PAPER – 5: ADVANCED MANAGEMENT ACCOUNTING

QUESTIONS

Total Quality Management – Quality Cost (Two Wheeler, Manufacturer)

1. Hindustan Bikes Ltd. (HBL) formerly known as HELCO is an Indian multinational company. It's headquarter is located in Bengaluru, India. It has been founded in the year 1990 as a manufacturer of locomotives. The company is presently listed locally as well as in international stock market. HBL's parent company is Hindustan Group. The management of HBL recognizes the need to establish a culture at the company so that -

   "Do the right things, right the first time, every time".

   Management has provide you following actual information for the most recent month of the current year:

   Cost Data ₹

Customer Support Centre Cost	35 per hr.
Equipment Testing Cost	18 per hr.
Warranty Repair Cost	1,560 per bike
Manufacturing Rework Cost	228 per bike

   Volume and Activity Data

Bikes Requiring Manufacturing Rework	3,200 bikes
Bikes Requiring Warranty Repair	2,600 bikes
Production Line Equipment Testing Time	1,600 hrs.
Customer Support Centre Time	2,000 hrs.

   Additional information

   HBL carried out a quality review of its existing suppliers to enhance quality levels during the month at a cost of ₹1,25,000. Due to the quality issues in the month, the bike production line experienced unproductive 'down time' which cost ₹7,70,000.

   Required:

   Prepare a statement showing 'Total Quality Cost'.

Life Cycle Analysis

2. P & G International Ltd. (PGIL) has developed a new product "K" which is about to be launched into the market and anticipates to sell 80,000 of these units at a sales price of ₹300 over the product's life cycle of four years. Data pertaining to product "K" are as follows:

Costs of Design and Development of Molds, Dies, and Other Tools	₹8,25,000
Manufacturing Costs	₹125 per unit
Selling Costs	₹12,500 per year + ₹100 per unit
Administration Costs	₹50,000 per year
Warranty Expenses	5 Replacement Parts per 25 units at ₹10 per part ; 1 Visit per 500 units (Cost ₹ 500 per visit)

Required:

(i) Compute the product "K"'s 'Life Cycle Cost'.

(ii) Suppose PGIL can increase sales volume by 25% through 10% reduction in selling price. Should PGIL choose the lower price?

Decision Making using BEP Analysis

3. You have been approached by a friend who is seeking your advice as to whether he should give up his job as an engineer, with a current salary of ₹14,800 per month and go into business on his own assembling and selling a component which he has invented. He can procure the parts required to manufacture the component from a supplier.

It is very difficult to forecast the sales potential of the component, but after some research, your friend has estimated the sales as follows:

(i) Between 600 to 900 components per month at a selling price of ₹250 per component.

(ii) Between 901 to 1,250 components per month at a selling price of ₹ 220 per component for the entire lot.

The costs of the parts required would be ₹ 140 for each completed component. However if more than 1,000 components are produced in each month, a discount of 5% would be received from the supplier of parts on all purchases.

Assembly costs would be ₹ 60,000 per month up to 750 components. Beyond this level of activity assembly costs would increases to ₹ 70,000 per month.

Your friend has already spent ₹ 30,000 on development, which he would write – off over the first five years of the venture.

Required:

(i) Calculate for each of the possible sales levels at which your friend could expect to benefit by going into the venture on his own.

(ii) Calculate the 'Break – Even Point' of the venture for each of the selling price.

(iii) Advice your friend as to the viability of the venture.

Minimum Price – Relevant Cost Concept

4. XL Polymers, located in Sahibabad Industrial Area, manufactures high quality industrial products. AT Industries has asked XL Polymers for a special job that must be completed within one week.

   Raw material R_1 (highly toxic) will be needed to complete the AT Industries' special job. XL Polymers purchased the R_1 two weeks ago for ₹7,500 for a job 'A' that recently was completed. The R_1 currently in stock is the excess from that job and XL Polymers had been planning to dispose of it. XL Polymers estimates that it would cost them ₹1,250 to dispose of the R_1. Current replacement cost of R_1 is ₹6,000.

   Special job will require 250 hours of labour G_1 and 100 hours of labour G_2. XL Polymers pays their G_1 and G_2 employees ₹630 and ₹336 respectively for 42 hours of work per week. XL Polymers anticipates having excess capacity of 150 [G_1] and 200 [G_2] labour hours in the coming week. XL Polymers can also hire additional G_1 and G_2 labour on an hourly basis; these part-time employees are paid an hourly wage based on the wages paid to current employees.

   Suppose that material and labour comprise XL Polymers's only costs for completing the special job.

   Required:

   Calculate the 'Minimum Price' that XL Polymers should bid on this job?

Flexible Budget – Basic Concepts

5. The PLN Co. presents the following static budgets for 4,000 units and 6,000 units activity levels for October 2014:

	Activity Level	
	4,000 units	**6,000 units**
Overhead A ₹ 12/hr. x 2 hr. / unit	96,000	1,44,000
Overhead B	1,40,000	1,90,000

   Overhead C was omitted to be listed out. It is a fixed plant overhead, estimated at ₹ 12.5/hr. at 4,000 units activity level. This has to also feature in the flexible budget. The actual production was 5,000 units and 9,600 hours were needed for production.

   Required:

   Prepare a statement showing the 'Flexible Budget' amount of each overhead to enable appropriate comparison with the actual figures.

Application of Sales Variances (Marketing Company)

6. Universal LTD. is engaged in marketing of wide range of consumer goods. M, N, O and P are the zonal sales officers for your zones. The company fixes annual sales target for them individually.

You are furnished with the following:

(a) The standard costs of sales target in respect of M, N, O and P are ₹ 5,00,000, ₹ 3,75,000, ₹ 4,00,000 and ₹ 4,25,000 respectively.

(b) M, N, O and P respectively earned ₹ 29,900, ₹ 23,500, ₹ 24,500 and ₹ 25,800 as commission at 5% on actual sales effected by them during the previous year.

(c) The relevant variances as computed by a qualified accountant are as follows:

Particulars	M (₹)	N (₹)	O (₹)	P (₹)
Sales Price Variance	4,000 (F)	6,000 (A)	5,000 (A)	2,000 (A)
Sales Volume Variance	6,000 (A)	26,000 (F)	15,000 (F)	8,000 (F)
Sales Margin Mix Variance	14,000 (A)	8,000 (F)	17,000 (F)	3,000 (A)

Note: (A) = Adverse variance and (F) = Favorable variance

Required:

(i) Compute the amount of 'Sales Target Fixed' and the 'Actual Margin Earned' in case of each of the zonal sales officer.

(ii) Evaluate the overall performance of these zonal sales officers taking three relevant base factors and then recommend whose performance is the best.

Interpretation of Variances and CSFs (Spices Manufacturer)

7. Natural Spices manufactures and distributes high-quality spices to gourmet food shops and top quality restaurants. Gourmet and high-end restaurants pride themselves on using the freshest, highest-quality ingredients.

Natural Spices has set up five state of the art plants for meeting the ever growing demand. The firm procures raw material directly from the centers of produce to maintain uniform taste and quality. The raw material is first cleaned, dried and tested with the help of special machines. It is then carefully grounded into the finished product passing through various stages and packaged at the firm's ultraclean factory before being dispatched to customers.

The following variances pertain to last week of operations, arose as a consequence of management's decision to lower prices to increase volume.

Sales Volume Variance	18,000 (F)
Sales Price Variance	14,000 (A)
Purchase Price Variance	10,000 (F)
Labour Efficiency Variance	11,200 (F)
Fixed Cost Expenditure Variance	4,400 (F)

Required:

(i) Identify the 'Critical Success Factors' for Natural Spices.

(ii) Evaluate the management's decision with the 'Overall Corporate Strategy' and 'Critical Success Factors'.

Transfer Pricing Based on Opportunity Cost

8. Division Z is a profit center which produces four products A, B, C and D. Each product is sold in the external market also. Data for the period is:

	A	B	C	D
Market Price *per unit* (₹)	150	146	140	130
Variable Cost of Production *per unit* (₹)	130	100	90	85
Labour Hours Required *per unit*	3	4	2	3

Product D can be transferred to Division Y, but the maximum quantity that may be required for transfer is 2,500 units of D.

The maximum sales in the external market are:

A 2,800 units

B 2,500 units

C 2,300 units

D 1,600 units

Division Y can purchase the same product at a price of ₹125 per unit from outside instead of receiving transfer of product D from Division Z.

Required:

Calculate the 'Transfer Price' for each unit for 2,500 units of D, if the total labour hours available in Division Z are 20,000 hours?

Balance Score Card (Banking Company)

9. Your Bank Ltd., was established on the 30th September, 1940 under the provisions of Co-operative Societies Act by the eminent professionals to encourage self-help, thrift, cooperation among members. Bank was issued Banking License under Banking

Regulation Act, 1949 on October 25, 1986 to carry out the Banking Business within the national capital and since then the Bank has been growing continuously. At present, Bank has large number of membership of individuals from different sections. The Bank has 12 branches in the NCT of Delhi. Bank offers 'traditional counter service'. Opening hours are designed to coincide with local market days.

Board of Directors were worried from growing popularity of new style banks. These banks offer *diverse range* of services such as direct access to executive management, a single point of contact to coordinate all banking needs, appointment banking to save time, free online banking services 24/7, free unlimited ATM access etc.

It has now been decided that the bank will focus on "What Customers Want" and will use a balanced scorecard to achieve this goal.

Required:

Produce, for each of the three non-financial perspectives of a 'Balanced Scorecard', an *objective* and a *performance measure* that the bank could use with *appropriate reason*.

Customer Profitability Analysis (Pharmaceutical Firm)

10. Oxford Medical Care Co. (OMCC) is a pharmaceutical firm, operating its entire business through its four customers Ox_1, Ox_2, Ox_3, and Ox_4. Ox_1 and Ox_2 are small pharmaceutical stores while Ox_3 and Ox_4 are large discount stores with attached pharmacies. OMCC uses discount pricing strategy and prices its products at variable cost plus 25%.

Item	Small Pharmaceuticals		Large Pharmaceuticals		Activity Rate
	Ox_1	Ox_2	Ox_3	Ox_4	
Number of Orders	4	9	6	3	₹750
Order Size	₹40,000	₹20,000	₹4,25,000	₹4,00,000	n/a
Average Discount	4.50%	9.50%	17.50%	11.50%	n/a
Regular Deliveries	4	9	6	3	₹375
Expedited Deliveries	2	0	2	0	₹1,250
General Administration Cost	₹20,250		₹48,375		

Required:

(i) Prepare a 'Customer Profitability Statement' that shows the profit from each customer and each customer channel.

(ii) Recommend some points to improve OMCC's profit.

Balance Score Card (Fitness Centre)

11. Fitness Solution is a family owned fitness club, founded in 2010 by Peter and Albert with traditional style equipment. Club commenced operations in February 2011 within a

shopping mall so that members after working out, can conveniently shop, dine, pick up their children from enrichment classes or go to the cinema.

Peter and Albert, the owners, pride themselves for providing a customized / tailored program by taking into account a person's medical history, present fitness level, fitness goals, fitness interests and offer many other small amenities that might be difficult to get in a larger Fitness Centre. They believe –

"Each individual is unique and requires a specialized program plan which should be customized and tailored to his/her needs."

They have a number of loyal members even though they offer the traditional style equipment.

Peter and Albert take care of most of the routine operations, along with a small permanent staff, and temporary staff.

Required:

(i) Identify at least three 'Critical Success Factors' for Fitness Solution.

(ii) Construct a 'Balance Scorecard' for Fitness Solution. *(2 measures for each of the 4 perspectives are sufficient).*

Linear Programming – Simplex Method

12. Given below is an iteration in a simplex table for a maximization objective linear programming product mix problem for products x, y and z. Each of these products is processed in three machines KA-07, KB-27 & KC-49 and each machine has limited available hours.

$C_j \rightarrow$			30	40	20	0	0	0
C_B	Basic Variable (B)	Value of Basic Variables b ($=X_B$)	x	y	z	s_1	s_2	s_3
30	x	250	1	0	-26/16	10/16	-12/16	0
40	y	625	0	1	31/16	-7/16	10/16	0
0	s_3	125	0	0	11/16	-3/16	1/8	1

s_1, s_2 and s_3 are slack variables for machine KA-07, KB-27 and KC-49 respectively. Answer the following questions, giving reasons in brief:

(i) Does the table above give an 'Optimal Solution'?

(ii) Are there more than one 'Optimal Solution' / 'Alternate Optimal Solution'?

(iii) Is this solution 'Feasible'?

(iv) Is this solution 'Degenerate'?

(v) Write down the 'Objective Function' of the problem.

(vi) Write the 'Optimal Product Mix' and 'Profit' shown by the above solution.

(vii) Which of these machines is being used to the full capacity when producing according to this solution?

(viii) How much would you be prepared to pay for another hour of capacity each on machine KA-07, machine KB-27, and machine KC-49?

(ix) If the company wishes to expand the production capacity, which of the three resources should be given priority?

(x) What happens if 16 machine hours are lost due to some mechanical problem in machine KB-27?

(xi) A customer would like to have one unit of product z and is willing to pay higher price for z in order to get it. How much should the price be increased so that the company's profit remains unchanged?

(xii) A new product is proposed to be introduced which would require processing time of 4 hours on machine KA-07, 2 hours on machine KB-27 and 4 hours on machine KC-49. It would yield a profit of ₹12 per unit. Do you think it is advisable to introduce this product?

Transportation Problem – Change in Resource Capacities AND/ OR Destination Requirements

13. The following table shows all the necessary information on the available supply from each warehouse, the requirement of each market and the unit transportation cost in rupees from each warehouse to each market.

Warehouses	Markets				Supply
	I	II	III	IV	
A	5	2	4	3	22
B	4	8	1	6	15
C	4	6	7	5	8
Requirement	7	12	17	9	45/45

The shipping clerk has worked out the following schedule from experience:

12 units from A to II, 1 unit from A to III, 9 units from A to IV, 15 units from B to III, 7 units from C to I and I unit from C to III.

(i) Check if the clerk has made the 'Optimal Schedule'.

(ii) Find the 'Optimal Schedule' and 'Minimum Total Shipping Cost'.

(iii) Carrier of route C to II offers to transport entire supply of warehouse C at a reduced price. By how much must the rate be reduced by the Carrier before the clerk should consider giving him business?

(iv) If the supply from warehouse B reduces to 11 units and simultaneously the requirement of market III reduces to 13 units, find the 'Optimal Transportation Schedule'.

(v) Further, if supply from warehouse A also reduces to 19 units and simultaneously the requirement of III reduces further to 10 units, will the optimal solution of part (iv) change?

Assignment Problem – The Travelling Salesman Problem

14. A salesman has to visit five cities. He wishes to start from a particular city, visit each city once and then return to his starting point. Cost (in ₹ '000) of travelling from one city to another is given below:

	P	Q	R	S	T
P	-	5	14	20	2
Q	17	-	8	23	5
R	23	20	-	11	20
S	35	11	17	-	14
T	2	8	5	23	-

Required:

Find out the 'Least Cost Route'.

Application of Simulation Technique in Project Management

15. The following table gives the activities in a construction project and the time durations with associated probability of each activity:

Activity	Predecessors	Time (in Days)	Probability
A	---	6	0.50
		8	0.50
B	---	4	0.30
		5	0.20
		6	0.50
C	A	8	0.50
		16	0.50

D	A, B	8	0.30
		10	0.70
E	C, D	2	0.20
		4	0.80

To simulate the project, use the following random numbers taking the first five random numbers digits (representing the five activities) for each trial and so on:

11, 16, 23, 72, 94; 83, 83, 02, 97, 99; 83, 10, 93, 4, 33; 53, 49, 94, 37, 7

Required:

Determine the 'Critical Path' and the 'Project Duration' for each trial.

Learning Curve – Steady State

16. AUD International Co. is a multiproduct firm. It is planning to launch a new product 'X-500' in coming months. Production will be in batches of 1,000 units throughout the life of the product. It is also possible to achieve 90% learning rate but the learning would cease after 64th batch. Other relevant data of product 'X-500' is as follows:

Expected Life	2,56,000 units
Selling Price *per unit*	₹123
Direct Material per unit	₹36
Direct Labour Cost *first batch*	₹52,500
Other Variable Costs	₹24
Specific Fixed Cost	₹38,75,000

Required:

(i) Calculate the 'Expected Profit' to be earned from the product over its lifetime.

Note: The learning index for a 90% learning curve is -0.152; $(64)^{-0.152} = 0.5314$; $(63)^{-0.152} = 0.5327$

(ii) It is now thought that a learning effect will continue for all of the 256 batches that will be produced. Calculate the 'Rate of Learning' required to achieve a lifetime product profit of ₹1,00,00,000, assuming that a constant rate of learning applies throughout the product's life.

SUGGESTED ANSWERS/ HINTS

1. Statement Showing "Total Quality Cost"

Particulars of Costs	₹
Prevention Costs	
Supplier Review	1,25,000
Appraisal Costs	
Equipment Testing (₹18 × 1,600 hrs.)	28,800
Internal Failure Costs	
Down Time	7,70,000
Manufacturing Rework (₹228 × 3,200 bikes)	7,29,600
External Failure Costs	
Customer Support (₹35 × 2,000 hrs.)	70,000
Warranty Repair (₹1,560 × 2,600 bikes)	40,56,000
Total Quality Costs	**57,79,400**

2. (i) Statement Showing "K's Life Cycle Cost (80,000 units)"

Particulars	Amount (₹)
Costs of Design and Development of Molds, Dies, and Other Tools	8,25,000
Manufacturing Costs (₹125 × 80,000 units)	1,00,00,000
Selling Costs (₹100 × 80,000 units + ₹12,500 × 4)	80,50,000
Administration Costs (₹50,000 × 4)	2,00,000
Warranty (80,000 units / 25 units × 5 parts × ₹10) (80,000 units / 500 units × 1 visit × ₹500)	 1,60,000 80,000
Total Cost	1,93,15,000

(ii) Statement Showing "K's Life Cycle Cost (1,00,000 units)"

Particulars	Amount (₹)
Costs of Design and Development of Molds, Dies, and Other Tools	8,25,000
Manufacturing Costs (₹125 × 1,00,000 units)	1,25,00,000
Selling Costs (₹100 × 1,00,000 units + ₹12,500 × 4)	1,00,50,000

Administration Costs (₹50,000 × 4)	2,00,000
Warranty (1,00,000 units / 25 units × 5 parts × ₹10) (1,00,000 units / 500 units × 1 visit × ₹500)	 2,00,000 1,00,000
Total Cost	2,38,75,000

Statement Showing "K's Life Time Profit"

Particulars	Amount (₹) 80,000 units	Amount (₹) 100,000 units
Sales	2,40,00,000 (80,000 × ₹300)	2,70,00,000 (1,00,000 × ₹270)
Less: Total Cost	1,93,15,000	2,38,75,000
Profit	46,85,000	31,25,000

Decision

Reducing the price by 10% will decrease profit by 33% (₹15,60,000). Therefore, PGIL should not cut the price.

3. The salary of ₹14,800 per month is a benefit foregone by going into business. It should therefore be considered as a minimum profit which must be earned p.m. from the new venture in order to be not worse – off than before.

Sum of ₹30,000 spent on the development work of the new venture cannot be recovered irrespective of the decision and thus it should be ignored.

At a Selling Price of ₹250

Contribution *per unit* (₹250 – ₹140) ₹110

Minimum Sales (units) to recover *assembly costs* of ₹60,000 p.m. and earn a *profit* of ₹14,800 p.m. (Break – even Sales Level)

$$\frac{₹60,000 + ₹14,800}{₹110} = 680 \text{ units}$$

Note that at 600 units and up to 679 units i.e. units below the break-even level the loss would be ₹110/- per unit. From 680 units up to 750 units i.e. on additional 70 units the total profit would be ₹ 7,700 (70 units × ₹110).

Minimum Sales (units) to recover *assembly cost* of ₹70,000 p.m. and earn a *profit* of ₹14,800 p.m. (Break – even Sales Level)

$$\frac{₹70,000 + ₹14,800}{₹110} = 770.909 \text{ units}$$

If the sales units are more than 770.909 units and up to 900 units, profit would be made. The total amount of profit comes to ₹14,200 [(900 units – 770.909 units) × ₹110]

It is not worthwhile to proceed if the demand of components is less than 680 units or between 750 to 770.909 units.

At a Selling Price of ₹220

Minimum Sales (units) to recover *assembly cost* of ₹70,000 p.m. and earn a *profit* of ₹14,800 p.m. (Break even – Sales Level)

$$\frac{₹70,000 + ₹14,800}{₹220 - ₹140} = 1,060 \text{ units}$$

Minimum Sales (units) to recover *assembly cost* of ₹70,000 p.m. and earn a profit of ₹14,800 p.m.; after availing a discount of 5% on the purchases of all parts.

$$\frac{₹70,000 + ₹14,800}{₹220 - \left(₹140 - \frac{5}{100} \times ₹140\right)} = 974.712 \text{ units}$$

Or 975 units

Conclusion

It is not worthwhile to sell between 900 and 1,000 units when no discount is available. Also, it is worthwhile selling at ₹220 if sales units are in excess of 1,000 units and a discount of 5% is available on the purchase of all components–parts.

Profit on the Sale (1,250 units) ₹23,950 (1,250 units × ₹87 – ₹84,800)

Advice on the viability of the venture

At a selling price of ₹250 he will not be at a loss if the demand of the component exceeds 680 units to 750 units and 770.909 units to 900 units.

At a selling price of ₹220, it is not worthwhile to sell if the demand is less than 1,000 components without availing a discount of 5%.

4. Opportunity Cost of Labour - The G_2 labour has zero opportunity cost as there is no other use for the time already paid for and is available. However, XL Polymers needs to pay an additional amount for G_1 labour. This amount can be save if the special job were not there.

G_1 labour:	
Hours Required	250
Hours Available	150
Extra Hours Needed	100
Cost *per hour* (₹630/42hrs)	₹15
Opportunity Cost	₹1,500

Thus, the 'Opportunity Cost of Labour' for completing the special job is ₹1,500.

Opportunity Cost of Material – XL Polymers has no alternative use for the R_1, they must dispose of it at a cost of ₹1,250. Thus, XL Polymers actually *saves* ₹1,250 by using the materials for the AT Industries' special job. Consequently, the 'Opportunity Cost of Material' is - ₹1,250 (i.e., the opportunity cost of this resource is negative).

The *minimum price* is the price at which XL Polymers just recovers its 'Opportunity Cost'. XL Polymers's 'Total Opportunity Cost' is ₹250 (₹1,500 − ₹1,250). Accordingly, minimum Price for the Special Job is ₹250.

5. Statement Showing "Flexible Budget for 5,000 units Activity Level"

Particulars	Amount (₹)
Overhead A (₹12.00 *per hour* × 2 hrs. *per unit* × 5,000 units)	1,20,000
Overhead B* (₹40,000 + ₹ 25 × 5,000 units)	1,65,000
Overhead C (₹12.50 *per hour* × 2 hrs. *per unit* × 4,000 units)	1,00,000
Total	3,85,000

Working Note (*):

Overhead B

$$\text{Variable Cost (per unit)} = \frac{\text{Change in Overhead Cost}}{\text{Change in Production Units}}$$

$$= \frac{₹1,90,000 - ₹1,40,000}{6,000\text{ units} - 4,000\text{ units}}$$

$$= ₹25$$

$$\text{Fixed Cost} = ₹1,40,000 – 4,000\text{ units} \times ₹25$$

$$= ₹40,000$$

6. Statement Showing "Sales Target Fixed and Actual Margin"

Particulars	Zonal Sales Officers			
	M (₹)	N (₹)	O (₹)	P (₹)
Commissioned Earned	29,900	23,500	24,500	25,800
Actual Sales (Commission Earned/ 5%)	5,98,000	4,70,000	4,90,000	5,16,000
Sales Price Variance	4,000(F)	6,000(A)	5,000(A)	2,000(A)
Sales Volume Variance	6,000(A)	26,000(F)	15,000(F)	8,000(F)

Sales Target (Budgeted Sales)	6,00,000	4,50,000	4,80,000	5,10,000
Standard Cost of Sales Target	5,00,000	3,75,000	4,00,000	4,25,000
Budgeted Margin	1,00,000	75,000	80,000	85,000
Sales Margin Mix Variance	14,000(A)	8,000(F)	17,000(F)	3,000(A)
Sales Price Variance	4,000(F)	6,000(A)	5,000(A)	2,000(A)
Actual Margin	90,000	77,000	92,000	80,000

*Note: Since no information has been given about Sales Margin Quantity Variance, therefore for calculating actual margin the same has been assumed to be **zero**.*

Statement Showing "Evaluation of the Performance of Zonal Sales Officers"

Particulars	Zonal Sales Officers			
	M	N	O	P
Efficiency towards the Target Sales				
(a) Whether target achieved	No	Yes	Yes	Yes
(b) Actual Sales to Target Sales Ratio	99.67%	104.44%	102.08%	101.18%
(c) Rank	IV	I	II	III
Contribution Approach				
(a) Contribution Earned (₹)	90,000	77,000	92,000	80,000
(b) Rank	II	IV	I	III
Margin Vs Sales Ratio				
(a) Budgeted Margin/ Sales Target Ratio	16.67%	16.67%	16.67%	16.67%
(b) Actual Margin Vs Actual Sales Ratio	15.05%	16.38%	18.78%	15.50%
(c) Rank	IV	II	I	III

An analysis on performance of four Zonal Sales Officers based on three base factors, the performance of officer O is the best.

7. **(i)** Gourmet and high-end restaurants recognises Natural Spices on the basis of its *high quality* of spices. Therefore, quality is most critical success factor of Natural Spices. There are other factors which cannot be ignore such as price, delivery options, attractive packing etc. But all are secondary to the quality.

(ii) Deliberate action of cutting price to increase sales volume indicates that firm is intending to expand its market to retail market and street shops which is price sensitive.

Purchase Price Variance is clearly indicating that firm has purchased raw material at lower price which may be due to buying of lower quality of material. Similarly positive *Efficiency Variance* is indicating cost cutting and stretching resources.

It appears that firm is intending to expand its market to retail market and street shops by not only reducing the price but also compromising its quality which is opposing its current strategy of *high quality*.

Management should monitor the trends of variances on regular basis and take appropriate action in case of evidence of permanent decline in quality. Here, customer feedback is also very important.

8. "Ranking of Products When Availability of Time is the Key Factor"

Products	A	B	C	D
Market Price (₹)	150	146	140	130
Less: Variable Cost (₹)	130	100	90	85
Contribution *per unit* (₹)	20	46	50	45
Labour Hours *per unit*	3 hrs.	4 hrs.	2 hrs.	3 hrs.
Contribution *per Labour Hour*	6.66..	11.50	25.00	15.00
Ranking	IV	III	I	II
Maximum Demand (units)	2,800	2,500	2,300	1,600
Total No. of Hours	8,400	10,000	4,600	4,800
Allocation of 20,000 Hours on the Basis of Ranking	600*	10,000	4,600	4,800

(*) Balancing Figure

Note -Time required to meeting the demand of 2,500 units of Product D for Division Y is 7,500 hrs. This requirement of time viz. 7,500 hrs for providing 2,500 units of Product D for Division Y can be met by sacrificing 600 hours of Product A (200 units) and 6,900 hours of Product B (1,725 units).

Transfer Price = Variable Cost + Opportunity Cost

$$= ₹85 + \frac{(6{,}900 \text{ hrs.} \times ₹11.5 + 600 \text{ hrs.} \times ₹6.66...)}{2{,}500 \text{ units}}$$

$$= ₹85 + \frac{₹79{,}350 + ₹4{,}000}{2{,}500 \text{units}}$$

= ₹85 + ₹33.34

= ₹118.34

9. Internal Business Process Perspective

Objective: Cross-sell Products

Measure: Products Purchased *per customer*

Reason: Cross-selling, or encouragement customers to purchase additional products e.g. insurance, forex etc. is a *measure of customer satisfaction*. Only if a service is perceived as highly satisfactory the service would be repeated/ additional products or services would be accepted.

Learning and Growth Perspective

Objective: Increase the Number of New Products or Services Sold

Measure: Number of Customers Buying the New Products/ New Services

Reason: Long term financial success requires bank to create new products / services (e.g. internet banking, ATM access) that will meet emerging needs of current / future customers such as 24/7 banking.

Customer Perspective

Objective: Increase Customer Loyalty

Measure: Number of Accounts Closed or Closure Request Received

Reason: Customer loyalty describes the extent to which bank maintains durable relations to its customers. The share of existing customers should have a high importance as it indicates about image and reputation. Closure request is not a good sign. Bank should investigate reasons for the same and take appropriate actions to improve services offered to retain customers.

☞ Other **Objectives** and **Measures** are also possible but they must relate to the bank's **Goal**.

10. Statement Showing "Customer Profitability Analysis"

Particulars	Ox_1	Ox_2	Channel Total	Ox_3	Ox_4	Channel Total
	Small Stores			Large Stores		
Revenue	1,60,000	1,80,000	3,40,000	25,50,000	12,00,000	37,50,000
Discount	7,200	17,100	24,300	4,46,250	1,38,000	5,84,250
Net Revenue	1,52,800	1,62,900	3,15,700	21,03,750	10,62,000	31,65,750
Variable Costs	1,28,000	1,44,000	2,72,000	20,40,000	9,60,000	30,00,000
Contribution Margin	24,800	18,900	43,700	63,750	1,02,000	1,65,750
Order Processing	3,000	6,750	9,750	4,500	2,250	6,750
Regular Deliveries	1,500	3,375	4,875	2,250	1,125	3,375
Expedited Deliveries	2,500	---	2,500	2,500	---	2,500

Customer Profit	17,800	8,775	26,575	54,500	98,625	1,53,125
Channel Cost			20,250			48,375
Channel Profit			6,325			1,04,750

Recommendations

Small Pharmaceuticals

Even though Ox_1 has lower sales volume (11% lesser from Ox_2), it is contributing around 67% of small store's profit as its order is for larger quantities and discount offered is very less.

OMCC is only just at breakeven point with small pharmaceuticals. To improve profit OMCC should:

(i) Coordinate with Ox_2 to *increase order size* and try to *negotiate a smaller discount*.

(ii) Try to work with Ox_1 to *reduce expedited deliveries*.

Large Pharmaceuticals

OMCC makes substantial profit from the large pharmaceuticals. Ox_4 alone contributing around 55% of total customer's profit and its order is for larger quantities. Therefore, Ox_4 is most favorable customer and may be given *little extra attention*. For Ox_3, OMCC may have *no options* but to treat it as less profitable customer as Ox_3 accounts more than 60% of sales.

11. (i) Fitness Solution's main **Critical Success Factors** are

(a) Developing and maintaining a high level of customer satisfaction.

(b) Offering facilities that are not much below that offered by competition.

(c) Keeping a tight cap on costs as there is considerable competitive pressure in this industry and entry barriers are not high.

(ii) The following is a possible **Balance Scorecard** for Fitness Solution

Financial Perspective	Operating expenses relative to budget
	Cash flow
	Total daily operating revenue
Customer Perspective	Turnover rate among members
	Customer satisfaction rate
Internal Perspective	Number of employee complaints
	Number of equipment not available on average day (due to maintenance)
Innovation and Learning	Number of new equipment put into service
	Number of staff participating in training courses

12. (i) Yes, the given solution is optimal because all $C_j - Z_j$ are less than, or equal to, zero.

$C_j \rightarrow$			30	40	20	0	0	0
C_B	Basic Variable (B)	Value of Basic Variables b ($=X_B$)	x	y	z	s_1	s_2	s_3
30	x	250	1	0	-26/16	10/16	-12/16	0
40	y	625	0	1	31/16	-7/16	10/16	0
0	s_3	125	0	0	11/16	-3/16	1/8	1
		$Z_j = \sum C_{Bi}X_j$	30	40	115/4	5/4	5/2	0
		$C_j - Z_j$	0	0	-35/4	-5/4	-5/2	0

(ii) No, because for each of the **non - basic variables** z, s_1 and s_2, the $C_j - Z_j$ is strictly negative. Alternate optimal solution (s) exist when either of non-basic variables has a zero $C_j - Z_j$.

Non Basic Variables	z	s_1	s_2
$C_j - Z_j$	-35/4	-5/4	-5/2

(iii) Yes, because the given solution has no artificial variable in the basis.

(iv) No, solution is not degenerate as none of the basic variables has zero quantity.

Basic Variables	x	y	s_3
Quantity	250	625	125

(A solution degenerates if the Quantity of one or more basic variables is zero)

(v) Maximize Z = 30x + 40y + 20z

(vi) According to the given solution, 250 units of x and 625 units of y are being produced. The total profit is ₹32,500 (250 units × ₹30 + 625 units × ₹40).

(vii) Machine KA-07 and KB-27 are being used to the full capacity because, the slack variable s_1 and s_2 corresponding to them has a zero value in the solution.

(viii) The shadow price of hours on machine KA-07, machine KB-27 and machine KC-49 are being ₹5/4, ₹5/2 and ₹0, respectively, these are the maximum prices one would be prepared to pay for another hour of capacity for these three machines.

(ix) Machine KB-27 may be given priority as its shadow price is the highest.

(x) When 16 hours are lost, then production of x would increase by 12 units and that of y would decrease by 10 units and the total profit decrease by ₹40.

(xi) $C_j - Z_j$ for z being -35/4, production of each unit of z would cause a reduction of 35/4 rupee. Thus, the price for z should be increased by at least 35/4 rupee to ensure no reduction of profits.

(xii) Shadow prices of times on machines KA-07, KB-27 and KC-49 are ₹5/4, ₹5/2 and ₹0. Production of a unit of the proposed new product would, therefore, reduce profit by ₹10 [(4 hrs. × ₹5/4) + (2 hrs. × ₹5/2) + (4 hrs. × ₹0)]. Since the product would yield a profit of ₹12, it would result in a net increase in profit at a rate of ₹2 per unit. It is advisable, therefore to introduce it.

13. (i) The Initial basic solution worked out by the shipping clerk is as follows-

Warehouse	Market				Supply
	I	II	III	IV	
A	5	2 [12]	4 [1]	3 [9]	22
B	4	8	1 [15]	6	15
C	4 [7]	6	7 [1]	5	8
Req.	7	12	17	9	45

The initial solution is tested for optimality. The total number of independent allocations is 6 which is equal to the desired (m +n –1) allocations. We introduce u_i's (i = 1, 2, 3) and v_j's (j = 1, 2, 3, 4). Let us assume $u_1 = 0$, remaining u_i's and v_j's are calculated as below-

($u_i + v_j$) Matrix for Allocated / Unallocated Cells

					u_i
	1	2	4	3	0
	-2	-1	1	0	-3
	4	5	7	6	3
v_j	1	2	4	3	

Now we calculate $\Delta_{ij} = C_{ij} - (u_i + v_j)$ for non basic cells which are given in the table below-

Δ_{ij} Matrix

4			
6	9		6
	1		-1

Since one of the Δ_{ij}'s is negative, the schedule worked out by the clerk is not the optimal solution.

(ii) Introduce in the cell with negative Δ_{ij} [R_3C_4], an assignment. The reallocation is done as follows-

	12	1	9
		15	
7		1	

(+1 at 9, -1 at 15, -1 at 1, +1 at the empty cell)

Revised Allocation Table

	12	2	8
		15	
7			1

Now we test the above improved initial solution for optimality-

($u_i + v_j$) Matrix for Allocated / Unallocated Cells

					u_i
	2	2	4	3	0
	-1	-1	1	0	-3
	4	4	6	5	2
v_j	2	2	4	3	

Now we calculate $\Delta_{ij} = C_{ij} - (u_i + v_j)$ for non basic cells which are given in the table below-

Δ_{ij} Matrix

3			
5	9		6
	2	1	

Since all Δ_{ij} for non basic cells are positive, the solution as calculated in the above table is the optimal solution. The supply of units from each warehouse to markets, along with the transportation cost is given below-

Warehouse	Market	Units	Cost per unit (₹)	Total Cost (₹)
A	II	12	2	24
A	III	2	4	8
A	IV	8	3	24
B	III	15	1	15
C	I	7	4	28
C	IV	1	5	5
			Minimum Total Shipping Cost	104

(iii) If the clerk wants to consider the carrier of route C to II only, instead of 7 units to I and 1 unit to IV, it will involve shifting of 7 units from (A, II) to (A, I) and 1 unit to (A, IV) which results in the following table-

Warehouse	Market				Supply
	I	II	III	IV	
A	5 [7]	2 [4]	4 [2]	3 [9]	22
B	4	8	1 [15]	6	15
C	4	6 [8]	7	5	8
Req.	7	12	17	9	45

The transportation cost will become-

Warehouse	Market	Units	Cost per unit (₹)	Total Cost (₹)
A	I	7	5	35
A	II	4	2	8
A	III	2	4	8
A	IV	9	3	27
B	III	15	1	15
C	II	8	6	48
			Minimum Total Shipping Cost	141

The total shipping cost will be ₹141.

