	Dolphy D'Souza	BCAJ	50-B/Part 2	69
RBI audit of IL & FS group makes Independent Directors Jittery	Joel Rebello & Kala Vijay Raghuvan	E T	10/1/2018	9

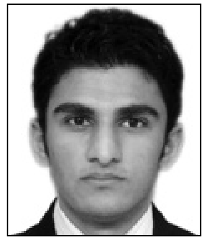
Topic	Author	Magazine	Volume	Page
B'				
Benami Property Transactions Act				
Salient features of Prohibition of Benami Property Transactions Act as amended in 2016	Narayan Jain & Dilip Loyalka	Taxman	258	1
Benami Act – No Longer a Paper Tiger! – Part II	Dr. Dilip K. Sheth	BCAJ	50-B/Part 1	29
Notices to 10000 depositors post Demo	Sachin Dave	ET	10/15/2018	19
Business Restructuring				
Business Restructuring through slump exchange – An efficacious tool for tax planning	Nipun Mohanka	Taxman	258	83
'C'				
Capital Gains				
No abuse investment in Canada through a company located in another country to save capital gains; Tax Court of Canada rules	Kanwal Gupta	Taxman	258	13
Corporate Laws				
Recent Changes in Annual Return and Board's Report	Anshul Jain & Anshu Agarwal	CJ	Vol.VII/No.1	11
Important Aspects of Company Formation	Atul Mehta	CJ	Vol.VII/No.1	16
Section 42 of Companies Act, 2013-A suge towards enhanced Governance – Major changes in fund raising provisions (Private Placement)	Mahavir Lunawat	CJ	Vol.VII/No.1	25
An Interpretatioal Study of the New Section 185 of the Companies Act, 2013	K. R. Chandratre	CJ	Vol.VII/No.1	30
Whether LLP can merge in Company?	Makrand Joshi	CJ	Vol.VII/No.1	42
Related Party Transactions	Siddharth Banwat & Kush Vatsaraj	CJ	Vol.VII/No.1	45
Privileges of Private Company and Small Company	Dharmesh Zaveri	CJ	Vol.VII/No.1	56
Analysis of the Order/Judgment dated August 3, 2018 passed by the Hon'ble High Court of Madras in the matter of Bhagavan Das Dhananjaya Das versus Union of India and Anr.	Anoj Menon	CJ	Vol.VII/No.1	63
Companies Act				
MCA weighs proposals to update Companies Act	Rajat Arora	ET	10/24/2018	17
Recent Amendments in Schedule III to the Companies Act, 2013	Zubin Billimoria	CJ	Vol.VII/No.2	143
Life to get less taxing for minor violations of Co's Act	Sidhartha	TOI	11/24/2018	17

Topic	Author	Magazine	Volume	Page
'D'				
Deemed Dividend				
Taxability of Proportionate Deemed Dividend in case of Loans to Concerns	Pradip Kapasi, Gautam Nayak and Bhadresh Doshi	BCAJ	50-B/Part 2	65
'E'				
E Comm				
Consultations on e Comm policy to start afresh	Deepshikha Sikarwar	E T	11/24/2018	4
Education Cess				
Whether allowable as expense under Income-tax Act, 1961?	Manoj Mehta	Taxman	258	86
'G'				
GST				
GST – Gyan – Crossing Borders with GST	Divyesh Lapsiwala & Amit Bothra	C J	Vol.VII/No.1	94
Taxation of Works Contract under GST	C. B. Thakar & Rahul C. Thakar	AIFTPJ	21/No.07	45
Impact of GST and Issues under GST on Real Estate Transactions	Kuntal Parekh	AIFTPJ	21/No.07	70
Service Exports from India Scheme and Taxability of such Notified Export of Services under GST Act	Dilip V. Satbhai	CAJ	67/No.04	572
Job-Work : Old Wine in Better Bottle? (Part-1)	Sunil Gabhawalla, Rishabh Singhvi and Parth Shah	BCAJ	50-B/Part 1	101
Job-Work : Old Wine in Better Bottle? (Part-2)	Sunil Gabhawalla, Rishabh Singhvi and Parth Shah	BCAJ	50-B/Part 2	79
Role of Auditors in GST Form	Deepak Mata	C J	Vol.VII/No.2	11
Reconciliation Statement (From GSTR-9C) – Some Issues	Sushil Solanki & Govind G. Goyal	C J	Vol.VII/No.2	15
Statutory Provisions under CGST Act Governing Audit/ Certifications, Role and Responsibility of Auditors	Naresh K. Sheth	C J	Vol.VII/No.2	20
Books of Accounts, Documentation and Records and GST Act	Rajat Talati	C J	Vol.VII/No.2	29
Auditing Framework for GST Audit	Tejas Parikh	C J	Vol.VII/No.2	36
Key Action Points for filing GST Annual Return by 31st December	Bimal Jain	C J	Vol.VII/No.2	42

