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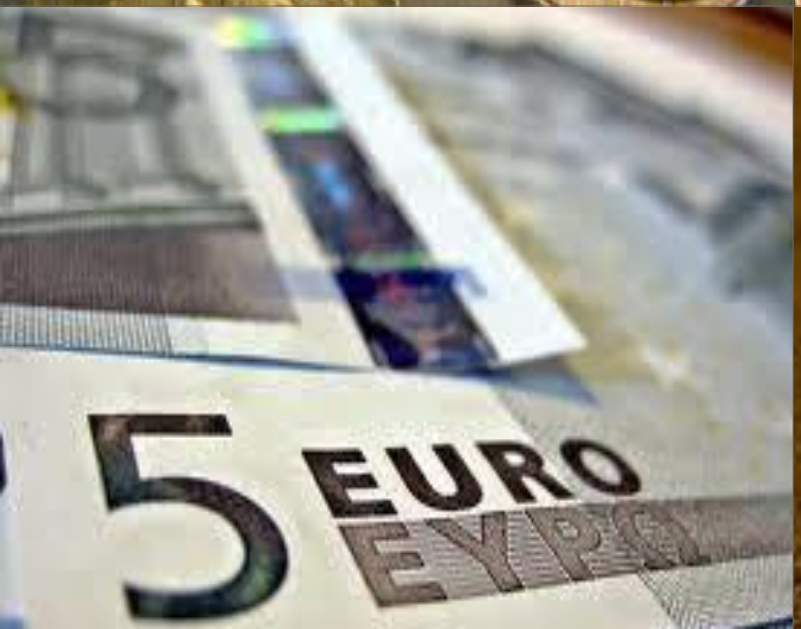
DIRECT TAX REVIEW

SEPTEMBER 2021



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SUPREME COURT RULINGS

Benefits under section 10(23C)(via) available to the hospitals which exists solely for philanthropic purpose and not for the purpose of business.

Facts

The appellant has been granted benefit under section 10(23C)(via) for ten years but then it was put to learned counsel that the same cannot ipso facto entitle the appellant for the benefit in the relevant AYs. On perusal of the order passed by the CCIT-II, Pune, the exemption was been denied. The denial of the exemption has been upheld by the High Court in terms of the impugned judgment. There is a dual reasoning permeating both the orders which seek to deny the exemption. Firstly, that remuneration has been paid from the earnings of the IPD to the doctors who may not be working in that department and, secondly, that rates being charged by appellant are at par with other hospitals which run on commercial basis.

Ruling

SC, in the present case held that a reading of the aforesaid leaves no manner of doubt that while referring to the remuneration payable to member doctors with regard to IPD patients' receipts, the same is not confined to the doctors performing the task. Ld. counsel for the appellant did seek to canvas, despite this, as if only doctors performing the task in the IPD are paid. However, that would run contrary to the own pleading of the appellant which makes it clear that the receipts from IPD are distributed across the board for doctors. We are, thus, of the view that the decision on facts made by the competent authority and as affirmed by the High Court cannot be said to be perverse or having complete absence of rationality for us to interfere in the same. Further, SC made it clear that if the appellant wants to rectify the position, as emerging from aforesaid, that would not preclude the appellant from claiming exemptions for relevant subsequent years. The civil appeal stood dismissed accordingly.

Source: SC in Ashwini Sahakari Rugnalaya vs CCIT
Civil Appeal No 3453, dated September 15, 2021

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HIGH COURT RULINGS

Availability of tangible material would be sufficient for the purpose of invoking the powers under Section 147 of the Act.

Facts

The petitioner being a Company incorporated in New South Wales, Australia was a subsidiary of Cairn Energy PLC based in Edinburgh and is engaged in the business of exploration and production of oil and gas in India since 1996. The case of the petitioner was selected for scrutiny and was referred to Transfer Pricing Officer, who in turn, submitted a report on the Arm's length price. In response, the respondent company filed its return of income and requested to furnish reasons which were supplied to the petitioners. The petitioner

held that initiation of reopening proceedings admittedly is beyond the period of four years and submitted its detailed objections on the reasons furnished which were rejected by the respondents and was disposed of. The assessee contended that the requirement contemplated under Section 147 that the AO must have 'reason to believe' is not satisfied.