Additional Transportation Cost ₹37.

The carrier of C to II must reduce the cost by ₹4.63 (₹37/8) so that the total cost of transportation remains the same and clerk can give him business.

(iv) Revised transportation table is shown below-

Warehouse	Market				Supply
	I	II	III	IV	
A	5	2 [12]	4 [2]	3 [8]	22
B	4	8	1 [11]	6	15/11
C	4 [7]	6	7	5 [1]	8
Req.	7	12	17/13	9	45

Since the alterations are restricted to allocated cells only, the present alterations do not disturb the optimal allocation schedule.

(v) In this situation, alterations are not restricted to allocated cells since allocation in cell (A, III) is **2** units only while reduction in requirement of Market III as well as supply of Warehouse A is **3** units. Therefore, it is essential to make alterations in allocations, check solution for optimality test and iterate if required.

14. Row Operation-

	P	Q	R	S	T
P	-	3	12	18	0
Q	12	-	3	18	0
R	12	9	-	0	9
S	24	0	6	-	3
T	0	6	3	21	-

Column Operation-

	P	Q	R	S	T
P	-	3	9	18	0
Q	12	-	0	18	0
R	12	9	-	0	9
S	24	0	3	-	3
T	0	6	0	21	-

We know check if optimal assignment can be made in below table or not. Proceeding, we get following table-

	P	Q	R	S	T
P	-	3	9	18	0
Q	12	-	0	18	0
R	12	9	-	0	9
S	24	0	3	-	3
T	0	6	0	21	-

The above solution is optimum solution with two routes-

P to T to P and

Q to R to S to Q

Above table provides the optimum solution but do not satisfy travelling condition. To solve this problem we have to bring next minimum element in the matrix i.e.3. Now the possible *new assignments* are

P to Q instead of P to T,

S to R instead of S to Q and

S to T instead of S to Q.

Let us consider each of the new assignment independently.

Situation 1-

We make 'assignment' in cell (P, Q) instead of 'assignment' in cell (P, T). The resulting table is shown below-

	P	Q	R	S	T
P	-	[3]	9	18	0
Q	12	-	[0]	18	0
R	12	9	-	[0]	9
S	24	0	3	-	[3]
T	[0]	6	0	21	-

The feasible solution is P to Q to R to S to T to P and it involves a cost of ₹40,000 (₹5,000 + ₹8,000 + ₹11,000 + ₹14,000 + ₹2,000).

Situation 2-

We make 'assignment' in cell (S, R) instead of 'assignment' in cell (S, Q). The resulting table is shown below-

	P	Q	R	S	T
P	-	[3]	9	18	0
Q	12	-	0	18	[0]
R	12	9	-	[0]	9
S	24	0	[3]	-	3
T	[0]	6	0	21	-

The resulting solution is P to Q to T to P, R to S to R, which is not feasible as it does not satisfy the travelling condition.

Situation 3-

We make 'assignment' in cell (S, T) instead of 'assignment' in cell (S, Q). The resulting table is shown below-

	P	Q	R	S	T
P	-	3	9	18	0
Q	12	-	0	18	0
R	12	9	-	0	9
S	24	0	3	-	3
T	0	6	0	21	-

The resulting table is same as in Situation 1 which gives the feasible solution P to Q to R to S to T to P with cost of ₹40,000.

Hence least cost route is P to Q to R to S to T to P with cost of ₹40,000.

15. Random Numbers Allocation for *each activity*

Activity	Time (in Days)	Probability	Cumulative Probability	Allocated Random Number
A	6	0.50	0.50	00-49
	8	0.50	1.00	50-99
B	4	0.30	0.30	00-29
	5	0.20	0.50	30-49
	6	0.50	1.00	50-99
C	8	0.50	0.50	00-49
	16	0.50	1.00	50-99
D	8	0.30	0.30	00-29
	10	0.70	1.00	30-99
E	2	0.20	0.20	00-19
	4	0.80	1.00	20-99

Simulation Table

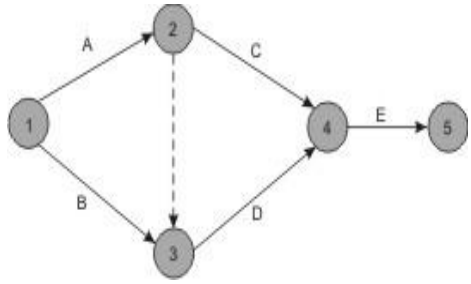
Trial	A		B		C		D		E	
	R. No.	Time	R. No.	Time	R. No.	Time	R. No.	Time	R. No.	Time
1	11	6	16	4	23	8	72	10	94	4
2	83	8	83	6	02	8	97	10	99	4
3	83	8	10	4	93	16	4	8	33	4
4	53	8	49	5	94	16	37	10	7	2

Determination of "Critical Path and Project Duration for *each trial*"

Trial	Project Duration			Critical Path
	1–2–4–5 (A–C–E)	1–2–3–4–5 (A–D–E)	1–3–4–5 (B–D–E)	
1	18 (6 + 8 + 4)	**20** (6 + 10 + 4)	18 (4 + 10 + 4)	1–2–3–4–5 (A–D–E)
2	20 (8 + 8 + 4)	**22** (8 + 10 + 4)	20 (6 + 10 + 4)	1–2–3–4–5 (A–D–E)
3	**28** (8 + 16 + 4)	20 (8 + 8 + 4)	16 (4 + 8 + 4)	1–2–4–5 (A–C–E)
4	**26** (8 + 16 + 2)	20 (8 + 10 + 2)	17 (5 + 10 + 2)	1–2–4–5 (A–C–E)

Working Note

The Network for the given problem:



16. (i) Total Direct Labour Cost for **first 64 batches** based on learning curve of 90% (when the direct labour cost for the first batch is ₹52,500)

The usual learning curve model is

$$y = ax^b$$

Where

y = Average Direct Labour Cost *per batch* for x batches

a = Direct Labour Cost for *first batch*

x = Cumulative No. of batches produced

b = Learning Coefficient /Index

$y = ₹52,500 \times (64)^{-0.152}$

= ₹52,500 × 0.5314

= ₹27,898.50

Total Direct Labour Cost for first 64 batches

= 64 batches × ₹27,898.50

= ₹17,85,504

Total Direct Labour Cost for **first 63 batches** based on learning curve of 90% (when the direct labour cost for the first batch is ₹52,500)

$y = ₹52,500 \times (63)^{-0.152}$

= ₹52,500 × 0.5327

= ₹27,966.75

Total Direct Labour Cost for first 63 batches

= 63 batches × ₹27,966.75

= ₹17,61,905

Direct Labour Cost for **64th batch** = ₹17,85,504 - ₹17,61,905

= ₹23,599

Total Labour Cost over the Product's Life

= ₹17,85,504 + (192 batches × ₹23,599)

= ₹63,16,512

Statement Showing "Life Time Expected Profit"

Particulars	Amount (₹)
Sales (₹123 × 2,56,000 units)	3,14,88,000
Less: Direct Material (₹36 × 2,56,000 units)	92,16,000
Less: Direct Labour	63,16,512
Less: Other Variable Cost (₹24 × 2,56,000 units)	61,44,000
Less: Specific Fixed Cost	38,75,000
Profit	59,36,488

(ii) In order to achieve a Profit of ₹1,00,00,000 the Total Direct Labour Cost over the Product's Lifetime would have to equal ₹22,53,000.

Statement Showing "Life Time Direct Labour Cost"

Particulars	Amount (₹)
Sales (₹123 × 2,56,000 units)	3,14,88,000

Less: Direct Material (₹36 × 2,56,000 units)	92,16,000
Less: Other Variable Cost (₹24 × 2,56,000 units)	61,44,000
Less: Specific Fixed Cost	38,75,000
Less: Profit	1,00,00,000
Direct Labour	22,53,000

Average Direct Labour Cost *per batch* for 256 batches is ₹8,800.78 (₹22,53,000 / 256 batches).

Total Direct Labour Cost for **256 batches** based on learning curve of r% (when the direct labour cost for the first batch is ₹52,500)

$$y = ₹52,500 \times (256)^{b}$$

$$₹8,800.78 = ₹52,500 \times (256)^{b}$$

$$0.1676 = (256)^{b}$$

$$\log 0.1676 = b \times \log 2^{8}$$

$$\log 0.1676 = b \times 8 \log 2$$

$$\log 0.1676 = \left(\frac{\log r}{\log 2}\right) \times 8 \log 2$$

$$\log 0.1676 = \log r^{8}$$

$$0.1676 = r^{8}$$

$$r = \sqrt[8]{0.1676}$$

$$r = 80\%$$

PAPER – 6: INFORMATION SYSTEMS CONTROL AND AUDIT

QUESTIONS

Concepts of Governance and Management of Information Systems

1. "The success of the process of ensuring business value from the use of IT can be measured by evaluating the benefits realized from IT enabled investments and services portfolio and how transparency of IT costs, benefits and risks is implemented." Explain some of the key metrics which can be used for such evaluation.
2. Discuss the seven enablers of COBIT 5.
3. Write short note on Internal Controls as per Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Information System Concepts

4. What is Executive Information System (EIS)? Explain the major characteristics of an EIS.
5. "Decision Support Systems are widely used as part of an Organization's Accounting Information system". Give examples to support this statement.
6. Discuss some major characteristics of Computer based Information Systems in brief.

Protection of Information Systems

7. Discuss in detail the following:
   (a) "Data Resource Management Controls" under Managerial Controls.
   (b) "Systems Development Management Controls" under Managerial Controls.
8. Discuss Logical Access Controls across the system in brief.
9. Discuss the arrangements a company XYZ should emphasize in order to tighten its Physical Security for protecting its IT assets.

Business Continuity Planning and Disaster Recovery Planning

10. Discuss broadly the administrative procedures that need to be considered during any BCP Audit.
11. A company has decided to outsource its recovery process to a third party site. What are the issues that should be considered by the security administrators while drafting the contract?
12. Discuss the major areas that form a part of Disaster Recovery Planning (DRP) Document.

Acquisition, Development and Implementation of Information Systems

13. What are the characteristics of a good coded application and program?
14. (a) Mention different functions of steering Committee under SDLC.

(b) "Maintaining the system is an important aspect of SDLC". Considering this statement; list out various categories of System Maintenance in SDLC.

15. Discuss various areas that should be considered while designing systems input.

Auditing of Information Systems

16. What do you understand by Control Risk? Mention different types of information which auditors may collect using System Control Audit Review File (SCARF)?

17. Discuss the Accounting and Operations Audit Trails with respect to Communication Controls.

Information Technology Regulatory Issues

18. Discuss the provision given in IT (Amendment) Act 2008, that gives power to issue directions for blocking for public access of any information through any computer resource?

19. Discuss Information Technology Infrastructure Library (ITIL) Service Lifecycle.

Emerging Technologies

20. Discuss the similarities and differences between Cloud Computing and Grid Computing.

Short Note Based Questions

21. Write short notes on following:
    (a) Phishing, Hacking and Cracking
    (b) Auditor's Selection Norms
    (c) Mobile Computing and Buy Your Own Devices (BYOD)
    (d) General Controls
    (e) Data Flow Diagram (DFD)

22. Differentiate between the following:
    (a) Cold Site and Hot Site
    (b) Phased Changeover and Pilot Changeover
    (c) Structured English and Flowchart
    (d) Inherent Risk and Detection Risk
    (e) Emergency Plan and Recovery Plan

Questions based on the Case Studies

23. A manufacturing company ABC having information flow within departments, operating with in-house developed software till now. Its profit margins are very low due to inefficiency and disorganized work culture. To survive in the competitive market, it has to

improve the efficiency of its internal processes and synchronize onto streamlined business processes so that work culture is improved. Hence it has decided by the top management to purchase and implement real time software. In order to improve its margin, it is decided to transact with suppliers and customer electronically and maintain all records in electronic form. They furnish all books of accounts and report to the controller. Security of information is a key activity of this process which must be taken care of from the beginning. As a member of implementation team, you are required to answer the following:

(a) Explain the major points for evaluation of effectives Management Information System (MIS).

(b) Explain the advantages of Business Continuity Management (BCM).

(c) Explain the penalty for failure to furnish information return under Section 44 of IT Act, 2000.

(d) Explain the various user related issues in achieving the system development objectives.

24. XYZ Technical University, a newly formed university, decided to launch a web based knowledge portal to facilitate their students of distance education for different courses. It proposed to upload the course materials, e - lectures and e-reference books. It is expected to provide various resources easily on anytime and anywhere basis. Therefore, an initial study or investigation under all dimensions was done. As a part of this, the management of the university invited various technical experts for a capable and good solution as per the requirements and guidelines of the university. Also the University decided to encourage people to collaborate and share information online through social networks.

(a) According to you as an IS Auditor, what are the validation methods for approving the vendors' proposals?

(b) If you consider Web 2.0 as an ideal platform for implementing and helping social networks to grow, what are the major components of Web 2.0?

(c) The university will facilitate the communication system to interact with their students effectively and economically by using Electronic Mail systems. What are the features of the Electronic Mail System?

(d) What are the important backup options that should be considered by security administrators?

25. ASK International proposes to launch a new subsidiary to provide e-consultancy services for organizations throughout the world, to assist them in system development, strategic planning and e-governance areas. The fundamental guidelines, programmes modules and draft agreements are all preserved and administered in the e-form only.

The company intends to utilize the services of a professional analyst to conduct a preliminary investigation and present a report on smooth implementation of the ideas of

the new subsidiary. Based on the report submitted by the analyst, the company decides to proceed further with three specific objectives (i) reduce operational risk, (ii) increase business efficiency and (iii) ensure that information security is being rationally applied.

(a) What are the two primary methods through which the analyst would have collected the data?

(b) To retain their electronic records for specified period, what are the conditions laid down by Section 7, Chapter III of Information Technology Act, 2000?

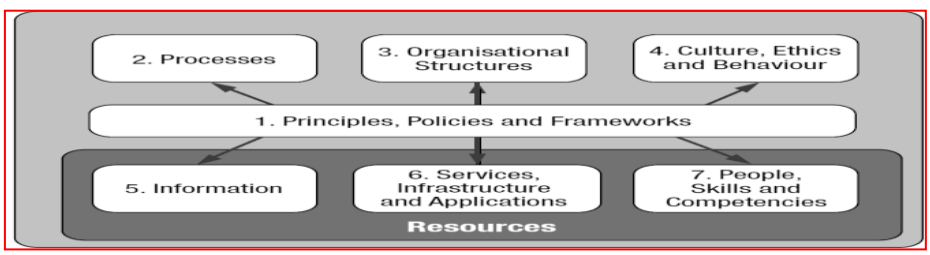
SUGGESTED ANSWERS/HINTS

1. "The success of the process of ensuring business value from the use of IT can be measured by evaluating the benefits realized from IT enabled investments and services portfolio and how transparency of IT costs, benefits and risks is implemented." Some of the key metrics, which can be used for such evaluation, are as follows:

- Percentage of IT enabled investments where benefit realization monitored through full economic life cycle;
- Percentage of IT services where expected benefits realized;
- Percentage of IT enabled investments where claimed benefits met or exceeded;
- Percentage of investment business cases with clearly defined and approved expected IT related costs and benefits;
- Percentage of IT services with clearly defined and approved operational costs and expected benefits; and
- Satisfaction survey of key stakeholders regarding the transparency, understanding and accuracy of IT financial information.

2. **Enablers of COBIT 5:** Enablers are factors that individually and collectively, influence whether something will work; in case of COBIT 5, Governance and Management over enterprise IT. The COBIT 5 framework describes seven categories of enablers, which are shown in Figure and discussed as below:

(i) **Principles, Policies and Frameworks** are the vehicle to translate the desired behaviour into practical guidance for day-to-day management.



Seven Enablers of COBIT 5

(ii) **Processes** describe an organized set of practices and activities to achieve certain objectives and produce a set of outputs in support of achieving overall IT-related goals.

(iii) **Organizational structures** are the key decision-making entities in an enterprise.

(iv) **Culture, Ethics and Behaviour** of individuals and of the enterprise are very often underestimated as a success factor in governance and management activities.

(v) **Information** is pervasive throughout any organization and includes all information produced and used by the enterprise. Information is required for keeping the organization running and well governed, but at the operational level, information is very often the key product of the enterprise itself.

(vi) **Services, Infrastructure and Applications** include the infrastructure, technology and applications that provide the enterprise with information technology processing and services.

(vii) **People, Skills and Competencies** are linked to people and are required for successful completion of all activities and for making correct decisions and taking corrective actions.

3. As per Committee of Sponsoring Organizations of the Treadway Commission (COSO), Internal Control is comprised of five interrelated components:

- **Control Environment:** For each business process, an organization needs to develop and maintain a control environment including categorizing the criticality and materiality of each business process, plus the owners of the business process.
- **Risk Assessment:** Each business process comes with various risks. A control environment must include an assessment of the risks associated with each business process.
- **Control Activities:** Control activities must be developed to manage, mitigate, and reduce the risks associated with each business process. It is unrealistic to expect to eliminate risks completely.
- **Information and Communication:** Associated with control activities are information and communication systems. These enable an organization to capture and exchange the information needed to conduct, manage, and control its business processes.
- **Monitoring:** The internal control process must be continuously monitored with modifications made as warranted by changing conditions.

4. **Executive Information Systems (EIS) –** It is sometimes referred to as an Executive Support System (ESS). It serves the strategic level i.e. top level managers of the organization. ESS creates a generalized computing and communications environment rather than providing any preset applications or specific competence.

Characteristics of EIS – Major Characteristics of an EIS are given as follows:

- EIS is a Computer-based-information system that serves the information need of top executives.
- EIS enables users to extract summary data and model complex, problems without the need to learn query languages statistical formulas or high computing skills.
- EIS provides rapid access to timely information and direct access to management reports.
- EIS is capable of accessing both internal and external data.
- EIS provides extensive online analysis tool like trend analysis, market conditions etc.
- EIS can easily be given as a DSS support for decision making.

5. Decision Support Systems are widely used as a part of an organization's Accounting Information System. The complexity and nature of decision support systems vary. Many are developed in-house using either a general type of decision support program or a spreadsheet program to solve specific problems. Below are several illustrations:

- **Cost Accounting System:** The health care industry is well known for its cost complexity. Managing costs in this industry requires controlling costs of supplies, expensive machinery, technology, and a variety of personnel. Cost accounting applications help health care organizations calculate product costs for individual procedures or services. Decision support systems can accumulate these product costs to calculate total costs per patient. Health care managers may combine cost accounting decision support systems with other applications, such as productivity systems. Combining these applications allows managers to measure the effectiveness of specific operating processes
- **Capital Budgeting System:** Companies require new tools to evaluate high-technology investment decisions. Decision makers need to supplement analytical techniques, such as net present value and internal rate of return, with decision support tools that consider some benefits of new technology not captured in strict financial analysis. Example- Auto Man is a DSS designed to support decisions about investments in automated manufacturing technology that allows decision makers to consider financial, nonfinancial, quantitative, and qualitative factors in their decision-making processes.
- **Budget Variance Analysis System:** Financial institutions rely heavily on their budgeting systems for controlling costs and evaluating managerial performance. One institution uses a computerized decision support system to generate monthly variance reports for division comptrollers. The system allows these comptrollers to graph, view, analyze, and annotate budget variances, as well as create additional one-and five-year budget projections using the forecasting tools provided in the

system. The decision support system thus helps the comptrollers create and control budgets for the cost-center managers reporting to them.

- **General Decision Support System:** Some planning languages used in decision support systems are general purpose and therefore have the ability to analyze many different types of problems. In a sense, these types of decision support systems are a decision-maker's tools. The user needs to input data and answer questions about a specific problem domain to make use of this type of decision support system. An example is a program called Expert Choice that supports a variety of problems requiring decisions. The user works interactively with the computer to develop a hierarchical model of the decision problem. The decision support system then asks the user to compare decision variables with each other. For instance, the system might ask the user how important cash inflows are versus initial investment amount to a capital budgeting decision. The decision maker also makes judgments about which investment is best with respect to these cash flows and which requires the smallest initial investment. Expert Choice analyzes these judgments and presents the decision maker with the best alternative.

6. Major characteristics of Computer based Information Systems (CBIS) are as follows:

- All systems work for predetermined objectives and the system is designed and developed accordingly.
- In general, a system has a number of interrelated and interdependent subsystems or components. No subsystem can function in isolation; it depends on other subsystems for its inputs.
- If one subsystem or component of a system fails; in most of the cases, the whole system does not work. However, it depends on 'how the subsystems are interrelated'.
- The way a subsystem works with another subsystem is called interaction. The different subsystems interact with each other to achieve the goal of the system.
- The work done by individual subsystems is integrated to achieve the central goal of the system. The goal of individual subsystem is of lower priority than the goal of the entire system.

7. (a) **Data Resource Management Controls:** Data is a critical resource that must be managed properly and therefore, accordingly, centralized planning and control are implemented. For data to be managed better; users must be able to share data that must be available to users when it is needed, in the location where it is needed, and in the form in which it is needed. Further it must be possible to modify data fairly easily and the integrity of the data be preserved. If data repository system is used properly, it can enhance data and application system reliability. It must be controlled carefully, however, because the consequences are serious if the data definition is compromised or destroyed. Careful control should be exercised over the roles by appointing senior, trustworthy persons, separating duties to the extent possible and

maintaining and monitoring logs of the data administrator's and database administrator's activities.

These Controls fall in two categories:

- **Access Controls:** These are designed to prevent unauthorized individual from viewing, retrieving, computing or destroying the entity's data. User Access Controls are established through passwords, tokens and biometric Controls; and through Data Encryption that keeps the data in database in encrypted form.
- **Back-up Controls:** These ensure the availability of system in the event of data loss due to unauthorized access, equipment failure or physical disaster; the organization can retrieve its files and databases. Backup refers to making copies of the data so that these additional copies may be used to restore the original data after a data loss. Various backup strategies are given as follows:
    - **Dual recording of data:** Under this strategy, two complete copies of the database are maintained and are concurrently updated.
    - **Periodic dumping of data:** This strategy involves taking a periodic dump of all or part of the database onto some backup storage medium – magnetic tape, removable disk, Optical disk. The dump may be scheduled.
    - **Logging input transactions:** This involves logging the input data transactions which cause changes to the database. Normally, this works in conjunction with a periodic dump.
    - **Logging changes to the data:** This involves copying a record each time it is changed by an update action. The changed record can be logged immediately before the update action changes the record, immediately after, or both.

(b) Systems Development Management Controls: System Development controls are targeted to ensure that proper documentations and authorizations are available for each phase of the system development process. It includes controls at controlling new system development activities which are as follows:

- **System Authorization Activities:** All systems must be properly authorized to ensure their economic justification and feasibility. As with any transaction, system's authorization should be formal.
- **User Specification Activities:** The user can create a detailed written description of the logical needs that must be satisfied by the system. The creation of a user specification document often involves the joint efforts of the user and systems professionals.
- **Technical Design Activities:** The technical design activities in the System Development Life Cycle (SDLC) translate the user specifications into a set of

detailed technical specifications of a system that meets the user's needs. The scope of these activities includes systems analysis, general systems design, feasibility analysis, and detailed systems design.

- **Internal Auditor's Participation:** The auditor should become involved at the inception of the SDLC process to make conceptual suggestions regarding system requirements and controls. Auditor's involvement should be continued throughout all phases of the development process and into the maintenance phase.
- **Program Testing:** All program modules must be thoroughly tested before they are implemented. The results of the tests are then compared against predetermined results to identify programming and logic errors.
- **User Test and Acceptance Procedures:** Just before implementation, the individual modules of the system must be tested as a unified whole. A test team comprising user personnel, systems professionals, and internal audit personnel subjects the system to rigorous testing. Once the test team is satisfied that the system meets its stated requirements, the system is formally accepted by the user department(s).

To conclude, we can say that the Systems Development Management has responsibility for the functions concerned with analyzing, designing, building, implementing, and maintaining information systems. Three different types of audits that may be conducted during system development process are discussed below.

- **Concurrent Audit:** Auditors are members of the system development team and assist the team in improving the quality of systems development for the specific system.
- **Post-Implementation Audit:** Auditors seek to help an organization learn from its experiences in the development of a specific application system. In addition, they might be evaluating whether the system needs to be scrapped, continued, or modified in some way.
- **General Audit:** Auditors evaluate systems development controls overall. They seek to determine whether they can reduce the extent of substantive testing needed to form an audit opinion about management's assertions relating to the financial statements or systems effectiveness and efficiency.

Note: *Referring to the relevant January 2015 edition; students are advised to read the "**Section 3.9.6 Data Management Controls**" subsequent to the "**Section 3.7.4 Data Resource Management Controls**" under the topic "**Data Resource Management Controls**" and "**Section 3.9.7 System Development Controls**" subsequent to "**Section 3.7.2 System Development Management Controls**" under the topic "**System Development Management Controls**". Both the controls are to be considered as a part of "**Section 3.7 Managerial Controls and their Categories**".*

8. **Logical Access Controls:** Logical Access Controls serve as one of the means of information security. The purpose of Logical Access Controls is to restrict access to information assets/resources. They are expected to provide access to information resources on a need to know and need to do basis using principle of least privileges. It means that the access should not be so restrictive that it makes the performance of business functions difficult or it should not be so liberal that it can be misused i.e. it should be just sufficient for one to perform one's duty without any problem or restraint. The data, an information asset, can be:

   - Used by an application (Data at Process);
   - Stored in some medium (Back up) (Data at Rest); or
   - It may be in transit (being transferred from one location to another).

   Logical access controls is all about protection of these assets wherever they reside. The details are given below:

   (i) User Access Management

   - **User registration:** Information about every user is documented. For example: Why is the user granted the access?; Has the data owner approved the access? etc.
   - **Privilege management:** Access privileges are to be aligned with job requirements and responsibilities. For example, an operator at the order counter shall have direct access to order processing activity of the application system.
   - **User password management:** Passwords are usually the default screening point for access to systems. Allocations, storage, revocation, and reissue of password are password management functions.
   - **Review of user access rights:** A user's need for accessing information changes with time and requires a periodic review of access rights to check anomalies in the user's current job profile, and the privileges granted earlier.

   (ii) User Responsibilities: User awareness and responsibility is also an important factor:

   - **Password use:** Mandatory use of strong passwords to maintain confidentiality.
   - **Unattended user equipment:** Users should ensure that none of the equipment under their responsibility is ever left unprotected. They should also secure their PCs with a password, and should not leave it accessible to others.

   (iii) Network Access Control: An Internet connection exposes an organization to the entire world. This brings up the issue of benefits the organization should derive along with the precaution against harmful elements. This can be achieved through the following means:

- **Policy on use of network services:** Selection of appropriate services and approval to access them aligned with the business need for using the Internet services is the first step.
- **Enforced path:** Based on risk assessment, it is necessary to specify the exact path or route connecting the networks; e.g., internet access by employees will be routed through a firewall and proxy.
- **Segregation of networks:** Based on the sensitive information handling function; say a VPN connection between a branch office and the head-office, this network is to be isolated from the internet usage service
- **Network connection and routing control:** The traffic between networks should be restricted, based on identification of source and authentication access policies implemented across the enterprise network facility.
- **Security of network services:** The techniques of authentication and authorization policy should be implemented across the organization's network.

(iv) Operating System Access Control: Operating System provides the platform for an application to use various Information System resources and perform the specific business function. If an intruder is able to bypass the network perimeter security controls, the operating system is the last barrier to be conquered for unlimited access to all the resources. Hence, protecting operating system access is extremely crucial.

Automated terminal identification; Terminal log-on procedures, User identification and authentication; Password management system; Use of system utilities; Duress alarm to safeguard users; Terminal time out and limitation of connection time are some of vital steps to control unlimited access.

(v) Application and Monitoring System Access Control:

- **Information access restriction:** The access to information is prevented by application specific menu interfaces, which limit access to system function. A user is allowed to access only to those items, s/he is authorized to access.
- **Sensitive system isolation:** Based on the critical constitution of a system in an enterprise, it may even be necessary to run the system in an isolated environment.
- **Event logging:** In Computer systems, it is easy and viable to maintain extensive logs for all types of events. It is necessary to review if logging is enabled and the logs are archived properly.
- **Monitor system use:** Based on the risk assessment, a constant monitoring of some critical systems is essential. This defines the details of types of accesses, operations, events and alerts that will be monitored.

- **Clock synchronization:** Event logs maintained across an enterprise network plays a significant role in correlating an event and generating report on it. Hence, the need for synchronizing clock time across the network as per a standard time is mandatory.

(vi) Mobile Computing: In today's organizations, computing facility is not restricted to a particular data centre alone. Ease of access on the move provides efficiency and results in additional responsibility on the management to maintain information security. Theft of data carried on the disk drives of portable computers is a high risk factor. Both physical and logical access to these systems is critical. Information is to be encrypted and access identifications like fingerprint, eye-iris, and smart cards are necessary security features.

9. Physical Security: The security required for computer system can be categorized as security from Accidental Breach and Incidental Breach.

- Accidental breach of security due to such natural calamities as fire, flood and earthquake etc. may cause total destruction of important data and information.
- Incidental or fraudulent modification or tampering of financial records maintained by the organization can cause considerable amount of money to be disbursed to fraudulent personnel. Similarly, unauthorized access to secret records of the organization can cause leakage of vital information. Hence, there is a great need for physical security of the computer system. Physical security includes arrangements that are discussed below:
- **Fire Damage:** It is a major threat to the physical security of a computer installation. Some of the major features of a well-designed fire protection system are given below:
  - Both automatic and manual fire alarms are placed at strategic locations;
  - A control panel may be installed which shows where in the location an automatic or manual alarm has been triggered;
  - Besides the control panel, master switches may be installed for power and automatic fire suppression system;
  - Manual fire extinguishers can be placed at strategic locations;
  - Fire exits should be clearly marked. When a fire alarm is activated, a signal may be sent automatically to permanently manned station;
  - All staff members should know how to use the systems Like - Fire Alarms, Extinguishers, Sprinklers, Instructions / Fire Brigade Nos., Smoke detectors, and Carbon dioxide based fire extinguishers; and
  - Less Wood and plastic should be in computer rooms.

- **Water Damage:** Some of the major ways of protecting the installation against water damage are as follows:
  - Wherever possible have waterproof ceilings, walls and floors;
  - Ensure an adequate positive drainage system exists;
  - Install alarms at strategic points within the installation;
  - In flood areas have the installation above the upper floors but not at the top floor;
  - Use a gas based fire suppression system;
  - Water proofing; and
  - Water leakage Alarms.
- **Power Supply Variation:** Voltage regulators and circuit breakers protect the hardware from temporary increase or decrease of power. UPS Battery back-up can be provided in case a temporary loss of power occurs. A generator is needed for sustained losses in power for extended period.
- **Pollution Damage:** The major pollutant in a computer installation is dust. Due consideration should be given for dust free environment in the computer room. Regular cleaning of walls, floors and equipment etc. is essential.
- **Unauthorized Intrusion:** Physical entry may be restricted to the computer room by various means so that unauthorized intrusion does not take place. A badge system may be used to identify the status of personnel inside the computer room. Various devices are available to detect the presence of bugs by the intruder, that are physically or electronically logging; Guard, dogs; Entry in computer area restricted; Log books; Alarms; Preventing wire tapping; Physical Intrusion detectors; and Security of Documents, data & storage media.

10. The Administrative Procedures that need to be considered during any Business Continuity Planning (BCP) Audit are as follows:

- Does the disaster recovery/ business resumption plan cover administrative and management aspects in addition to operations? Is there a management plan to maintain operations if the building is severely damaged or if access to the building is denied or limited for an extended period of time?
- Is there a designated emergency operations center where incident management teams can coordinate response and recovery?
- Determine if the disaster recovery/ business resumption plan covers procedures for disaster declaration, general shutdown and migration of operations to the backup facility.
- Have essential records been identified? Do we have a duplicate set of essential records stored in a secure location?

- To facilitate retrieval, are essential records separated from those that will not be needed immediately?

11. If a third-party site is to be used for recovery purposes, security administrators must ensure that a contract is written to cover the following issues:

- How soon the site will be made available subsequent to a disaster;
- The number of organizations that will be allowed to use the site concurrently in the event of a disaster;
- The priority to be given to concurrent users of the site in the event of a common disaster;
- The period during which the site can be used;
- The conditions under which the site can be used;
- The facilities and services the site provider agrees to make available;
- Procedures to ensure security of company's data from being accessed/damaged by other users of the facility; and
- What controls will be in place for working at the off-site facility.

12. The Disaster Recovery Planning (DRP) document may include the following major areas:

- The conditions for activating the plans, which describe the process to be followed before each plan, are activated.
- Emergency procedures, which describe the actions to be taken following an incident which jeopardizes business operations and/or human life. This should include arrangements for public relations management and for effective liaisoning with appropriate public authorities e.g. police, fire, services and local government.
- Fallback procedures, which describe the actions to be taken to move essential business activities or support services to alternate temporary locations, to bring business process back into operation in the required time-scale.
- Resumption procedures, which describe the actions to be taken to return to normal business operations.
- A maintenance schedule, which specifies 'how and when the plan will be tested', and the process for maintaining the plan.
- Awareness and education activities, which are designed to create an understanding of the business continuity, process and ensure that the business continues to be effective.
- The responsibilities of individuals describing who is responsible for executing which component of the plan. Alternatives should be nominated as required.
- Contingency plan document distribution list.

- Detailed description of the purpose and scope of the plan.
- Contingency plan testing and recovery procedure.
- List of vendors doing business with the organization, their contact numbers and address for emergency purposes.
- Checklist for inventory taking and updating the contingency plan on a regular basis.
- List of phone numbers of employees in the event of an emergency.
- Emergency phone list for fire, police, hardware, software, suppliers, customers, back-up location, etc.
- Medical procedure to be followed in case of injury.
- Back-up location contractual agreement, correspondences.
- Insurance papers and claim forms.
- Primary computer centre hardware, software, peripheral equipment and software configuration.
- Location of data and program files, data dictionary, documentation manuals, source and object codes and back-up media.
- Alternate manual procedures to be followed such as preparation of invoices.
- Names of employees trained for emergency situation, first aid and life saving techniques.
- Details of airlines, hotels and transport arrangements.

13. A good coded application and program should have the following characteristics:

- **Reliability:** It refers to the consistency with which a program operates over a period of time. However, poor setting of parameters and hard coding of some data subsequently could result in the failure of a program after some time.
- **Robustness:** It refers to the applications' strength to uphold its operations in adverse situations by taking into account all possible inputs and outputs of a program in case of least likely situations.
- **Accuracy:** It refers not only to 'what program is supposed to do', but should also take care of 'what it should not do'. The second part becomes more challenging for quality control personnel and auditors.
- **Efficiency:** It refers to the performance per unit cost with respect to relevant parameters and it should not be unduly affected with the increase in input values.
- **Usability:** It refers to a user-friendly interface and easy-to-understand internal/ external documentation.

- **Readability:** It refers to the ease of maintenance of program even in the absence of the program developer.

14. (a) Some of the functions of Steering Committee are given as follows:

- To provide overall directions and ensures appropriate representation of affected parties;
- To be responsible for all cost and timetables;
- To conduct a regular review of progress of the project in the meetings of steering committee, which may involve co-ordination and advisory functions; and
- To undertake corrective actions like rescheduling, re-staffing, change in the project objectives and need for redesigning.

(b) "Maintaining the system is an important aspect of SDLC". To achieve this objective, System Maintenance can be categorized in the following ways:

- **Scheduled Maintenance:** Scheduled maintenance is anticipated and can be planned for operational continuity and avoidance of anticipated risks. For example, the implementation of a new inventory coding scheme can be planned in advance, security checks may be promulgated etc.
- **Rescue Maintenance:** Rescue maintenance refers to previously undetected malfunctions that were not anticipated but require immediate troubleshooting solution. A system that is properly developed and tested should have few occasions of rescue maintenance.
- **Corrective Maintenance:** Corrective maintenance deals with fixing bugs in the code or defects found during the executions. A defect can result from design errors, logic errors coding errors, data processing and system performance errors. The need for corrective maintenance is usually initiated by bug reports drawn up by the end users. Examples of corrective maintenance include correcting a failure to test for all possible conditions or a failure to process the last record in a file.
- **Adaptive Maintenance:** Adaptive maintenance consists of adapting software to changes in the environment, such as the hardware or the operating system. The term environment refers to the totality of all conditions and influences, which act from outside upon the system, for example, business rule, government policies, work patterns, software and hardware operating platforms.
- **Perfective Maintenance:** Perfective maintenance mainly deals with accommodating to the new or changed user requirements and concerns functional enhancements to the system and activities to increase the system's performance or to enhance its user interface.