Topic	Author	Magazine	Volume	Page
Reconciliation Statement Form 9C (Parts I & III of Form 9C)	Chirag B. Mehta	CJ	Vol.VII/No.2	50
Reconciliation Statement Form 9C (Parts IV & V of Form 9C)	Vasant Bhat	CJ	Vol.VII/No.2	65
Importance of other Reconciliations in GST Audit	Manindar Karkala	CJ	Vol.VII/No.2	72
Certifications/Audits under GST Act and Professional Ethics	C. N. Vaze	CJ	Vol.VII/No.2	76
GST Compliance : Global Trends	Dinesh Tejwani	CJ	Vol.VII/No.2	83
GST – Gyan – Place of Supply under GST	Rishabh Singhvi & Avni Asher	CJ	Vol.VII/No.2	105
Co's may have to show ledgers for claiming GST credit over ₹ 25L	Deepshikha Sikarwar	ET	10/1/2018	15
Travel portals seeks clarity on TCS provisions under GST	Deepshikha Sikarwar	ET	10/4/2018	15
Cos grapple with audit woes as GST deadline nears	Sachin Dave	ET	11/17/2018	5
GST Audit in Form GSTR 9C – Some Issues	Rajat Talati	STR	65/ No 8	20
An Insight into GST Audit	Ritesh R Mehta	STR	65/ No 8	29
Important Valuation Provisions Under GST – Part 2	Umang Talati	STR	65/ No 7	25
ITC on demo cars used for sales promotion	Pranav Mehta	STR	65/ No 7	30
GST Audit				
Overview of Audit and Annual Return Under G S T	M. L. Patodi & Rohit Patodi	AIFTPJ	21/No.08	8
Glossary of terms in Annual Return and Audit Report on GST	Sujata Rangnekar	AIFTPJ	21/No.08	14
Issues Relating to Determining and Disclosing Outward Supply in Annual Return	Mukul Gupta	AIFTPJ	21/No.08	18
Issues Relating to Determining and Disclosing Inward Supply in Annual Return and GST Audit Report	C. B. Thakar	AIFTPJ	21/No.08	25
Challenges and Issues in Annual Return	Ashit Shah	AIFTPJ	21/No.08	39
Audit under Goods and Services Tax Law	S. Venkataramani, Hanish S. & Siddeshwar Yelamali	AIFTPJ	21/No.08	43
Annual Returns – Consequences of Non-Filing	S. S. Satyanarayana	AIFTPJ	21/No.08	52
CGST Act & IGST Act				
Recent Amendments to CGST Act & IGST Act : An Analysis	Kiran G. Garkar	AIFTPJ	21/No.07	52