Ruling

HC, Madras in the present case held that based on the return of income filed by the petitioner assessee, the assessment order has been passed and subsequently certain new tangible materials were traced out for the purpose of reopening, therefore, the AO has 'reason to believe' that income chargeable to tax has escaped assessment. Under these circumstances, the assessee cannot say that he has produced all the material facts and books of accounts etc., Even if such materials are produced, if the authorities formed an opinion that the tax escaped assessment, then they are empowered to initiate reopening proceedings. In the present case, the assessment is reopened beyond a period of four years and therefore, **mere availability of tangible material would be sufficient for the purpose of invoking the powers under Section 147 of the Act.** This failure on the part of the petitioner was considered for reopening of assessment and the finding is given that the assessee company has misleading the assessing authorities by furnishing incorrect particulars. HC held that the reasons furnished in the case of the petitioner would be sufficient for the purpose of reopening of assessment as the case of the petitioner is initiated beyond a period of four years and therefore, the petitioner is bound to participate in the reopening proceedings for the purpose of defending their case by availing the opportunities to be provided by the authorities in accordance with law. The writ was accordingly dismissed.

Source: HC, Madras in Carin India Ltd. vs. DDIT
WP. No. 12359 of 2013, dated September 01, 2021

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Power to issue the notice was preceded with a new provision of law and thereby Section 148 is to read with Section 148-A of the Income Tax Act, 1961.

Facts

The petitioner has filed the income tax return for the AY 2015-16. Subsequent thereto on the basis of some information available

initially a scrutiny was done however no concealment was found but again a notice under Section 148 was issued. The power to issue the notice was preceded with a new provision of law. Accordingly, a new section 148A was inserted which prescribed that before issuing the notice under Section 148 of the Income Tax Act, the AO was bound to conduct an enquiry giving an opportunity of hearing to the assessee with the prior approval of specified authority and show cause notice in detail was necessary specifying particular date for hearing. The petitioner stated that since the operation of Section 148A came into being on 01-04-2021, as such, the notice issued to the petitioner on 30-06-2021 u/s 148, without following the procedure laid down in section 148A and without giving an opportunity of hearing would be illegal and contrary to the provisions of Section 148A and therefore the same cannot be sustained. It is further submitted that the respondents though have placed reliance

on certain notification of Ministry of Finance but when the law has been enacted by the Parliament then in such case the notification issued by the Ministry of Finance would not over ride even to extend the period of operation of section of the old Act of Section 148 of the Income Tax Act. It was also stated that Section 148A came with certain obligations on the part of the AO, therefore without giving any opportunity of hearing the notice under section 148 of the Act, 1961 would be alleged and therefore submitted that the impugned notice is illegal and is liable to be quashed.

Ruling

By introduction of Section 148A, it was mandated that the AO before issuing any notice under Section 148 shall conduct an enquiry, if required, with the prior approval of specified authority, provide an opportunity of being heard and show cause notice to be served and time was also prescribed. The question here in this case comes for consideration that whether with the promulgation of the Act on 01-04-2021, whether the notice directly issued under Section 148 on 30-06-2021 is valid or not as bar of 148A was created by insertion of Section on 01-04-2021. The reference here has been made to the notifications dated 31-03-2021 and 27-04-2021. For the reasons of lock down during pandemic as all the activities like filing of return, assessment was arrested, the Parliament enacted the Taxation & Others Laws (Relaxation & Amendment of Certain Provisions) Act, 2020 wherein time limit specified or prescribed or notified under specified Act between 20th March 2020 to 31st December 2021 or other date thereafter, after December 2021, CG was given the power to notify.