- **Preventive Maintenance:** Preventive maintenance concerns with the activities aimed at increasing the system's maintainability, such as updating documentation, adding comments, and improving the modular structure of the system.

15. Input design consists of developing specifications and procedures for data preparation, developing steps which are necessary to put transactions data into a usable form for processing, and data-entry, i.e., the activity of putting the data into the computer for processing. Major areas that should be considered while designing systems input are as follows:

(i) **Content:** The analyst is required to consider the types of data that are needed to be gathered to generate the desired user outputs. Sometimes, the data needed for a new system are not available within the organization. Hence, the system designer has to prepare new documents for collecting such information.

(ii) **Timeliness:** In data processing, it is very important that data is inputted to computer in time because outputs cannot be produced until certain inputs are available. Hence, a plan must be established regarding when different types of inputs will enter the system.

(iii) **Media:** Various user input alternatives are available in the market such as workstations, magnetic disc, OCR, pen-based computers and voice input etc. A suitable medium may be selected depending on the application to be computerized.

(iv) **Format:** After the data contents and media requirements are determined, input formats are considered. While specifying the record formats, for instance, the type and length of each data field as well as any other special characteristics must be defined. Designing input formats often requires the assistance of a professional programmer or database administrator.

(v) **Input Volume:** Input volume refers to the amount of data that has to be entered in the computer system at any one time. For example, in some decision-support systems and many real-time transaction processing systems, input volume is light which involves data entry department using key-to-tape or key-to-disk systems.

16. **Control Risk:** Control Risk is the risk that could occur in an audit area, and which could be material, individually or in combination with other errors, will not be prevented or detected and corrected on a timely basis by the internal control system. Control Risk is a measure of the auditor's assessment of the likelihood that risk exceeding a tolerable level and will not be prevented or detected by the client's internal control system. This assessment includes an assessment of whether a client's internal controls are effective for preventing or detecting gaps and the auditor's intention to make that assessment at a level below the maximum (100 percent) as a part of the audit plan.

System Control Audit Review File (SCARF): The SCARF technique involves embedding audit software modules within a host application system to provide continuous monitoring of the system's transactions. The information collected is written onto a special audit file- the

SCARF master files. Auditors then examine the information contained on this file to see if some aspect of the application system needs follow-up. Auditors might use SCARF to collect the following types of information:

- **Application System Errors** - SCARF audit routines provide an independent check on the quality of system processing, whether there are any design and programming errors as well as errors that could creep into the system when it is modified and maintained.
- **Policy and Procedural Variances** - Organizations have to adhere to the policies, procedures and standards of the organization and the industry to which they belong. SCARF audit routines can be used to check when variations from these policies, procedures and standards have occurred.
- **System Exception** - SCARF can be used to monitor different types of application system exceptions. For example, salespersons might be given some leeway in the prices they charge to customers. SCARF can be used to see how frequently salespersons override the standard price.
- **Statistical Sample** - Some embedded audit routines might be statistical sampling routines, SCARF provides a convenient way of collecting all the sample information together on one file and use analytical review tools thereon.
- **Snapshots and Extended Records** - Snapshots and extended records can be written into the SCARF file and printed when required.
- **Profiling Data** - Auditors can use embedded audit routines to collect data to build profiles of system users. Deviations from these profiles indicate that there may be some errors or irregularities.
- **Performance Measurement** - Auditors can use embedded routines to collect data that is useful for measuring or improving the performance of an application system.

17. **Communication Controls:** Communication Controls maintain a chronology of the events from the time a sender dispatches a message to the time a receiver obtains the message.

Accounting Audit Trail

- Unique identifier of the source/sink node;
- Unique identifier of each node in the network that traverses the message; Unique identifier of the person or process authorizing dispatch of the message; Time and date at which the message was dispatched;
- Time and date at which the message was received by the sink node;
- Time and date at which node in the network was traversed by the message; and
- Message sequence number; and the image of the message received at each node traversed in the network.

Operations Audit Trail

- Number of messages that have traversed each link and each node;
- Queue lengths at each node; Number of errors occurring on each link or at each node; Number of retransmissions that have occurred across each link; Log of errors to identify locations and patterns of errors;
- Log of system restarts; and
- Message transit times between nodes and at nodes.

18. Section 69A is the provision in IT (Amendment) Act 2008 that gives power to issue directions for blocking for public access of any information through any computer resource and is discussed below:

***[Section 69A]* Power to issue directions for blocking for public access of any information through any computer resource**

(1) Where the Central Government or any of its officers specially authorized by it in this behalf is satisfied that it is necessary or expedient so to do, in the interest of sovereignty and integrity of India, defence of India, security of the State, friendly relations with foreign states or public order or for preventing incitement to the commission of any cognizable offence relating to above, it may subject to the provisions of sub-section (2), for reasons to be recorded in writing, by order, direct any agency of the Government or intermediary to block access by the public or cause to be blocked for access by public any information generated, transmitted, received, stored or hosted in any computer resource.

(2) The procedure and safeguards subject to which such blocking for access by the public may be carried out, shall be such as may be prescribed.

(3) The intermediary who fails to comply with the direction issued under sub-section (1) shall be punished with an imprisonment for a term which may extend to seven years and shall also be liable to fine.

19. Information Technology Infrastructure Library (ITIL) Service Lifecycle involves the following:

- **IT Service Generation:** IT Service Management (ITSM) refers to the implementation and management of quality information technology services and is performed by IT service providers through People, Process and Information Technology.
- **Service Portfolio Management:** IT portfolio management is the application of systematic management to the investments, projects and activities of enterprise Information Technology (IT) departments.

- **Financial Management:** Financial Management for IT Services' aim is to give accurate and cost effective stewardship of IT assets and resources used in providing IT Services.
- **Demand Management:** Demand management is a planning methodology used to manage and forecast the demand of products and services.
- **Business Relationship Management:** Business Relationship Management is a formal approach to understanding, defining, and supporting a broad spectrum of inter-business activities related to providing and consuming knowledge and services via networks.

20. Some pertinent similarities between Grid Computing and Cloud Computing are as follows:

- Cloud Computing and Grid Computing both are scalable. Scalability is accomplished through load balancing of application instances running separately on a variety of operating systems and connected through Web services. CPU and network bandwidth is allocated and de-allocated on demand. The system's storage capacity goes up and down depending on the number of users, instances, and the amount of data transferred at a given time.
- Both computing types involve multi-tenancy and multitasking, meaning that many customers can perform different tasks, accessing a single or multiple application instances. Sharing resources among a large pool of users assists in reducing infrastructure costs and peak load capacity. Cloud and grid computing provide Service-Level Agreements (SLAs) for guaranteed uptime availability of, say, 99 percent. If the service slides below the level of the guaranteed uptime service, the consumer will get service credit for receiving data not in stipulated time.

Some pertinent differences between Grid Computing and Cloud Computing are as follows:

- While the storage computing in the grid is well suited for data-intensive storage, it is not economically suited for storing objects as small as 1 byte. In a data grid, the amounts of distributed data must be large for maximum benefit. While in cloud computing, we can store an object as low as 1 byte and as large as 5 GB or even several terabytes.
- A computational grid focuses on computationally intensive operations, while cloud computing offers two types of instances: standard and high-CPU.

21. (a) Phishing: It is the act of attempting to acquire information such as usernames, passwords, and credit card details (and sometimes, indirectly, money) by masquerading as a trustworthy entity in an electronic communication. Communications purporting to be from popular social web sites, auction sites, online payment processors or IT administrators are commonly used to lure the unsuspecting public.

Hacking: It refers to unauthorized access and use of computer systems, usually by means of personal computer and a telecommunication network. Normally, hackers do not intend to cause any damage.

Cracking: Crackers are hackers with malicious intentions, which means, un-authorized entry. Now across the world hacking is a general term, with two nomenclatures namely: Ethical and Un-ethical hacking. Un-ethical hacking is classified as Cracking.

(b) Auditor's Selection Norms: There are various norms for selection of Auditors, which are given as follows:

- Auditor must have minimum 3 years of experience in IT audit of Securities Industry participants e.g. stock exchanges, clearing houses, depositories etc. The audit experience should have covered all the Major Areas mentioned under SEBI's Audit Terms of Reference (TOR).
- The Auditor must have experience in/direct access to experienced resources in the areas covered under TOR. It is recommended that resources employed shall have relevant industry recognized certifications e.g. CISA (Certified Information Systems Auditor) from ISACA, CISM (Certified Information Securities Manager) from ISACA, GSNA (GIAC Systems and Network Auditor), CISSP (Certified Information Systems Security Professional) from International Information Systems Security Certification Consortium, commonly known as $(ISC)^2$.
- The Auditor should have IT audit/governance frameworks and processes conforming to industry leading practices like CoBIT.
- The Auditor must not have any conflict of interest in conducting fair, objective and independent audit of the Exchange/Depository. It should not have been engaged over the last three years in any consulting engagement with any departments/units of the entity being audited.
- The Auditor may not have any cases pending against its previous auditees, which fall under SEBI's jurisdiction, which point to its incompetence and/or unsuitability to perform the audit task.

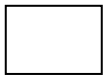
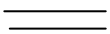
(c) Mobile Computing and Buy Your Own Devices (BYOD): Mobile computing, including BYOD is the single most radical shift in business since the PC revolution of the 1980s. Over the next decade, it will have a huge impact on how people work and live, how companies operate, and on the IT infrastructure. These services will focus on the issues and opportunities surrounding the new way to communicate and consume computing services. Mobile computing is not just PCs on the move. Mobile devices such as smart phones, tablets, and the iPod Touch, the last PDA standing are a radically different kind of devices, designed from the ground up as end points of data networks both internal corporate networks and the Internet rather than

primarily as stand-alone devices. They are optimized for mobility, which means that they have to be light, easy to handle, and maximize battery life. Where laptops has a three hour battery life, the tablet and smartphone regularly run 12 hours or more between charging and serve as windows into the Cloud.

(d) General Controls: General Controls are those that control the design, security, and use of computer programs and the security of data files in general throughout an organization. On the whole, General Controls apply to all computerized applications and consist of a combination of system software and manual procedures that create an overall control environment.

(e) Data Flow Diagram (DFD): A Data Flow Diagram uses few simple symbols to illustrate the flow of data among external entities (such as people or organizations, etc.), processing activities and data storage elements. A DFD is composed of four basic elements: Data Sources and Destinations, Data Flows, Transformation processes, and Data stores. These have different symbols that are combined to show how data are processed.

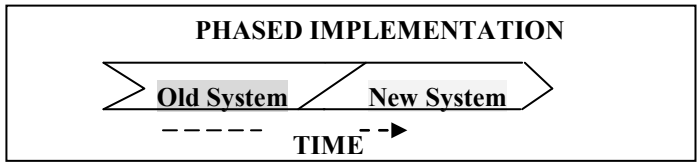
Data Flow Diagram Symbols

Symbol	Name	Explanation
	Data Sources and destinations	The people and organizations that send data to and receive data from the system are represented by square boxes called Data destinations or Data Sinks.
	Data flows	The flow of data into or out of a process is represented by curved or straight lines with arrows.
	Transformation process	The processes that transform data from inputs to outputs are represented by circles, often referred to as bubbles.
	Data stores	The storage of data is represented by two horizontal lines.

22. (a) Cold Site: If an organisation can tolerate some downtime, cold-site backup might be appropriate. A cold site has all the facilities needed to install a mainframe system-raised floors, air conditioning, power, communication lines, and so on. An organisation can establish its own cold-site facility or enter into an agreement with another organisation to provide a cold-site facility.

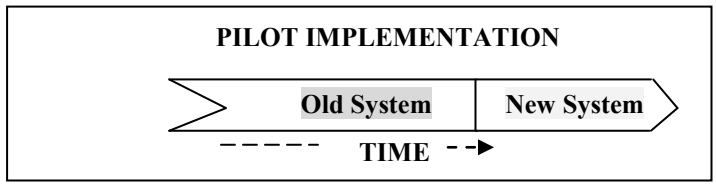
Hot Site: If fast recovery is critical, an organisation might need hot site backup. All hardware and operations facilities will be available at the hot site. In some cases, software, data and supplies might also be stored there. A hot site is expensive to maintain. They are usually shared with other organisations that have hot-site needs.

(b) Phased Changeover: With this strategy, implementation can be staged with conversion to the new system taking place gradually. For example, some new files may be converted and used by employees whilst other files continue to be used on the old system i.e. the new is brought in stages (phases). If a phase is successful then the next phase is started, eventually leading to the final phase when the new system fully replaces the old one as shown in Figure.



Phased Changeover

Pilot Changeover: With this strategy, the new system replaces the old one in one operation but only on a small scale. Any errors can be rectified or further beneficial changes can be introduced and replicated throughout the whole system in good time with the least disruption. For example - it might be tried out in one branch of the company or in one location. If successful then the pilot is extended until it eventually replaces the old system completely. Figure below depicts Pilot Implementation.



Pilot Changeover

(c) Structured English: Structured English, also known as Program Design Language (PDL), is the use of the English language with the syntax of structured programming. Thus, Structured English aims at getting the benefits of both the programming logic and natural language. Program logic that helps to attain precision and natural language that helps in getting the convenience of spoken languages. A better structured, universal and precise tool is referred to as pseudo code.

Flowchart: Flowcharting is a pictorial representation technique that can be used by analysts to represent the inputs, outputs and processes of a business process. It is a common type of chart that represents an algorithm or process showing the steps as boxes of various kinds, and their order by connecting these with arrows. Flowcharts are used in analyzing, designing, documenting or managing a process or program in various fields.

(d) Inherent Risk: Inherent Risk is the susceptibility of information resources or resources controlled by the information system to material theft, destruction,

disclosure, unauthorized modification, or other impairment, assuming that there are no related internal controls. Inherent risk is the measure of auditor's assessment that there may or may not be material vulnerabilities or gaps in the audit subject exposing it to high risk before considering the effectiveness of internal controls. If the auditor concludes that there is a high likelihood of risk exposure, ignoring internal controls, the auditor would conclude that the inherent risk is high. For example, inherent risk would be high in case of auditing internet banking in comparison to branch banking or inherent risk would be high if the audit subject is an off-site. Example - ATM. Internal controls are ignored in setting inherent risk because they are considered separately in the audit risk model as control risk. It is often an area of professional judgment on the part of an auditor.

Detection Risk: Detection Risk is the risk that the IT auditor's substantive procedures will not detect an error which could be material, individually or in combination with other errors. For example, the detection risk associated with identifying breaches of security in an application system is ordinarily high because logs for the whole period of the audit are not available at the time of the audit. The detection risk associated with lack of identification of disaster recovery plans is ordinarily low since existence is easily verified.

(e) Emergency Plan: The Emergency Plan specifies the actions to be undertaken immediately when a disaster occurs. Management must identify those situations that require the plan to be invoked e.g., major fire, major structural damage and terrorist attack. The actions to be initiated can vary depending on the nature of the disaster that occurs.

When the situations that evoke the plan have been identified, four aspects of the emergency plan must be articulated. First, the plan must show 'who is to be notified immediately when the disaster occurs - management, police, fire department, medicos, and so on'. Second, the plan must show actions to be undertaken, such as shutdown of equipment, removal of files, and termination of power. Third, any evacuation procedures required must be specified. Fourth, return procedures (e.g., conditions that must be met before the site is considered safe) must be designated. In all cases, the personnel responsible for the actions must be identified, and the protocols to be followed must be specified clearly.

Recovery Plan: The backup plan is intended to restore operations quickly so that information system function can continue to service an organization, whereas, recovery plans set out procedures to restore full information system capabilities. Recovery plan should identify a recovery committee that will be responsible for working out the specifics of the recovery to be undertaken. The plan should specify the responsibilities of the committee and provide guidelines on priorities to be followed. The plan might also indicate which applications are to be recovered first. Members of a recovery committee must understand their responsibilities. Again, the problem is that they will be required to undertake unfamiliar tasks. Periodically, they

must review and practice executing their responsibilities so they are prepared should a disaster occur. If committee members leave the organization, new members must be appointed immediately and briefed about their responsibilities.

23. (a) The evaluation of effective Management Information System (MIS) should take into account the following major points:

- Examining whether enough flexibility exists in the system to cope with any expected or unexpected information requirement in future.
- Ascertaining the views of users and the designers about the capabilities and deficiencies of the system.
- Guiding the appropriate authority about the steps to be taken to maintain effectiveness of MIS.

(b) The advantages of Business Continuity Management (BCM) are that the enterprise:

- is able to proactively assess the threat scenario and potential risks;
- has planned response to disruptions which can contain the damage and minimize the impact on the enterprise; and
- is able to demonstrate a response through a process of regular testing and trainings.

(c) [Section 44] Penalty for failure to furnish information return, etc.

If any person who is required under this Act or any rules or regulations made thereunder to -

(a) furnish any document, return or report to the Controller or the Certifying Authority, fails to furnish the same, he shall be liable to a penalty not exceeding one lakh and fifty thousand rupees for each such failure;

(b) file any return or furnish any information, books or other documents within the time specified therefor in the regulations fails to file return or furnish the same within the time specified therefor in the regulations, he shall be liable to a penalty not exceeding five thousand rupees for every day during which such failure continues;

(c) maintain books of account or records, fails to maintain the same, he shall be liable to a penalty not exceeding ten thousand rupees for every day during which the failure continues.

(d) User Related Issues: It refers to those issues where user/customer is reckoned as the primary agent. Some of the aspects with regard to this problem are as follows:

- **Shifting User Needs:** User requirements for IT are constantly changing. As these changes accelerate, there will be more requests for Information systems development and more development projects. When these changes occur

during a development process, the development team faces the challenge of developing systems whose very purpose might change since the development process began.

- **Resistance to Change:** People have a natural tendency to resist change, and information systems development projects signal changes - often radical - in the workplace. When personnel perceive that the project will result in personnel cutbacks, threatened personnel will dig in their heels, and the development project is doomed to failure.
- **Lack of User Participation:** Users must participate in the development efforts to define their requirements, feel ownership for project success, and work to resolve development problems. User participation also helps to reduce user resistance to change.
- **Inadequate Testing and User Training:** New systems must be tested before installation to determine that they operate correctly. Users must be trained to effectively utilize the new system.

24. (a) **Methods of Validating the proposal:** Large organizations would naturally tend to adopt a sophisticated and objective approach to validate the vendor's proposal. Some of the validation methods for approving the vendor's proposal are as follows:

- **Checklists:** It is the most simple and a subjective method for validation and evaluation. The various criteria are put in check list in the form of suitable questions against which the responses of the various vendors are validated. For example, Support Service Checklists may have parameters like Performance; System development, Maintenance, Conversion, Training, Back-up, Proximity, Hardware and Software.
- **Point-Scoring Analysis:** Point-scoring analysis provides an objective means of selecting a final system. There are no absolute rules in the selection process, only guidelines for matching user needs with software capabilities. Thus, even for a small business, the evaluators must consider such issues as the company's data processing needs, its in-house computer skills, vendor reputations, software costs, and so forth.
- **Public Evaluation Reports:** Several consultancy as well as independent agencies compare and contrast the hardware and software performance for various manufacturers and publish their reports in this regard. This method has been frequently and usefully employed by several buyers in the past and is particularly useful where the buying staffs have inadequate knowledge of facts.
- **Benchmarking Problems related Vendor's Solutions:** Benchmarking problems related to vendors' proposals are accomplished by sample programs that represent at least a part of the buyer's primary work load and include considerations and can be current applications that have been designed to

represent planned processing needs. That is, benchmarking problems are oriented towards testing whether a solution offered by the vendor meets the requirements of the job on hand of the buyer.

- **Testing Problems:** Test problems disregard the actual job mix and are devised to test the true capabilities of the hardware, software or system. For example, test problems may be developed to evaluate the time required to translate the source code (program in an assembly or a high level language) into the object code (machine language), response time for two or more jobs in multi-programming environment, overhead requirements of the operating system in executing a user program, length of time required to execute an instruction, etc.

(b) Major components that have been considered in Web 2.0 include the following:

- **Communities:** These are an online space formed by a group of individuals to share their thoughts, ideas and have a variety of tools to promote Social Networking. There are a number of tools available online, now-a-days to create communities, which are very cost efficient as well as easy to use.
- **Blogging:** Blogs give the users of a Social Network the freedom to express their thoughts in a free form basis and help in generation and discussion of topics.
- **Wikis:** A Wiki is a set of co-related pages on a particular subject and allow users to share content. Wikis replace the complex document management systems and are very easy to create and maintain.
- **Folksonomy:** Web 2.0 being a people-centric technology has introduced the feature of Folksonomy where users can tag their content online and this enables others to easily find and view other content.
- **File Sharing/Podcasting:** This is the facility, which helps users to send their media files and related content online for other people of the network to see and contribute.
- **Mashups:** This is the facility, by using which people on the internet can congregate services from multiple vendors to create a completely new service. An example may be combining the location information from a mobile service provider and the map facility of Google maps in order to find the exact information of a cell phone device from the internet, just by entering the cell number.

(c) Various features of Electronic Mail are stated below:

- **Electronic Transmission -** The transmission of messages with email is electronic and message delivery is very quick, almost instantaneous. The confirmation of transmission is also quick and the reliability is very high.

- **Online Development and Editing -** The email message can be developed and edited online before transmission. The online development and editing eliminates the need for use of paper in communication. It also facilitates the storage of messages on magnetic media, thereby reducing the space required to store the messages.
- **Broadcasting and Rerouting -** Email permits sending a message to a large number of target recipients. Thus, it is easy to send a circular to all branches of a bank using Email resulting in a lot of saving of paper. The email could be rerouted to people having direct interest in the message with or without changing or and appending related information to the message.
- **Integration with other Information Systems -** The E-mail has the advantage of being integrated with the other information systems. Such integration helps in ensuring that the message if accurate and the information required for the message is accesses quickly.
- **Portability -** Email renders the physical location of the recipient and sender irrelevant. The email can be accessed from any Personal computer/tablet/smart phones equipped with the relevant communication hardware, software and link facilities.
- **Economical -** The advancements in communication technologies and competition among the communication service providers have made Email the most economical mode for sending and receiving messages. The email is very helpful for formal communication as well as informal communication within the enterprise.

(d) Various types of back-ups are given as follows:

- **Full Backup:** A Full Backup captures all files on the disk or within the folder selected for backup. With a full backup system, every backup generation contains every file in the backup set. However, the amount of time and space such a backup takes prevents it from being a realistic proposition for backing up a large amount of data.
- **Incremental Backup:** An Incremental Backup captures files that were created or changed since the last backup, regardless of backup type. This is the most economical method, as only the files that changed since the last backup are backed up. This saves a lot of backup time and space.

  Normally, incremental backup are very difficult to restore. One will have to start with recovering the last full backup, and then recovering from every incremental backup taken since.
- **Differential Backup:** A Differential Backup stores files that have changed since the last full backup. Therefore, if a file is changed after the previous full backup, a differential backup takes less time to complete than a full back up.

Comparing with full backup, differential backup is obviously faster and more economical in using the backup space, as only the files that have changed since the last full backup are saved.

- **Mirror back-up:** A Mirror Backup is identical to a full backup, with the exception that the files are not compressed in zip files and they cannot be protected with a password. A mirror backup is most frequently used to create an exact copy of the backup data.

25. (a) Two primary methods through which the analyst would have collected the data are given as follows:

(1) **Reviewing internal documents:** The analyst first tries to learn about the organization involved in or affected by the project. For example, to review an inventory system proposal, s/he will try to know 'how the inventory department operates' and 'who are the managers and supervisors'. S/he will examine organization charts and written operating procedures.

(2) **Conducting interviews:** Written documents tell the analyst 'how the system should operate' but they may not include enough details to allow a decision to be made about the merits of a system proposal nor do they present users' views about current operations. To learn these details, analysts use interviews. Preliminary investigation interviews involve only management and supervisory personnel.

(b) [Section 7] Retention of Electronic Records

(1) Where any law provides that documents, records or information shall be retained for any specific period, then, that requirement shall be deemed to have been satisfied if such documents, records or information are retained in the electronic form, if -

(a) the information contained therein remains accessible so as to be usable for a subsequent reference;

(b) the electronic record is retained in the format in which it was originally generated, sent or received or in a format which can be demonstrated to represent accurately the information originally generated, sent or received;

(c) the details which will facilitate the identification of the origin, destination, date and time of dispatch or receipt of such electronic record are available in the electronic record:

PROVIDED that this clause does not apply to any information which is automatically generated solely for the purpose of enabling an electronic record to be dispatched or received.

(2) Nothing in this section shall apply to any law that expressly provides for the retention of documents, records or information in the form of electronic records.

PAPER –7: DIRECT TAX LAWS

PART – III : QUESTIONS AND ANSWERS

QUESTIONS

Basic Concepts

1. Mr. Ganesh is a wholesale trader and his total income for the last few years ranged between ₹ 7 lakh to ₹ 9 lakh. He celebrated his 50th birthday on a large scale on 19th June, 2014 by hosting a cruise party in the luxury cruise liner "Silver Sea", for which he had spent ₹ 25 lakh. The Assessing Officer, in the course of scrutiny assessment of Mr. Ganesh, asked him to explain the source of such expenditure. The explanation offered by Mr. Ganesh that the same was out of his savings for the last few years, was not found satisfactory by the Assessing Officer, since a couple of years ago, he had spent to tune of ₹ 50 lakh on the grand wedding celebrations of his twin daughters at Seshmahal in Chennai. You are required to examine the tax consequences.

Income which do not form part of total income [Charitable Trusts]

2. Discuss the correctness or otherwise of the claims made by the following charitable trusts, registered under section 12AA, while computing income for the P.Y.2014-15:

   (a) Kasturba charitable trust, having its main object as relief of the poor, earned the following income during the P.Y.2014-15:

	Particulars	₹ in lakh
(i)	Dividend income	0.75
(ii)	Income from mutual funds specified under section 10(23D)	1.25
(iii)	Agricultural income	4.75

   The trust claims exemption under section 10(1), 10(34) and 10(35) in respect of its agricultural income, dividend and income from mutual funds, respectively, without complying with the conditions laid down under section 11.

   (b) Kamaraj charitable trust, having its main object as promoting education in rural areas, purchased computers and laptops for ₹ 18 lakh in March, 2014 for the purposes of the trust and claimed the same as application of income in the P.Y.2013-14. It also claims depreciation @ 60% on such computers and laptops for P.Y.2014-15, while computing income for the purpose of application for that year.

Profits and gains of business or profession

3. Omega Ltd. has two units – Unit Phi, which carries on the specified business of operating a warehousing facility for storage of foodgrains and Unit Rho which carries on non-specified business of operating a warehousing facility for storage of edible oil. Unit Phi commenced operations on 1st October, 2013 and for A.Y.2014-15, it claimed deduction of ₹ 300 lakhs under section 35AD, being 150% of ₹ 200 lakhs, incurred on purchase of two

buildings for ₹ 100 lakhs each (for operating a warehousing facility for storage of foodgrains) on 1.11.2013. Unit Phi, however, transferred one of the buildings to Unit Rho in March, 2015. Examine the tax implications of such transfer in the hands of Omega Ltd.

4. Omicron Ltd., engaged in the business of manufacture of machine tools and equipments, furnishes the following particulars pertaining to P.Y. 2014-15.

	Particulars	₹ in crores
1.	Written down value of plant and machinery (15% block) as on 1.4.2014	10.00
2.	Sold plant and machinery on 5.5.2014 (15% block)	2.00
3.	Purchase of second hand machinery (15% block) on 7.7.2014 for business purpose (the machinery was put to use immediately)	8.00
4.	Purchased new computers (60% block) on 1.12.2014 for office use	0.50
5.	Acquired and installed new plant and machinery (15% block) on 4.9.2014 (₹ 15 crore) and on 10.1.2015 (₹ 12 crore)	27.00
6.	New air conditioners purchased and installed in office premises on 18.8.2014	0.20

Work out the deduction allowable under section 32 and section 32AC for A.Y.2015-16, while computing its income under the head "Profits and gains of business or profession". Also, determine the written down value of plant and machinery as on 1.4.2015.

5. Delta Ltd. credited the following amounts to the account of resident payees in the month of March, 2015 without deduction of tax at source. What would be the consequence of non-deduction of tax at source by Delta Ltd. on these amounts during the financial year 2014-15, assuming that the resident payees in all the cases mentioned below, have not paid the tax, if any, which was required to be deducted by Delta Ltd.?

	Particulars	Amount in ₹
(1)	Salary to its employees (credited and paid in March, 2015)	12,00,000
(2)	Non-compete fees to Mr. Rajesh (credited and paid in March, 2015)	1,10,000
(3)	Directors' remuneration (credited in March, 2015 and paid in April, 2015)	28,000

Would your answer change if Delta Ltd. has deducted tax on directors' remuneration in April, 2015 at the time of payment and remitted the same in July, 2015?

6. Discuss the deductibility of the following expenditure while computing business income –

   (a) Alpha Ltd. incurred expenditure of ₹ 25 lakhs on slum area development, which qualifies as a CSR activity as per section 135 of the Companies Act, 2013 read with Schedule VII thereto, and claimed the same as deduction under section 37. It also

made contribution of ₹ 8 lakhs to Prime Minister's National Relief Fund as part of its CSR obligation.

(b) Delta Ltd. paid royalty to Zeta Inc., a Finnish company, in March, 2015 after deducting tax at source at the rates in force. The tax so deducted was, however, deposited only in August, 2015.

(c) Theta Ltd. invested ₹ 8 crore in land and ₹ 4 crore in new plant and machinery in April, 2014 for setting up and operating a semi-conductor wafer fabrication manufacturing unit which commences operations on 1st May, 2014.

Capital Gains

7. Ms. Smita purchased a land at a cost of ₹ 15 lakhs in the financial year 1990-91 and held the same as her capital asset till 31st March, 2012. She started her real estate business on 1st April, 2012 and converted the said land into stock-in-trade of her business on the said date, when the fair market value of the land was ₹ 180 lakhs.

She constructed 10 flats of equal size, quality and dimension. Cost of construction of each flat is ₹ 10 lakhs. Construction was completed in January, 2015. She sold 8 flats at ₹ 30 lakhs per flat in February and March, 2015. The remaining 2 flats were held in stock as on 31st March, 2015.

She invested ₹ 30 lakhs in bonds issued by Rural Electrification Corporation Ltd. in March, 2015 and ₹ 40 lakhs in bonds issued by National Highways Authority of India in April, 2015.

Compute the amount of chargeable capital gain and business income in the hands of Ms. Smita arising from the above transactions for Assessment Year 2015-16 indicating clearly the reasons for treatment for each item.

Cost Inflation Index: F.Y. 1990-91: 182; F.Y. 2012-13: 852; F.Y. 2014-15: 1024.

Capital Gains & Income from other sources

8. Mr. Rohan has acquired a residential house property in Faridabad on 4th June, 2001 for ₹ 73,71,600 and decided to sell the same on 3rd September, 2005 to Ms. Nidhi and an advance of ₹ 3,00,000 was taken from her. The balance money was not paid by Ms. Nidhi and hence, Mr. Rohan has forfeited the entire advance sum. In May, 2014, he once again entered into negotiations for sale of the said property to Ms. Mutka, and received ₹ 4,25,000 as advance, but the transfer did not materialize and hence, the advance was forfeited. On 18th February, 2015, he finally sold this house to Ms. Shilpa for ₹ 2,75,00,000. In the meantime, in January, 2015, he had purchased a residential house in Pune for ₹ 52,00,000 and made full payment for the same. However, Mr. Rohan does not possess any legal title till 31st March, 2015, as such transfer was not registered with the registration authority.

Mr. Rohan had purchased another house in Baroda in November, 2014 from Ms. Premlata, an Indian resident, by paying ₹ 43,00,000 and the purchase was registered with the appropriate authority.

Determine the taxable capital gain arising from above transactions in the hands of Mr. Rohan for the A.Y. 2015-16 [Cost Inflation Index - 2001-02: 426; 2005-06: 497; 2014-15:1024].

Deductions from gross total income

9. Spectrum Ltd. raises the following issues in connection with its eligibility for claiming deduction under section 80-IB for your consideration and advice for the A.Y. 2015-16:

   (i) It operates two separate industrial units. One unit is eligible for deduction under section 80-IB, while the other unit is not eligible for such deduction. If the eligible unit has profit and the other unit has loss, should it claim deduction after setting off the loss of the other unit against profit of the eligible unit?

   (ii) If the company had not claimed deduction under section 80-IB in the first three years, can it claim the deduction for the remaining years during the period of eligibility?

   (iii) Can DEPB benefit and Duty Drawback be treated as "profit derived from the business of the industrial undertaking" to be eligible for deduction under section 80-IB?

   (iv) Can it treat the persons employed by it on contractual basis as workers to satisfy the condition of employment of ten or more "workers" for availing benefit of deduction under section 80-IB, if such workers were employed throughout the year for manufacturing process?

10. From the following details, compute the total income of Mr. Akash, Mr. Barun and Mr. Chirag for A.Y.2015-16 –

Particulars		Akash	Barun	Chirag
		₹	₹	₹
(i)	Salary (computed)	8,73,000	9,87,000	10,92,000
(ii)	Interest income (on fixed deposits)	81,000	94,000	1,13,000

Mr. Akash, Mr. Barun and Mr. Chirag are new retail investors who have made the following investments in equity shares/units of equity oriented fund of Rajiv Gandhi Equity Savings Scheme, 2013 for the P.Y.2014-15:

Particulars		Akash	Barun	Chirag
		₹	₹	₹
(i)	Investment in listed equity shares	22,000	58,000	18,000
(ii)	Investment in units of equity-oriented fund	23,000	-	30,000

The particulars of their other investments/payments made during the P.Y.2014-15 are given hereunder -

<table>
<tr><th></th><th>Particulars</th><th>₹</th></tr>
<tr><td>(1)</td><td>Mr. Akash made a five-year term deposit (tax saver) with SBI</td><td>1,50,000</td></tr>
<tr><td>(2)</td><td>Life insurance premium paid by Mr. Chirag, the details of which are as follows –
<table>
<tr><th></th><th>Date of issue of policy</th><th>Person insured</th><th>Actual capital sum assured (₹)</th><th>Insurance premium paid during P.Y.2014-15 (₹)</th></tr>
<tr><td>(i)</td><td>22/8/2010</td><td>Self</td><td>80,000</td><td>18,000</td></tr>
<tr><td>(ii)</td><td>14/9/2012</td><td>Spouse</td><td>90,000</td><td>10,000</td></tr>
<tr><td>(iii)</td><td>20/6/2013</td><td>Handicapped Son - section 80U disability</td><td>1,25,000</td><td>20,000</td></tr>
</table></td><td></td></tr>
<tr><td>(3)</td><td>Payment of medical insurance premium by the following persons to insure their health:
<table>
<tr><th>Payer</th><th>Amount in ₹</th><th>Mode of payment</th></tr>
<tr><td>Mr. Akash (47 years)</td><td>18,000</td><td>Account payee cheque</td></tr>
<tr><td>Mr. Barun (46 years)</td><td>12,000</td><td>Cash</td></tr>
<tr><td>Mr. Chirag (51 years)</td><td>15,000</td><td>Crossed cheque</td></tr>
</table></td><td></td></tr>
<tr><td>(4)</td><td>Mr. Barun paid interest on loan taken for the purchase of house in which he currently resides. He is claiming benefit of self-occupation under section 23(2) in respect of this house. He does not own any other house.</td><td>2,20,000</td></tr>
<tr><td></td><td>Repayment of principal amount of loan taken for purchase of the said house
(The housing loan of ₹ 23 lakhs was sanctioned by HDFC on 3.4.2013 and disbursed in full on 10.4.2013, being the date of purchase of house property, the cost of which was ₹ 35 lakhs. Mr. Barun paid ₹ 2,40,000 as interest on loan during the previous year 2013-14).</td><td>1,70,000</td></tr>
<tr><td>(5)</td><td>Contribution by Mr. Akash by cheque to National Children's Fund during the year.</td><td>45,000</td></tr>
<tr><td>(6)</td><td>Mr. Barun makes the following donations during the P.Y.2014-15 -</td><td></td></tr>
<tr><td></td><td>Donation to an electoral trust by account payee cheque</td><td>75,000</td></tr>
<tr><td></td><td>Donation to a political party by cash</td><td>60,000</td></tr>
</table>

What would be the tax consequence if Mr. Akash and Mr. Chirag sold their entire investment in units of equity oriented fund in June, 2015?