Topic	Author	Magazine	Volume	Page
'I'				
Insolvency and Bankruptcy Code, 2016				
Section 29A of the Insolvency and Bankruptcy Code, 2016 : Harsh on Promoters?	Karan Sahi	S & C Law	149 / Part-6	63
Guarantors too will be in insolvency net	Sidhartha & John Sarkar	T O I	10/8/2018	17
Income from Other Sources				
Income from Other Sources	S. Balakrishnan	ITR	407	38
ICDS				
Securities held by Banks – Impact of ICDS – read with				
Relevant Case Laws	Mudit Agarwal	CAJ	67/No.04	580
Interest				
Scope of the Definition of the Term "Interest" – Section 2 (28a)	Pradip Kapasi, Gautam Nayak and Bhadresh Doshi	BCAJ	50-B/Part 1	71
International Taxation				
The "Hard Facts" of the "Soft Charges" of Intra-Group Service (IGS) and Possible Solutions!	Amit Dhadphale & Abhishek Apte	CAJ	67/No.05	744
Decoding the Consequences of POEM in India	Mayur B. Nayak, Tarunkumar G. Singhal and Anil D. Doshi	BCAJ	50-B/Part 1	83
'L'				
Capital Gains				
Higher Long Term Capital Gains tax for those, betting on Mergers	Pavan Burgula	E T	10/9/2018	14
Loan Waiver				
An Analysis of SC Ruling in case of Mahindra & Mahindra on Loan Waiver	Nehal Shah & Mukesh Dholakiya	Taxman	258	67
'N'				
Negotiable Instruments Act				
Overview of Section 138 of the Negotiable Instruments Act	Dr. Anup P. Shah	BCAJ	50-B/Part 2	103
NBFC's				
Off Balance Sheet Solution can Resolve NBFC's crisis of Confidence	R. Sridhar	E T	10/17/2018	22

Topic	Author	Magazine	Volume	Page
'P'				
Penalties and Prosecution				
Penalties and Prosecution under the Income-tax Act, 1961	V. P. Gupta	AIFTPJ	21/No.07	20
Provident Fund Act				
Latest Update on Provident Fund Act	Ramesh L. Soni	AIFTPJ	21/No.07	80
'R'				
RTI				
RTI Act is being steadily emasculated by spurious use by personal information exemption	Shailesh Gandhi	TOI	11/17/2018	16
'S'				
Survey, Search and Seizure				
Admissions & Retractions in I.T. proceedings with reference to Survey, Search and Seizure	Narayan Jain	AIFTPJ	21/No.07	29
Service Charge				
Restaurants seek Clarity on CBDT's Service Charge Directive	Sambhavi Anand & Anumeha Chaturvedi	E T	11/24/2018	5
Securities Laws				
Advised SEBI Move to Separate Chairman-CEO's Post in Companies	Jayant M. Thakur	BCAJ	50-B/Part 1	118
Managerial Remuneration - Shackles Finally Removed	Jayant M. Thakur	BCAJ	50-B/Part 2	95
'T'				
Turnkey Projects				
Key facets on taxation of turnkey projects	Nivetha Veni K.	Taxman	258	18
Tax Havens				
Tax havens-An aerial view ...!!	Prabhakar K. S.	Taxman	258	77
Tax Law				
Tax Law – Changes, Challenges & Compliances	N. M. Ranka	AIFTPJ	21/No.07	14
'V'				
Valuation Standards				
An attempt to standardise subjectivity	Anand Bathiya	BCAJ	50-B/Part 2	29
VAT				
Set off *vis-à-vis* Gross receipts for Rule 53(6)(b) of the MVAT Rules	G. G. Goyal & C. B. Thakar	BCAJ	50-B/Part 1	109



Rahul Sarda, *Advocate*

Best of the Rest

Arbitration and Conciliation Act, 1996 – Bill of Lading containing Arbitration clause – Whether an unsigned Arbitration Agreement invalid?

The appeal arose before the Supreme Court out of a document styled as "Multimodal Transport Document/Bill of Lading". The Respondent to the appeal was the consignor/shipper and the appellant was the agent who facilitated transport. The opening clause of the said Bill of Lading specified that the Merchant accepted and expressly agreed to be bound by all the terms, conditions, clauses and exceptions printed on both the sides of the Bill of Lading whether typed, printed or otherwise. One of the printed conditions in the Bill of Lading was the arbitration clause. The Respondent filed a Suit to recover certain sums from the Appellant on the basis of the cause of action that arose out of the Bill of Lading. The Appellant thereafter filed an Interim Application under Section 8 of the Arbitration & Conciliation Act, 1996, *inter alia* stating that there existed an arbitration clause as per Clause 25 in the Bill of Lading between the parties and that an Arbitrator be appointed under Section 11 of the said Act.