Reading of the aforesaid notification, the time limit for issuance of notice under Section 148, was initially extended up till on 30-04-2021 and subsequently again the due date was further extended up till 30-06-2021. By effect of such notification, the individual identity of Section 148, which was prevailing prior to amendment and insertion of section 148A was insulated and saved up till 30-06-2021. Here in this case, the power to issue notice under Section 148 which was prior to the amendment was also saved and the time was extended. In a result, the notice issued on 30-06-2021 would also be saved. Therefore, no interference is required to be made in the said issuance of notice and accordingly the petition is dismissed and issue decided in the favor of the assessee.

Source: HC, Chattisgarh in M/s Anant Rice Mill vs. Union of India WP. No. 158 of 2021, dated September 01, 2021

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Personal hearing is part and parcel of the principles of natural justice and comes within the domain of the writ jurisdiction

Facts

That the petitioner is a firm engaged in trading edible oil. The case of the petitioner was selected for scrutiny. The assessee seems to have given certain sources for unsecured credit, notice was given under Section 133(6), to the assessee and to the lenders, who claimed to have given unsecured loan or credit to the Assessee. From those details furnished by the assessee, with regard to the identity, credit-worthiness of the lenders, the revenue was able to find out that, one of the creditors, who had filed ITR for the AY 2018-19. for a total income of Rs. 2.26

crores, however, another lender, is concerned, it has filed ITR for the AY only for a total income of Rs. 1.35 lacs. In view of these revelations, the revenue thought of invoking Section 68 of the Act, and accordingly, the revenue issued a SCN, proposing an addition under Section 68 of the Act, on account of the unsecured loan taken from the second lender. The assessee stated that though notices have been given, response have been received from the assessee, in order to explain through the documents produced to establish that the transactions in question was genuine transaction, there must be a personal hearing, which could have been asked by the assessee, but, due to the change of procedure under Faceless Assessment Scheme, under which the present assessment has been made, the petitioner, inadvertently, has missed it. Therefore, after invoking the power under Section 68, the genuineness and credit-worthiness of the lender was assessed and examined by scrutinizing the documents submitted both by the assessee as well as the lender, and thereafter only, after thorough scrutiny, the revenue has come to the conclusion that, the amount of more than 40 Crores rupees considered as unsecured loan, is to be added in the account of the petitioner as an additional income.

Ruling

HC held that instead of relegating the assessee to approach the appellate authority to raise the same point of getting a personal hearing from the revenue, felt that, since the chance of getting a personal hearing is part and parcel of the principles of natural justice, therefore, it comes within the domain of the writ jurisdiction, and on that ground, HC entertained this writ petition, and accordingly, disposed that the impugned order for the aforesaid reasons and discussions hereinabove made, is hereby set aside, and the matter is remitted back to the respondent Assessing Authority for reconsideration. HC also held that while reconsidering the same, the respondent revenue shall give one day personal hearing to the petitioner, for which advance notice shall be given by the respondent to the petitioner, and on receipt of the same, the petitioner, without fail, shall appear on the date so fixed for personal hearing and produce all documents, if not anything already produced and try to explain, to the satisfaction of the revenue, the case of the Assessee. And thereafter it is open to the revenue to proceed to pass a fresh order of assessment, in accordance with law and on merits. However, there shall be no order as to costs.

Source: HC, Madras in Nagalinga Nadar vs. ACIT
WP. No. 16695 of 2021, dated September 16, 2021

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Assessment order not having been passed in conformity with the requirements of the Faceless Assessment Scheme, 2019 has to be treated as non-est and shall be deemed to have never been passed.

Facts

A notice dated 22-09-2019 under section 143(2) initiating scrutiny proceedings was received by the petitioner. During the proceedings, a notice dated 18-01-2021 calling upon to show cause as to why the assessment should not be completed as per the draft assessment order. The petitioner held that it is not a draft assessment order but a notice calling upon petitioner to provide further details and documentary evidences. Petitioner fled a reply on 26-01-2021 stating that petitioner's Tax Consultant had undergone Prostate Surgery and that he has appointed another CA and sought

time. Petitioner also stated that a personal hearing is required to be granted. The petitioner followed by another reply once again requested a personal hearing. Thereafter, petitioner fled a third response dated 01-02- 2021 whereby remaining requirements of the notice issued were provided. On 01-02-2021, petitioner received a fresh notice calling upon to show cause as to why assessment should not be completed as per the draft assessment order. In our view, this also was not a draft assessment order because petitioner is seeking further documentary evidences. The petitioner placed on records that the assessment order has been passed in breach of the provisions of the Faceless Assessment Scheme, 2019 that was introduced by way of Notification No. 60/2020 dated 13th August, 2020 in as much as petitioner's request for personal hearing has been ignored and mandatory draft assessment order has not been issued to petitioner.