Assessment of various entities

11. Mr. Jacob, carrying on the business of operating a cold chain facility, has a total income of ₹ 82 lakhs for the P.Y.2014-15. He commenced operations of the business in May, 2014. In computing the total income for the P.Y.2014-15, he had claimed deduction under section 35AD in respect of investment of ₹ 70 lakhs in building (in June, 2014) for operating the cold chain facility. Compute his tax liability for A.Y.2015-16.

12. Zeta Limited, engaged in the business of manufacturing, shows a net profit of ₹ 182 lakhs for the year ended 31st March, 2015 after debiting and crediting the following items to its Statement of Profit & Loss:

    (a) Depreciation provided on straight line basis debited to the Statement of Profit & Loss was ₹ 32 lakhs.

    (b) ₹ 8 lakhs on salary for its research assistants and ₹ 5 lakhs spent on purchase of materials for in-house research and development facility approved by the prescribed authority.

    (c) Legal expenses in connection with issue of Bonus Shares ₹ 3 lakhs, and issue of Rights shares ₹ 4 lakhs.

    (d) The opening and closing stocks of the company were undervalued by 10%. [Opening stock ₹ 22 lakhs; Closing Stock ₹ 32 lakhs].

    (e) Payment of ₹ 10 lakhs to an employee in connection with his voluntary retirement in accordance with a scheme of voluntary retirement.

    (f) The company adopts a policy of providing 5% of the Sundry Debtors in the beginning of the year as provision for doubtful debts. Sundry Debtors outstanding as on 01.04.2014 is ₹ 600 lakhs.

    (g) No tax has been deducted from a sum of ₹ 8 lakhs credited to a contractor, who is a resident firm for some of the works outsourced. However, the contractor has considered the same in the return of income filed by him on 30th July, 2015 and has paid the taxes due on such income.

    (h) Cash donation given to an electoral trust ₹ 12 lakhs.

    Additional information:

    (i) Normal depreciation allowable is ₹ 28 lakhs which includes depreciation on new plant and machinery costing ₹ 25 lakhs acquired and installed in February, 2015.

    (ii) Addition to fixed assets given in (i) above during the year includes ₹ 18 lakhs on account of machinery acquired for its in-house scientific research and development facility approved by the prescribed authority.

(iii) Bad debts actually written off during the year by adjusting provision for bad debts account was ₹ 15 lakhs.

Compute income-tax payable by Zeta Limited for Assessment Year 2015-16 indicating reasons for treatment of each item. Ignore Minimum Alternate Tax.

13. Sigma Ltd., a domestic company, purchases its own unlisted shares on 16th September, 2014. The consideration for buyback amounted to ₹ 22 lakhs, which was paid on the same day. Sigma Ltd. had received ₹ 14 lakhs on issue of these shares one year back. Compute the additional income-tax payable by Sigma Ltd. Further, determine the interest, if any, payable if such tax is paid to the credit of the Central Government on 11th December, 2014. Would there be any tax implication in the hands of the shareholders? Discuss.

Transfer Pricing

14. Discuss whether transfer pricing provisions under the Income-tax Act, 1961 are attracted in respect of the following cases -

(i) Transfer of technical knowhow by Alpha Ltd., an Indian company, to Beta Inc., a French company, which guarantees 15% of the borrowings of Alpha Ltd.

(ii) Purchase of plant and machinery by Phi Ltd., an Indian company, from Rho Inc., a Swedish company. Phi Ltd. is the subsidiary of Rho Inc.

(iii) Ms. Nidhi, a resident Indian, is a director of Delta Ltd, an Indian company. Delta Ltd. pays salary of ₹ 45 lakhs per annum to Yashasvi, who is Ms. Nidhi's daughter.

(iv) Alpha Ltd., an Indian company, has two units Sun & Moon. Sun, which commenced business three years back, is engaged in the development of a highway project, for which purpose an agreement has been entered into with the Central Government. Moon is carrying on the business of trading in cement. Moon transfers cement of the value of ₹ 65 lakhs to Sun for ₹ 45 lakhs.

(v) Scientific research services provided by Sigma Inc., a German company to Theta Ltd., an Indian company. Sigma Inc. is a "specified foreign company" as defined in section 115BBD, in relation to Theta Ltd.

15. Mr. Manas, a non-resident individual, is due to receive interest of ₹ 6,25,000 in March 2015 from a notified infrastructure debt fund eligible for exemption under section 10(47). He incurred expenditure amounting to ₹ 32,000 for earning such income. Assuming that Mr. Manas is a resident of a Notified Jurisdictional Area (NJA), discuss the tax implications in his hands and the applicability of provisions relating to deduction of tax at source from such interest.

Income-tax Authorities

16. Discuss the correctness or otherwise of the following statements, with reference to the provisions of the Income-tax Act, 1961 –

(i) The maximum time period for retaining books of account or documents impounded by an income-tax authority under section 133A without obtaining the approval of the higher authorities specified thereunder is ten days (exclusive of holidays).

(ii) The Finance (No.2) Act, 2014 has expanded the scope of powers of an income-tax authority acting under section 133A.

Assessment Procedure

17. What is the time limit for completing assessment in the following cases –

(i) Best judgment assessment under section 144 in respect of A.Y.2014-15.

(ii) Reassessment under section 147, in respect of which notice under section 148 was served on 1.5.2013.

(iii) Assessment under section 143(3) in respect of A.Y.2013-14, where reference under section 92CA(1) is made on 1.12.2014.

Advance Rulings

18. "The expansion of scope of advance rulings and consequent strengthening of the constitution of the Authority for Advance Rulings by the Finance (No.2) Act, 2014 has underlined the significance of advance rulings in minimising tax litigation"- Elucidate.

Miscellaneous Provisions/Penalties

19. Section 285BA requires furnishing of statement of financial transaction or reportable account by *inter alia* a prescribed reporting financial institution.

(i) Can the prescribed income-tax authority require furnishing of statement under section 285BA(1), where the person, being a prescribed reporting financial institution, has not furnished the same within the specified time?

(ii) How can a defect in the statement be rectified if the same is discovered by the person, being a prescribed reporting financial institution which has furnished the statement under section 285BA(1) or in pursuance of a notice issued under section 285BA(5)?

(iii) Are penal provisions attracted in case where the person, being a prescribed reporting financial institution, provides inaccurate information in the statement? Elucidate.

Provisions for deduction and collection of tax at source

20. Examine the applicability of the provisions for tax deduction at source under section 194DA in the respect of the following payments due to be made in respect of maturity proceeds of LIC policy -

	Resident payees	Maturity proceeds due to be paid (₹)	Due date of payment (Maturity date)	Date of policy	Sum Assured (₹)	Annual premium (₹)
(1)	Mr. Shiva	5,25,000	31/3/2015	1/4/2011	5,00,000	1,00,000

(2)	Mr. Vishnu	3,20,000	31/3/2015	1/4/2012	3,00,000	80,000
(3)	Mr. Ganesh	98,000	31/12/2014	1/1/2011	90,000	18,500
(4)	Mr. Krishna	4,50,000	31/8/2014	1/9/2010	4,00,000	90,000

SUGGESTED ANSWERS/HINTS

1. If any expenditure is incurred by an assessee in any financial year in respect of which he is not able to offer explanation about the source of such expenditure or the explanation offered by him is not satisfactory in the opinion of the Assessing Officer, then the amount of such unexplained expenditure may be deemed as income of the assessee for such financial year as per section 69C.

Therefore, in this case, since the Assessing Officer is not satisfied with the explanation offered by Mr. Ganesh, the expenditure of ₹ 25 lakh incurred by him in the financial year 2014-15 in hosting a grand cruise party may be deemed as his income for such financial year as per section 69C.

Further, such unexplained expenditure which is deemed as the income of Mr. Ganesh shall not be allowed as deduction under any head of income.

Where the total income of Mr. Ganesh includes such unexplained expenditure of ₹ 25 lakh, which is deemed as his income under section 69C, such deemed income would be taxed at the rate of 30% as per section 115BBE.

Further, no basic exemption or allowance or expenditure shall be allowed to him under any provision of the Income-tax Act, 1961 in computing such deemed income.

Penalty under 271(1)(c) is also leviable for concealment of income.

2. **(a)** Section 11(7) provides that where a trust has been granted registration under section 12AA and the registration is in force for a previous year, then, such trust cannot claim any exemption under any provision of section 10 [other than exemption of agricultural income under section 10(1) and exemption available under section 10(23C)].

Therefore, a charitable trust cannot claim exemption under section 10(35) in respect of income from mutual funds and exemption under section 10(34) in respect of dividends, since it has voluntarily opted for the special dispensation under sections 11 to 13, and consequently has to be governed by the provisions of these sections. However, it can claim exemption under section 10(1) in respect of agricultural income, since section 11(7) provides an exception in respect of such income.

Therefore, the claim of Kasturba charitable trust, as regards exemption under section 10(34) and section 10(35), is not correct.

(b) Section 11(6) provides that income for the purposes of application shall be determined without allowing any deduction for depreciation or otherwise in respect of any asset, the cost of acquisition of which has been claimed as an application of income under section 11 in the same or any other previous year.

Accordingly, in this case, since the cost of computers and laptops (i.e., ₹ 18 lakh) has been claimed and allowed as application of income under section 11 while computing the income of the trust for the P.Y.2013-14, depreciation on computers and laptops will not be allowed for the purpose of determining income for the purposes of application in the P.Y.2014-15.

Therefore, the depreciation claim made by Kamaraj charitable trust is not correct.

3. Since the capital asset in respect of which deduction of ₹ 150 lakhs (150% of ₹ 100 lakhs) was claimed under section 35AD in the A.Y.2014-15, has been transferred by Unit Phi carrying on specified business to Unit Rho carrying on non-specified business in the P.Y.2014-15, the deeming provision under section 35AD(7B) is attracted while computing business income of Omega Ltd. for A.Y.2015-16, since the asset (building, in this case) in respect of which deduction was claimed and allowed under section 35AD in the A.Y.2014-15 is used for a purpose other than the specified business during the period of eight years from P.Y.2013-14, being the previous year in which the asset was acquired.

Accordingly, the deduction of ₹ 150 lakhs claimed and allowed in the A.Y.2014-15 in respect of such asset, as reduced by the amount of depreciation allowable in accordance with the provisions of section 32 for A.Y.2014-15 as if no deduction has been allowed under section 35AD, shall be deemed to be the income of Omega Ltd. chargeable under the head "Profits and gains of business or profession" of the P.Y.2014-15, being the previous year in which the asset is transferred to non-specified business.

Particulars	**₹**
Deduction allowed under section 35AD for A.Y.2014-15 (in respect of one building transferred to Unit Rho)	1,50,00,000
Less: Depreciation (7.5% of Rs.100 lakhs, since the asset was put to use for less than 180 days during the P.Y.2013-14)	7,50,000
Deemed income under section 35AD(7B)	**1,42,50,000**

4. Computation of depreciation allowance under section 32 for the A.Y. 2015-16

Particulars	**Plant & Machinery**	
	15%	**60%**
	(₹ in crores)	
WDV as on 01.04.2014	10.00	-

Add: Plant and Machinery acquired during the year			
- Second hand machinery	8.00		
- New plant and machinery	27.00		
- Air conditioner installed in office	0.20		
		35.20	
Computers acquired during the year		-	0.50
		45.20	0.50
Less: Asset sold during the year		2.00	Nil
Written down value before charging depreciation		43.20	0.50
Less: Depreciation for the P.Y.2014-15 (***See Note 1 below***)		9.78	0.15
WDV as on 1.4.2015		**33.42**	**0.35**
Note 1 : Computation of depreciation for the P.Y.2014-15			
Normal depreciation [Under section 32(1)(ii)]			
Depreciation @ 30% on computers put to use for less than 180 days (50% of 60% × ₹ 0.50 crore)		-	0.15
Depreciation on plant and machinery (15% block)		5.58	
(₹ 12 crore × 7.5%) + [(₹ 43.20 crore - ₹ 12 crore) × 15%]			
Additional depreciation [Under section 32(1)(iia)]			
New plant and machinery installed on -			
- 4.9.2014 (₹ 15 crore × 20%)	3.00		
- 10.1.2015 (₹ 12 crore × 10%)	1.20	4.20	Nil
Total depreciation		**9.78**	**0.15**

Computation of deduction under section 32AC for the A.Y.2015-16

Particulars	(₹ in crore)
15% of ₹ 27 crore, being aggregate investment in new plant and machinery acquired and installed during the P.Y.2014-15	4.05

Note – For the A.Y.2015-16, the company would be entitled for deduction under section 32AC(1A) since the investment in new plant and machinery acquired and installed during the P.Y.2014-15 is ₹ 27 crores (i.e., more than ₹ 25 crores). The deduction under section 32AC would be in addition to the depreciation allowable under section 32 for that year. However, the deduction under section 32AC would not be reduced to arrive at the written down value of plant and machinery.

It may be noted that investment in second hand plant and machinery and air-conditioners and computers installed in office would neither be eligible for deduction under section 32AC nor additional depreciation under section 32(1)(iia).

5. With effect from A.Y.2015-16, non-deduction of tax at source on any sum payable to a resident on which tax is deductible at source as per the provisions of Chapter XVII-B would attract disallowance under section 40(a)(ia). Therefore, non-deduction of tax at source on any sum paid by way of salary on which tax is deductible under section 192 or any sum credited or paid by way of non-compete fees and directors' remuneration on which tax is deductible under section 194J, would attract disallowance@30% under section 40(a)(ia). Whereas in case of salary, tax has to be deducted under section 192 at the time of payment, in case of non-compete fees and directors' remuneration, tax has to be deducted at the time of credit of such sum to the account of the payee or at the time of payment, whichever is earlier. Therefore, in all the three cases i.e., salary, non-compete fees and directors' remuneration, tax is deductible in the P.Y.2014-15, since salary was paid in that year and non-compete fees and directors' remuneration was credited in that year. Therefore, the amount to be disallowed under section 40(a)(ia) while computing business income for A.Y.2015-16 is as follows –

	Particulars	**Amount paid in ₹**	**Disallowance u/s 40(a)(ia) @ 30%**
(1)	Salary [tax is deductible under section 192]	12,00,000	3,60,000
(2)	Non-compete fees to Mr. Rajesh [tax is deductible under section 194J]	1,10,000	33,000
(3)	Directors' remuneration [tax is deductible under section 194J without any threshold limit]	28,000	8,400
Disallowance under section 40(a)(ia)			**4,01,400**

If the tax is deducted on directors' remuneration in the next year i.e., P.Y.2015-16 at the time of payment and remitted to the Government, the amount of ₹ 8,400 would be allowed as deduction while computing the business income of A.Y.2016-17.

6. **(a)** For the purposes of section 37(1), any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and hence, shall not be allowed as deduction under section 37.

Accordingly, the expenditure of ₹ 25 lakhs incurred by Alpha Ltd. on slum area development, being an activity qualifying as a CSR activity as per section 135 of the Companies Act, 2013 read with Schedule VII thereto, is not allowable as deduction under section 37.

₹ 8 lakhs, being contribution to Prime Minister's National Relief Fund, though not eligible for deduction while computing business income, would be eligible for 100% deduction under section 80G from gross total income

Note : *The Explanatory Memorandum to the Finance (No.2) Bill, 2014 clarifies that expenditure on CSR activities, which is of the nature described in sections 30 to 36, shall be allowed as deduction under those sections subject to fulfillment of conditions, if any, specified therein.*

Under section 35AC, 100% deduction is eligible in respect of the expenditure incurred on eligible projects/schemes specified under Rule 11K, which includes, inter alia, any programme for uplift of the rural poor or the urban slum dwellers as the Central Government may, by notification in the Official Gazette, specify in this behalf on the recommendation of the National Committee, being a committee constituted by the Central Government, from amongst persons of eminence in public life.

Therefore, if the expenditure of ₹ 25 lakhs on slum area development is incurred for the uplift of the rural poor or the urban slum dwellers and the other conditions mentioned under section 35AC are fulfilled by Alpha Ltd., it can claim deduction of such expenditure under section 35AC.

(b) Disallowance under section 40(a)(i) would not be attracted in this case since the tax deducted at source under section 195 in the P.Y.2014-15 has been deposited on or before the due date of filing of return under section 139(1). Hence, Delta Ltd. can claim deduction of royalty while computing its business income.

(c) Theta Ltd. would be eligible for investment-linked tax deduction under section 35AD@100% in respect of amount of ₹ 4 crore invested in new plant and machinery in April, 2014 for setting up and operating a semi-conductor wafer fabrication manufacturing unit which commences operation on 1st May, 2014, being a date falling on or after 1st April, 2014. However, such unit must be notified by the CBDT in accordance with the prescribed guidelines and the expenditure must be capitalized in the books of account of Theta Ltd. on 1st May, 2014. ₹ 8 crore, being the cost of land, would not qualify for investment-linked tax deduction under section 35AD.

7. Computation of capital gains and business income of Ms. Smita for A.Y.2015-16

Particulars	₹
Capital Gains	
Fair market value of land on the date of conversion deemed as the full value of consideration for the purposes of section 45(2)	1,80,00,000
Less: Indexed cost of acquisition [₹ 15,00,000 × 852/182]	70,21,978
	1,09,78,022

Proportionate capital gains arising during A.Y.2015-16 [₹ 1,09,78,022 × 8/10]	87,82,418
Less: Exemption under section 54EC	50,00,000
Capital gains chargeable to tax for A.Y.2015-16	**37,82,418**
Business Income	
Sale price of flats [8 × ₹ 30 lakhs]	2,40,00,000
Less: Cost of flats	
Fair market value of land on the date of conversion [₹ 180 lakhs × 8/10]	1,44,00,000
Cost of construction of flats [8 × ₹ 10 lakhs]	80,00,000
Business income chargeable to tax for A.Y.2015-16	**16,00,000**

Notes:

(1) The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade.

(2) However, as per section 45(2), the capital gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold.

(3) The indexation benefit for computing indexed cost of acquisition would, however, be available only up to the year of conversion of capital asset to stock-in-trade and not up to the year of sale of stock-in-trade.

(4) For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset.

In this case, since only 80% of the stock-in-trade (8 flats out of 10 flats) is sold in the P.Y.2014-15, only proportionate capital gains (i.e., 80%) would be chargeable in the A.Y.2015-16.

(5) On sale of such stock-in-trade, business income would arise. The business income chargeable to tax would be the difference between the price at which the stock-in-trade is sold and the fair market value on the date of conversion of the capital asset into stock-in-trade.

(6) In case of conversion of capital asset into stock-in-trade and subsequent sale of stock-in-trade, the period of 6 months is to be reckoned from the date of sale of stock-in-trade for the purpose of exemption under section 54EC [*CBDT Circular No.791 dated 2.6.2000].* In this case, since the investment in bonds of RECL and NHAI has been made within 6 months of sale of flats, the same qualifies for exemption under section

54EC. However, the maximum exemption under section 54EC would be restricted to ₹ 50 lakhs, even though the total investment in bonds of RECL and NHAI within the six month period is ₹ 70 lakhs.

8. Computation of taxable capital gain of Mr. Rohan for the A.Y.2015-16

Particulars	₹
Sale proceeds	2,75,00,000
Less: Indexed cost of acquisition **(See Notes 1 & 2)**	1,69,98,400
Long-term capital gain	1,05,01,600
Less: Exemption under section 54 in respect of investment in house at Pune **(See Notes 3 & 4)**	52,00,000
Taxable long-term capital gain	**53,01,600**

Notes:

(1) Computation of indexed cost of acquisition

Particulars	₹
Cost of acquisition	73,71,600
Less: Advance taken in the previous year 2005-06 and forfeited	3,00,000
Cost for the purpose of indexation	70,71,600
Indexed cost of acquisition (₹ 70,71,600 x 1024/426)	1,69,98,400

(2) Advance of ₹ 4,25,000 taken by Mr. Rohan from Ms. Mukta in May, 2014, which was forfeited due to the transaction not materializing, is taxable under section 56(2)(ix). Hence, such amount would not be reduced to compute the indexed cost of acquisition while computing capital gains on sale of the property in February, 2015.

(3) In order to avail exemption of capital gains under section 54, one residential house should be purchased within 1 year before or 2 years after the date of transfer or constructed within a period of 3 years after the date of transfer. In this case, Mr. Rohan has purchased the residential house in Pune within one year before the date of transfer and paid the full amount as per the purchase agreement, though he does not possess any legal title till 31.3.2015 since the transfer was not registered with the registration authority. However, for the purpose of claiming exemption under section 54, holding of legal title is not necessary. If the taxpayer pays the full consideration in terms of the purchase agreement within the stipulated period, the exemption under section 54 would be available. It was so held in *Balraj v. CIT(2002) 254 ITR 22 (Del.) and CIT v. Shahzada Begum (1988) 173 ITR 397 (A.P.).*

(4) The Finance (No.2) Act, 2014 has clarified that exemption under section 54 can be availed only in respect of one residential house. It would be more beneficial for

Mr. Rohan to claim exemption in respect of the Pune house since the cost of the same is higher than the cost of the Baroda house.

9. (i) Section 80-IB(13) provides that the provisions contained in section 80-IA(5) shall, so far as may be, apply to the eligible business under section 80-IB. Accordingly, for the purpose of computing the deduction under section 80-IB, the profits and gains of an eligible business shall be computed as if such eligible business was the only source of income of the assessee.

Therefore, Spectrum Limited should claim deduction under section 80-IB on profit from the eligible unit without setting off loss suffered in the other unit. It may be noted that the aggregate deduction under Chapter VIA, however, cannot exceed the gross total income of the assessee.

(ii) On this issue, the Delhi High Court, in *Praveen Soni v. CIT (2011) 333 ITR 324***,** held that the provisions of section 80-IB nowhere stipulated a condition that the claim for deduction under this section had to be made from the first year of qualification of deduction failing which the claim will not be allowed in the remaining years of eligibility. Therefore, the deduction under section 80-IB should be allowed to the assessee for the remaining years up to the period for which his entitlement would accrue, provided the conditions mentioned under section 80-IB are fulfilled.

Accordingly, Spectrum Ltd. can claim deduction for the remaining years during the period of eligibility, even if it has not claimed deduction in the first three years, subject to fulfilment of conditions mentioned in section 80-IB.

(iii) Under section 80-IB, where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking referred to in the section, there shall be allowed, in computing the total income of the assessee, a deduction from such profits and gains at the specified percentage and for such number of years as specified in the section.

In *Liberty India vs. CIT (2009) 317 ITR 218 (SC),* it was held that incentive profits are not profits derived from eligible business under section 80-IB. They belong to the category of ancillary profits of such undertaking.

Incentive profits such as DEPB/Duty drawback cannot be credited against the cost of manufacture of goods debited in the profit and loss account and they do not fall within the expression "profits derived from industrial undertaking" under section 80-IB. Hence, duty drawback receipts and DEPB benefits do not form part of the profits derived from the eligible business for the purpose of deduction under section 80-IB.

Therefore, Spectrum Ltd. cannot treat DEPB benefit and duty drawback as “profit derived from the industrial undertaking” for claiming benefit of deduction under section 80-IB.

(iv) On this issue, the Bombay High Court, in *CIT v. Jyoti Plastic Works Private Limited (2011) 339 ITR 491,* observed that the expression "worker" is neither defined under section 2 of the Income-tax Act, 1961, nor under section 80-IB(2)(iv) of the Act. Therefore, it would be reasonable to hold that the expression "worker" in section 80-IB(2)(iv) is referable to the persons employed by the assessee directly or by or through any agency (including a contractor) in the manufacturing activity carried on by the assessee. The employment of ten or more workers is what is relevant and not the mode and the manner in which the workers are employed by the assessee.

Further, the Delhi High Court has, in *CIT v. Nanda Mint and Pine Chemicals Ltd. (2012) 345 ITR 60,* observed that for compliance with the condition of employment of ten or more workers stipulated in section 80-IB(2)(iv), the contractual workers who were working under the direct supervision and control of the assessee and were paid salary by the assessee, are also to be considered.

Therefore, Spectrum Ltd. can treat the persons employed by it on contractual basis as "workers" to satisfy the condition of employment of ten or more workers as required under section 80-IB(2)(iv) for availing the benefit of deduction under section 80-IB, since the workers were employed throughout the year for the manufacturing process.

10. Computation of total income for A.Y.2015-16

	Particulars	Akash	Barun	Chirag
		₹	₹	₹
	Salary	8,73,000	9,87,000	10,92,000
	Income from house property ***[See Note 4]***		(2,00,000)	
	Income from other sources (Interest)	81,000	94,000	1,13,000
(A)	**Gross total income**	**9,54,000**	**8,81,000**	**12,05,000**
	Less: **Deductions under Chapter VIA**			
	Under section 80C			
	Five year term deposit with SBI ***[See Note 5]***	1,50,000		
	LIC premium paid ***[See Note 1]***			43,750
	Principal repayment of housing loan (restricted to ₹ 1,50,000) ***[See Note 5]***		1,50,000	
	Under section 80CCG			
	Investment in listed equity shares/units of equity oriented fund of Rajiv Gandhi Equity Savings Scheme ***[See Note 2]***	22,500	25,000	Nil

	Under section 80D			
	Medical insurance premium ***[See Note 3]***	15,000	Nil	15,000
	Under section 80EE			
	Interest on housing loan ***[See Note 5]***		10,000	
	Under section 80G			
	Contribution to National Children's Fund ***[See Note 6]***	45,000		
	Under section 80GGC ***[See Note 7]***			
	Donation to an electoral trust by account payee cheque		75,000	
	Cash donation to a political party		Nil	
(B)	**Total deduction under Chapter VIA**	**2,32,500**	**2,60,000**	**58,750**
(C)	**Total Income (A) – (B)**	**7,21,500**	**6,21,000**	**11,46,250**

Notes:

(1) Deduction u/s 80C in respect of life insurance premium paid by Mr. Chirag

Date of issue of policy	Person insured	Actual capital sum assured	Insurance premium paid during 2014-15	Restricted to % of sum assured	Deduction u/s 80C
22/8/2010	Self	80,000	18,000	20%	16,000
14/9/2012	Spouse	90,000	10,000	10%	9,000
20/6/2013	Handicapped Son (section 80U disability)	1,25,000	20,000	15%	18,750
			Total		**43,750**

(2) Deduction under section 80CCG in respect of investment made as per the Rajiv Gandhi Equity Savings Scheme

Particulars	Mr. Akash	Mr. Barun
	₹	₹
(i) Investment in listed equity shares	22,000	58,000
(ii) Investment in units of equity-oriented fund	23,000	-
Total investment	**45,000**	**58,000**
50% of the above	22,500	29,000
Deduction under section 80CCG (restricted to a maximum of ₹ 25,000)	**22,500**	**25,000**

	Mr. Chirag is not eligible for deduction under section 80CCG since his gross total income exceeds ₹ 12 lakh.
(3)	**Medical Insurance Premium** (i) Medical insurance premium of ₹ 18,000 paid by account payee cheque by Mr. Akash is allowed as a deduction under section 80D, subject to a maximum of ₹ 15,000. (ii) Medical insurance premium paid by cash is not allowable as deduction. Hence, Mr. Barun is not eligible for deduction under section 80D in respect of medical insurance premium of ₹ 12,000 paid in cash. (iii) Mr. Chirag is eligible for deduction of ₹ 15,000 under section 80D in respect of medical insurance premium paid by crossed cheque.
(4)	With effect from A.Y.2015-16, the maximum amount eligible for deduction under section 80C shall not exceed ₹ 1,50,000. Further, the limit in five year term deposit with bank has also been increased from ₹ 1,00,000 to ₹ 1,50,000. Since Mr. Akash has no other investment under section 80C during the P.Y.2014-15, Mr. Akash would be eligible for deduction of ₹ 1,50,000 in respect of investment in term deposit with bank.
(5)	**Deduction in respect of interest and principal repayment of housing loan** Mr. Barun is eligible for a maximum deduction of ₹ 2,00,000 under section 24 in respect of interest on housing loan taken in respect of a self-occupied property, for which he is claiming benefit of "Nil" annual value. Therefore, ₹ 2,00,000 would represent his loss from house property. ₹ 90,000 (₹ 2,40,000 - ₹ 1,50,000) is the amount remaining after providing for deduction of ₹ 1,50,000 under section 24 for the previous year 2013-14. The said amount of ₹ 90,000 would have been deductible under section 80EE in the A.Y.2014-15, since the following conditions are satisfied – (i) The loan is sanctioned by HDFC, a financial institution, during the period between 1.4.2013 and 31.3.2014; (ii) The loan amount sanctioned is less than ₹ 25 lakh; (iii) The value of the house property is less than ₹ 40 lakh; (iv) He does not own any other house property. Since the interest payable, allowed as deduction under section 80EE for A.Y.2014-15, was less than ₹ 1,00,000, Mr. Barun is now eligible for deduction of balance ₹ 10,000 (₹ 1,00,000 – ₹ 90,000) under section 80EE in the A.Y.2015-16. Further, with effect from A.Y.2015-16, the maximum amount eligible for deduction under section 80C is ₹ 1,50,000. Since, Mr. Barun has no other investment under section 80C during the previous year 2014-15, he would be eligible for deduction of ₹ 1,50,000 in respect of principal repayment of housing loan.

(6)	Contribution to National Children's Fund qualifies for 100% deduction under section 80G. Therefore, Mr. Akash is entitled to 100% deduction of the sum of ₹ 45,000 contributed by him by way of cheque to National Children's Fund.
(7)	Mr. Barun is eligible for deduction under section 80GGC in respect of donation to an electoral trust made otherwise than by way of cash. However, cash donations to a political party will not qualify for deduction under section 80GGC.

Note *– In case Mr. Akash sells all the units of equity oriented fund in June 2015, the amount of ₹ 11,500 (i.e., 50% of ₹ 23,000), being deduction allowed to him under section 80CCG in A.Y.2015-16, would be subject to tax in the A.Y.2016-17, since the condition of the minimum fixed lock-in period of one year from the end of P.Y.2014-15 stipulated under the Rajiv Gandhi Equity Scheme, 2013, has been violated in this case. However, in the case of Mr. Chirag, since deduction under section 80CCG was not allowed during the A.Y.2015-16 on account of his gross total income exceeding ₹ 12 lakh, no amount relating to that year can be subject to tax in the A.Y.2016-17, being the year of violation of condition.*

11. Computation of tax liability of Mr. Jacob for A.Y.2015-16

Particulars		**₹ in lakh**
Tax liability on total income of ₹ 82 lakhs under the normal provisions of the Income-tax Act, 1961 [₹ 1.25 lakhs (tax on income upto ₹ 10 lakhs) + 30% of ₹ 72 lakhs (₹ 82 lakhs – ₹ 10 lakhs)]		22.85
Add: Education cess and SHEC@3%		0.69
Total tax liability		**23.54**
Computation of Adjusted Total Income	**₹ in lakh**	
Total Income		82.00
Add: Deduction under section 35AD [150% of ₹ 70 lakhs]	105.00	
Less: Depreciation under section 32 [10% of ₹ 70 lakhs]	7.00	98.00
Adjusted Total Income		**180.00**
Computation of Alternate Minimum Tax (AMT)		**₹ in lakh**
Alternate Minimum Tax (AMT)@18.5%		33.30
Add: Surcharge@10% (since adjusted total income > ₹ 100 lakh)		3.33
		36.63
Add: Education cess@2% and SHEC@1%		1.10
Tax liability under section 115JC		**37.73**

Since the regular income-tax payable is less than the AMT payable, the adjusted total income of ₹ 180 lakhs shall be deemed to be the total income of Mr. Jacob and tax is payable@18.5% thereof plus surcharge@10% and cess@3%. Therefore, the tax liability is ₹ 37.73 lakhs.	
AMT Credit to be carried forward under section 115JD	
Tax liability under section 115JC	37.73
Less: Tax liability under the regular provisions of the Income-tax Act, 1961	23.54
	14.19

Notes:

(1) The Finance (No.2) Act, 2014 has brought the investment-linked tax deduction claimed under section 35AD within the scope of AMT. Accordingly, section 115JC has been amended to provide that total income shall be increased by the deduction claimed under section 35AD, as reduced by the depreciation allowable under section 32, as if no deduction under section 35AD was allowed in respect of the asset for which such deduction is claimed.

(2) The specified business of setting up and operating a cold chain facility is eligible for weighted deduction@150% of capital expenditure under section 35AD, if operations were commenced on or after 1.4.2012.

(3) AMT Credit can be carried forward for a maximum period of ten assessment years immediately succeeding the assessment year for which the tax credit becomes allowable. Such credit is allowed to be set-off against the tax payable on total income in an assessment year in which the tax is computed in accordance with the regular provisions of the Income-tax Act, 1961, to the extent of excess of such tax payable over the AMT of that year.

12. Computation of total income of Zeta Ltd. for the A.Y.2015-16

Particulars		₹	₹
Net profit as per profit and loss account			1,82,00,000
Add :	Depreciation debited to profit and loss account	32,00,000	
	Salary and purchase of materials for in-house research and development, considered separately under section 35(2AB) **[See Note 1]**	13,00,000	
	Legal expenses for issue of rights shares **[See Note 2]**	4,00,000	
	Under valuation of stock [₹ 32 lakhs - ₹ 22 lakhs] x 10/90 **[See Note 3]**	1,11,111	
	Payment in connection with voluntary retirement **[See Note 4]**	8,00,000	

	Provision for doubtful debts **[See Note 5]**	30,00,000	
	Amount paid to contractor without deduction of tax at source – 30% of Rs.8 lakh **[See Note 6]**	2,40,000	
	Cash donation to electoral trust **[See Note 7]**	12,00,000	1,02,51,111
			2,84,51,111
Less:	Deduction for in-house scientific research under section 35(2AB) **[See Note 1]**	62,00,000	
	Bad debts actually written off **[See Note 5]**	15,00,000	
	Depreciation as per section 32 **[See Note 8]**	27,35,000	1,04,35,000
Business Income / Gross Total Income			**1,80,16,111**
Less:	**Deduction under Chapter VI-A**		
	Under section 80GGB **[See Note 7]**		Nil
Total Income			**1,80,16,111**
Total Income (rounded off)			**1,80,16,110**

Tax on total income as computed under the Income-tax Act, 1961

Particulars	₹
Tax@30% on total income of ₹ 1,80,16,110	54,04,833
Add: Surcharge@5% (since total income exceeds ₹ 1 crore but does not exceed ₹ 10 crore)	2,70, 242
	56,75,075
Add: Education cess @ 2%	1,13,501
Secondary and higher education cess@1%	56,751
Tax on total income	**58,45,327**

Notes:

(1) Both revenue and capital expenditure (other than expenditure on land and building) on in-house scientific research approved by the prescribed authority is eligible for weighted deduction@200% under section 35(2AB) in case of, *inter alia,* a company engaged in manufacture or production of an article or thing.

In this case, the revenue expenditure on scientific research is ₹ 13 lakhs (salary and purchase of materials) and capital expenditure (i.e. machinery) on scientific research is ₹ 18 lakhs. The total expenditure of ₹ 31 lakhs qualifies for weighted deduction@200% under section 35(2AB), since the research and development facility is approved by the prescribed authority. Hence, the eligible deduction under section 35(2AB) is ₹ 62 lakhs, being 200% of ₹ 31 lakhs.

(2) There is no fresh inflow of funds or increase in capital employed on account of issue of bonus shares and there is only reallocation of the company's fund. Consequently, since there is no increase in the capital base of the company, legal expenses in connection with issue of bonus shares is a revenue expenditure and is hence, allowable as deduction. It was so held by the Supreme Court, in *CIT v. General Insurance Corpn. (2006) 286 ITR 232.*

However, ₹ 4 lakhs, being legal expenses in relation to issue of rights shares is directly related to expansion of the capital base of the company and is, hence, a capital expenditure. Therefore, the same is not allowable as deduction. It was so held by the Supreme Court in *Brooke Bond India Ltd. v. CIT (1997) 225 ITR 798*.

(3) The under valuation of both opening and closing stocks will have an impact on the profits for the year. The under-valuation in the amount of opening stock has to be deducted and under-valuation in the amount of closing stock has to be added back. In this case, since the under-valuation in the amount of closing stock exceeds the under-valuation in the amount of opening stock, the net difference in valuation of stock has, accordingly, been added back.