The Lower Court *inter alia* held that the terms and conditions stated in the Bill of Lading would not be binding upon the parties which was upheld by the High Court in its appellate jurisdiction and revisionary jurisdiction.

Before the Supreme Court, the Appellant contended that the parties were expressly bound by the terms and conditions of the Bill of Lading which was in writing and that there was a reference to arbitration clause in the Bill of Lading. The Respondent placed reliance on Section 7(4)(a) that the Arbitration Act as per which arbitration agreement should be in writing and duly signed by the parties, whereas in the present case, the Bill of Lading was not signed by the parties and therefore the terms and conditions stated therein were not binding upon the parties.

The Supreme Court held that a bare reading of the document in question specifically states in clause 25 that the parties to it are bound by the terms and conditions and an arbitration clause was included in the printed terms annexed to the said document. Furthermore, the Respondent itself relied on the Bill of Lading in the Suit filed by it.

Held, that the arbitration agreement ought to be in writing though it need not be signed and the only pre-requisite was that it be in writing. Hence, held there was a valid arbitration agreement between the parties.

M/s. Caravel Shipping Services Pvt. Ltd. vs. M/s. Premier Sea Foods Exim Pvt. Ltd. - Civil Appeal No. 10800 - 10801 of 2018 dated 29-10-2018 - Supreme Court

Maharashtra Shops and Establishments (Regulation of Employment and Conditions of Service) Act, 2017 – Definition of "establishment" – To include medical practitioners

The challenge in this petition was as to the definition of "establishment" under Section 2(4) of the Maharashtra Shops and Establishments (Regulation of Employment and Conditions of Service) Act, 2017 (the "New Act"), brought into force with effect from 7-9-2017, to the extent it applied to the profession and the establishment of any medical practitioner (including hospital, dispensary, clinic, polyclinic, maternity home and such others) and requiring such establishment to comply with the provisions of the Act. The challenge was on the ground that it violated the guarantee of the Petitioner contained in Article 19(1)(g) of the Constitution of India to practise profession or to carry on any occupation or business and that it was beyond the competence of the State Legislature.

The High Court observed that The Maharashtra Shops and Establishments Act, 1948 (the "Old Act") was brought into force with effect from 11-1-1948 and it was to consolidate and amend the law relating to the regulation of conditions of work and employment in shops and commercial establishments, residential hotels, restaurants, eating houses, theatres, other places of amusement or entertainment and other establishments. Under the old Act, it was held that the intention of the Legislature in enacting Section 2(4) was to include only those professions which were carried on in a commercial manner and, therefore, a dispensary of a doctor did not fall within the definition of "Commercial establishment". The Court further observed that the enactments similar to the old Act were prevailing in various States in the country but were deficient, inadequate and suffering from shortcomings in providing social security benefits to all the employees covered by it.

However, the definition of "establishment" in the new Act was wide to include "establishment of any medical practitioner (including hospital, dispensary, clinic, polyclinic, maternity home and such others), architect, engineer, accountant, tax consultant or any other technical or professional consultant". Held, the word "Commercial" which was suffixed to "establishment" under the Old Act did not find place in the New Act. The word "profession" or the words "an establishment of medical practitioner" in the definition of "establishment" in Section 2(4) of the New Act were not preceded or associated by the words "business, trade" so as to take such colour, as was there under the Old Act. Thus, the Court observed that there was a drastic change in the complexion of the legislative scheme after bringing into force the New Act, and the grounds on which the Courts construed the various provisions under the Old Act no longer survived to challenge the provision of Section 2(4) contained in the New Act. Therefore, the challenge failed and the bringing of medical practitioners within the purview of the New Act was upheld.