Ruling

Notwithstanding this request respondent has neither granted personal hearing nor stated in the assessment order why the personal hearing was not granted. HC based its opinion on the below mentioned facts:

- As noted, no draft assessment order has been issued at all let alone on 01-02-2021. The said notice was issued for seeking further documentary evidences and those evidences were sought for the first time. When respondent is seeking documentary evidences, that communication by no stretch of imagination can be even referred to as a draft assessment order.
- The Faceless Assessment Scheme, 2019 as per the circular dated 13-08-2020, provides that where a modification is proposed, the National e-Assessment Centre shall provide an opportunity to the assessee by serving a notice calling upon him to show cause as to why the assessment should not be completed as per draft assessment order. This has not been complied with.

HC thereafter held that in the circumstances, the assessment order not having been passed in conformity with the requirements of the Faceless Assessment Scheme, 2019 has to be treated as non-est and shall be deemed to have never been passed.

Source: HC, Bombay in Chander Arjandas Manwani vs. NFAC
WP. No. 3195 of 2021, dated September 21, 2021

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ITAT RULINGS

Deduction u/s 24 is concerned with the ownership of the property, irrespective of the fact whether the assessee has taken the possession of the same or not.

Facts

During the course of the assessment proceedings, it was observed by the AO that the assessee had under the head 'Income from House property' claimed deduction of interest paid on borrowed capital of Rs. 2 lacs under Sec. 24(b) of the Act. On being queried, it was submitted by the assessee that the aforesaid claim for deduction of interest pertained to the funds which were borrowed by him for purchasing a residential property. However, the AO taking note of the fact that the assessee had not taken possession of the aforementioned property in question, thus, disallowed his aforesaid claim for deduction of interest u/s 24(b) of the Act and accordingly passed order u/s 143(3). Aggrieved, the assessee assailed the

assessment order before the CIT(A). However, the CIT(A) not finding favor with the contentions advanced by the assessee upheld the disallowance of the assessee's claim for deduction u/s 24(b) of the Act.

Ruling

The assessee being aggrieved with the order passed by the CIT(A) has carried the matter in appeal before ITAT. ITAT held that we find that the same therein contemplates that an assessee shall be entitled to claim deduction of any interest payable on the capital borrowed by him for acquiring, constructing, repairing, renewing or reconstructing a property. ITAT stated that we are unable to persuade ourselves to accept the view of the CIT(A) that as in the absence of any control/domain over the property in question the assessee would not be in receipt of any income from the same, therefore, allowing of deduction under Sec. 24(b) qua the said property would be beyond comprehension. We are afraid that the said view of the CIT(A) is absolutely misconceived and in fact divorced of any force of law. Insofar the determination of the 'annual lettable value' of a property is concerned, the same as per Sec. 22 read with Sec. 23 of the Act is dependent on the 'ownership' of the property, irrespective of the fact whether the assessee has taken the possession of the same or not. Accordingly, as in the case before us the assessee had admittedly paid interest of Rs. 2,69,842.12 on the capital that was borrowed by him for acquiring the property in question, which was duly evidenced on the basis of the certificate that was filed in the course of the assessment proceedings, therefore, we are unable to concur with the lower authorities who had declined his aforesaid claim for deduction of interest under Sec. 24(b) of the Act. We, thus, not finding favor with the view taken by the CIT(A) therein set-aside his order and direct the A.O to allow the assessee's claim for deduction of Rs. 2 lacs under Sec. 24(b) of the Act. The appeal filed by the assessee is allowed in terms of our aforesaid observations.