(4) As per section 35DDA, where in any previous year, any expenditure is incurred by way of payment of any sum to an employee in connection with voluntary retirement, one-fifth of the amount so paid shall be deducted in computing profits and gains of business for that previous year, and the balance shall be deducted in equal installments in the immediately succeeding four previous years. Therefore, out of ₹ 10,00,000, an amount of ₹ 2,00,000 is deductible in assessment year 2015-16 and the balance shall be disallowed in this assessment year. Therefore, ₹ 8,00,000 has to be added back.

(5) The deduction under section 36(1)(viia) for provision for doubtful debts is allowable only in case of banks and certain financial institutions specified thereunder. It is not allowable in case of other assessees. Therefore, the sum of ₹ 30 lakhs debited in its profit and loss account towards provision for doubtful debts is not an allowable deduction for Zeta Ltd., since it is a manufacturing company.

However, the amount actually written off as bad debts in the books of account can be claimed as deduction under section 36(1)(vii) in the case of all assessees. Hence, ₹ 15 lakhs, being the bad debts actually written off can be claimed as deduction under section 36(1)(vii).

(6) Disallowance under section 40(a)(ia) would be attracted in the P.Y.2014-15 in respect of payment to contractor without deduction of tax at source. In case the tax has been paid by the contractor (being a resident firm), the date on which it has furnished its return of income i.e., 31st July, 2015, would be deemed as the date of deduction and payment of taxes by Zeta Ltd.

Consequently, 30% of the payment would be disallowed under section 40(a)(ia) in the year in which the said expenditure is incurred. The same will be allowed as deduction

in the subsequent year in which the return of income is furnished by the resident payee, since tax is deemed to have been deducted and paid by Zeta Ltd. in that year.

(7) Donation given to electoral trust is not an allowable expenditure while computing business income. The same is also not allowable as deduction under section 80GGB from the gross total income, since it is paid in cash.

(8) Depreciation allowable under the Income-tax Act, 1961 has to be calculated after considering the following -

No deduction under any other provision of the Act shall be allowable in respect of expenditure which has been claimed as weighted deduction under section 35(2AB). Therefore, depreciation is not allowable in respect of ₹ 18 lakhs incurred on fixed assets, in respect of which weighted deduction@200% under section 35(2AB) has been claimed. Since the figure of ₹ 28 lakhs representing normal depreciation, includes depreciation on such fixed assets, the same has to be reduced from the said figure. Since the fixed assets were acquired only in February 2015, the depreciation would have been restricted to 7.5% (i.e., 50% of the normal rate of 15% applicable to plant and machinery). Therefore, 7.5% of ₹ 18 lakhs (cost of machinery) has to be reduced from the normal depreciation of ₹ 28 lakhs.

Further, additional depreciation under section 32 is not allowable in respect of such machinery, the whole of the actual cost of which has been allowed as deduction, whether by way of depreciation or otherwise. Accordingly, additional depreciation is not allowable in respect of new plant and machinery costing ₹ 18 lakhs which has been acquired for the purpose of in-house research and development, and is eligible for deduction under section 35(2AB). Therefore, additional depreciation is allowable only in respect of ₹ 7 lakhs (₹ 25 lakhs – ₹ 18 lakhs), being new machinery acquired other than for the purpose of in-house research and development. The additional depreciation is also restricted to 10% (i.e. 50% of 20%), since the new machinery is put to use for less than 180 days in the year.

Particulars	₹
Normal depreciation	28,00,000
Less: Depreciation @ 7.5% on ₹ 18 lakhs, being asset acquired for scientific research eligible for deduction u/s 35(2AB)	1,35,000
	26,65,000
Add: Additional depreciation on new plant and machinery@10% on ₹ 7 lakhs	70,000
Depreciation allowable under section 32	**27,35,000**

13. Chapter XII-DA, comprising of sections 115QA, 115QB and 115QC levies additional income-tax on buyback of unlisted shares by domestic companies. As per section 115QA, the distributed income would be subject to additional income-tax@20% (plus

surcharge@10% and education cess@2% and secondary and higher education cess@1%) in the hands of the domestic company. Distributed income is the consideration paid by the company for buyback of its own unlisted shares which is in excess of the sum received by the company at the time of issue of such shares.

Accordingly, Sigma Ltd is liable to pay ₹ 1,81,280 as additional income-tax, which is the amount calculated @22.66% (20% plus surcharge@10% plus cess@3%) on ₹ 8 lakh, being its distributed income (i.e., ₹ 22 lakh – ₹ 14 lakh).

The additional income-tax was payable on or before 30th September, 2014. However, the same was paid only on 11th December, 2014.

Interest under section 115QB is attracted@1% for every month or part of the month on the amount of tax not paid or short paid for the period beginning from the date immediately after the last date on which such tax was payable and ending with the date on which the tax is actually paid.

In this case, the period for which interest@1% per month or part of a month is leviable is calculated as under -

Period	No. of months/ part of month
1st October - 31st October, 2014 (whole of first month)	1
1st November – 30th November, 2014 (whole of second month)	1
1st December – 11th December, 2014 (part of third month)	1
Total number of months	**3**

Interest under section 115QB is payable @1% per month for 3 months on the amount of additional tax payable i.e., ₹ 1,81,280. Therefore, interest payable under section 115QB is ₹ 5,438.

The income arising to the shareholders in respect of such buyback of unlisted shares by Sigma Ltd. would be exempt under section 10(34A) in their hands.

14. (i) The scope of the term "intangible property" has been amplified to include, *inter alia*, technical knowhow, which is a technology related intangible asset. Transfer of intangible property falls within the scope of the term "international transaction". Since Beta Inc. guarantees not less than 10% of the borrowings of Alpha Ltd., Beta Inc. and Alpha Ltd. are associated enterprises. Therefore, since transfer of technical knowhow by Alpha Ltd., an Indian company, to Beta Inc., a French company, is an international transaction between associated enterprises, the provisions of transfer pricing are attracted in this case.

(ii) Purchase of tangible property falls within the scope of "international transaction". Tangible property includes plant and machinery. Rho Inc. and Phi Ltd. are associated enterprises, since Rho Inc., being a holding company of Phi Ltd., fulfils

the condition of holding shares carrying not less than 26% of the voting power in Phi Ltd. Therefore, purchase of plant and machinery by Phi Ltd., an Indian company, from Rho Inc., a Swedish company, is an international transaction between associated enterprises, and consequently, the provisions of transfer pricing are attracted in this case.

(iii) This transaction falls within the meaning of "specified domestic transaction" under section 92BA, since the salary payment has been made to a related person referred to in section 40A(2)(b) i.e., relative (i.e., daughter) of Ms. Nidhi, who is a director of Delta Ltd. However, such a transaction would be treated as a "specified domestic transaction" to attract transfer pricing provisions only if the aggregate of such transactions as specified in section 92BA during the year by Delta Ltd. exceeds a sum of ₹ 5 crore.

(iv) Unit Sun is eligible for deduction@100% of the profits derived from its eligible business (i.e., the business of developing an infrastructure facility, namely, a highway project in this case) under section 80-IA. However, Unit Moon is not engaged in any "eligible business". Since Unit Moon has transferred cement to Unit Sun at a price lower than the fair market value, it is an inter-Unit transfer of goods between eligible business and other business, where the consideration for transfer does not correspond with the market value of goods. Therefore, this transaction would fall within the meaning of "specified domestic transaction" to attract transfer pricing provisions, if the aggregate value of transactions specified in section 92BA during the year exceeds a sum of ₹ 5 crore.

(v) The *Explanation* to section 92B amplifies the scope of the term "international transaction". According to the said *Explanation*, international transaction includes, *inter alia*, provision of scientific research services. Sigma Inc. is a specified foreign company in relation to Theta Ltd. Therefore, the condition of Theta Ltd. holding shares carrying not less than 26% of the voting power in Sigma Inc is satisfied. Hence, Sigma Inc. and Theta Ltd. are associated enterprises. Since the provision of scientific research services by Sigma Inc. to Theta Ltd. is an "international transaction" between associated enterprises, transfer pricing provisions are attracted in this case.

15. The interest income received by Mr. Manas, a non-resident, from a notified infrastructure debt fund would be subject to a concessional tax rate of 5% under section 115A on the gross amount of such interest income. Therefore, the tax liability of Mr. Manas in respect of such income would be ₹ 32,188 (being 5% of ₹ 6,25,000 plus education cess@2% and secondary and higher education cess@1%).

Under section 194LB, tax is deductible @5% on interest paid by such fund to a non-resident. However, since Mr. Manas is a resident of a Notified Jurisdictional Area (NJA), tax would be deductible@30% as per section 94A, and not@ 5% specified under section 194LB. This is on account of the provisions of section 94A(5), which provides that

"**Notwithstanding anything contained in any other provision of this Act,** where a person located in a NJA is entitled to receive any sum or income or amount on which **tax is deductible under Chapter XVII-B,** the **tax shall be deducted at the highest of the following rates**, namely –

(a) at the rate or rates in force;

(b) at the rate specified in the relevant provision of the Act;

(c) at the rate of thirty per cent."

16. (i) The statement is not correct.

An income-tax authority acting under section 133A has the powers as conferred upon it under section 131(1), i.e., it has the same powers as are vested in a court under the Code of Civil Procedure, 1908, when trying a suit in respect of the following matters, namely, -

(1) discovery and inspection;

(2) enforcing the attendance of any person, including any officer of a banking company and examining him on oath;

(3) compelling the production of books of account and other documents; and

(4) issuing commissions.

Under section 131(3), an extended time limit of 15 days (exclusive of holidays) [as against time limit of 10 days under section 133A] has been provided upto which an income-tax authority may retain in his custody, books of account or other documents impounded, without obtaining the approval of the higher authorities specified thereunder i.e., Principal Chief Commissioner or Chief Commissioner, Principal Director General or Director General etc.

In order to align the time period under section 133A with the time period under section 131(3), section 133A(3) has been amended to provide that an income-tax authority shall not retain in his custody any such books of account or other documents for a period exceeding **fifteen days** (exclusive of holidays) without obtaining the approval of the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General or Principal Commissioner or Commissioner or Principal Director or Director therefor, as the case may be.

(ii) The statement is correct.

New sub-section (2A) has been inserted in section 133A to provide that an income-tax authority may, **for the purpose of verifying that tax has been deducted or collected at source in accordance with the provisions of Chapter XVII-B or Chapter XVII-BB**, as the case may be, enter-

(1) any office, or a place where business or profession is carried on, within the limits of the area assigned to him, or

(2) any such place in respect of which he is authorised for the purposes of this section by such income-tax authority who is assigned the area within which such place is situated, where books of account or documents are kept.

The income-tax authority may, for this purpose, enter an office, or a place where business or profession is carried on after sunrise and before sunset.

Further, such income-tax authority may require the deductor or the collector or any other person who may at the time and place of survey be attending to such work,—

(1) to afford him the necessary facility to inspect such books of account or other documents as he may require and which may be available at such place, and

(2) to furnish such information as he may require in relation to such matter.

An income-tax authority may -

(1) place marks of identification on the books of account or other documents inspected by him and take extracts and copies thereof;

(2) record the statement of any person which may be useful for, or relevant to, any proceeding under the Act.

Note *- While acting under section 133A(2A), the income-tax authority, however, shall* ***not*** *impound and retain in his custody, any books of account or documents inspected by him or make an inventory of any cash, stock or other valuable articles or thing checked or verified by him.*

17. The time limits for completion of such assessments are given in section 153.

(i) 31st March, 2017, being two years from the end of A.Y.2014-15, which is the assessment year in which the income was first assessable.

(ii) 31st March, 2015, being one year from the end of F.Y.2013-14, the year in which notice under section 148 was served.

(iii) 31st March, 2017, being three years from the end of A.Y.2013-14, which is the assessment year in which the income was first assessable

18. The scope of advance rulings has been expanded by the Finance (No.2) Act, 2014 by including a determination by the Authority for Advance Rulings(AAR) in relation to the tax liability of a resident applicant, arising out of a transaction which has been undertaken or is proposed to be undertaken by such applicant within the definition of "advance ruling" under section 245N(a). Consequently, a resident referred to in section 245N(a)(iia) falling within any such class or category of persons as the Central Government may notify in this behalf has been included in the definition of "applicant" under section 245N(b).

In order to cope up with the resultant increase in the number of cases before the AAR, the constitution of the AAR has been strengthened by stepping up its composition, constituting benches to be located in different parts of the country and specifying the composition of these benches.

The Authority for Advance Rulings would now consist of a Chairman and such number of Vice Chairman, revenue Members and law Members as the Central Government may by notification appoint. The Chairman has to be a person who has been a judge of the Supreme Court; A person who has been a Judge of a High Court would qualify for appointment as a Vice Chairman; A Revenue Member from the Indian Revenue Service has to be a person who is a Principal Chief Commissioner or Principal Director General or Chief Commissioner or Director General**;** A law Member from the Indian legal service has to be a person who is an Additional Secretary to the GoI.

Sub-section (6) of section 245-O provides for constitution of benches and sub-section (7) provides for the composition of these benches. The powers and functions of the AARs may be discharged by its Benches as may be constituted by the Chairman from amongst its Members thereof. The Bench shall consist of

- the Chairman or the Vice-Chairman;
- one revenue member; and
- one law member.

The Bench shall be located at such places as the Central Government may, by notification, specify.

Thus, through these provisions, the scope of advance rulings has been expanded and the constitution of the Authority for Advance Rulings has been strengthened by the Finance (No.2) Act, 2014, thereby underlining the significance of advance rulings in minimising tax litigation.

19. (i) Where a person who is required to furnish a statement under section 285BA(1), has not furnished the same within the specified time, the prescribed income-tax authority may serve upon such person a notice requiring him to furnish such statement within a period not exceeding thirty days from the date of service of such notice and the statement has to be furnished within the time specified in the notice [Section 285BA(5)].

In this case, since the prescribed reporting financial institution has not furnished a statement under section 285BA(1), therefore, the prescribed income-tax authority may serve a notice requiring it to furnish such statement within a period not exceeding 30 days from the date of service of such notice.

(ii) If the person, being a prescribed reporting financial institution, having furnished a statement under section 285BA(1), or in pursuance of a notice issued under section 285BA(5), comes to know or discovers any inaccuracy in the information provided in the statement, it shall, within a period of ten days inform the income-tax authority or other authority or agency referred to in section 285BA(1), the inaccuracy in such statement and furnish the correct information in the prescribed manner [Section 285BA(6)].

(iii) New section 271FAA has been inserted to provide for levy of penalty in case of a person, being a prescribed reporting financial institution, who is required to furnish a statement of financial transaction or reportable account, where such person provides inaccurate information in the statement.

In such a case, the prescribed income-tax authority may direct levy of penalty of ₹ 50,000, subject to further satisfaction of any one of the following conditions –

(1) The inaccuracy is due to a failure to comply with the due diligence requirement prescribed under section 285BA(7) or is deliberate on the part of that person; or

(2) The person is aware of the inaccuracy at the time of furnishing the statement of financial transaction or reportable account, but does not inform the prescribed income-tax authority or such other authority or agency; or

(3) The person discovers the inaccuracy after furnishing the statement of financial transaction or reportable account but fails to inform and furnish correct information within ten days, being the time specified under section 285BA(6).

20. (i) Since the annual premium does not exceed 20% of sum assured in respect of a policy taken before 1.4.2012, the maturity proceeds of ₹ 5.25 lakhs payable on 31.3.2015 are exempt under section 10(10D) in the hands of Mr. Shiva. Hence, no tax is required to be deducted at source under section 194DA on such sum payable to Mr. Shiva.

(ii) Since the annual premium exceeds 10% of sum assured in respect of a policy taken on 1.4.2012, the sum of ₹ 3.20 lakhs due to Mr. Vishnu would not be exempt under section 10(10D) in his hands. Therefore, tax is required to be deducted@2% under section 194DA on the maturity proceeds of ₹ 3.20 lakhs payable to Mr. Vishnu, at the time of payment.

(iii) Even though the annual premium exceeds 20% of sum assured in respect of a policy taken before 1.4.2012, and consequently, the maturity proceeds of ₹ 98,000 would not be exempt under section 10(10D) in the hands of Mr. Ganesh, the tax deduction provisions under section 194DA are not attracted since the maturity proceeds are less than ₹ 1 lakh.

(iv) Even though the annual premium exceeds 20% of sum assured in respect of a policy taken before 1.4.2012, and consequently, the maturity proceeds of ₹ 4,50,000 would not be exempt under section 10(10D) in the hands of Mr. Krishna, the tax deduction provisions under section 194DA are not attracted since the maturity proceeds are payable on 31.8.2014 and the TDS provisions under section 194DA are effective only from 1.10.2014.

Applicability of Finance Act, Assessment Year etc. for November, 2015 – Final Examination

Paper 7 : Direct Tax Laws & Paper 8 : Indirect Tax Laws

The provisions of direct and indirect tax laws, as amended by the Finance (No.2) Act, 2014, including notifications and circulars issued up to 30th April, 2015, are applicable for November, 2015 examination. The relevant assessment year for Paper 7: Direct Tax Laws is A.Y.2015-16.

In Paper 7: Direct Tax Laws, the Wealth-tax Act, 1957 and Rules thereunder are **not** applicable for November 2015 examination.

ANNEXURE

Part – I: Statutory Update – Direct Tax Laws

Significant Notifications and Circulars issued between 1st May, 2014 and 30th April, 2015

Study Material for Direct Tax Laws [November, 2014 edition] contains all the relevant amendments made by the Finance (No.2) Act, 2014 and circulars/notifications issued up to 30.04.2014. However, for students appearing in November, 2015 examination, amendments made by notifications, circulars and other legislations made between 01.05.2014 and 30.04.2015 are also relevant. Such amendments are given hereunder:-

I. NOTIFICATIONS

1. Notification of Cost Inflation Index for F.Y.2014-15 (Notification No. 31/2014, dated 11-6-2014)

The Central Government has, in exercise of the powers conferred by *clause (v) of Explanation to section 48*, vide this notification specified the Cost Inflation Index for the financial year 2014-15 as 1024.

S. No.	Financial Year	Cost Inflation Index	S. No.	Financial Year	Cost Inflation Index
1.	1981-82	100	18.	1998-99	351
2.	1982-83	109	19.	1999-2000	389
3.	1983-84	116	20.	2000-01	406
4.	1984-85	125	21.	2001-02	426
5.	1985-86	133	22.	2002-03	447
6.	1986-87	140	23.	2003-04	463
7.	1987-88	150	24.	2004-05	480
8.	1988-89	161	25.	2005-06	497
9.	1989-90	172	26.	2006-07	519
10.	1990-91	182	27.	2007-08	551
11.	1991-92	199	28.	2008-09	582
12.	1992-93	223	29.	2009-10	632
13.	1993-94	244	30.	2010-11	711
14.	1994-95	259	31.	2011-12	785
15.	1995-96	281	32.	2012-13	852
16.	1996-97	305	33.	2013-14	939
17.	1997-98	331	**34.**	**2014-15**	**1024**

2. Increase in ceiling limit for investment in Public Provident Fund [Notification No. G.S.R. 588 (E), dated 13-8-2014]

In exercise of the powers conferred by Section 3(4) of the Public Provident Fund Act, 1968, the Central Government has increased annual ceiling limit for deposit in PPF A/c from ₹ 1 lakh to ₹ 1.50 lakhs by amending the Public Provident Fund Scheme, 1968.

3. Rate of depreciation in respect of windmills installed on or after 01.04.2014 (Notification No. 43/2014, dated 16-9-2014)

The Central Board of Direct Taxes has, vide this notification amended the rate of depreciation on certain renewable energy devices. Accordingly, the following renewable energy devices would be eligible for depreciation @80% from A.Y. 2015-16, if they are installed on or after 1st April 2014 –

(a) Wind mills and any specially designed devices which run on wind mills;

(b) Any special devices including electric generators and pumps running on wind energy

This implies that if the aforesaid renewable energy devices were installed on or before 31st March 2014, they would be eligible for depreciation @ 15% from A.Y. 2015-16.

The applicable rate of depreciation for A.Y. 2014-15 and A.Y. 2015-16, based on date of installation of such renewable energy devices, have been tabulated hereunder for a better understanding of the amendment made vide this notification.

Date of installation	Rate of depreciation	
	A.Y. 2014-15	A.Y. 2015-16
On or before 31.03.2012	80%	15%
Between 1.04.2012 to 31.03.2014	15%	15%
On or after 01.04.2014	N.A	80%

4. Commissioner of Income-tax (Exemptions) to act as "prescribed authority" for the purposes of section 10(23C)(iv)/(v)/(vi)/(via) [Notification Nos. 75/2014 & 76/2014 dated 1-12-2014]

For the purposes of claiming exemption under section 10(23C)(iv) and (v), a fund or institution established for charitable purposes and/or a trust or institution wholly for public religious purposes or wholly for public religious and charitable purposes, requires approval of the "prescribed authority".

Likewise, for the purposes of claiming exemption under section 10(23C)(vi) and (via), any university or other educational institution, existing solely for educational purposes and not for purposes of profit and any hospital or other institution, existing solely for philanthropic purposes and not for profit motive, requires approval of the "prescribed authority".

Accordingly, the CBDT has, through these notifications, authorized the Commissioner of Income-tax (Exemptions) to act as "prescribed authority" for the purpose of section 10(23C)(iv)/(v)/(vi)/(via) w.e.f. 15th November, 2014.

5. Percentage of Government grant for determining whether a university or other educational institution, hospital or other institution referred under section 10(23C)(iiiab)/(iiiac) is substantially financed by the Government prescribed [Notification No. 79/2014, dated 12-12-2014]

Income of certain educational institutions, universities and hospitals which exist solely for educational purposes or solely for philanthropic purposes, and not for purposes of profit and **which are wholly or substantially financed by the Government** are exempt under section 10(23C).

The Finance (No. 2), Act, 2014 inserted an *Explanation* after section 10(23C)(iiiac) to clarify that if the government grant to a university or other educational institution, hospital or other institution during the relevant previous year **exceeds a prescribed percentage of the total receipts** (including any voluntary contributions), of such university or other educational institution, hospital or other institution, as the case may be, then, such university or other educational institution, hospital or other institution shall be considered as being **substantially financed by the Government** for that previous year.

Accordingly, in exercise of the powers conferred by section 295 read with section 10(23C)(iiiab)/(iiiac), the CBDT has notified Rule 2BBB to provide that any university or other educational institution referred under section 10(23C)(iiiab) and hospital or other institution referred under section 10(23C)(iiiac) shall be considered as being substantially financed by the Government for any previous year, if the Government grant to such university or other educational institution, hospital or other institution **exceeds 50% of the total receipts including any voluntary contributions,** of such university or other educational institution, hospital or other institution, as the case may be, during the relevant previous year.

6. Deposit in 'Sukanya Samriddhi Account' eligible for deduction under section 80C(2)(viii) [Notification No.9/2015, dated 21-1-2015]

Section 80C provides for deduction from gross total income in respect of sums paid and investments made through specified modes like life insurance premia, Public Provident Fund etc. Under clause (viii) of section 80C(2), deduction is available in respect of sums paid or deposited in the previous year by the assessee as subscription to any such deposit scheme as may be notified by the Central Government.

Accordingly, the Central Government, in exercise of the powers conferred by section 80C(2)(viii) of the Income-tax Act, 1961, has specified the ***'Sukanya Samriddhi Account'*** scheme for the welfare of Girl child.

7. Safe Harbour Rules notified for Specified Domestic Transactions in respect of a Government company engaged in business of generation, transmission or distribution of electricity [Notification No.11/2015, dated 4-2-2015]

Section 92CB(1) provides that the determination of arm's length price under section 92C or section 92CA shall be subject to safe harbour rules. Section 92CB(2) empowers the CBDT to prescribe safe harbour rules.

Safe harbour means circumstances in which the income tax authorities shall accept the transfer price declared by the assessee.

Accordingly, in exercise of the powers conferred by section 92CB read with section 295 of the Income-tax Act, 1961, the CBDT had, vide Notification No. 73/2013, dated 18.09.2013, prescribed safe harbour rules in respect of international transactions.

The CBDT has, vide this notification, in exercise of the powers conferred by section 92CB and 92D, read with section 295, inserted Rules 10TH, 10THA, 10THB, 10THC & 10THD providing the safe harbour rules for specified domestic transactions.

Rule	Rule heading	Particulars
10TH	**Definitions:** Appropriate Commission	Meaning assigned to it in section 2(4) of the Electricity Act, 2003. Appropriate Commission means the Central Regulatory Commission referred to in sub-section (1) of section 76 or the State Regulatory Commission referred to in section 82 or the Joint Commission referred to in section 83, as the case may be.
	Government Company	Meaning assigned to it in section 2(45) of the Companies Act, 2013. Government company means any company in which not less than 51% of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company.
10THA	Eligible assessee	• A person who has exercised a valid option for application of safe harbour Rules in accordance with the provisions of Rule 10THC, **AND** • is a Government company engaged in the business of generation, transmission or distribution of electricity.
10THB	Eligible Specified Domestic Transaction	A specified domestic transaction undertaken by an eligible asseessee and which comprises of: (i) supply of electricity by a generating company; or (ii) transmission of electricity; or (iii) wheeling of electricity.
10THC	Safe harbour	(1) Where an eligible assessee has entered into an eligible specified domestic transaction in any previous year relevant to an assessment year and the option exercised by the said assessee is treated to be validly exercised under Rule 10THD, the transfer price

<table>
<tr><td></td><td></td><td>declared by the assessee in respect of such transaction for that assessment year shall be accepted by the income-tax authorities, if it is in accordance with the circumstances specified in Rule 10THC(2).
(2) The following are the circumstances in respect of the eligible specified domestic transaction.
<table>
<tr><th>S. No.</th><th>Eligible specified domestic Transaction</th><th>Circumstances</th></tr>
<tr><td>1</td><td>Supply of electricity, transmission of electricity, wheeling of electricity</td><td>The tariff in respect of supply of electricity, transmission of electricity, wheeling of electricity, as the case may be, is determined by the Appropriate Commission in accordance with the provisions of the Electricity Act, 2003.</td></tr>
</table>
(3) No comparability adjustment and allowance under the second proviso to section 92C(2) shall be made to the transfer price declared by the eligible assessee and accepted by the income-tax authority.
(4) The provisions of sections 92D relating to maintenance and keeping of information and document and section 92E for submission of report from an accountant in respect of a specified domestic transaction shall apply irrespective of the fact that the assessee exercises his option for safe harbour in respect of such transaction.</td></tr>
<tr><td>10THD</td><td>Procedure</td><td><u>Furnishing of Form 3CEFB</u>
The assessee shall furnish a Form 3CEFB, complete in all respects, to the Assessing Officer on or before the due date for furnishing the return of income for the relevant assessment year specified in Explanation 2 to section 139(1), for exercising the option of safe harbour.
The return of income should be furnished on or before the date of submitting the Form 3CEFB.
However, in respect of eligible specified domestic transactions undertaken during the previous year relevant to the assessment year 2013-14 or 2014-15, Form 3CEFB can be furnished by the assessee on or before 31st March, 2015.</td></tr>
</table>

		Order by Assessing Officer The Assessing Officer shall pass the order declaring the option exercised by the assessee as invalid within a period of 3 months from the end of the month in which Form 3CEFB is received by him. No order can be passed declaring the option exercised by the assessee invalid unless an opportunity of being heard is given to him. **Filing of objections against the order of Assessing Officer by the assessee** If the assessee objects to the order of the Assessing Officer declaring the option to be invalid, he may file his objections with the Principal Commissioner or the Commissioner or the Principal Director or the Director, as the case may be, to whom the Assessing Officer is subordinate, **within 15 days of receipt of the order of the Assessing Officer.** The Principal Commissioner or Commissioner or Principal Director or Director, as the case may be, shall, after providing an opportunity of being heard to the assessee, pass appropriate order, **within a period of 2 months from the end of the month** in which the objection filed by the assessee is received by him, in respect of the validity or otherwise of the option exercised by the assesee. If the Assessing Officer or the Principal Commissioner or the Commissioner or the Principal Director or the Director, as the case may be, does not pass an order within the specified time, then the option for safe harbour exercised by the assessee shall be treated as valid.

Information and documents to be maintained under section 92D in respect of eligible specified domestic transaction [Rule 10D(2A)]

Section 92D provides that every person who has entered into an international transaction or specified domestic transaction shall keep and maintain prescribed information and document.

Rule 10D(1) provides for information and documents to be maintained under section 92D. Sub-rule (2A) has been inserted in Rule 10D to provide that nothing contained in Rule 10D(1) in so far as it relates to specified domestic transaction referred to in Rule 10THB, shall apply in the case of an eligible assessee referred to in Rule 10THA.
The information and documents to be maintained by an eligible assessee referred to in Rule 10THA relating to an eligible specified domestic transaction referred to in Rule 10THB are given in Rule 10D(2A) as follows:

(i) a description of the ownership structure of the assessee enterprise with details of shares or other ownership interest held therein by other enterprises;

(ii) a broad description of the business of the assessee and the industry in which the assessee operates, and of the business of the associated enterprises with whom the assessee has transacted;

(iii) the nature and terms (including prices) of specified domestic transactions entered into with each associated enterprise and the quantum and the value of each such transaction or class of such transaction;

(iv) a record of proceedings if any before the regulatory commission and orders of such commission relating to the specified domestic transaction;

(v) a record of the actual working carried out for determining the transfer price of the specified domestic transaction;

(vi) the assumptions, policies and price negotiations, if any, which have critically affected the determination of the transfer price;

(vii) any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the transfer price

8. Rules for rollback of an Advance Pricing Agreement notified [Notification No. 23/2015, dated 14-03-2015]

Section 92CC empowers the CBDT to enter into an advance pricing agreement with any person, determining the arm's length price or specifying the manner in which arm's length price is to be determined in relation to an international transaction to be entered into by that person.

The CBDT can do so with the approval of the Central Government. Section 92CC(9) empowers the CBDT to prescribe a scheme specifying therein the manner, form and procedure in respect of such advance pricing agreement. Further, to reduce current pending as well as future litigation in respect of the transfer pricing matters, section 92CC(9A) provides a roll back mechanism in the advance pricing agreement scheme. Accordingly, the advance pricing agreement may, subject to such prescribed conditions, procedure and manner, provide for determining the arm's length price or for specifying the manner in which arm's length price is to be determined in relation to an international transaction entered into by a person **during any period not exceeding four previous years preceding the first of the previous years** specified in the agreement and the arms length price of such international transaction shall be determined in accordance with the said agreement.

The CBDT has, vide this notification, in exercise of the powers conferred by section 92CC(9) and 92CC(9A) read with section 295, prescribed the following conditions, procedure and manner for determining the arm's length price or for specifying the manner in which arm's length price is to be determined in relation to an international transaction:

Rule	Particulars	Amendment
10F(ba)	Definition of Applicant	A person who has made an application.
10F(ha)	Definition of Rollback year	Any previous year, falling within the period **not exceeding four previous years,** preceding the first of the five consecutive previous years referred to in section 92CC(4).

10H(1)	Pre-filing consultation	**Any** person proposing to enter into an agreement under these rules **may**, by an application in writing, make a request for a pre-filing consultation. Making a request for a pre-filing consultation has, therefore, become optional. As per Rule 10H(5), the pre-filing consultation shall, among other things, - (i) determine the scope of the agreement (ii) identify transfer pricing issues (iii) determine the suitability of international transaction for the agreement. (iii) discuss broad terms of the agreement
10-I	Application for advance pricing agreement.	Earlier, any person who has entered into a pre-filing consultation as referred to in Rule 10H was eligible to file an application for advance pricing agreement. This rule has now been amended to provide that any person referred to in Rule 10G i.e. any person who has undertaken an international transaction or is contemplating to undertake an international transaction will be eligible to make an application for advance pricing agreement. Therefore, an application requesting for pre-filing consultation is not mandatory for making an application for advance pricing agreement.
10M	Terms of the agreement	Rule 10M provides for the terms of the advance pricing agreement. Rule 10M(1) provides that an agreement may among other things, include, the international transactions covered by the agreement, the agreed transfer pricing methodology, if any, the determination of ALP, if any etc.. Clause (va) has now been inserted in Rule 10MA(1) to include rollback provision referred to in Rule 10MA.
10MA	Roll back of the agreement	The said rule provides the following: 1. the agreement may provide for determining the arm's length price or specify the manner in which arm's length price shall be determined in relation to the international transaction entered into by the person during the rollback year (hereinafter referred as "rollback provision"). 2. **Conditions for applying for rollback provisions:** The agreement shall contain rollback provision in respect of an international transaction subject to the following, namely:- (i) the international transaction is same as the

		international transaction to which the agreement (other than the rollback provision) applies; (ii) the return of income for the relevant rollback year has been or is furnished by the applicant before the due date as specified in *Explanation 2* of section 139(1). (iii) the report in respect of the international transaction had been furnished in accordance with section 92E; (iv) the applicability of rollback provision, in respect of an international transaction, has been requested by the applicant for all the rollback years in which the said international transaction has been undertaken by the applicant; and (v) the applicant has made an application seeking rollback in Form 3CEDA in accordance with sub-rule (5); 3. **Non-applicability of Rollback provision:** Rollback provision shall not be provided in respect of an international transaction for a rollback year, if,- (i) The determination of arm's length price of the said international transaction for the said year has been subject matter of an appeal before the Appellate Tribunal and the Appellate Tribunal has passed an order disposing of such appeal at any time before signing of the agreement; or (ii) the application of rollback provision has the effect of reducing the total income or increasing the loss, as the case may be, of the applicant as declared in the return of income of the said year. 4. **Manner for determining arm length price to be the same for rollback years and other previous years:** Where the rollback provision specifies the manner in which arm's length price shall be determined in relation to an international transaction undertaken in any rollback year then such manner shall be the same as the manner which has been agreed to be provided for determination of arm's length price of the same international transaction to be undertaken in any previous year to which the agreement applies, not being a rollback year.

		5. **Time limit for filling application for rollback provision:** The applicant may furnish along with the application for advance pricing agreement, the request for rollback provision in Form No. 3CEDA with proof of payment of an additional fee of ₹ 5 lakh at any time – (i) before the first day of the previous year relevant to the first assessment year for which the application for advance pricing agreement is made, in respect of transactions which are of a continuing nature from dealings that are already occurring; or (ii) before undertaking the transaction in respect of remaining transactions. [However, where an application has been filed before 31.03.2015, application for rollback provision along with the proof of payment of additional fee may be filed at any time on or before the 30.6.2015 or the date of entering into the agreement, whichever is earlier. Further, where an agreement has been entered into on or before 31.03.2015, application for rollback provision along with the proof of payment of additional fee may be filed at any time on or before 30.06.2015 and such agreement may be revised to provide for the rollback provision notwithstanding anything contained in Rule 10Q (which provides for revision of advance pricing agreement)][1].
10RA	Procedure for giving effect to rollback provision of an Agreement	Rule 10RA has been inserted to provide the "Procedure for giving effect to rollback provision of an Agreement" as follows: (i) The applicant shall furnish **modified return of income** referred to in section 92CD in respect of a rollback year to which the agreement applies along with the proof of payment of any additional tax arising as a consequence of and computed in accordance with the rollback provision. (ii) The modified return in respect of rollback year shall be furnished along with the modified return to be furnished in respect of first of the previous years for which the agreement has been requested for in the application.

[1] As amended by Notification No.33/2015, dated 01.04.2015

		(iii) If any appeal filed by the applicant is pending before the Commissioner (Appeals), Appellate Tribunal or the High Court for a rollback year, on the issue which is the subject matter of the rollback provision for that year, the said appeal to the extent of the subject covered under the agreement shall be withdrawn by the applicant before furnishing the modified return for the said year. (iv) If any appeal filed by the Assessing Officer or the Principal Commissioner or Commissioner is pending before the Appellate Tribunal or the High Court for a rollback year, on the issue which is subject matter of the rollback provision for that year, the said appeal to the extent of the subject covered under the agreement, shall be withdrawn by the Assessing Officer or the Principal Commissioner or the Commissioner, as the case may be, within three months of filing of modified return by the applicant. (v) The applicant, the Assessing Officer or the Principal Commissioner or the Commissioner, shall inform the Dispute Resolution Panel or the Commissioner (Appeals) or the Appellate Tribunal or the High Court, as the case may be, the fact of an agreement containing rollback provision having been entered into along with a copy of the same as soon as it is practicable to do so. (vi) In case effect cannot be given to the rollback provision of an agreement in accordance with this rule, for any rollback year to which it applies, on account of failure on the part of applicant, the agreement shall be cancelled. Consequently, clause (iv) of Rule 10R(1) providing for cancellation of agreement, has been amended to provide that the CBDT shall cancel an agreement if it is to be cancelled under Rule 10RA.