Dr. Pradeep Arora vs. The State of Maharashtra – WP No. 7590 of 2017 dated 2-11-2018 – Bombay High Court

Right to Information Act, 2005 – Disclosure of development plans, layout plans etc. – Whether disclosure is mandatory – Private disputes between parties

A party filed an application under the RTI Act before the MCGM seeking certified copies of PR cards, plans including amendments, layouts, sub-division plans, development plans, reports submitted to Municipal Commissioner etc., in respect of some plots of land of which he was owner and had granted development rights to a developer. The developer objected to the application on the ground that the information did not serve any social or public interest but was for the private interest of the party which had filed suit against the developer in the Bombay High Court. The developer also contended that the applicant was a competitor in business and hence disclosure would cause harm and injury to developer's competitive position. The application of information was rejected. The first appellate authority granted disclosure in respect of some of the information while rejecting disclosure of other information. The second appellate authority allowed the applicant's appeal on the ground that development of the property has connection with public interest, as flats erected thereon would be purchased by the citizens at large which was upheld by the High Court.

The Supreme Court held that even private documents submitted to public authorities may, under certain situations, form part of public record and unless information sought for falls under the specific exceptions, disclosure thereof was mandatory. And, the test of larger public interest would arise only if the information falls within these exceptions. Furthermore, as per the MOFA, a promoter, who constructs or intends to construct a block or building of flats was required to comply with many disclosure requirements including the information sought by the applicant. Thus, it could hardly be said that while a purchaser could get the information, the person who administers the land as owner and grants the authority through a Power of Attorney to develop the land, would not have such a right. Even as per RERA, with the object of bringing greater transparency, the promoter was required to make available to the allottee information about sanctioned plans, layout plans along with specifications, approved by the competent authority. Hence, the appeal of the developer was dismissed.

The Court further observed that keeping in mind the provisions of RERA and their objective, the developer should mandatorily display at the site the sanction plan. Furthermore, keeping in mind the ground reality of rampant violations and the consequences thereof, the Court held that it was advisable to issue directions for display of such sanction plan/layout plans at the site, apart from any other manner provided by the Regulations made by the Authority and this aspect should be given appropriate publicity as part of enforcement of RERA.

Ferani Hotels Pvt. Ltd. vs. The State Information Commissioner Greater Mumbai and Ors. 2018 (13) SCALE 672

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CA Anish Thacker & CA Parag Ved, *Hon. Jt. Secretaries*

The Chamber News

Important events and happenings that took place between 7th November, 2018 to 7th December, 2018 are being reported as under:

I. Admission of New Members

1) The following new members were admitted in the Managing Council Meeting held on 16th November, 2018.

Life Membership			
1	Mr. Gupta Ankit	B.Com	New Delhi
2	Mr. Parasmal Dilip Kumar	CA	Bengaluru
3	Mr. Saini Dinesh Arjun	CA	Kolkata
4	Mr. Narula Gawesh	GSTP	New Delhi
5	Mr. Lakhwani Rahul	Adv.	Jaipur
6	Mr. Dharod Nihar Suresh	CA	Mumbai
7	Mr. Anchaliya Suchek Suresh	CA	Mumbai
Ordinary Membership			
1	Mr. Upadhyay Rishabh Girish	CA	Bengaluru
2	Miss. Kulkarni Pooja Raghavendra	CA	Bengaluru
3	Miss. Krishnakumar Dhanusha	CA	Bengaluru
4	Mr. Rishab Kothari Jain	CA	Bengaluru
5	Miss. Chopra Nikitha Nemichand	CA	Bengaluru
6	Mr. Parmar Mohit Ashok	CA	Bengaluru
7	Mr. K. H. Vikram	CA	Bengaluru
8	Mr. Murthy Abhishek R.	CA	Bengaluru
9	Mr Manik Tarun Ashok	CA	Mumbai