Source: ITAT, Mumbai in Abeezar Faizullabhoy vs. CIT
ITA. No. 4831/MUM/2019, dated September 1, 2021

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There cannot be two different fair market value in respect of the very same property, i.e. one at the hands of the seller and the other at the hands of the buyer- Benefit of SDV given to seller cannot be denied to the buyer.

Facts

The assessee, an individual, is engaged in the business of trading in imitation jewellery. In course of assessment proceedings, the AO, based on information available on record, noticed that in the year under consideration the assessee had purchased four immovable properties. From the details furnished, the AO found that the declared sale consideration shown by the assessee is lesser than the SDV determined by the stamp duty authority. The assessee in response to the SCN submitted that the declared value as per the sale agreement is based on the value on the date of agreement on 30-12-2014, whereas, he submitted, the agreements were registered on 13-01-2015 and 21-01-2015. Assessee also submitted that the difference in the market value of property as per the stamp duty authority was due to delay in registration of the sale agreements. Further, assessee also submitted that there are various other reasons for which the declared sale consideration is the actual market value and not the

stamp duty value. The AO invoked the provisions of section 56(2)(vii)(b)(ii) of the Act and added back the difference. The CIT-A thereafter upheld the additions made by the AO.

Ruling

ITAT in the present case held that it is further relevant to observe, section 50C or for that matter section 56(2)(vii)(b)(ii) are identical provisions. Only difference being, 50C is applicable to the seller of an immovable property, whereas, the later provision is applicable to the buyer of the property. Therefore, a benefit given to a seller of the property in respect of marginal variation cannot be denied to the buyer of the property, since, they stand on the same footing. This aspect of the issue has also been considered by the co-ordinate bench in case of Shri Sandip Patil vs ITO (supra), wherein, the co-ordinate bench has held that there cannot be two different fair market value in respect of the very same property, i.e. one at the hands of the seller and the other at the hands of the buyer. Thus, in our view, if the difference in valuation between the value determined by the stamp duty authority and the declared sale consideration is less than 10%, no addition can be made under section 56(2)(vii)(b)(ii) of the Act. Having held so, the second aspect of the issue which requires consideration is whether the exception to section 50C(1) by way of third proviso and section 56(2)(x)(b)(B) would apply prospectively or retrospectively. The Tribunal has consistently expressed the view that since the aforesaid amendments made by Finance Act, 2018 with effect from 01-04-2019 are curative in nature and beneficial provisions, it would apply retrospectively..

Source: ITAT, Mumbai in Joseph Mudaliar vs. DCIT

ITA. No. 6912/Mum/2019, dated September 14, 2021

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Provisions of section 68 duly applicable where the assessee is beneficiary of a sophisticated racket involved in routing unaccounted monies to those willing to buy these entries.

Facts

The assessee being a private limited company engaged in the business of 'investment company'. The assessment was reopened on the basis of certain information flowing in from the investigation wing. The information so received indicated that the assessee has received monies, in the form of share application money, from an entity but that money, though subjected to routing through several layers, ultimately has its source in of huge cash deposits in one of the branches of ICICI Bank. It was found that high value cash deposits, just below Rs 10 lacs, were regularly deposited in 19 different bank accounts maintained with ICICI Bank. This is what was referred to as 'Layer 1' accounts. There were certain addition bank accounts also where cash was deposited regularly, and those amounts also ultimately found their way to these accounts. These accounts were closed within a very short span of time after making high value cash transactions, and the amounts therein, were transferred to other bank accounts known as 'Layer 2'. The funds so credited in other accounts were transferred to the bank accounts of beneficiaries of this money laundering racket, or to some other bank accounts (collectively referred to as Layer 3). When bank accounts of these Layer 3 companies were examined further, it was found that these amounts were finally credited to the accounts of Layer 4. The AO held that what was thus deposited in cash in an ICICI Bank branch, or found its way through the said ICICI Bank branch, ultimately found its

way, though through at least four layering covering its tracks, to the assessee company. The AO ultimately invoked provisions of section 68.