9. Notification of class of persons, for determination of tax liability by Authority for Advance Ruling (AAR) in relation to the tax liability of a resident applicant falling within such class [Notification No. 73/2014, dated 28-11-2014]

Sub-clause (iia) has been inserted in Section 245N(a) defining "advance ruling" by the Finance (No.2) Act, 2014, to include a determination by the AAR in relation to the tax liability of a resident applicant, arising out of a transaction which has been undertaken or is proposed to be undertaken by such applicant. Further, sub-clause (iia) has been inserted in section 245N(b) defining an "applicant" to include thereunder, any person who

is a resident referred to section 245N(a)(iia) falling within such class or category of persons as the Central Government may specify by notification.

Accordingly, the Central Government has, vide this notification, in exercise of the powers conferred by section 245N(b)(iia), specified such class of persons, so that a resident falling within such class of persons would qualify as an "applicant" under section 245N(b). Accordingly, a resident, in relation to his tax liability arising out of **one or more transactions valuing ₹ 100 crore or more in total** which has been undertaken or proposed to be undertaken, would be an "applicant" for the purposes of Chapter XIX-B of the Income-tax Act, 1961.

II. CIRCULARS

1. Eligibility of deduction under section 80-IA for unexpired period, in case of an undertaking or enterprise developing an infrastructure facility, industrial park, SEZ and transferring the same to another enterprise or undertaking for operation and maintenance [Circular No. 10/2014 dated 06-05-2014]

Under section 80-IA, deduction is available in respect of profits & gains derived by an undertaking or enterprise engaged in developing, operating and maintaining any infrastructure facility, industrial park etc. The undertakings or enterprises eligible for availing deduction under this section have been specified under sub-section (4) of section 80-IA and can broadly be classified as under:

(i) enterprise carrying on the business of developing or operating & maintaining or developing, operating & maintaining infrastructure facilities [80-IA(4)(i)];

(ii) undertaking providing basic or cellular telecommunication services [80-IA(4)(ii)];

(iii) undertaking which develops, develops & operates or maintains & operates an industrial park or SEZ [80-IA(4)(iii)];

(iv) undertaking set up for generation / generation & distribution of power or laying of network / renovation or modernization of network of transmission / distribution lines [80-IA(4)(iv)] or

(v) set up for reconstruction or revival of power generation plant [80-IA(4)(v)].

The provisions of section 80-IA also contain the conditions to be satisfied for being eligible for deduction. As per section 80-IA(3), undertakings mentioned in (ii) and (iv) above **should <u>not</u> be formed by splitting up or reconstruction of an existing business**.

The proviso to clause (i) and clause (iii) of sub-section (4) of section 80-IA deal with the situation where operation and maintenance of infrastructure facility or operation and maintenance of industrial park / SEZ, respectively, is transferred to another enterprise in the manner provided therein and **the transferee undertaking <u>can</u> avail deduction for the unexpired period**.

Section 80-IA(12A) provides that where the enterprise or undertaking of an Indian Company entitled to the deduction under the said section is transferred on or after 01.04.2007 in a scheme of amalgamation or demerger, **<u>no</u>** deduction shall be available to

the amalgamated or the resulting company.

The vital factor in determining the eligibility criteria for availing deduction u/s 80-IA would be verification of factual issues so as to ascertain whether

(a) there has been splitting up or reconstruction of a business already in existence,

(b) transfer is in accordance with the proviso to clause (i) or clause (iii) of sub-section (4) of section 80-IA, or

(c) transfer of an enterprise or undertaking is in a scheme of amalgamation or demerger.

The CBDT has, through this circular, clarified that if –

(i) an enterprise or undertaking develops an infrastructure facility, industrial park or special economic zone, as the case may be; **and**

(ii) transfers it to another enterprise or undertaking for operation and maintenance in accordance with the proviso to clause (i) or clause (iii) of sub-section (4) of section 80-IA; **and**

(iii) this transfer is **not** by way of amalgamation or demerger,

(iv) the transferee **shall be eligible** for the deduction for the unexpired period.

The profit for the purposes of deduction in the case of transferee shall be computed in accordance with sub-sections (5) to (10) of section 80-IA.

2. Taxation of Alternative Investment Funds having status of Non-charitable trusts under Income-tax Act, 1961 [Circular No. 13/2014, dated 28-07-2014]

The SEBI (Alternative Investment Funds) Regulations, 2012 (AIF Regulations), aims at regulating all forms of private pool of funds in India. These regulations divide AIFs into three broad categories – Category I, Category II and Category III AIFs, on the basis of the operational strategies, objectives and fund structure. Category I AIFs include Venture Capital Funds which are established as a trust and Venture Capital Companies. Category I AIFs are eligible for "pass through status" under section 10(23FB) read with section 115U, in respect of income which arises to the fund from investment in venture capital undertaking (VCU), provided they comply with the additional conditions laid down under the Income-tax Act, 1961. Such income accruing or arising or received by a person out of investment made in a Category I AIF fulfilling the prescribed conditions under the Income-tax Act, 1961 shall be taxable in the like manner as if the person had made a direct investment in the VCU. In effect, the VCF (falling under Category I AIF) enjoys a pass through status in respect of such income under section 10(23FB).

A large number of AIF's registered with SEBI have been set up in the form of non-charitable trusts. In this regard, clarification was sought from the CBDT about tax treatment in cases of AIFs being non-charitable trusts where the name of investor and beneficial interest are not explicitly known on the date of its creation owing to such information becoming available only when the fund starts accepting contributions from the investors. The issue is whether the income of such funds would be taxable in the

hands of the trustees of the AIF in the capacity of a 'Representative assessee as defined in section 160(1)(iv) or in the hands of investors.

In this regard, the CBDT has clarified that where the trust deed does not specify the name of investors or their beneficial interests, the provisions of section 164(1) would apply and the entire income of fund shall be liable to be taxed at Maximum Marginal Rate of income tax in the hands of the trustees of such AIF's in their capacity as 'Representative Assessee'. Consequently, the provisions of section 166 need not be invoked in the hands of the investor, as the income has already been subject to the tax in the hands of the Representative Assessee in accordance with section 164(1).

However, in case of funds, where the name of beneficiaries and their interest in the Fund are determined i.e., stated in the trust deed, the tax on whole of the income of the fund - consisting of or including profit and gains of business, would be leviable upon the trustees of such AIF, being 'Representative Assessee' at maximum marginal rate in accordance with the provisions of section 161(1A).

The Circular further clarifies that the tax treatment given above will not be operative in the area falling in the jurisdiction of a High Court which has taken or takes a contrary decision on the issue.

3. Allowability of deduction under section 10AA on transfer of technical manpower in the case of software industry [Circular No. 14/2014, dated 8-10-2014]

The CBDT had earlier clarified *vide* Circular No.12/2014 dated 18th July, 2014 that mere transfer or re-deployment of existing technical manpower from an existing unit to a new SEZ unit in the first year of commencement of business will not be construed as splitting up or reconstruction of an existing business, provided the number of technical manpower so transferred does not exceed 20% of the total technical manpower actually engaged in developing software at any point of time in the given year in the new unit.

The limit of 20% was considered inadequate and restrictive and it impacted the competitiveness of Indian Software Industry in global market. Consequently, the matter was re-examined by the CBDT, and in supersession of Circular No.12/2014 dated 18th July, 2014, it has now been decided that the transfer or re-deployment of technical manpower from existing unit to a new unit located in SEZ, in the first year of commencement of business, shall not be construed as splitting up or reconstruction of an existing business, provided the number of technical manpower so transferred as at the end of the financial year should not exceed 50% of the total technical manpower actually engaged in development of software or IT enabled products in the new unit. Alternatively, if the assessee-enterprise is able to demonstrate that the net addition of the new technical manpower in all units of the assessee-enterprise is at least equal to the number that represents 50% of the total technical manpower of the new SEZ unit during such previous year, deduction under section 10AA would not be denied provided the other prescribed conditions are also satisfied. The assessee-enterprise will have the choice of complying with any one of the two alternatives given above to avail the benefit of deduction under section 10AA.

The Circular also clarifies that:

(a) it shall be applicable only in the case of assessees engaged in the development of software or in providing IT enabled services in SEZ units eligible for deduction under section 10AA. .

(b) it shall not apply to the assessments which have already been completed. Further, no appeal shall be filed by the Department in cases where the issue is decided by an appellate authority in consonance with this circular.

4. Approval of long-term bonds and rate of interest for the purpose of section 194LC of the Income-tax Act, 1961 [Circular No. 15/2014, dated 17-10-2014]

Section 194LC, inserted by the Finance Act, 2012, provides for a concessional rate of withholding tax @ 5% on interest payment by an Indian company to a non-corporate non-resident or a foreign company. The concessional rate of tax and TDS was applicable if the borrowing is made in foreign currency between 1.7.2012 and 30.6.2015, from a source outside India, *inter alia,* by way of issue of long-term infrastructure bonds, as approved by the Central Government in this behalf.

This year, the Finance (No.2) Act, 2014 has expanded the scope of deduction of tax at a concessional rate of 5% under section 194LC to cover interest payable to a non-corporate non-resident or a foreign company by an **Indian company or a business trust** on money borrowed by it in foreign currency from a source outside India **by issue of any long-term bond, including long-term infrastructure bond, as approved by the Central Government in this behalf, at any time between 1.10.2014 and 30.6.2017.** It may be noted that the concessional rate of tax deducted at source would continue to be applicable in respect of long term infrastructure bonds issued during the period 1.7.2012 to 30.9.2014.

Considering the fact that a large number of bond issues have to be undertaken by Indian companies, the Government is providing an approval mechanism to avoid approval for each and every specific case, which would lead to avoidable compliance burden on the borrower/issuer of bond. Accordingly, the CBDT conveys the approval of Central Government for issue of long-term bonds including long-term infrastructure bonds by Indian companies which satisfy the following conditions:

(a) The bond shall be issued at any time on or after 1st October, 2014 but before 1st July, 2017.

(b) The bond issue shall comply the relevant provisions of Foreign Exchange Management Act, 1999, read with relevant ECB regulations, either under automatic route or approval route.

(c) The bond issue should have Loan Registration Number issued by Reserve Bank of India.

(d) The term "long term" means that the bond to be issued should have original maturity term of three years or more.

Further, the Central Government has also approved the interest rate for the purpose of section 194LC in respect of borrowing by way of issue of long term bond including long

term infrastructure bond, as any rate of interest which is within the All-in-cost ceilings specified by the RBI under ECB regulations as is applicable to the borrowing through a long term bond issue having regard to the tenure thereof.

Any bond issue satisfying the above conditions would be treated as approved by the Central Government for the purpose of section 194LC. Further, it has also been clarified that consequent to the amendment to section 194LC, the approval of Central Government contained in Circular No. 7/2012, in so far as they apply to borrowings by way of a loan agreement, shall be valid for the borrowings made on or before 30/06/2017 instead of 30/06/2015 as mentioned in the said Circular.

5. Interest under section 234A not chargeable on self assessment tax paid before the due date of filing of return of income [Circular No.2/2015, dated 10-2-2015]

Interest under section 234A is charged in case of default in furnishing return of income by an assessee. The interest is charged at the specified rate on the amount of tax payable on the total income, as reduced by the amount of advance tax, TDS/TCS, any relief of tax allowed under section 90 and 90A, any deduction allowed under section 91 and any tax credit allowed in accordance with section 115JAA and section 115JD. Since self-assessment tax is not mentioned as a component of tax to be reduced from the amount on which interest under section 234A is chargeable, interest is being charged on the amount of self-assessment tax paid by the assessee even if such tax is paid before the due date of filing of return.

However, it has been held by Hon'ble Supreme Court in the case of *CIT vs Prannoy Roy (2009), 309 ITR 231* that interest under section 234A on default of furnishing return of income shall be payable only on the amount of tax that has not been deposited before the due date of filing of the income-tax return for the relevant assessment year.

Accordingly, the CBDT reviewed the present practice of charging interest and decided that **no interest under section 234A shall be charged on self assessment tax paid by the assessee before the due date of filing of return.**

6. Clarification regarding disallowance of 'other sum chargeable' under section 40(a)(i) [Circular No.3/2015, dated 12-02-2015]

If there has been a failure in deduction or in payment of tax deducted in respect of any interest, royalty, fees for technical services or other sum chargeable under the Act either payable in India to a non-corporate non-resident or a foreign company or payable outside India, then, disallowance of the related expenditure/payment is attracted under section 40(a)(i) while computing income chargeable under the head "Profits and gains of business or profession".

The interpretation of the term 'other sum chargeable' in section 195 has been clarified in this circular i.e. whether this term refers to the whole sum being remitted or only the portion representing the sum chargeable to income-tax under the Act.

In its Instruction No.2/2014, dated 26.02.2014, the CBDT has clarified that the Assessing Officer shall determine the appropriate portion of the sum chargeable to tax as mentioned in section 195(1), to ascertain the tax liability on which the deductor shall be deemed to

be an assessee-in-default under section 201, in cases where no application is filed by the deductor for determining the sum so chargeable under section 195(2).

In this circular, the CBDT has, in exercise of its powers under section 119, clarified that for the purpose of making disallowance of 'other sum chargeable' under section 40(a)(i), the appropriate portion of the sum which is chargeable to tax shall form the basis of disallowance. Further, the appropriate portion shall be the same as determined by the Assessing Officer having jurisdiction for the purpose of section 195(1). Also, where the determination of 'other sum chargeable' has been made under sub-section (2), sub-section (3) or sub-section (7) of section 195, such a determination will form the basis for disallowance, if any, under section 40(a)(i).

7. Clarification regarding applicability of *Explanation 5* to section 9(1)(i) to dividend declared and paid by a foreign company outside India in respect of shares which derive its value substantially from the assets located in India [Circular No. 4/2015, dated 26-03-2015]

Section 9 provides for incomes which are deemed to accrue or arise in India. As per section 9(1)(i), all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situated in India is deemed to accrue or arise in India.

Explanation 5 to section 9(1)(i) was inserted by the Finance Act, 2012 to clarify that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India".

The Explanatory Memorandum to the Finance Bill, 2012 clearly provides that the amendment of section 9(1)(i) was to reiterate the legislative intent in respect of taxability of gains having economic nexus with India irrespective of the mode of realisation of such gains. Thus, the amendment sought to clarify the source rule of taxation in respect of income arising from indirect transfer of assets situated in India.

Accordingly, Explanation 5 would be applicable in relation to deeming any income arising outside India from any transaction in respect of any share or interest in a foreign company or entity, which has the effect of transferring, directly or indirectly, the underlying assets located in India, as income accruing or arising in India.

Declaration of dividend by a foreign company outside India, however, does not have the effect of transfer of any underlying assets located in India. This circular, therefore, clarifies that **the dividends declared and paid by a foreign company outside India in respect of shares which derive their value substantially from assets situated in India would NOT be deemed to be income accruing or arising in India by virtue of the provisions of Explanation 5 to section 9(1)(i).**

8. Applicability of tax on capital gains in the hands of the unit holders where the term of the units of Mutual Funds under the Fixed Maturity Plans has been extended [Circular No. 6/2015, dated 09-04-2015]

Fixed Maturity Plans (FMPs) are closed ended funds having a fixed maturity date wherein the duration of investment is decided upfront. Prior to amendment by the Finance (No. 2) Act, 2014, units of a mutual fund under the FMPs held for a period of more than twelve months qualified as long term capital asset. The amendment in sub-section (42A) of section 2 by the Finance (No. 2) Act, 2014 required the period of holding in case of unlisted shares and units of a mutual fund [other than an equity oriented fund] **to be more than thirty-six months** to qualify as long term capital asset.

As a result, gains arising out of any investment in the units of FMPs made earlier and sold/redeemed after 10.07.2014 would be taxed as short term capital gains if the unit was held for a period of thirty-six months or less. To enable the FMPs to qualify as a long term capital asset, some Asset Management Companies (AMCs) administering mutual funds have offered extension of the duration of the FMPs to a date beyond thirty-six months from the date of the original investment by providing to the investor an option of roll-over of FMPs in accordance with the provisions of Regulation 33(4) of the SEBI (Mutual Funds) Regulation, 1996.

The CBDT has, vide this Circular, clarified that the roll over in accordance with the aforesaid regulation will not amount to transfer as the scheme remains the same. Accordingly, no capital gains will arise at the time of exercise of the option by the investor to continue in the same scheme. The capital gains will, however, arise at the time of redemption of the units or opting out of the scheme, as the case may be.

9. Non-applicability of TDS provisions on payments made to Corporations whose income is exempt under section 10(26BBB) [Circular No. 7/2015, dated 23-04-2015]

The CBDT had earlier issued Circular No. 4/2002 dated 16.07.2002 which laid down that there would be no requirement for tax deduction at source in respect of payments made to such entities, whose income is unconditionally exempt under section 10 of the Income-tax Act, 1961 and who are statutorily not required to file return of income as per the section 139. The said Circular also lists the entities which are unconditionally exempt under section 10 and who are statutorily not required to file return of income as per section 139.

Subsequently, section 10(26BBB) was inserted in the Income-tax Act, 1961 vide Finance Act, 2003 w.e.f. 01.04.2004 to provide that any income of a corporation established by a Central, State or Provincial Act for the welfare and economic upliftment of ex-service-men being the citizens of India does not form part of the total income.

The corporations covered under section 10(26BBB) satisfy the two conditions of Circular No. 4/2002 i.e., such corporations are statutorily not required to file return of income as per section 139 and their income is also unconditionally exempt under section 10. Accordingly, the CBDT has extended the benefit of the said Circular to such corporations whose income is exempt under section 10(26BBB). Hence, there would be no requirement for tax deduction at source from the payments made to such corporations, since their income is in any case exempt under the Income-tax Act, 1961.

Part II : Judicial Update – Direct Tax Laws

Significant Recent Legal Decisions

"Select Cases in Direct and Indirect Tax Laws – An Essential Reading for the Final Course" is a compilation of the significant decisions of Supreme Court, High Court and Authority for Advance Rulings. October, 2014 edition of the said publication is relevant for November, 2015 examination. Students may note that in addition to the cases reported in the said publication, following significant recent legal decisions are also relevant for November, 2015 examination:-

Basic Concepts

1. Can capital contribution of the individual partners credited to their accounts in the books of the firm be taxed as cash credit in the hands of the firm, where the partners have admitted their capital contribution but failed to explain satisfactorily the source of receipt in their individual hands?

CIT v. M.Venkateswara Rao (2015) 370 ITR 212 (T & AP)

Facts of the case: The assessee-firm was constituted in the year 1982 and its return for the assessment year 1993-94 was selected for scrutiny under section 143(3). The controversy was in relation to the capital contribution of ten partners aggregating to ₹ 76.57 lakhs. The assessee-firm's explanation that the partners have paid various amounts towards contribution of their share in the capital was not accepted since the source of income for the partners was not explained. The Commissioner (Appeals) observed that the amounts credited in the names of four partners were valid and that cash credits in the accounts of six other partners in the books of the firm were to be considered afresh by the Assessing Officer.

Issue under consideration: The issue before the High Court was whether the Assessing Officer was justified in treating the capital contribution of partners as income of the firm by invoking section 68?

High Court's Opinion: Section 68 directs that if an assessee fails to explain the nature and source of credit entered in the books of account of any previous year, the same can be treated as income. In this case, the amount sought to be treated as income of the firm is the contribution made by the partners to the capital. In a way, the amount so contributed constitutes the very substratum for the business of the firm and it is difficult to treat the pooling of such capital as credit. It is only when the entries are made during the course of business, they can be subjected to scrutiny under section 68.

Where the firm explains that the partners have contributed capital, section 68 cannot be pressed into service. At the most, the Assessing Officer can make an enquiry against the individual partners and not the firm when the partners have also admitted their capital contribution in the firm. The High Court made reference to decision in the case of *CIT v. Anupam Udyog 142 ITR 130 (Patna)* where it was held if there are cash credits in the books of the firm in the accounts of the individual partners and it is found as a fact that cash was received by the firm from its partner, then, in the absence of any material to

indicate that they are the profits of the firm, the cash credits cannot be assessed in the hands of the firm, though they may be assessed in the hands of individual partners.

High Court's Decision: The High Court, accordingly, held that the view taken by the Assessing Officer that the partnership firm has to explain the source of income of the partners as regards the amount contributed by them towards capital of the firm, in the absence of which the same would be treated as the income of the firm, was not tenable.

Charitable Trusts

2. In a case where properties bequeathed to a trust could not be transferred to it due to ongoing court litigation and pendency of probate proceedings, can violation of the provisions of section 11(5) be attracted?

DIT (Exemption) v. Khetri Trust (2014) 367 ITR 723 (Del)

Facts of the case: As per the 'will' of Late Raja Bahadur Sardar Singh, the entire property, including immovable property and shares in foreign companies, were bequeathed to the trust. However, the properties could not be transferred to or acquired by the trust because of ongoing litigation in the Court. In the probate proceedings, the 'will' was challenged and the probate proceedings are still pending.

The trustees paid ₹ 1,10,000 for raising a memorial for late Raja Bahadur Sardar Singh and the said amount was given to a business entity for this purpose, but due to the ongoing dispute, such project was not completed. The business entity, however, paid interest on the said amount. The Assessing Officer denied the benefit of exemption under section 11, on the ground that the asset held in the form of shares of foreign company and the advance given to business entity were contrary to the mandate of section 11(5) and thus, the condition specified in section 13(1)(d) has been violated.

Appellate Authorities' views: The Commissioner (Appeals) observed that the validity of the will has been challenged in the probate proceedings; therefore, till the 'will' is probated and affirmed as genuine, the trust would not acquire the legal right on the property for the purpose of Income-tax Act, 1961. In case the probate is denied, the properties would not devolve on the trust. The shares in foreign company were still in the name of the donor, Late Raja Bahadur Sardar Singh, and its acquisition by the trust is dependent upon the adjudication of the probate.

Further, with regard to the advance given to the business entity, the Commissioner (Appeals) found that the said amount cannot be treated as an investment which was covered and regulated by section 11(5), since the intent and purpose behind the payment was not investment.

These views of the Commissioner (Appeals) were confirmed by the Tribunal.

High Court's Decision: Based on the above factual findings, elucidated and affirmed by the Commissioner (Appeals) and the Tribunal, the High Court held that there was no violation of section 11(5) in this case.

3. Is the approval of Civil Court mandatory for amendment of trust deed, even in a case where the settler has given power to the trustees to alter the trust deed?

DIT (Exemptions) v. Ramoji Foundation (2014) 364 ITR 85 (AP)

Facts of the case: The settler gave power to the trustees to amend, alter, change or modify the objects of the trust deed with the approval of two-third majority. Such additional or altered object, however, must be of charitable nature falling within the definition thereof under the relevant provisions of the Income-tax Act, 1961. Based on these provisions of the trust deed and referring to the Supreme Court decision in *CIT v. Kamla Town Trust (1996) 217 ITR 699,* the Tribunal held that the trust deed can be amended without approaching the Civil Court. Therefore, the Tribunal directed the DIT (Exemptions) to grant registration to the assessee-trust under section 12AA on the basis of the amended trust deed.

Issue: The issue under consideration before the High Court is whether the Tribunal was correct in holding that the amendment to the trust deed can be made without approaching the Civil Court, on the basis of the decision in the case of *Kamla Town Trust (Supra)*.

High Court's Observations: The High Court observed that the power has been given to the trustees by the settler to amend the trust deed without approaching the Civil Court, provided all the conditions laid down by the settler are fulfilled. The sanction of Civil Court is required only when there is no such power. When the power has been specifically given to the trustees by the settler, no further power from the Civil Court is required.

The High Court made reference to the *Kamla Town Trust's* case and observed that it has not been stated anywhere in the Supreme Court's decision that in spite of the power given to them by settler to amend the trust deed, the trustees have to approach the Civil Court to get the trust deed rectified.

High Court's Decision: Accordingly, in this case, the High Court held that the Tribunal has correctly dealt with the matter and the trust deed amended by the trustees can be relied upon by the Revenue authorities for the purpose of granting registration under section 12AA.

Profits and gains from business or profession

4. Is the expenditure on replacement of dies and moulds, being parts of plant and machinery, deductible as current repairs?

CIT v. TVS Motors Ltd (2014) 364 ITR 1 (Mad)

Facts of the case: The assessee company, engaged in manufacture of motor cycles and spares, filed its return of income for the relevant assessment year. It later filed a revised return in which it claimed deduction under section 31 in respect of expenditure incurred on replacement of dies and moulds in the place of worn out dies and moulds. The claim

was rejected by the Assessing Officer on the ground that the assessee had claimed depreciation in respect of such expenditure in the earlier years.

Assessee's contention: The assessee contended that dies and moulds are not plant and machinery but are attachments to make plant and machinery function as per the requirements of the business. The assessee relied on the Madras High Court decision in the case of *Super Spinning Mill Ltd v. Asstt.CIT (2013) 357 ITR 720,* where expenditure on replacement of machinery parts was allowed as revenue expenditure.

High Court's Observations: The High Court referred to the Supreme Court ruling in *CIT v. Mahalakshmi Textile Mills Ltd. (1967) 66 ITR 710* and observed that as long as there was no change in the performance of the machinery and the parts that were replaced were performing precisely the same function, the expenditure has to be considered as current repairs of plant and machinery. In that case, the Supreme Court also observed that if grant of relief to an assessee is justified on another ground, the Revenue is bound to consider such claim of granting the relief. Accordingly, in this case, even though the assessee has claimed depreciation in the earlier years, the claim of the assessee for deduction of expenditure on replacement of moulds and dies as 'current repairs" is justified on the ground that there was no change in the performance of the machinery on account of such replacement.

The High Court also referred to its decision in the case of *CIT v. Machado Sons (2014) 2 ITR – OL 385* holding that **when the object of the expenditure was not for bringing into existence a new asset or to obtain a new advantage, the said expenditure qualifies as 'current repairs' under section 31.**

High Court's Decision: Applying the rationale of above decisions, the High Court held that "moulds & dies" are not independent of plant and machinery but are parts of plant and machinery. Once the dies are worn out, they had to be replaced so that the machine can produce the product according to business specifications. Thus, the expenditure incurred by the assessee towards replacement of parts of machinery to ensure its performance without bringing any new asset or advantage, is eligible for deduction as 'current repairs' under section 31.

5. Is guarantee commission paid by a company to its employee directors deductible as its business expenditure, where such guarantee was given by the employee directors to the bank for enabling credit facility to the company?

Controls & Switchgear Contractors Ltd v. Dy.CIT (2014) 365 ITR 312 (Del)

Facts of the case: The assessee, a listed company, wanted some credit facilities from the bank for its business purpose. The banker insisted on personal guarantee of the directors as a pre-condition for providing financial assistance to the company. The directors were employees of the company who were drawing salary from the company. A resolution was passed for paying commission to the directors and a sum of ₹ 24.37 lakhs each was paid as commission calculated at the rate of 1.5% of the principal sum, in respect of which personal guarantee was furnished by the directors to the bank.

Assessing Officer's Contention: The Assessing Officer applied section 36(1)(ii) and held that if the amount was not paid to them as commission, the same would have been payable as profits or dividend. Accordingly, the Assessing Officer contended that the assessee-company avoided dividend distribution tax under section 115-O which was otherwise payable. The appellate authorities also confirmed the disallowance of expenditure.

High Court's Observations and Decision: The High Court observed that the directors of the company are employees of the company and are entitled to remuneration for the services rendered as employees. The assessee-company passed a resolution resolving that the directors be paid commission for providing their personal guarantees for the financial assistance availed by the assessee-company from the bank. This act of providing personal guarantee was clearly beyond the scope of their services as employees of the company. The assessee-company, in its commercial wisdom, had agreed to pay a commission for furnishing of such guarantees by the director employees, which cannot be faulted. In such a case, the Assessing Officer only has to determine whether the transactions are real and genuine. It is not within his jurisdiction to impose his views as regards the necessity or the quantum of expenditure undertaken by the assessee. As regards section 36(1)(ii) the recipient directors were not entitled to receive the amount as commission in lieu of bonus or dividend. Dividend is paid to all the shareholders and the recipient directors were not the only shareholders of the company. The payment of commission, hence, cannot be taken as payment of dividend, since payment of dividend would result in payment to all the shareholders and not to select shareholders.

The High Court, therefore, set aside the Tribunal's order and directed rectification of the disallowance of amount paid as commission to directors.

6. Can employees contribution to Provident Fund and Employee's State Insurance be allowed as deduction where the assesssee-employer had not remitted the same on or before the "due date" under the relevant Act but remitted the same on or before the due date for filing of return of income under section 139(1)?

CIT v. Gujarat State Road Transport Corpn (2014) 366 ITR 170 (Guj)

Facts of the case: The assessee collected employees' contribution to Provident Fund and ESI which were remitted, after the due date under the relevant Acts but before the 'due date' for filing the return specified in section 139(1). The assessing authority held that the amount collected by way of employees' contribution to PF and ESI are income under section 2(24)(x) and their remittance is governed by section 36(1)(va). The time limit prescribed for remitting the contribution is the 'due date' prescribed under the Provident Funds Act, Employees' State Insurance Act, rule, order or notification issued thereunder or under any standing order, award, contract or service or otherwise.

Issue: The issue under consideration is whether extended time limit upto the due date of filing the return contained in section 43B would be available in respect of remittances which are governed by section 36(1)(va).

High Court's Observations: The High Court noted that section 43B(b) pertaining to employer's contribution cannot be applied with respect to employees' contribution which is governed by section 36(1)(va). So far as the employee's contribution is concerned, the *Explanation* to section 36(1)(va) continues to remain in the statute and there is no provision for applying the extended time limit provided under section 43B for remittance of employee's contribution. The amount of employee's contribution to PF and ESI is an income upon recovery from salary and its remittance within the 'due date' as specified in *Explanation* to section 36(1)(va) makes it eligible for deduction. Employees' contribution recovered by the employer is not eligible for extended time limit upto the due date of filing of return, which is available under section 43B in the case of employer's own contribution.

High Court's Decision: The High Court, accordingly, held that the delayed remittance of employees' contribution beyond the 'due date' prescribed in section 36(1)(va), is not deductible while computing the business income, even though such remittance has been made before the due date of filing of return of income under section 139(1).

Note: *A contrary view was expressed by Uttrakhand High Court in the case of CIT v. Kichha Sugar Co. Ltd. (2013) 356 ITR 351 holding that the employees' contribution to provident fund, deducted from the salaries of the employees of the assessee, shall be allowed as deduction from the income of the employer-assessee, if the same is deposited by the employer-assessee with the provident fund authority on or before the due date of filing the return for the relevant previous year.*

7. Is interest paid by the holding company as guarantor for the amount borrowed by the subsidiary company deductible under section 36(1)(iii)?

JK Synthetics Ltd v. CIT (2014) 369 ITR 310 (All)

Facts of the case: The assessee is a public limited company engaged in the manufacture and sale of synthetic yarn and cement. It stood as guarantor to the loans taken by its subsidiary company. The subsidiary company incurred heavy losses and as a result became a defaulter in paying its debts. The assessee was a guarantor to the loans taken by the subsidiary company for the purpose of protecting its own business interest. Since the subsidiary company could not adhere to the repayment of its liabilities, the assessee-holding company started repayment of loan installments on behalf of the subsidiary company and claimed ₹ 8 lakhs, being interest paid, as deduction under section 36(1)(iii). The claim of the assessee was rejected in assessment.

High Court's Opinion: To claim deduction under section 36(1)(iii) the following conditions are to be satisfied viz., (i) interest should have been payable; (ii) there should be a borrowing; and (iii) capital must have been borrowed or taken for business purposes. The High Court observed that if the capital borrowed is not utilized for the purposes of the business, the assessee will not be entitled to deduction under the clause.

It made reference to the Apex Court ruling in *Madhav Prasad Jatia v. CIT (1979) 118 ITR 200* where the expression '**for the purpose of business**' occurring in section

36(1)(iii) was held as wider in scope than the expression 'for the purpose of earning income, profits or gains'. The Apex Court observed that where a holding company has a deep interest in its subsidiary and advances money to the subsidiary and the same is used by the subsidiary for its business purposes, the lending-holding company would be entitled to deduction of interest on its borrowed loans.

High Court's Decision: Applying the rationale of the above Apex Court ruling to this case, the High Court observed that the assessee had deep business interest in the existence of subsidiary and therefore, repaid installments of loan to financial institutions. Such loans were given for the purpose of business. The High Court, thus, held that the claim for deduction of interest by the assessee-holding company is allowable.

8. Is expenditure incurred for construction of transmission lines by the assessee for supply of power to UPPCL by the assessee deductible as revenue expenditure?

Addtl. CIT v. Dharmpur Sugar Mill (P) Ltd (2015) 370 ITR 194 (All)

Facts of the case: The assessee was engaged in the business of manufacture and sale of sugar, chemicals and power and had a distillery. It paid ₹ 8.48 crores to Uttar Pradesh Power Corporation Ltd (UPPCL) for construction of transmission line and other supporting work for supply of power to UPPCL. The assessee generated power which was sold to UPPCL, its only customer. The agreement between the assessee and UPPCL stipulated that the entire expenditure for erection and installation of power transmission lines, towers and ancillaries from the point of power generation to sub-grid station would be incurred by the assessee. The UPPCL is to ensure quality control of the equipment and material and the work has to be carried out under its supervision and prior approval. The agreement stipulated that the entire power transmission line including towers and erection would be property of UPPCL which would provide for the subsequent supervision and maintenance. The assessee claimed the entire expenditure as a deduction under section 37(1). The claim of the assessee was disallowed by the Assessing Officer. However, the Commissioner (Appeals) deleted the disallowance by holding that by incurring the expenditure the assessee acquired right to make use of the asset for facilitating efficient conduct of its business and making it more profitable but without getting any advantage of enduring benefit to itself. The assessee did not acquire any asset to get covered by section 32 and hence, the expenditure incurred was revenue in nature. The Tribunal, too, confirmed the order of the Commissioner (Appeals).

High Court's Opinion: The High Court made reference to *Empire Jute Co Ltd v. CIT (1980) 124 ITR 1,* where the Supreme Court held that the true test is to consider the nature of the advantage in a commercial sense and it is only where the advantage is in the capital field that the expenditure would be disallowed. If the advantage consists in merely facilitating its trading operations or conducting its business while leaving the capital field untouched, the expenditure would be on revenue account.

A similar precedent in *CIT v. Gujarat Mineral Development Corpn. Ltd (1981) 132 ITR 377 (Guj)* was also cited to hold that the expenditure incurred in the laying of transmission lines was on revenue account.

The Allahabad High Court also made reference to the Rajasthan High Court ruling in *CIT v. Hindustan Zinc Ltd. (2009) 221 CTR (Raj) 637*, wherein it was observed that the erection of power lines by the assessee was for facilitating its routine operations and for smooth functioning of its business. The power lines remained the property of the Electricity Board. The High Court, therefore, held that the assessee had not acquired a capital asset or any enduring benefit or advantage.

High Court's Decision: Following the principle of law laid down by the Supreme Court in *Empire Jute Mills'* case, the Allahabad High Court, in this case, held that the expenditure which was incurred by the assessee in the laying of transmission lines was clearly on the revenue account. The transmission lines, upon erection, vested absolutely in UPPCL. The expenditure which was incurred by the assessee was for aiding efficient conduct of its business since the assessee had to supply electricity to its sole consumer UPPCL. This was not an advantage of a capital nature.

9. Where the assessee-company came into existence on bifurcation of a Joint Venture Company (JVC), can the amount paid by it to the JVC for use of customer database and transfer of trained personnel be claimed as revenue expenditure?

CIT v. IBM Global Services India P Ltd (2014) 366 ITR 293 (Karn)

Facts of the case: The assessee-company came into existence on the bifurcation of a joint venture company floated earlier by two other companies. The assessee-company paid ₹ 530 lakhs for use of domestic customer database to the joint venture company, which gave information about various customers who patronized the company in the past and who continued to have service maintenance contract. This enabled the assessee to provide maintenance support services and effectively run its software business. Also, certain skilled and trained employees of the joint venture company were transferred to the assessee-company for which it made a payment of ₹ 938.58 lakhs to the joint venture company. The assessee claimed both the payments viz. payment for use of domestic customer database and absorption of trained employees, as revenue expenditure. The claim of the assessee was disallowed by the Assessing Officer.

Assessing Officer's Contentions: The Assessing Officer contended that domestic customer database is a capital asset which provides an enduring advantage or benefit to the assessee, since by utilizing the same, the assessee can successfully run its business activities over a considerable period of time. Hence, he treated the payment made for acquisition of domestic customer database as the payment made towards acquisition of capital asset. The Assessing Officer also contended that compensation paid by the assessee to the joint venture company for transfer of human skill is a capital expenditure, since the expenditure incurred on recruitment and training of transferred personnel would provide an enduring benefit.