10	Mr. Gupta Pankaj Kumar	CA	Hardoi
11	Mr. Subramaniam Chandrasekhar	CA	Bengaluru
12	Mr. Upadhyay Rishabh Girish	CA	Bengaluru
13	Miss Kulkarni Pooja Raghavendra	CA	Bengaluru
14	Mr. Sancheti Santosh Chandulalji	CA	Pune
15	Mr. Sanghani Ilesh Hasmukh	CA	Mumbai
Student Membership			
1	Mr. Shah Alam Khan	ICAI	Mumbai

II. Past Programmes

1. CORPORATE COMMITTEE

Lecture meeting on "Laws Relating to Significant Beneficial Owner" was held on 20th November, 2018 at Babubhai Chinai Committee Room, IMC, Churchgate. The meeting was addressed by Mr. Richie Sancheti, Advocate and Mr. Srikanth Vasudeva, Advocate.

2. MEMBERSHIP & P.R. COMMITTEE

- Workshop on GST Annual Returns & GST Audit Report was held on 3rd November, 2018 at Shree Vishveshwarya MSEB Hall, Kolhapur. The workshop was addressed by CA Pranav Kapadia and CA Rajiv Luthia.
- Workshop on GST Annual Returns & GST Audit Report was held on 1st December, 2018 at Solapur. The workshop was addressed by CA Ashit Shah and CA Mandar Telang Workshop on GST Annual Returns & GST Audit Report was held on 1st December, 2018 at New Seminar Hall, B. K. Birla College, Gauripada, Kalyan. The workshop was addressed by CA Rajiv Luthia and CA Vasant Bhat.

3. IT CONNECT COMMITTEE

Seminar on Records Retention: Legal Provisions and Document Management Solutions was held on 7th December, 2018 at Babubhai Chinai Committee Room, IMC, Churchgate. The seminar was addressed by CA Amlesh Gupta, CA Maitri Chedda and CA Anand Paurana.

4. CTC PUNE STUDY GROUP

Workshop on GST Annual Returns & GST Audit Report was held on 1st December, 2018 at ELTIS Building, Off Symbiosis, Pune. The workshop was addressed by CA Naresh Sheth and CA Vikram Mehta.

5. DIRECT TAXES COMMITTEE

Half day Seminar on Penalty & Prosecution was held on 1st December, 2018 at Babubhai Chinai Committee Room, IMC, Churchgate. The seminar was addressed by Mr. Ajay Singh, Advocate, CA Bhadresh Doshi and CA Jagdish Punjabi.

III. FUTURE PROGRAMMES

1. INDIRECT TAXES COMMITTEE

- Workshop on GST Annual Returns & GST Audit Report is scheduled to be held on 15th December, Walchand Hirachand Hall, 4th Floor, IMC, Churchgate.
- 7th Residential Refresher Course on GST is scheduled to be held from 24th to 27th January, 2019 at Hotel Novotel, Hitec City, Hyderabad.

2. INTERNATIONAL TAXATION COMMITTEE

- Intensive Study Course on FEMA is scheduled to be held on 21st and 22nd December, 2018 at Hotel West End, next to Bombay Hospital, Churchgate.
- 13th Residential Refresher Course on International Taxation, 2019 is scheduled to be held from 20th June, 2019 to 23rd June, 2019 at The Grand Bhagwati, Surat.

3. RESIDENTIAL REFRESHER COURSE & SKILL DEVELOPMENT COMMITTEE

- "Surila Yaarana" A Musical Evening is scheduled to be held on 20th December, 2018 at Club W-Ballroom, Level P-6, Lodha World Tower, Lower Parel.
- 42nd Residential Refresher Course is scheduled to be held from 28th February, 2019 to 3rd March, 2019 at Hotel Ramada, Hyderabad.

4. CORPORATE CONNECT COMMITTEE

Lecture Meeting on Compulsory Dematerialisation of Shares and Companies Amendment (Ordinance), 2018 is scheduled to be held on 20th December, 2018 at Banquet Hall, Dadar Club, Lane No. 3, Lokmanya Tilak Colony, Near BAPS Shri Swami Narayan Mandir, Dadar East, Mumbai-400014.