Ruling

ITAT held that the onus is on the assessee to prove genuineness of the transaction to the satisfaction of a fact finding authority something which he has miserably failed in, to justify the huge share premium received by the assessee something which the material on record does not justify, and to demonstrate that the facts and circumstances of the transaction as whole must point towards the impugned transaction being a regular transaction in the normal course of business- something which is clearly missing. ITAT placed reliance on **Hon'ble Supreme Court in the case Durga Prasad More (supra)**, to the effect that "Science has not yet invented any instrument to test the reliability of the evidence placed before a court or tribunal. Therefore, the courts and Tribunals have to judge the evidence before them by applying the test of human probabilities". It also held that human minds may differ as to the reliability of a piece of evidence but in that sphere the decision of the final fact-finding authority is made conclusive by law", and it is in this light, and being alive to the immense faith put in this Tribunal by Hon'ble Courts above, that we have taken the above call. In the result, the appeal of Revenue is allowed.

Source: ITAT, Mumbai in DCIT vs Leena Power Tech Engineers Pvt Ltd ITA. No. 1313/Mum/20, dated September 21, 2021

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ITAT RULINGS

Functionally different companies cannot be selected as comparables

Facts

The assessee company is engaged in the business of providing Information Technology Enabled Services (ITES) call centre operations. The assessee is a 100% subsidiary of HWP Investment Holding (India) Ltd., and provides voice-based customer contact centre services (ITES) to Hutchison 3G Australia Pty Ltd., and Hutchison 3G UK Ltd., (Associated Enterprises-AEs). The ITES services rendered by assessee are mainly in relation to handling services related queries, dealer related queries, mobile number portability related queries, handset related queries, network related queries and price plan related services. The assessee characterized the transaction in respect of provision of ITES services to its AE as a low risk service provider. The assessee benchmarked its international transactions by adopting Transaction Net Margin Method (TNMM); by adopting Profit Level Indicator (PLI) as Operating Profit / Total Cost (OP/TC); taking assessee as a tested party and having the 8 Comparables.

The assessee OP/TC was 18.35% and arithmetic mean of the comparables was 5.74%. The ld. TPO by applying various filters and after, including the comparables chosen by the assessee and excluding certain comparables by the assessee and including fresh comparables, arrived at the arithmetic mean of comparable companies at 39.95%, choosing another set of different set of companies in comparables. Accordingly, the ld. AO made an adjustment of Rs.105,74,53,035/- to arm's length price in respect of provision of ITES services, against which the assessee preferred the current appeal before the Tribunal.

Ruling

Referring to the Tribunal's own order No.7520/Mum/2012 for A.Y.2008-09, it held that the following six companies were held to be functionally not comparable:

- A is engaged in the field of medical transcription services and hence, functionally not comparable with the BPO operations carried
- out by the assessee in the field of tele-communication related services.
- AC is engaged in providing engineering design services which is functionally different from the services provided by the assessee.
- C company is mainly engaged in data processing services which is functionally different from the services provided by the
- assessee company.
- CO had derived major revenue from translation business which is functionally not comparable with the services provided by the
- assessee company.
- E This company is data analytics knowledge process outsourcing service provider which is different from BPO services provided
- by the assessee company.

- G is a specialized geospatial service provider which is different from regular BPO services provided by the assessee company.

Respectfully following the Tribunal order in assessee's own case for A.Y.2008-09, wherein the aforesaid six comparables were held to be functionally not comparable, the Tribunal directed the TPO to exclude these six comparables from the final list of comparables while benchmarking the international transaction of the assessee.

Source:ITAT Bombay in Tech Mahindra Business Services Ltd vs. DCIT ITA No. No. 1326/Mum/2014, dated September 15, 2021

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Compare the controlled transaction with other uncontrolled transactions; royalty not ingrained in the purchase of goods