High Court's Observations and Decision: The High Court observed that the expenditure incurred for use of customer database did not result in acquisition of any capital asset. The assessee got the right to use the database and the company which

provided the database was not precluded from using such database. Therefore, the expenditure incurred was for use of data base and not for acquisition of such data base and, hence, is deductible as revenue expenditure.

As regards payment for obtaining trained and skilled employees, it was held that the joint venture company spent a lot of money to give training to employees who were transferred to the assessee-company. They were trained in the field of software. They have opted for employment with the assessee, and for their past services with the joint venture company, expenditure has been incurred. In effect, the payment made by the assessee-company was towards expenditure incurred for their training and recruitment. Such expenditure was in the revenue field, and therefore, the payment made by the assessee-company as per agreement to save such expenditure was also revenue in nature. Therefore, the expenditure incurred for obtaining trained and skilled employees cannot be termed as capital expenditure though the benefit may be of enduring nature. The High Court, thus, held that both the expenditures claimed were allowable as revenue expenditure.

10. Is release of retention money to the assessee-contractor on the basis of furnishing bank guarantee taxable as income of the assessee, where the assessee's right to receive retention money is subject to certain conditions including certification by the engineer in-charge?

Amarshiv Construction P Ltd v. Dy.CIT (2014) 367 ITR 659 (Guj

Facts of the case: The assessee-company was engaged in the business of civil construction. It was awarded a construction contract by Sardar Sarovar Narmada Nigam Ltd for construction of a part of the Sardar Sarovar Dam. Out of the bills raised by the assessee for such construction work, a certain portion was retained by the payer as retention money. This would be released only upon being certified by the engineer in-charge that the construction was carried out without any defects. The contract agreement was subsequently modified to permit greater liquidity to the assessee-contractor by allowing release of retention money where the contractor provides a matching bank guarantee for the sum to be released. Such bank guarantee would be encashed to the extent of dues or any defect found in the construction carried out or discharged at the end of the warranty period.

Issue: The issue before the High Court was whether the release of retention money based on bank guarantee results in accrual of income to the assessee-contractor.

High Court's Observations: The High Court observed that the crucial question is the point of time at which the assessee gets the right to receive such sum as his income. The High Court referred to the various decisions holding that **whenever the retention money of a contractor for performance of guarantee was held back by the employer of the contract, it cannot be taxed at that point of time and would accrue only when the release of retention money becomes an enforceable right to the contractor.** The moot point was a change in terms of the contract for release of retention money based on furnishing of bank guarantee by the contractor.

All the amounts received would not mean receipt of income. Whether income did accrue or not would depend on the fact of whether the right to receive the same had accrued to the payee or not. The fact that tax was deducted at source by the payer would also be of no consequence. The contractor i.e., the payee, has no control over tax deduction by the payer. Mere tax deduction will not decide the taxability of receipt. The manner in which the recipient has accounted the receipt in the books is also not a criterion for deciding the character of receipt. The amount was released based on furnishing of bank guarantee which cannot be equated or interpreted as conferring a right on the contractor-assessee to seek release of funds and to tax the same as income. The amount received is not a free entitlement and the bank guarantee could be invoked for recovery of dues for the defects in the work performed. Accordingly, the amount released based on bank guarantee with pending procedural formalities for approval of the work performed could not be taxed as income. This is because the income did not accrue when the funds were released as the release is based on bank guarantee and not on approval of performance appraisal.

There was no material change in the terms of contract, since both before and after the amendment of the agreement, the right to receive the amount was subject to the vital conditions of recoveries and adjustments against the amounts found due or defects in the work completed by the contractor. The right to receive the amount is also subject to certification by the engineer-in-charge that no liability was attached to the contractor. Therefore, the character of the amount received on furnishing of bank guarantee did not undergo any change. It still retained the character of retention money

High Court's Decision: The High Court, therefore, held that the release of retention money against furnishing of bank guarantee was a receipt not chargeable to tax.

11. Is interest income on margin money deposited with bank for obtaining bank guarantee to carry on business, taxable as business income?

CIT v. K and Co. (2014) 364 ITR 93 (Del)

Facts of the case: The assessee running a lottery, deposited certain funds with a bank in order to obtain bank guarantee to be furnished to the State Government of Sikkim. Such guarantee enabled the assessee to carry on the business of printing lottery tickets and for conducting lotteries on behalf of the State Government of Sikkim. The funds which were held as margin money, earned some interest.

Issue: The issue under consideration is whether such interest income would be taxable under the head 'Profits and Gains from Business or Profession' or under the head 'Income from other sources'.

High Court's Observations: The High Court noted that the interest income from the deposits made by the assessee is inextricably linked to the business of the assessee and such income, therefore, cannot be treated as income under the head 'Income from other sources'. The margin money requirement was an essential element for obtaining the bank guarantee which was necessary for the contract between the State Government of

Sikkim and the assessee. If the assessee had not furnished bank guarantee, it would not have got the contract for running the said lottery

High Court Decision: The High Court, accordingly, held that the interest income received on funds kept as margin money for obtaining the bank guarantee would be taxable under the head "Profits and gains of business or profession".

12. Under which head of income is franchise fee received by an assessee in tourism business, against special rights given to franchisees to undertake hotel business in assessee's property, taxable?

Tamil Nadu Tourism Development Corporation Ltd v. Dy. CIT (2014) 368 ITR 533 (Mad)

Facts of the case: The assessee-company, a wholly owned Government of Tamil Nadu Undertaking, was engaged in the business of development of tourism in the State. It leased some of its loss making hotel units to various franchisees for a consideration. The agreement envisaged leasing of hotels with attendant conditions including display of its name above the name of the franchisee in the name board, quality of food supplied, maintenance of rooms and buildings etc. to be followed by the franchisee. The assessee offered franchise fee as "Income from house property" and claimed deduction at 30% of Net Annual Value (NAV) under section 24, which was negatived in the assessment.

Appellate Authorities' Views: The Commissioner (Appeals) observed that the assessee was not engaged in any commercial or business activity to earn business income and thus, upheld the contention of the assessee that such income is taxable under the head "Income from house property". The Tribunal, however, observed that the assessee had not withdrawn from the business of carrying on tourism activities and it was only to earn more profits from its loss making units that it has let out the properties including business to franchisees. Thus, it held that the income arising from letting out of such properties is chargeable to tax as income from business. It negatived the claim for deduction of 30% of NAV made by the assessee.

High Court's Opinion: The issue before the High Court is whether the income by way of franchisee fee is taxable as income from business or as income from house property.

The High Court looked into the contract between the assessee and the franchisees which contained various conditions ranging from obtaining of permits and licences, maintenance of rooms, common area, garden maintenance, catering, Bar etc with 33 clauses. The assessee had not simply leased the land and building but had imposed further conditions as to how the business of franchisees' should be conducted with regard to the hotels given on lease.

The special conditions stipulated in the contract clearly indicated that the name of the assessee should be prominently indicated in the name board and that the name of the franchisee should be below the name of the assessee, thereby, making it clear that the assessee continued to operate the business through the franchisees. Thus, these special conditions were a clear indicator that the assessee continued to be in the business of tourism activities, though not directly but through the franchisees, and received income

as franchisee fee. The assessee received franchisee fee for giving a special right or privilege to the franchisees to undertake tourism business in the property.

High Court's Decision: The High Court, accordingly, held that the income earned by the assessee by way of franchisee fee is in the nature of business income and not income from house property.

13. Does payment of net present value of deferred sales tax liability result in remission of liability assessable under section 41(1)?

CIT v. Sulzer India Ltd (2014) 369 ITR 717 (Bom)

Facts of the case: The Government of Maharashtra, in order to grant incentives for establishing units in industrially backward or hilly areas, announced a sales tax deferral scheme. Under the scheme, the eligible units were permitted to collect sales tax and retain the same for a specified period of time. After the specified period, the amounts are to be remitted to the exchequer. The amount retained was treated as deemed payment of tax for which a certificate was given. Subsequently, the Government announced a scheme whereby the units could opt to prematurely pay the sales tax liability at net present value.

The assessee, in this case, had a deferred sales tax liability of ₹ 752.01 lakhs for which the payment at net present value was ₹ 337.13 lakhs. The assessee transferred the balance ₹ 414.88 lakhs to its capital reserve account.

The Assessing Officer made an addition of ₹ 414.88 lakhs to the income of the assessee, being remission of loan liability for premature payment of the amount of net present value by invoking section 41(1).

The Tribunal held that the amount credited to the capital reserve account in the books of the assessee and cannot be termed as remission / cessation of liability. Consequently, no benefit had arisen to the assessee in terms of section 41(1)(a). The issue before the High Court was regarding the taxability of the amount gained by the assessee by discharging the sales tax liability at net present value.

Revenue's contention *vis-à-vis* Assessee's contention: The Revenue argued that sales tax is always a trading receipt and the amount foregone by the State is a benefit by way of reduction in liability which is chargeable to tax under section 41(1).

The assessee contended that the sales tax liability in this case was not a liability in praesenti. The liability has been ascertained and determined in terms of the rules. The net present value is taken into consideration. Thus, the liability is not wiped out but its present value is ascertained and determined and that has been paid. There was no concession. There is absolutely no settlement negotiated or otherwise.

High Court's Opinion: The High Court observed that to apply section 41(1), the first requirement is that the allowance or deduction is made in respect of loss, expenditure or a trading liability incurred by the assessee and subsequently, the assessee obtained benefit in respect of such trading liability by way of remission or cessation thereof. In this

case, there was no evidence to show that there has been any remission or cessation of the liability by the State Government. Thus, one of the requirements of section 41(1)(a) has not been fulfilled in this case.

The Tribunal, while deciding the case, held that there was no remission or cessation of liability and the amount credited is a capital receipt. The High Court referred to Karnataka High Court decision in the case of *CIT v. Mcdowell & Co Ltd (2014) 369 ITR 684 (Karn)* and concurring with the reasoning of the Karnataka High Court, held that the amount retained under the deferral scheme was nothing but a loan given by the Government by way of incentive for setting up the industrial unit in a rural area. The said loan could have been retained for 15 years but an option for early repayment at net present value was given and on such payment, the entire liability to pay tax / loan stood discharged. It is not a benefit conferred on an assessee. Therefore section 41(1) is not attracted to facts of the case.

High Court's Decision: The High Court, accordingly, held that the remittance of deferred sales tax liability at net present value will not result in any income chargeable to tax under section 41(1).

Income from Other Sources

14. Does repair and renovation expenses incurred by a company in respect of premises leased out by a shareholder having substantial interest in the company, be treated as deemed dividend?

CIT v. Vir Vikram Vaid (2014) 367 ITR 365 (Bom)

Facts of the case: The assessee holds more than 75% of equity shares in a company and is the executive director of the company. In his personal capacity, he is the owner of certain premises in which he was carrying on a proprietary business. Subsequently, the assessee ceased to carry on the business of proprietary concern and hence, let out the premises to the company. The company incurred ₹ 2.51 crores towards construction and improvement of factory premises, which it continued to use otherwise than as the owner of the premises. The Assessing Officer held that the amounts spent by the company towards repair and renovation is taxable as deemed dividend in the hands of the assessee. In the alternative, the said amount was to be treated as a perquisite taxable in the hands of the assessee.

Appellate Authorities' Views: The Commissioner (Appeals) noted the assessee's submission that he had leased out the said premises for a rent lower than the prevailing market rate with an understanding that all expenditure for its upkeep and maintenance would be spent by the company on account of the assessee having stopped business activities. According to the Commissioner (Appeals), the assessee failed to substantiate his claim. The Commissioner (Appeals) was of the view that all the conditions provided under section 2(22)(e) for deemed dividend were satisfied. On the other hand, the Tribunal concluded that the payment was neither a deemed dividend nor a perquisite chargeable to tax.

High Court's Observations: The challenge before the High Court by the Revenue was only with regard to applicability of section 2(22)(e) in this case. The High Court observed that no money had been paid by way of advance or loan to the shareholder who has substantial interest in the company. Further, the amount spent was towards repairs and renovation of the premises owned by the assessee but occupied by the company as lessee. There is no dispute that the company had taken on rent the aforesaid premises.

The High Court observed that the expenditure incurred by virtue of repairs and renovation on the premises cannot be brought within the definition of advance or loan given to the shareholder having substantial interest in the company, though he is the owner of the premises. It cannot be treated as payment by the company on behalf of the shareholder or for the individual benefit of such shareholder. If held in such manner, it is a mere assumption not tenable in law.

High Court's Decision: The High Court, accordingly, held that the repair and renovation expenses in respect of premises occupied by the company cannot be treated as deemed dividend in the hands of shareholder being the owner of the building.

Assessment of various entities

15. Where land inherited by three brothers is compulsorily acquired by the State Government, whether the resultant capital gain would be assessed in the status of "Association of Persons" (AOP) or in their individual status?

CIT v. Govindbhai Mamaiya (2014) 367 ITR 498 (SC)

Facts of the case: Three brothers inherited a property consequent to demise of their father. A part of this bequeathed land was acquired by the State Government and compensation was paid for it. On appeal, compensation was enhanced and the enhanced compensation was paid with interest.

Issue: The issue under consideration is regarding the status in which capital gain arising on transfer of property would be assessed. The assessees' offered income in their status as "individual" but the Revenue sought to tax the same in their status as "Association of Persons" (AOP).

High Court's Observations: The High Court found that the parties inherited the property and there was no material on record to suggest consensus *ad idem* between the brothers for formation of AOP. It referred to *CWT v. Chander Sen (1986) 161 ITR 370 (SC)* to hold that as per section 4 of the Hindu Succession Act, 1956, income from the asset inherited by a son from his father has to be assessed as income of the son individually. Further, as per section 8 of the Hindu Succession Act, 1956, the property of the father devolves on his son in his individual capacity and not as karta of HUF. Thus, it was held that the income is chargeable to tax in their individual status and not as AOP.

Supreme Court's Observations: The Supreme Court referred to its earlier decision in the case of *Meera & Co v. CIT (1997) 224 ITR 635* in which the earlier precedent in the case of *CIT v. Indira Balakrishna (1960) 39 ITR 546 (SC)* was followed. The Apex Court

noted that "Association of Persons" means an association in which two or more persons join in a common purpose or common action.

The Supreme Court also referred to its judgment in *G. Murugesan & Bros. v. CIT (1973) 4 SCC 211*. In that case, it was held that an association of persons could be formed only when two or more persons voluntarily combined together for certain purposes.

In this case, the property in question came to the assessees' possession through inheritance i.e., by operation of law. It is not a case where any 'association of persons" was formed by volition of the parties. Further, even the income earned in the form of interest is not because of any business venture of the three assessees, but is the result of the act of the Government in compulsorily acquiring the said land. Thus, the basic test to be satisfied for making an assessment in the status of AOP is absent in this case.

Apex Court's Decision: The Apex Court, accordingly, held that the income from asset inherited by the legal heirs is taxable in their individual hands and not in the status of AOP.

Income-tax Authorities

16. Can the assessee's application, for adjustment of tax liability on income surrendered during search by sale of seized gold bars, be entertained, where assessment has not been completed?

Hemant Kumar Sindhi & Another v. CIT (2014) 364 ITR 555 (All)

Facts of the case: Consequent to a search in the premises of the assessee, some gold bars were seized from the locker. The assessee voluntarily disclosed some income during the course of search. The assessee filed an application for sale of the gold bars and adjustment of tax liability on undisclosed income out of the sale proceeds. This would obviate his liability to pay interest under sections 234B and 234C. The Assessing Officer dismissed the application on the reasoning that only when the assessment is completed and tax demand is crystallized, can recovery be initiated by the sale of gold bars. The assessee filed a writ contesting the dismissal of application by the Assessing Officer.

High Court's Observations: The High Court observed that section 132B(1)(i) uses the expression "the amount of any existing liability" and "the amount of the liability determined". The words "existing liability" postulates a liability that is crystallized by adjudication; Likewise, "a liability is determined" only on completion of the assessment. **Until the assessment is complete, it cannot be postulated that a liability has been crystallized.**

As per the first proviso to section 132B(1)(i), the assessee may make an application to the Assessing Officer for release of the assets seized. However, he has to explain the nature and source of acquisition of the asset to the satisfaction of the Assessing Officer. It is not the *ipse dixit* of the assessee but the satisfaction of the Assessing Officer on the basis of the explanation tendered by the assessee which is material.

High Court's Decision: The High Court, accordingly, held that the Assessing Officer was justified in his conclusion that it is only when the liability is determined on the completion of assessment that it would stand crystallized and in pursuance of which a demand can be raised and recovery can be initiated. Therefore, in the present case, the first proviso to section 132B(1)(i) would not be attracted. The High Court, thus, dismissed the writ petition.

Assessment Procedure

17. Can the Assessing Officer reassess the issues other than the issues in respect of which proceedings were initiated under section 147, when the original "reasons to believe" on the basis of which the notice was issued ceased to exist?

CIT v. Mehak Finvest P Ltd (2014) 367 ITR 769 (P&H)

Facts of the case: In the present case, reassessment proceedings were initiated against the assessee on the reason that various finance companies managed and controlled by certain persons were engaged in accommodation entries and the assessee-company was one among them. However, during the reassessment proceedings, the Assessing Officer noticed that fresh share application money amounting to ₹ 47 lakhs could not be explained by the assessee and hence invoked section 68 to bring to tax such sum. There was no addition on the basis of the original reason for which reassessment proceedings were initiated.

Issue: The issue under consideration is whether an addition can be made in reassessment when the original reasons on the basis of which notice for reassessment was issued did not survive.

Assessee's Contention vis-a-vis Revenue's Contention: The assessee contended that when the original reason prompting the initiation of reassessment proceedings did not survive, the question of making addition on some other fresh grounds was not possible. The basis of the assessee's contention was the Bombay High Court ruling in case of *CIT v. Jet Airways (I) Ltd (2011) 331 ITR 236 and Delhi High Court ruling in Ranbaxy Laboratories Ltd v. CIT (2011) 336 ITR 136*.

On the other hand, the Revenue placed reliance on the jurisdictional High Court decision in the case of *Majinder Singh Kang v. CIT (2012) 344 ITR 358* holding that reassessment can be made on the basis of additional grounds, even though the original reason forming the basis of issue of notice did not survive.

High Court's Observations: The High Court noted that *Explanation 3 to section 147* nowhere postulates or contemplates that the Assessing Officer cannot make any additions on any other ground unless some addition is made on the basis of the original ground for which reassessment proceeding was initiated. It cited the dismissal of special leave petition (SLP) against the High Court ruling in *Majinder Singh Kang's* case by the Supreme Court on 19.08.2011 as the binding precedent.

High Court's Decision: The High Court, accordingly, held that even though no addition is made on the original grounds which formed the basis of initiation of reassessment proceedings, the Assessing Officer is empowered to make additions on another ground for which reassessment notice might not have been issued but which came to his notice subsequently during the course of proceedings for reassessment.

Note : *A contrary view expressed by the Delhi High Court in Ranbaxy Laboratories Ltd.'s case has been reported in the October, 2014 edition of the publication "Select Cases in Direct and Indirect Tax Laws"*

18. Does the finding or direction in an appellate order that income relates to a different assessment year empower reopening of assessment for that assessment year, irrespective of the expiry of the six year time limit?

CIT v. PP Engineering Work (2014) 369 ITR 433 (Del)

Facts of the case: The Tribunal, in its order, directed that the cash credit of ₹ 32 lakhs found credited in the books of the assessee in the financial year 1999-2000 is chargeable to tax in the assessment year 2000-01 as against the assessment made by taxing the said amount in the assessment year 2001-02. In short, the Tribunal gave a finding that the cash credit under section 68 was assessable in a different assessment year than the assessment year in respect of which it heard the appeal. This prompted the Assessing Officer to issue a notice under section 148 in February, 2009 for reopening the proceedings for the A.Y.2000-01. The issue is validity of notice issued after a lapse of 6 years from the end of the relevant assessment year.

The Commissioner (Appeals) held that the reassessment is barred by time limitation and the Tribunal also upheld the order of the Commissioner (Appeals) without making reference to section 150 read with *Explanation 2* to section 153.

High Court's Opinion: The High Court made reference to section 150 which overrides the time limitation specified in section 149. Also, *Explanation 2* to section 153 makes it clear that when an order in appeal, revision or reference is made whereby any income is excluded from the total income of an assessee for an assessment year, an assessment of such income for another assessment year shall be deemed to be one made in consequence of or to give effect to any finding or direction contained in the said order for the purposes of section 150 and section 153.

The High Court made reference to the Delhi High Court ruling in the case of *Rural Electrification Corporation Ltd v. CIT (2013) 355 ITR 345* and opined that the findings of Commissioner (Appeals) and Tribunal on the question of limitation as legally untenable and incorrect.

High Court's Decision: The High Court observed that in view of the order of the Tribunal that the credit entries related to the earlier assessment year i.e., A.Y. 2000-01, the Assessing Officer initiated reassessment proceedings under section 147 by issue of notice under section 148 for the year and passed an order dated 29/12/2009 making an addition of ₹ 32 lakhs. The High Court held that by virtue of section 150 read with *Explanation 2* to section 153, the said order was not barred by limitation.

Note – *Under section 149(1)(b), the time limit for issue for notice under section 148 is six years from the end of the relevant assessment year, where the income chargeable to tax which has escaped assessment amounts to or is likely to amount to ₹ 1 lakh or more for that year.*

Section 150(1) states that notwithstanding anything contained in section 149, notice under section 148 may be issued at any time for the purpose of making an assessment or reassessment or recomputation in consequence of or to give effect to any finding or direction contained in an appellate or revisionary order.

Explanation 2 to section 153 provides that where by an order referred to in section 250, 254, 260, 262, 263 or 264, any income is excluded from the total income of the assessee for an assessment year, then, an assessment of such income for another assessment year shall, for the purposes of section 150 and section 153, be deemed to be one made in consequence of or to give effect to any finding or direction contained in the said order.

19. Is initiation of reassessment beyond a period of 4 years on the basis of subsequent Tribunal and High Court ruling valid, if there is no failure on the part of the assessee to disclose fully and truly all materials facts?

Allanasons Ltd v. Dy. CIT (2014) 369 ITR 648 (Bom)

Facts of the case: The assessee-company filed its return of income in which a claim for deduction under Chapter VI-A was made. The case was subjected to scrutiny assessment and order under section 143(3) was passed reducing the claim of deduction under Chapter VI-A. After 4 years from the end of the assessment year, a notice under section 148 was issued ascribing reasons such as subsequent tribunal and other court decisions which show that the deduction was excessively allowed in this case. The assessee challenged the reassessment proceedings by means of a writ before the court, contending that it is a settled position in law that the decision rendered by court subsequent to the assessment order does not by itself amount to failure on the part of the assessee to fully and truly disclose all material facts necessary for assessment.

High Court's Opinion: The High Court observed that it is well settled in terms of the proviso to section 147, that where any assessment is sought to be opened beyond a period of four years from the end of the relevant assessment year, two conditions have to be fulfilled cumulatively. The first condition is that there must be reason to believe that income chargeable to tax has escaped assessment. The second condition is that such escapement of income should have arisen due to failure on the assessee's part to fully and truly disclose all material facts required for the assessment.

Thus, escapement of income prompting reopening of assessment beyond the period of 4 years from the end of the assessment year is not possible unless it is due to the failure of the assessee to disclose fully and truly all material facts necessary for assessment.

Even a subsequent change of law cannot be taken as income escaping assessment for triggering reassessment provisions beyond 4 years from the end of the assessment year unless there was a failure on the part of the assessee to disclose fully and truly all material facts necessary for assessment. The High Court observed that in this case, the reasons recorded, when read as a whole did not indicate even remotely any failure on

the part of the assessee to disclose fully and truly any material fact necessary for assessment.

High Court's Decision: The High Court, accordingly, held that a subsequent decision of Tribunal or High Court by itself is not adequate for reopening the assessment completed earlier under section 143(3) unless there is a failure on the part of the assessee to disclose complete facts.

20. Is recording of satisfaction and quantification of escaped income a pre-condition for issuing notice under section 148 after 4 years from the end of the relevant assessment year?

Amarnath Agrawal v. CIT (2015) 371 ITR 183 (All)

Facts of the case: The assessee along with four others had obtained a lease of land and was in possession of the same from 1953. Subsequently, the State Government introduced a policy for conversion of lease-hold to free-hold. The assessee applied for conversion before the District Magistrate in 1997 and a sale deed was executed. The assessee deposited the necessary charges as demanded by the State Government and a freehold sale deed dated 25th March, 1998 was executed. The assessee sold a portion of the land during the F.Y. 1999-2000 and admitted the same as long-term capital gain taking into account the lease hold period also. In the assessment, the admission of income as long-term capital gain was accepted. However, after the expiry of four years from the end of the relevant assessment year, proceeding for reassessment of such income as short-term capital gains was resorted to by the Revenue on the ground that the lease hold period should not be considered for determining the period of holding of freehold land transferred. The assessee filed a writ challenging the validity of notice issued under section 148 stating that the requirements of section 149 read with section 151 were not considered by the Revenue.

High Court's Opinion and Decision: The High Court observed that two distinct conditions must be satisfied for assuming jurisdiction to issue a notice under section 148 after a period of 4 years viz. (i) escapement of income; and (ii) omission or failure on the part of the assessee to disclose fully and truly all material facts necessary for his assessment.

Under section 149(1)(b), it is imperative for the Assessing Officer, in his reasons, to state that the escaped income is likely to be ₹ 1 lakh or more. This is an essential ingredient for seeking approval and the basis on which satisfaction is to be recorded by the competent authority under section 151. If the condition precedent to substantiate the satisfaction of escapement of income is not made, the issuance of notice would be invalid.

In this case, since no reasons were recorded that the escaped income is likely to be ₹ 1 lakh or more so that the Chief Commissioner or Commissioner may record his satisfaction under section 151, the initiation of reassessment proceedings after four years was barred by time. The reasons recorded by the Assessing Officer were that the assessee had computed long-term capital gains tax liability, whereas he was liable to pay short-term capital gains tax, since he had sold a portion of the property within 3 years from the date of conversion of leasehold land into a freehold land.

The High Court observed that the property was held for more than 3 years and the conversion from leasehold to freehold being an improvement of the title did not have any effect on the taxability of profits. The reasons recorded by the Assessing Officer did not indicate any failure on the part of the assessee to disclose fully and truly all material facts at the time of assessment; it also did not indicate that the quantum of escapement of income exceeds ₹ 1 lakh. Accordingly, the High Court held that, in this case, the issue of notice under section 148 after the four year time period was not valid.

Appeals and Revision

21. Should the four year time limit for rectification of order by the Tribunal under section 254(2) be reckoned from the date of its order or from the date of receipt of order by the assessee?

Peterplast Synthetics P Ltd v. Asstt. CIT (2014) 364 ITR 16 (Guj)

Facts of the case: The assessee, dissatisfied with the order of Commissioner (Appeals), preferred an appeal before the Appellate Tribunal, which dismissed the appeal vide order dated February 20, 2007. The said order was, however, received by the assessee only on November 19, 2008. The assessee, after receipt of the order, preferred a rectification application against the same on May 9, 2012. The said rectification application was dismissed by the Tribunal on the ground that it is barred by law of limitation as provided under section 254(2) as the time limit of 4 years has to be reckoned from the date of order passed by the Tribunal i.e., from February 20, 2007. The assessee, being aggrieved with the dismissal of rectification application by the Tribunal, preferred a writ before the High Court.

Issue: The issue under consideration before the High Court is regarding the date to be reckoned for computing the period of limitation of four years under section 254(2) - whether the date of the Tribunal's order or the actual date of receipt of order by the assessee?

High Court's Observations: The High Court referred to the Bombay High Court ruling in *Petlad Bulakhidas Mills Co Ltd v. Raj Singh (1959) 37 ITR 264,* in which it was observed that the expression 'order' means an order, of which the affected party has actual or constructive notice. The right to make an application for revision is given to an assessee against an order, and that right can only be effectively exercised if the party affected had knowledge, either actual or constructive, of that order.

In that case, the Bombay High Court had observed that if the 'order' means a unilateral arriving at a decision by the appellate authority without the person affected having any knowledge of that decision, then, undoubtedly, the limitation would begin to run from the date when the authority chooses to pass the order. In such a case, the appellate authority may make the order, put it in a drawer, forget about it and if a year has passed after it, the right of the assessee to go for revision would be barred. Such contention is entirely untenable.

In this case, the Gujarat High Court observed that the effective right to appeal against the order or to seek rectification of the order could be exercised only when the affected party gets to know of the order. Thus, the right of appeal could be exercised only when the party affected by such order has knowledge of the order and hence, the limitation would start only from that date.

High Court's Decision: Applying the rationale of the above Bombay High Court ruling pronounced in relation to an application for revision, to the issue on hand pertaining to the date of reckoning the period of limitation for rectification under section 254(2), the Gujarat High Court held that the period of limitation has to be reckoned from the date of receipt of order by the assessee and not from the date of order. Therefore, the Tribunal had erred in dismissing the rectification application on the ground that it was barred by limitation by computing the time limit from the date of order instead of from the date of receipt of order by the assessee.

22. Is time limit under section 263 to be reckoned with reference to the date of assessment order or reassessment order, where the revision is in relation to an item which was not the subject matter of reassessment?

CIT v. Lark Chemicals Ltd (2014) 368 ITR 655 (Bom)

Facts of the case: The assessee-company, for the assessment year 2002-03, filed its return of income declaring a total income of ₹ 30.98 lakhs. This was accepted and the return was processed under section 143(1). Subsequently, it was reopened by issue of notice under section 148 and the order of reassessment was passed in June, 2006. The Commissioner assumed jurisdiction for revision of order by invoking section 263 in March, 2009. The subject matter of revision, however, was not related to any of the issues dealt with in the reassessment.

Issue under consideration: The issue before the High Court was whether the revision under section 263 is barred by limitation in view of the fact that the issues dealt with therein were not the subject matter of reassessment.

Tribunal's view: The Tribunal opined that jurisdiction under section 263 cannot be exercised in respect of those issues which were not the subject matter of consideration while passing the order of reassessment but were a part of the original assessment, the time limit for which had since expired. It relied on the Apex Court decision in the case of *CIT v. Alagendran Finance Ltd. (2007) 293 ITR 1,* wherein it was held that in such cases, the doctrine of merger would not apply and the period of limitation would commence from the date of original assessment and not from the date of reassessment.

High Court's Opinion: The High Court observed that if the revision happened to be in relation to issues dealt with in the reassessment proceedings, then, it would not be barred by limitation as the time limit would expire only on 31st March, 2009 i.e., two years from the end of the financial year in which the order sought to be revised under section 263, was passed. However, in this case, the revision proposed under section 263 was in respect of issues, other than the issues dealt with in the order of reassessment. The issues on which

the Commissioner sought to exercise jurisdiction under section 263 were concluded by virtue of intimation issued under section 143(1). The time period for revision under section 263 is two years from the end of the financial year in which order sought to be revised was passed [i.e., two years from the end of the financial year in which the intimation was issued under section 143(1)] and that time period has expired long ago.

High Court's Decision: The High Court, thus, held that the jurisdiction under section 263 could not be assumed on issues which were not the subject matter of issues dealt with in the order of reassessment but were part of the original assessment, for which the period of limitation expired long ago.

Penalties

23. Is concealment penalty leviable when the High Court admits the quantum appeal as involving substantial question of law?

CIT v. Nayan Builders & Developers (2014) 368 ITR 722 (Bom)

Facts of the case: In the assessment under section 143(3), the Assessing Officer made additions of (i) ₹ 104.76 lakhs towards income from a specified person; (ii) ₹ 10.79 lakhs towards disallowance of brokerage; and (iii) ₹ 2 lakhs towards disallowance of legal fee. The Tribunal upheld these additions in quantum proceedings. The Assessing Officer imposed penalty under section 271(1)(c) which was also confirmed by Commissioner (Appeals). The Tribunal was informed that the High Court had admitted substantial question of law with regard to those additions. Consequently, the Tribunal held that penalty was not leviable under section 271(1)(c).

Issue under consideration: The issue before the High Court was whether the Tribunal was correct in deleting the penalty under section 271(1)(c).

High Court's Opinion & Decision: The High Court observed that the issue of quantum addition was admitted by the High Court since it involved substantial question of law. When the High Court admits substantial question of law on an addition, it becomes apparent that the addition is certainly debatable. In such circumstances, penalty cannot be levied under section 271(1)(c). Thus, the High Court held that when the quantum proceeding is admitted by the High Court, it amounts to a debatable issue and hence, concealment penalty is not leviable.

24. Is penalty under section 271D imposable for cash loans/deposits received from partners?

CIT v. Muthoot Financiers (2015) 371 ITR 408 (Del)

Facts of the case: The assessee-firm, engaged in business of banking and money lending, had received huge amounts from the partners in the assessment years 1996-97 and 1998-99 by way of cash. The Assessing Officer levied penalty under section 271D. The Commissioner (Appeals) upheld the levy of penalty. The Tribunal observed that the advance made to the firm by the partners cannot be regarded as loan accepted by the

firm. It held that the amount advanced and accepted is capital of the firm and not loans which cannot be subjected to penalty under section 271D. The Revenue filed an appeal before High Court.

The assessee contended before the High Court that the amount advanced by the partners cannot be regarded as loan but is a capital of the firm. As the partnership firm has no separate legal entity, nor is there a separate identification between the firm and the partners, there is no violation of section 269SS in this case.

High Court's Opinion & Decision: The High Court referred to the case *CIT v. R.M. Chidambaram Pillai (1977) 106 ITR 292*, where the Apex Court was of the view that the firm is not a legal person even though it has some of the attributes of a personality. It held that the 'firm' is a collective noun, a compendious expression to designate an entity not a person. It also referred to *CIT v. Sivakumar. V (2013) 354 ITR 9 (Mad)*, where the High Court upheld the conclusion of the Tribunal to hold that there is no separate legal entity for the partnership firm and the partner is entitled to use the funds of the firm. In *CIT v. Lokhpat Film Exchange (Cinema) (2008) 304 ITR 172 (Raj)*, it was held that a partnership firm not being a juristic person, the *inter se* transaction between the firm and partners are not governed by the provisions of sections 269SS and 269T.

The High Court also noted the different view expressed by the Supreme Court in *CIT v. A.W. Figgies & Co. (1953) 24 ITR 405*, where it was held that the partners of the firm are distinct as civil entities while the firm as such is a separate and distinct unit for the purpose of assessment.

The High Court observed that the position that emerges is that there are three different Courts, which have held that section 269SS would not be violative when money is exchanged *inter se* between the partners and the firm.

The High Court further observed that, in this case, there was no dispute as regards the money brought in by the partners of the assessee-firm. The source of money was also not doubted. The transaction was bona fide and not aimed to avoid any tax liability. The credit worthiness of the partners and genuineness of the transactions coupled with relationship between the 'two persons' and two different legal interpretations put forward, could constitute a reasonable cause in a given case for not invoking sections 271D /271E read with section 273B.

The High Court held that the issue being a debatable one, there was reasonable cause for not levying penalty.

Miscellaneous Provisions

25. Can the Assessing Officer *suo moto* assume jurisdiction to declare sale of property as void under section 281?

Dr. Manoj Kabra v. ITO (2014) 364 ITR 541 (All)

Facts of the case: The assessee acquired a property for ₹ 7 lakhs though the stamp duty was paid in accordance with the circle rate which was ₹ 12 lakhs. Pursuant to the

sale deed, the assessee took possession of the property. Prior to the sale, the income tax assessment of vendor had been completed and a certain demand was raised against him in respect of the assessment year when the sale of the property was effected. The Assessing Officer issued a notice under section 281 to show cause as to why the sale deed executed in his favour (assessee-buyer) should not be treated as a void document. The assessee-buyer contended that he was a *bona fide* purchaser for adequate consideration and no notice of pendency of proceedings was to known him nor was it brought to his knowledge by the seller.

The assessee placed reliance on the decision of Supreme Court in the case of *TRO v. Gangadhar Vishwanath Ranade (Decd.) (1998) 234 ITR 188,* where it was held that section 281 of the Income-tax Act, 1961 is only a declaratory provision and not an adjudicatory provision entitling the income-tax authority to declare a document as a void document.