5. MEMBERSHIP & PR AND STUDENT COMMITTEE

CTC Box Cricket is scheduled to be held on 12th January, 2019 at Dr. Antonio D'Silva School Turf, S. K. Bole Road, Opp. Kabutar Khana, Dadar (W), Mumbai - 400 028.

6. STUDENT COMMITTEE

Chamber's Debate Competition is scheduled to be held on 18th & 19th January, 2019 at H. R. College of Commerce & Economics, Churchgate

(For details of the future programmes, kindly visit www.ctconline.org or refer The CTC News of December, 2018)

Membership & Public Relations Committee

Full day Workshop on GST Annual Return & GST Audit Report was held on 1st December, 2018 at Hotel Balaji Sarovar Premiere, Asara Chowk, Solapur.

Inauguration of the workshop. Seen from L to R: S/Shri CA Ashit Shah (Speaker), CA Prabhakar Gunjale (Secretary – Solapur Branch of WIRC of ICAI), Mr. Vairagkar, Advocate (President – STP & ITP Association of Solapur), CA Nandkishor Udgiri (Chairman – Solapur Branch of WIRC of ICAI), CA Sunil Ingale (Imm. Past Chairman – Solapur Branch of WIRC of ICAI) and CA Mandar Telang (Speaker)

CA Ashit Shah addressing the delegates

CA Mandar Telang addressing the delegates

Pune Study Group was held on 1st December, 2018 at English Language Teaching Institute of Symbiosis (ELTIS), Pune

CA Naresh Sheth addressing the delegates on the topic "GST Audit - Statutory Provisions and Concepts"

CA Vikram Mehta addressing the delegates on the topic "Analysis of Annual return in Form GSTR-9 & GSTR-9A"

Study Circle & Study Group Committee

Study Group on "Recent Judgments under Direct Taxes" was held on 2nd November, 2018 at the Bakulbhai Chinai Committee Room, IMC

CA Nitesh Joshi addressing the delegates

Study Circle on "Taxation of Shares & Securities – Part II" was held on 15th November, 2018 at the Bakulbhai Chinai Committee Room, IMC

CA Bhadresh Doshi addressing the delegates

Study Circle on "Provisions relating to Reopening of Assessment & Issues therein" was held on 29th November, 2018 at Kilachand Hall, 2nd Floor, IMC, Churchgate.

CA Reepal Tralshawala addressing the delegates

Chamber's Luncheon Meeting

International Taxation Committee

ISG on "The Impact of IND-AS, Select Issues" was held on 14th November, 2018 at the CTC Conference Room

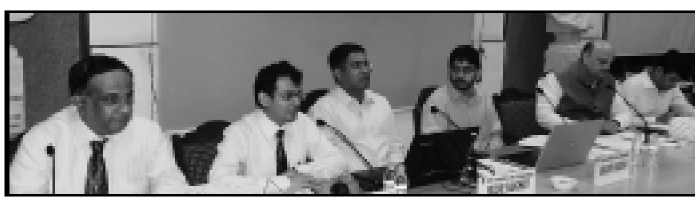
CA Bhaumik Goda addressing the delegates

Corporate Connect Committee

Lecture Meeting on "Laws Relating to Significant Beneficial Owner" was held on 20th November, 2018 at the Babubhai Chinai Committee Room, IMC.