Facts

Coim India, the assessee is a 100% subsidiary company of Coim S.P.A, Italy. It is engaged in trading in polyadditions (polyurethanes) products and manufacture and trading of polycondensation (ester) products and laminating adhesives for packaging industry under the brand name 'Novacote' and IMUTHANE-Hot cast polyurethane elastomers. Ld. Assessing Officer noticed that during the year under consideration, the assessee had undertaken transaction with its AE, and therefore, the international transactions entered into by the assessee with the AEs were referred to the Ld. TPO for determining the ALP. An amount of Rs.5,41,06,552/- as proposed as an adjustment to the price shown by the taxpayer in its books of account, to be treated as the cumulative adjustment u/s 92CA of the Act. Assessee filed objections before the Id. DRP and submitted that in so far as the royalty is concerned, the assessee is engaged in the business of trading and manufacturing of chemicals; that the company pays royalty for the non-exclusive license to manufacture, sell and use the trademark 'Novacote' in India; and that since the profitability from payment of royalty is inter-linked with other transactions in its chemical business, the same was benchmarked within the business activities using Transaction Net Margin Method (TNMM).

Ruling

The Tribunal observed that there was no dispute on the facts as to the assessee purchasing the material/traded goods from Coim Asia Pacific Pvt. Ltd. whereas the royalty to Coim SPA. Relevant agreements were produced before the authorities below to show that the assessee imported certain chemicals under the Trademark 'Novacote' and paid the royalty for use of such trademark to a separate entity and since the license owner to whom royalty is paid, namely Coim SPA is different from the seller of the material/goods, namely Coim Asia Pacific Pte Ltd., it cannot be said that the royalty is ingrained in the purchase of goods. It is also not in dispute that the commission sales by the assessee constitutes only about 0.42% of the total revenue of the assessee whereas 99.58% of income is from trading of chemicals, as pleaded by the assessee.

Further, the TPO compared the rate of commission charged by the assessee to one AE with the rate of commission charged by the assessee to other AEs. Such an exercise is not permissible under the provisions of section 92F(ii) read with section 92 of the Act, as has been held by the co-ordinate Bench in the case of assessee for the assessment year 2013-14 since the TPO

was supposed to compare the controlled transaction with other uncontrolled transactions. For these reasons, we are of the considered opinion that the orders of the authorities below do not stand the test of judicial scrutiny in so far as the adjustment on the aspect of royalty and commission are concerned and since there is no change in the facts and circumstances of the case from the assessment year 2013-14, while respectfully following the findings of the Tribunal in the order dated 07.05.2018 in ITA No. 7260/Del/2017, we hold that the adjustment in respect of royalty and commission cannot be sustained and the same shall be deleted.

Now, coming to the interest on receivables, the AO was of the opinion that any delay beyond the credit period shall be bench marked as an international transaction and by applying the same, the AO calculated the interest chargeable on receivables by taking the credit period as 30 days and the ld. TPO suggested adjustment of Rs.9,91,252/-. the assessee follows similar credit policy for both the AEs and non-AEs and since no interest is charged from uncontrolled transactions with non-AEs, the transaction disclosed by the assessee has to be held as at Arm's Length. Having regard to this set of facts and circumstances, we are of the considered opinion that the authorities below are not justified in making adjustment on account of interest receivable and therefore, impugned adjustment of Rs.9,91,253/- on account of interest receivable is directed to be deleted. Consequently, the appeal of the assessee deserves to be allowed.

ITA No. ITA No. 495/Del/2021, dated September 27, 2021

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Absent PE in India, the receipt cannot be included in total income on that score; Engineering Analysis (SC) referred

Facts

The assessee is a company incorporated in the USA. It is engaged in the development and manufacture of hydraulic and electro hydraulic and electro- hydraulic controls for off-highway and automotive applications. The assessee assists Original Equipment Manufacturers (OEMs) throughout the product development process. A return was filed declaring certain international transactions. The AO made a reference to the TPO for determining the ALP of the international transactions. The TPO accepted all the transactions at ALP. During the course of draft assessment proceedings, the AO observed that total receipts of the assessee from Indian operations amounted to Rs. 30.40 crores against which it had shown only receipts of Rs. 6.29 crores as income. The assessee was show caused as to why the remaining revenue amounting to Rs. 24 crores be not charged to tax. In the absence of any detail or explanation forthcoming from the side of the assessee, the AO held the remaining amount as receipts in the nature of Royalty/FTS within the meaning of section 9(1) (vi)/9(1)(vii) and added it to the total income. The assessee approached the DRP which allowed relief in respect of some of the items of revenue. For the remaining items of the revenue, the assessee has come up in appeal before the Tribunal.