Mr. Richie Sancheti, Advocate

Mr. Srikanth Vasudeva,



CA Paras. K. Savla (Chairman) welcoming the speakers. Seen from L to R: S/ Shri CA Kaushik Jhaveri (Member), Mr. Richie Sancheti, Advocate (Speaker), Mr. Srikanth Vasudeva, Advocate (Speaker), CA Hinesh Doshi (President) and CA Vitang Shah (Convenor)

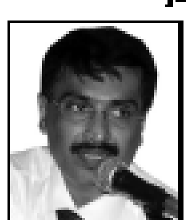
IT Connect Committee

SC on "How Artificial Intelligence is changing Accounting and Auditing" was held on 22nd November, 2018 at CTC Conference room

CA Malvik Majithia addressing the delegates

Indirect Taxes Committee

SC on Issues under GST Annual Return & GST Audit was held on 22nd November, 2018 at A. V. Hall, Jai Hind College, Churchgate



CA Pranav Kapadia (Chairman) addressing the delegates

CA Yash Parmar (Speaker) addressing the delegates

ML-262

Direct Taxes Committee

Half day Seminar on Penalty & Prosecution was held on 1st December, 2018 at the Babhubhai Chinai Committee Room, 2nd Floor, IMC, Churchgate

CA Hinesh Doshi (President) giving his opening remarks. Seen from L to R – S/ Shri CA Devendra Jain (Chairman), CA Bhadresh Doshi (Speaker) and CA Viraj Mehta (Convenor)

CA Devendra Jain (Chairman) welcoming the speakers. Seen from L to R – S/Shri CA Bhadresh Doshi (Speaker), CA Hinesh Doshi (President) and CA Viraj Mehta (Convenor)

Faculties

CA Bhadresh Doshi

CA Jagdish Punjabi

Mr. Ajay Singh, Advocate addressing the delegated. Seen from L to R: S/Shri CA Nimesh Chotani (Convenor), CA Devendra Jain (Chairman), CA Ketan Vajani (Hon. Treasurer) and CA Viraj Mehta (Convenor)

Webinar on "E-Assessment Procedures, Requirements and Way Ahead" was held on 3rd November, 2018

CA Avinash Rawani addressing the delegates

ISG on "Recent Important Decisions under Direct Taxes" was held on 22nd November, 2018 at the CTC Conference room

CA Tanmay Phadke addressing the delegates

CTC Bengaluru Study Group

CTC Bengaluru Study Group was held on 16th November, 2018 at FKCCI, K. G. Road, Bengaluru

CA S. Krishnan addressing the participants on the topic "Recent US Tax reforms and its Impact for Indian Companies"

CA Sharad Rao addressing the participants on the topic "Evolving concept of PE in light of recent decisions"

Membership & Public Relations Committee

Half Day Workshop on GST Annual Returns & GST Audit Report Jointly with Tax Consultants Association, Kolhapur was held on 3rd November, 2018 at Shree Vishveshwarya MSEB Hall, Kolhapur

CA Hinesh Doshi, (President) inaugurating the Workshop by lighting the lamp. Seen from L to R: S/Shri Kumar Chavan, Mr. P. H. Patil, Mr. S. D. Herlekar, Mr. Dhiraj Shah, CA Pranav Kapadia (Speaker) and CA Rajiv Luthia (Speaker)

CA Hinesh Doshi, (President) giving his opening remarks. Seen from L to R: S/Shri Dhiraj Shah and Mr. S. D. Herlekar

CA Rajiv Luthia addressing the delegates

CA Pranav Kapadia addressing the delegates

Dignitaries on the dais

Full day Workshop on GST Annual Return & GST Audit Report was held on 1st December, 2018 at the New Seminar Hall, B. K. Birla College, Gauripada, Kalyan.

CA Rajiv Luthia addressing the delegates

CA Vasant Bhat addressing the delegates

Dignitaries on dais Seen from L to R: S/ Shri Milind Naik, CA Vasant Bhat (Speaker), CA Sachin Gandhi (Co-Chairman), Mr. Vasant Phadke (Vice Principal, B. K. Birla College), Mr. Ganesh Shelke and Mr. Atul Popat

ML-266

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5 points to keep in mind before investing

1 Know your investment goal

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2 Know your investment timeframe

Having a defined time frame for your investments can help you prioritize your goals and helps you stay focused and disciplined.

3 Know your risk tolerance

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4 Know your asset allocation

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5 Know which product to invest

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THE CHAMBER'S JOURNAL

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