Ruling

Adverting to the facts as obtaining in the instant case, it is seen that the assessee acquired only a limited right of user in respect of specific software products from PTC Inc. and two other vendors, which are in the nature of copyrighted articles. As such, there cannot possibly be a situation of it passing on the copyright in them to its group entities. It

hardly needs to be accentuated that no one can transfer a better right in a product than he himself has. Since the assessee itself obtained only a limited access to the software products de hors the right to copy the same, the sequitur is that it could not have transferred anything more than that to its entities globally including India. Ergo, there can be no question of treating the amount received from the Indian entity on transfer of copyrighted articles as Royalty in the hands of the assessee within the meaning of Article 12(3) of the DTAA. Respectfully following the ratio decidendi in the case of Engineering Analysis Centre of Excellence Pvt. Ltd. (supra), we hold that the authorities below were not justified in including the amount in question in the total income of the assessee as Royalty by relying on the judgment in the case of Samsung (Karn)(supra), which is no more a good law after the advent of the Engineering Analysis (SC)(supra).

Resultantly, the receipt is held to be not taxable notwithstanding the rejection of the contention of Reimbursement. Article 7 of the DTAA deals with 'Business profits'. In order to bring any business profit within the fold of total income, it is sine qua non that the assessee must have a permanent establishment in India. Absent any permanent establishment of an assessee in India, the receipt cannot be included in the total income on that score.

The next issue raised in this appeal is against the taxability of Reimbursement of Travelling, Freight and other charges. The assessee contended before the DRP that it was a mere case of reimbursement of Travelling and related expenses incurred on behalf of its Indian entity without any mark up and hence the same did not constitute its income. The DRP did not accept the assessee's version on the ground that there was no evidence of reimbursement. The tribunal, going through the details of Travelling and Freight expenses incurred by the assessee and recovered from various group entities including the one in India. Details on the invoice submitted indicated three employees of the Indian entity and the charge is towards their transportation. Other invoices were in relation to Lodging and Boarding of Indian employees recovered from the Indian entity without any profit element. In view of the above discussion, it is clear that one-to-one link is overtly established between the amount paid by the assessee to third party vendors and that recovered from the Indian entity, which is evidently without any mark up. As it is only reimbursement of cost not containing any profit element, there can be no question of including such receipts in the total income of the assessee. This issue was determined in favor of the assessee.

Another issue raised in this appeal is against the rate of tax at which the income declared by the assessee has been charged. The authorities below have rejected the assessee's claim on the ground that it was not made in the income tax return. In our opinion, there can be no estoppel against the provisions of the Act. The purpose of an assessment is to determine the correct amount of income and tax payable thereon. If the Act provides for soft- peddling, then that cannot be whisked away by the Officers. As it is a matter of exercising the option and the assessee did it in a particular way which was more beneficial to it albeit during the course of the assessment proceedings itself, the claim ought not to have been denied. Be that as it may, even though the judgment in of Hon'ble Supreme Court in Goetz

(India) Ltd. Vs. CIT (2006) 284 ITR 323 (SC), provides that the AO has no power to entertain claim made otherwise than by way of a revised return, it unequivocally provides: 'that the issue in this case is limited to the power of the assessing authority and does not impinge on the power of the Tribunal under s. 254 of the IT Act, 1961'. Thus, it is evident, that there is no such constraint on the power of the Tribunal and it can grant rightful relief on a point for which no claim was made in the return of income. The Tribunal held that no fault can be found with the assessee exercising the option as per section 90(2) of the Act to be governed by the reduced rate of tax of 10% plus surcharge etc. in terms of section 115A of the Act. It is, therefore, directed that tax be charged on the declared income of the assessee from Royalty and FTS at 10% under the Act.

ITAT Pune in Husco International Inc. vs. ACIT

ITA No. 145/PUN/2021, dated Sep 27, 2021

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