High Court's Observation: The High Court observed that the issue in this case was squarely covered by above Apex Court decision which held that the legislature had no intention to confer any exclusive power or jurisdiction upon the income-tax authority to decide any question arising under section 281. The Income-tax Act, 1961, does not prescribe any adjudicatory machinery for deciding any question which may arise under section 281. In order to declare a transfer as fraudulent under section 281, an appropriate proceeding in accordance with law was required to be taken under section 53 of the Transfer of Property Act, 1882. The Assessing Officer is required to file a suit for declaration to the effect that the transaction of transfer was void under section 281 of the Income-tax Act; but he himself cannot assume jurisdiction to declare the sale deed as void.

High Court's Decision: Applying the rationale of the Apex Court ruling, the High Court held that the Assessing Officer has no jurisdiction under section 281 to *suo moto* declare the sale as void.

Deduction, Collection and Recovery of Tax

26. Is section 194A applicable in respect of interest on fixed deposits in the name of Registrar General of High Court?

UCO Bank v. Dy. CIT (2014) 369 ITR 335 (Del)

Facts of the case: The assessee-bank accepted ₹ 707.46 lakhs as fixed deposit in the name of Registrar General of the High Court and issued a fixed deposit receipt in compliance with a direction passed by the court in relation to certain proceedings. Subsequently, the Assistant Commissioner of Income-tax issued a show cause notice to the bank for not deducting tax at source on the interest accrued and to show cause as to why it should not be treated as an assessee-in-default under section 201(1)/201(1A). The bank replied that the FDRs in the name of Registrar General of the Court was as a custodian because the actual beneficiary was unknown as the matter was sub judice and tax at source would be deducted when the payment is made to beneficiary as and when it is decided by the court. The Assistant Commissioner, however, passed an order treating the bank as assessee-in-default and raised a demand of ₹ 40.33 lakhs and ₹ 14.20 lakhs under sections 201(1) and 201(1A), respectively. Further, he initiated penalty

proceedings under section 271C. The assessee preferred a writ challenging the order passed imposing penal interest and initiation of penalty proceedings.

High Court's Opinion and Decision: The High Court opined that in the normal course, the bank is obliged to deduct tax at source in respect of any credit or payment of interest on deposits made with it. However, in this case, the actual payee is not ascertainable and the person in whose name the interest is credited is not a person liable to pay tax under the Act. The deposits kept with the bank under the orders of the court were, essentially, funds which were in custodia legis, that is, funds in the custody of the court. The interest on that account – although credited in the name of the Registrar General – was also part of funds under the custody of the Court. The Registrar General is not the recipient of the income represented by interest that accrues on the deposits made in his name. The credit of interest is not a credit to the account of a person who is liable to be assessed to tax.

The High Court observed that in the absence of a payee, the machinery provisions for deduction of tax to his credit are ineffective. The expression "payee" under section 194A would mean the recipient of income whose account is maintained by the person paying interest. The Registrar General is neither recipient of the amount credited to his account nor to interest accruing thereon. Therefore, he cannot be considered as a 'payee' for the purposes of section 194A. The credit by the bank in the name of the Registrar General would, thus, not attract the provisions of section 194A.

The High Court was of the view that *Circular No.8/2011 dated 14.10.2011* makes an assumption that the litigant depositing the money is the account holder with the bank or is the recipient of the income represented by the interest accruing thereon. This assumption is basically erroneous as the litigant who is asked to deposit the money in Court ceases to have any control or proprietary right over these funds. The person to whom the funds would be paid ultimately is determined by the court order and at that stage, tax would be required to be deducted at source to the credit of the recipient. However, the litigant who deposits the funds cannot be stated to be the recipient of income.

The High Court allowed the writ and set aside the orders passed by the tax authorities.

27. Is payment made for use of passive infrastructure facility such as mobile towers subject to tax deduction under section 194C or section 194-I?

Indus Towers Ltd v. CIT (2014) 364 ITR 114 (Del)

Facts of the case: The assessee owned a network of telecom towers and infrastructure services which were let out to major telecom operators in the country. Under section 197, the assessee sought for lower tax deduction under section 194C for the financial year 2013-14 at 0.5% and whereas the Assessing Officer issued a certificate under section 197 for lower tax deduction at 2.5% under section 194-I. The assessee filed a writ before the Delhi High Court. The Court directed the assessee to prefer a revision petition before the Commissioner of Income-tax.

The Commissioner of Income-tax rejected the contention of the assessee for applying section 194C and upheld the order of the Assessing Officer applying section 194-I, on the ground that

the mobile operators had the right to install the equipment on the tower owned by the assessee, which tantamounts to use of the land or telecommunication site and the tower owned by the assessee. The assessee once again preferred a writ before the High Court.

Assessee's Contentions: The assessee explained that its responsibility is to provide the entire passive infrastructure service with the aid of equipment belonging to it which is fully operated, controlled and managed by it. The customers do not have access, control or possession over the towers, sites or designated areas which are limited to rectification or maintenance of any defects in the equipments installed by them. The assessee, further, contended that its customers do not pay for any leasing rights but only for the services. Therefore, the provisions of section 194-I would not be attracted in this case.

High Court's Observations: The High Court observed that it was the intention of the parties to use the technical and specialized equipment maintained by the assessee. The infrastructure was given for the use of mobile operators. The towers were the neutral platform without which the mobile operators could not operate. Each mobile operator has to carry out this activity, by necessarily renting premises and installing the same equipment. The dominant intention was the use of equipment or plant or machinery and the use of premises was only incidental.

High Court's Decision: The High Court held that the submission of the assessee that the transaction is not "renting" is incorrect. Also, the Revenue's contention that the transaction is primarily "renting of land" is also incorrect. The underlying object of the arrangement was the use of machinery, plant or equipment i.e., the passive infrastructure and it is incidental that it was necessary to house the equipment in some premises. It directed that tax deduction be made at 2% as per section 194-I(a), the rate applicable for payment made for use of plant and machinery.

28. Is payment made to an overseas agent, who did not perform any service in India, liable for tax deduction at source?

DIT (International Taxation) v. Wizcraft International Entertainment (P) Ltd (2014) 364 ITR 227 (Bom)

Facts of the case: The assessee, an event management company, engaged the services of an agent to bring artistes to India. The assessee-company (i) paid commission to overseas agent; (ii) reimbursed the expenses in connection with the visit of the artistes in India; and (iii) paid fees to the artistes in India. The assessee-company deducted tax at source on the fees paid to the international artistes in India but did not deduct tax at source on the commission paid to the agent and on the reimbursement of expenses incurred in India by the artistes.

Assessing Officer's view *vis-à-vis* Commissioner (Appeals) view: The Assessing Officer contended that the payments made by the assessee including the payment made by way of commission to the agent and payment for reimbursement of expenses in connection with the visit of the artistes to India are liable for tax deduction at source. The Commissioner (Appeals) was of the view that expenses incurred and reimbursed do not

constitute income derived by the artistes from their personal activities, so as to be taxable under Article 18 of the Double Taxation Avoidance Agreement between India and UK; and hence, the same is not liable for deduction of tax at source.

Issue: The issue under consideration before the High Court was with regard to deduction of tax on commission paid to overseas agent who never took part in the events organized in India and amount paid as reimbursement of expenses incurred on travelling of artistes.

High court's Observations: The High Court observed that the assessee has deducted tax on the payments made to artistes for the services rendered in India. In so far as reimbursement of expenses is concerned, it has been verified with supporting documents that it was towards their air travel on which no tax was required to be deducted. With regard to the payment of commission, the agent did not act as a performing artist or entertainer. He was concerned only with the services rendered outside India. Thus, the Tribunal had recorded the finding of fact that the income of the agent did not arise from the personal activities in the contracting status of an entertainer or artist. He only contacted the artistes and negotiated with them for performance in India in terms of the authority given by the assessee. Hence, the commission paid to the overseas agent was not liable to tax in India. Consequently, there was no obligation for deducting tax at source at the time of making payment to the overseas agent.

High Court's Decision: The High Court, therefore, affirmed the decision of the Tribunal and Commissioner (Appeals) holding that the service rendered by the agent was outside India and hence, was not chargeable to tax in India. Thus, the requirement for deducting tax at source under section 195 on such payment does not arise.

29. Can incentives given to stockists and distributors by a manufacturing company be treated as "commission" to attract –

(i) the provisions for tax deduction at source under section 194H; and

(ii) consequent disallowance under section 40(a)(ia) for failure to deduct tax at source?

CIT v. Intervet India P Ltd (2014) 364 ITR 238 (Bom)

Facts of the case: The assessee-company engaged in manufacture of biological vaccines and animal health care pharmaceutical products, sold the same either through consignment or commission agents or directly through distributors or stockists. During the relevant financial year, it introduced a sales promotion scheme to boost sales by way of product discounts and product campaign. It passed on the incentives to distributors through consignment agents by way of sales credit notes. The Assessing Officer held that as the assessee was paying the stockists/distributors for the services rendered by them for buying and selling goods, on the basis of quantum of sales effected, such payment has to be considered as commission, on which tax was deductible at source under section 194H. Consequently, disallowance under section 40(a)(ia) was attracted for failure to deduct tax at source.

High Court's Observations: The High Court observed that the assessee had undertaken sales promotion by way of product discount scheme under which it offered incentive to the stockists / distributors and dealers. **The relationship between the assessee and the distributors / stockists was that of principal to principal.** The products were firstly sold to distributors / stockists who in turn resold the goods in the market. No service was offered by the assessee to them except a discount under the product discount scheme/product campaign scheme to buy the assessee's product.

High Court's Decision: The High Court, accordingly, held that the stockists and distributors were not acting on behalf of the assessee and most of the credit was by way of goods on meeting the sales target which could not be said to be a commission within the meaning of the *Explanation (i)* to section 194H. Accordingly, the High Court affirmed the order of the Tribunal which held that such payment does not attract deduction of tax at source. Consequently, disallowance under section 40(a)(ia) would not be attracted.

30. Can the Tax Recovery Officer (TRO) adjudicate disputes regarding quantum of liability between the garnishee (petitioner company, in this case) and the defaulting company, by exercising his powers under section 226(3)?

Uttar Pradesh Carbon & Chemicals Ltd v. TRO (2014) 368 ITR 384 (All.)

Facts of the case: The petitioner is a public limited company and is engaged in the business of financial services having registered office at Varanasi (shifted from Kanpur with effect from March 1, 2006). M/s Rich Capital and Financial services Ltd. became a defaulter of income-tax dues and demand to the extent of ₹ 3.20 crores was raised against it by the tax department. It was alleged by the said company that the petitioner company is a debtor and owed a sum of ₹ 1.55 crores to it. On the basis of this assertion made by the defaulting company, the Tax Recovery Officer (TRO) issued a notice under section 226(3) to the garnishee (petitioner company, in this case) requiring the garnishee to pay within the time specified in the notice so much of the amount as was sufficient to pay the amount due from the defaulting company in respect of arrears of tax. The notice, however, was purportedly sent at the address of the earlier registered office at Kanpur, which was not received by the petitioner company. Subsequently, when no reply was received from the petitioner company nor any amount was deposited, the TRO issued a notice, treating the petitioner as an assessee-in-default for the amount specified in the notice, holding that further proceedings would be taken against the petitioner for realization of the amount as if it were an arrears of tax due from it in the manner provided under sections 222 to 225. Thereafter, the TRO attached the equity shares in the demat account and also the balance in the savings bank account of the petitioner for recovery of tax due.

Petitioner's contentions: The petitioner filed an affidavit in terms of section 226(3)(vi) stating that it does not owe any sum to the defaulting company. Still the TRO issued summons and treated the petitioner as an assessee-in-default. The petitioner preferred a writ against such attachment of shares held in demat account and its bank account and prayed for quashing of the entire proceedings initiated under section 226(3). The petitioner contended that once it has denied its liability to pay any amount to the

defaulting company under law, the TRO cannot proceed further for recovery of tax arrears and the entire proceeding against it had to be quashed. It was also contended that the TRO does not hold jurisdiction to decide any dispute arising out of the business transaction between the defaulting company and the petitioner, which could be adjudicated only by the appropriate forum, such as the civil court.

Revenue's Contentions: The Revenue contended that a notice was sent by Speed Post under section 226(3) to the last known address of the petitioner and since there was no response, the petitioner was treated as an assessee-in-default and its demat account and bank account were attached. It further contended that the issue of technical breach arising due to non-service of notice on the debtor of the defaulting company had become infructuous in view of section 292B, since the petitioner participated in the proceedings subsequently.

High Court's Observations: The High Court observed that section 226(3) covers not only any sum of money due to the defaulting company being subjected to attachment but also any sum of money which may become due subsequently to the defaulting company being eligible for recovery by means of attachment. Thus, the provision covers not only persons owing but also those who may owe later to the defaulting company for the purpose of recovery of tax due. Further, since the petitioner has participated in the proceedings subsequently, the invalidity of the notice was cured and the defect, if any, was removed.

However, when the garnishee (i.e. debtor of the defaulting company) makes a statement on oath that the sum demanded or part thereof is not due from him or that it does not hold any money for or an account of the defaulting company, no further proceeding for recovery can be made.

The High Court observed that the powers under section 226(3) could not be invoked for effecting a recovery of a claim which is disputed. The condition precedent for exercising the power under section 226(3) is that the money is due and payable by the person concerned to the assessee.

The High Court opined that section 226(3) does not give any power to the Assessing Officer or the TRO to adjudicate disputes relating to the quantum of liability between the garnishee and the defaulting company, which is a matter within the purview of the Civil Courts.

High Court's Decision: The High Court referred to Apex Court decision in *Beharilal Ramcharan v. ITO (1981) 131 ITR 129* to hold that under section 226(3)(vi), a limited enquiry could only be conducted by the TRO and that too, by following the principles of natural justice. When the claim of amount is disputed by the debtor, the TRO cannot proceed to adjudicate the dispute between the parties i.e., the defaulting company and its debtor, for recovery of tax.

Thus, the High Court directed that the order of the TRO treating the petitioner as an assessee in default for the amount alleged to be owed by it to the defaulting company, cannot be sustained.

PAPER – 8 : INDIRECT TAX LAWS

PART – III : QUESTIONS AND ANSWERS

QUESTIONS

Note: All questions have to be answered on the basis of position of law as amended by the Finance (No. 2) Act, 2014 and significant Notifications/Circulars issued till 30.04.2015.

Valuation of excisable goods and computation of net excise duty liability

1. Solid Ltd., a manufacturer of excisable goods, produced 1,00,000 units of product 'Z' during the month of January, 2015. 'Z' is a notified product under section 4A of the Central Excise Act, 1944. During January, 2015, 50% of the goods produced are consumed captively and remaining are sold. Excise duty is payable @ 12% and education cesses @ 3% thereon. Abatement permissible under section 4A of Central Excise Act, 1944 is 10%.

   You are required to determine the excise duty payable, in cash, by Solid Ltd. for the month of January, 2015 with the help of the following information provided by it -

Particulars	**(₹) [per unit of 'Z']**
Cost of direct materials (inclusive of central excise duty @ 12.36%)	1,236
Cost of direct salaries (includes house rent allowance of ₹ 120)	300
Depreciation of machinery	500
Quality control cost	50
Factory overheads	200
Administrative cost (25% relates to production capacity)	400
Selling and distribution cost	600
Cost incurred due to break down of machinery	150
Scrap value realized	200
Actual profit margin-15%	
Price at which goods are sold to the buyer (inclusive of excise duty and other taxes)	2,500
Retail Sale Price printed on the package of the product	4,000

   Note: CENVAT credit of the excise duty paid on direct materials is available. 'Z' is used captively to manufacture an exempted final product. Solid Ltd. is not eligible for SSI exemption under Notification No. 8/2003 CE dated 01.03.2003.

CENVAT credit – Eligible input services

2. Mr. X exported some goods on FOB basis. He availed CENVAT credit of service tax paid by him on customs house agents' (CHA) services and shipping agents and container services in respect of finished goods so exported. However, the Revenue objected to the CENVAT credit claimed on these services.

   The Revenue alleged that in this case, services had been availed after the goods were cleared from the factory, which is the place of removal. Further, they were not in relation to the manufacturing activities undertaken by the assessee nor were these pertaining to the activities of clearance of goods from the factory. These services, according to the Revenue, did not fall under the definition of the term 'input service' and thus, the related CENVAT credit availed was inadmissible.

   Discuss, with the help of a decided case law, if any, whether the Revenue's objection is valid in law.

CENVAT credit – Job work provisions

3. Narmada Manufacturers, a non-SSI unit, purchased some inputs and a machine (eligible as capital goods for CENVAT purpose) on first day of a month. The inputs required some further processing and the machine required re-conditioning. Therefore, on the same day, Narmada Manufacturers gave the direction to its suppliers to send the inputs and the machine directly to the premises of the job workers - Mr. A and Mr. B respectively. The goods were received in the premises of job worker on the same day.

   Narmada Manufacturers immediately availed CENVAT credit of the entire excise duty paid on those inputs and 50% of the excise duty paid on the capital goods on the same day. Mr. A and Mr. B carried out the job work and returned the inputs and capital goods to Narmada Manufacturers after 190 days from the date of receipt of such goods by them.

   You are required to determine:

   (i) whether Narmada Manufacturers was justified in availing the CENVAT credit on inputs and capital goods, although it had not received the same in its factory?

   (ii) whether Narmada Manufacturers is required to take any further action with respect to the CENVAT credit availed by it?

Penalty for failure to pay central excise duty

4. Shubham Pvt. Ltd. is a manufacturer of excisable goods. The excise duty liability of Shubham Pvt. Ltd. for the month of October, 2014, as declared in ER-1 for the said month, is ₹ 14,50,000. It paid the said duty along with applicable interest on 20.01.2015. Shubham Pvt. Ltd. is not eligible for SSI exemption under *Notification No. 8/2003 CE dated 01.03.2003*.

Discuss whether Shubham Pvt. Ltd. is liable to any penal action under rule 8 of Central Excise Rules, 2002.

Invoice under central excise

5. Examine the validity of the following statements with reference to the provisions of Central Excise Rules, 2002:-

   (a) A manufacturer cannot authenticate the invoices issued by it by means of a digital signature.

   (b) An importer who issues CENVATable invoices is liable to penalty under rule 25 of Central Excise Rules, 2002 for non-accountal of excisable goods stored in the warehouse.

Valuation of taxable service and computation of service tax liability

6. Mr. X, the owner of a residential building in a commercial locality, furnishes the following information relating to the said building for the quarter April-June, 2014:-

S.No.	Area of the building	Particulars
(i)	Basement	Leased to Mr. B, a wholesaler for a monthly rent of ₹ 80,000. Mr. B uses one-fifth of the basement for his office and remaining portion as a godown for storing his merchandise.
(ii)	Ground floor	Given on rent to Mr. C for a monthly rent of ₹ 60,000. Mr. C uses the same as his residence.
(iii)	First floor	Occupied by Mr. X. and his family
(iv)	Large vacant land in the backyard	Given on rent of ₹ 1,80,000 per month to a parking contractor, Mr. E who has set up a parking facility on the said land.
(v)	Terrace	Given on lease for quarterly rent of ₹ 5,20,000 to M/s. Universe Communications for erecting and maintaining a mobile communication tower.

Compute the service tax liability of Mr. X for the quarter April-June, 2014.

Notes:

(i) Separate rent/lease deeds have been executed in respect of each floor of the building and vacant land given on rent/lease. Rent in respect of the various portions of the building, vacant land and the terrace is received on the first day of each month/quarter.

(ii) Wherever applicable, service tax is included in the rent receipts.

(iii) Mr. X is eligible for small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.

Point of taxation

7. Sahu Ltd. provided taxable services to ABC Ltd. on 11.11.2014 and issued invoice for the same on 21.11.2014. ABC Ltd. made the payment for said services on 16.11.2014 by cheque which was entered in the books of accounts of Sahu Ltd. same day. However, the amount was credited in the bank account of Sahu Ltd. on 26.11.2014. You are required to determine the point of taxation in the given case.

Valuation of taxable service and computation of service tax liability

8. The Resident Welfare Association (RWA) of Blue Heaven Housing Society in Delhi provides the following information with respect to the various amounts received by it in the month of January, 2015.

Particulars	(₹)
Monthly subscription collected from member families (₹ 5,500 each from 100 families)	5,50,000
Electricity charges levied by State Electricity Board on the members of RWA [The same was collected from members and remitted to the Board on behalf of members.]	3,50,000
Electricity charges levied by State Electricity Board on the RWA in respect of electricity consumed for common use of lifts and lights in common area. [Bill was raised in the name of RWA. RWA collected the said charges by apportioning them equally among 100 families and then, remitted the same to the Board.]	4,00,000
Proceeds from sale of entry tickets to a cultural programme conducted by the RWA in the park of Blue Heaven Housing Society	40,000
Proceeds from sale of space for advertisement in Members' directory [from members ₹1,00,000 and from non-members ₹ 2,00,000].	3,00,000

Compute the value of taxable service and service tax liability of RWA of Blue Heaven Housing Society for the month of January, 2015.

Notes:

(i) Wherever applicable, service tax is included in the receipts of RWA.

(ii) RWA of Blue Heaven Housing Society is not eligible for small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.

(iii) Wherever applicable, the point of taxation falls in the month of January, 2015.

Taxability of service

9. Shankar Taluka, a co-operative society, rendered rent-a-cab service to M/s. ABCL. The members of the society were essentially agriculturists who formed the society after they lost their land when ABCL plant was being set up.

At the time, when Shankar Taluka started rendering the service to ABCL, there was no service tax levy on rent-a-cab service. However, service tax was imposed on rent-a-cab service subsequently. There had been a confusion regarding the liability of Shankar Taluka as ABCL denied to pay the service tax for the want of any clause to this effect in the service contract. However, with due negotiation and arbitration, it was decided that the disputed amount would first be paid by Shankar Taluka and the same would then be reimbursed by ABCL.

A show cause notice was issued on Shankar Taluka proposing to recover service tax with applicable penalty and interest. Shankar Taluka paid the entire disputed amount but refused to pay the penalty. Shankar Taluka contended that they did not pay service tax at the relevant point of time as it being a new levy; they were unaware of legal provisions. Also, there were divergent views of different Benches of Tribunal, which had added to the confusion, and the issue was debatable. Further, there had also been confusion regarding their liability as initially ABCL denied to pay service tax.

Discuss, with the help of a decided case law, whether penalty can be imposed for the delay in payment of service tax arising on account of confusion regarding tax liability and divergent views due to conflicting court decisions.

Valuation of taxable service portion in execution of works contract and computation of service tax liability

10. M/s. P Enterprises (sole proprietorship firm) entered into a contract with Skyline Builders (a partnership firm) on 05.04.2015 for construction of a building at a consideration of ₹ 95,00,000 (excluding all taxes). M/s. P Enterprises supplied steel and cement to Skyline Builders at ₹ 5,00,000 (excluding taxes). The fair market value of such steel and cement was ₹ 10,00,000 (excluding taxes). Determine the service tax liability of Skyline Builders.

    Will your answer be different, if Skyline Builders has provided the said services to P Ltd. instead of M/s. P Enterprises assuming all other particulars remain the same?

    Note: Skyline Builders is not eligible for small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.

Exemptions and abatements under service tax

11. Determine the net service tax liability to be paid in cash in each of the following independent cases assuming that none of the service provider is eligible for the small service provider's exemption under *Notification No. 33/2012 ST dated 20.06.2012*:

    (i) Shree Cabs Pvt. Ltd., a radio taxi operator, has provided services valuing ₹ 1,00,000 in December, 2014. It does not avail CENVAT credit on inputs, capital goods and input services used for providing the said service and intends to avail abatement, if any, granted for such service.

(ii) Surbhi Travels Ltd. is engaged in running non air-conditioned buses for point to point travel. The buses do not stop to pick or drop the passengers during the journey.

For October, 2014, value of taxable services of Surbhi Travels Ltd. is ₹ 5,50,000. It does not avail CENVAT credit on inputs, capital goods and input services used for providing the said service and intends to avail abatement, if any, granted for such service.

Note: Wherever applicable, service tax has been charged separately.

Abatement under service tax

12. LM Travels Pvt. Ltd., located in Hyderabad, is engaged in providing services of renting of motorcab. You are required to determine the net service tax liability of LM Travels Pvt. Ltd. (to be paid in cash) for the month of December, 2014 from the following details furnished by it:-

Particulars	(₹)
Value of services rendered (before availing abatement)	6,00,000
Value of services sub-contracted to ST Cabs Pvt. Ltd., which is also engaged in providing services of renting of motorcab	1,00,000
Service tax payable on value of services sub-contracted	12,360

Note: LM Travels Pvt. Ltd. avails abatement granted under Notification No. 26/2012 ST dated 20.06.2012 and service tax, wherever applicable, has been charged separately. LM Travels Pvt. Ltd. is not eligible for small service providers' exemption under Notification No. 33/2012 ST dated 20.06.2012.

Recovery of dues under service tax

13. Mr. Piyush transferred its entire business to Mr. Ankush on 10.11.2014. On the day of such transfer, an amount of ₹ 35,00,000 was payable by Mr. Piyush to the Service Tax Department under the relevant provisions of Finance Act, 1994. Mr. Piyush, however, did not deposit any amount with the Service Tax Department even after such transfer.

The Central Excise Officer, after obtaining the written approval of the Commissioner of Central Excise, attached and sold all the goods in the custody of Mr. Ankush for recovering the sums due from Mr. Piyush.

With reference to the provisions of section 87 of Finance Act, 1994, discuss the veracity of the action taken by Central Excise Officer.

Prosecution provisions under service tax

14. Mr. Jagannath, a taxable service provider, has collected service tax of ₹ 53 lakh from his clients for the quarter ending 30th September, 2014, but had not deposited the same with the account of Central Government till 30th April, 2015.

Explain with reasons whether Mr. Jagannath can be arrested for this offence without an arrest warrant.

If your answer is yes, who will pass an order for the arrest of Mr. Jagannath and what can be the maximum term of imprisonment in this case? Can Mr. Jagannath be imprisoned for a term of less than six months, if it is found that he has been convicted for the first time under Finance Act, 1994?

Refund under service tax

15. A service recipient, who has borne the incidence of service tax, is not entitled to claim refund of excess service tax paid (consequent upon the downward revision of charges already paid) as the expression "any person" in section 11B of the Central Excise Act, 1944 does not include the recipient of the service.

With the help of a decided case law, examine the correctness of the statement.

Valuation of export goods

16. Manchanda & Co. has exported some goods by aircraft. The FOB price of the goods exported is US $ 5,00,000. The shipping bill is presented electronically on 12.12.2014 and Let Export Order is passed on 25.12.2014. The rates of exchange notified by CBEC on 12.12.2014 and 25.12.2014 are 1 US $ = ₹ 60 and 1 US $ = ₹ 62 respectively.

You are required to compute export duty with the help of the following details provided by Manchanda & Co.:-

	Date	Rate of Export Duty
Presentation of shipping bill	12.12.2014	10%
Let Export Order	25.12.2014	8%

Will your answer change, if the goods are exported by a vehicle, date of filing of bill of export is 17.12.2014, rate of export duty prevalent on 17.12.2014 is 12%, rate of exchange notified by CBEC on 17.12.2014 is 1 US $ = ₹ 60 and the particulars relating to Let Export Order remain the same?

Valuation of imported goods on the basis of identical goods

17. Shine Enterprises imported some goods from Germany. On the basis of certain information obtained through a computer printout from the Customs House, Department alleged that during the period in question, large number of such goods were imported at a much higher price than the price declared by the Shine Enterprises.

Therefore, Department valued such goods on the basis of transaction value of identical goods as per rule 4 of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 and demanded the differential duty along with penalty and interest

from the Shine Enterprises. However, Department did not provide these printouts to Shine Enterprises.

Shine Enterprises contended that Department's demand was without any basis in law, without any legally admissible evidence and opposed to the principles of natural justice as the computer printout which formed the basis of such demand had not been supplied to them. Resultantly, they had no means of knowing as to whether any imports of comparable nature were made at the relevant point of time.

You are required to examine the contention of Shine Enterprises, with the help of a decided case law, if any.

Application for settlement of cases under customs laws

18. Examine the correctness of the following statements with reference to the provisions of the Customs Act, 1962:

    (a) Settlement application can be filed in respect of goods imported as baggage.

    (b) An application for settlement can be made only after the expiry of a period of 180 days from the date of seizure of dutiable goods.

Advance Ruling under Customs

19. Only public sector companies, resident public limited companies and resident private limited companies are notified under section 28E(c)(iii) of the Customs Act, 1962 as the class or category of resident persons who can apply for advance ruling in case of specified matters relating to customs duty.

    Examine the validity of the statement with reference to customs laws.

Foreign Trade Policy

20. George Inc., a US based company, sought architectural services from ABC India Pvt. Ltd. with regard to its newly established business in New York in April, 2015. ABC India Pvt. Ltd. charged US $ 50,000 as a consideration for the architectural services provided to George Inc. In addition, ABC India Pvt. Ltd. also exported goods worth US $ 15,000 to George Inc. and received the entire consideration of US $ 65,000 on 28.04.2015.

    Discuss the eligibility of ABC India Pvt. Ltd. for duty credit scrip entitlement under the Service Exports from India Scheme (SEIS).

    Notes:

    (i) ABC India Pvt. Ltd. has an active Importer Exporter Code (IEC) at the time of rendering such services.

    (ii) Net Foreign Exchange earnings of ABC India Pvt. Ltd. in the financial year 2014-15 is US $ 16,000.

    (iii) Notified rate of reward for architectural services is 5%.

    Will your answer be different if ABC India Pvt. Ltd. had provided telecom services to George Inc.?

SUGGESTED ANSWERS / HINTS

1. Since 'Z' is used captively to manufacture an exempted final product, the same will be liable to excise duty. Rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 [Valuation Rules] provides that where whole or part of the excisable goods are not sold by the assessee but are used for captive consumption, the value of goods meant for captive consumption shall be 110% of the cost of production or manufacture of such goods.

As per *CBEC Circular No. 692/8/2003 dated 13.02.2003,* cost of production has to be determined as per 'Cost Accounting Standard (CAS)-4: Cost of Production for Captive Consumption' issued by ICWAI.

Since in the present case, only a part of the excisable goods are used for captive consumption (50% of 1,00,000 units i.e., 50,000 units), assessable value of such 50,000 captively consumed units will be determined in accordance with rule 8 of Valuation Rules. The assessable value of remaining 50,000 units, which are sold, will be determined under section 4A of Central Excise Act, 1944 i.e., RSP less abatement. Thus, net excise duty liability of Solid Ltd. for the month of January, 2015 will be computed in the following manner:

Computation of excise duty payable, in cash, by Solid Ltd. for the month of January, 2015

Particulars	(₹)	(₹)
I. Duty payable on goods used for captive consumption (50,000 units)		
Cost of direct materials ₹ 1,236		
Less: Central excise duty $\frac{₹\ 1,236}{112.36} \times 12.36$ = ₹ 136 (rounded off) [Note 1]	1,100	
Cost of direct salaries (includes house rent allowance of ₹ 120)	300	
Depreciation of machinery	500	
Quality control cost	50	
Factory overheads	200	
Administrative cost (25% related to production capacity) [Note 2]	100	
Selling and distribution cost [Note 3]	-	
Cost incurred due to break down of machinery [Note 4]	-	
Total	2,250	

Less: Scrap value realized	200	
Cost of production	2,050	
Cost of production of 50,000 units used for captive consumption		10,25,00,000
Add: 10% as per rule 8	205	1,02,50,000
Assessable value of 50,000 units of 'Z' used for captive consumption	2,255	11,27,50,000
Duty payable @ 12.36% (A)		1,39,35,900
II. Duty payable on goods sold (50,000 units)		
Retail sale price	4,000	
Less: Abatement u/s 4A @ 10%	400	
Assessable value per unit of 'Z' sold	3,600	
Assessable value of total units of 'Z' sold (₹ 3,600 x 50,000 units)		18,00,00,000
Duty payable @ 12.36% (B)		2,22,48,000
Total excise duty payable [(A)+(B)]		3,61,83,900
Less: CENVAT credit [136 x 1,00,000 units]		1,36,00,000
Duty payable in cash		**2,25,83,900**

Notes:

(1) Since CENVAT credit is available on central excise duty paid on direct materials, it has been deducted from the cost of direct materials in accordance with the Cost Accounting Standard-4 [CAS-4].

(2) Administrative overheads in relation to activities other than manufacturing activities have not been included in cost of production [CAS-4].

(3) Selling and distribution cost have not been considered while computing the cost of production as they are not in relation to production activity [CAS-4].

(4) Abnormal cost like break down of machinery does not form part of cost of production [CAS-4].

2. No, Revenue's objection is not valid. The issue involved in the given case as to whether CENVAT credit can be availed of service tax paid on customs house agents' (CHA) services and shipping agents & container services used by a manufacturer of final product for the purpose of export when the export is on FOB basis, has been decided by Gujarat High Court in the case of *Commissioner v. Dynamic Industries Limited 2014 (35) STR 674 (Guj.)*.

In the instant case, the High Court referred to definition of 'input service' as also placed reliance on various cases dealing with the subject and made the following significant observations:-

(i) In case of all the services in relation to which substantial question of law has been framed, there is no specific inclusion of such services in the definition of input service.

(ii) Any service used by the manufacturer directly or indirectly in relation to manufacture of final products and clearing of final products upto the place of removal would certainly be covered within the definition of input service. In the present case, the place of removal would be the port and not the factory gate.

(iii) Revenue has not disputed the fact that the services in relation to which the CENVAT credit is claimed by the assessee were availed for the purpose of clearing the goods for the purpose of export.

(iv) As regards customs house agents' (CHA) services and shipping agents & container services, the decision of this Court in *Cadila Healthcare Ltd. 2013 (30) STR 3 (Guj.)* would apply and the definition of input service would cover these services, considering the nature of services and the place of removal being the 'port' in this case.

Based on the above observations, the High Court held that CENVAT credit in respect of customs house agents' (CHA) services and shipping agents & container services is admissible. Applying the ratio of the above-mentioned decision to the given situation, it can be concluded that the Revenue's objection to the CENVAT credit claimed is not admissible in law.

Further, CBEC vide *Circular No. 999/6/2015 CX dated 28.02.2015* has also clarified that in case of export of goods by the manufacturer exporter to his foreign buyer, place of removal will be the port where the shipping bill is filed by the manufacturer exporter and accordingly, the eligibility to CENVAT credit is to be determined.

In the light of said clarification, conclusion drawn earlier is reaffirmed that since services used in clearance of final product upto the place of removal are covered in the definition of input service, CENVAT credit would be admissible to the manufacturer exporter in the given case.

3. **(i)** Narmada Manufacturers was justified in availing the CENVAT credit on inputs and capital goods even though it had not received the same in its factory. With effect from 01.03.2015, CENVAT credit in respect of inputs or capital goods can be availed immediately on receipt of the same in the premises of job worker where inputs and/or capital goods are sent directly to the job worker on the direction of the manufacturer or the provider of output service, as the case may be [Rule 4(1) and rule 4(2)(a) of CENVAT Credit Rules, 2004].

(ii) With effect from 01.03.2015, rule 4(5)(a) *inter alia* provides that if the inputs or capital goods are not received back within 180 days and 2 years respectively, from the date of receipt of such goods by job worker, the manufacturer will have to pay an amount equivalent to the CENVAT credit attributable to the inputs or capital goods by debiting the CENVAT credit or otherwise. However, such credit may be retaken once the inputs or capital goods are received back in the factory.

In the given case, since the inputs have not been received back within 180 days, Narmada Manufacturers will have to pay an amount equivalent to the CENVAT credit attributable to the inputs by debiting the CENVAT credit or otherwise. However, it can re-take such credit after 190 days when such inputs are received back by it.

CENVAT credit attributable to the capital goods, however, need not be reversed as the same have been received in the factory of the manufacturer within 2 years of the receipt of the same by job worker.

4. With effect from 01.10.2014, all assessees are mandatorily required to pay excise duty through internet banking [Rule 8(1B) of Central Excise Rules, 2002]. Further, in case of assessees not entitled to SSI exemption, duty is payable on monthly basis and the due date for e-payment of excise duty of a month is 6th day of the month immediately following the said month. Thus, Shubham Pvt. Ltd. should have paid the excise duty liability for the month of October, 2014 by 06.11.2014. However, Shubham Pvt. Ltd. defaulted in payment of duty and paid the same after a delay of more than two months.

With effect from 11.07.2014, sub-rule (3A) of rule 8 of Central Excise Rules, 2002 has been substituted with a new rule to provide that if the assessee fails to pay the duty declared as payable by him in the return within a period of 1 month from the due date, then he would be liable to pay penalty @ 1% on such amount of the duty not paid, for each month or part thereof calculated from the due date, for the period during which such failure continues. Here, "month" means the period between two consecutive due dates for payment of duty.

Thus, Shubham Pvt. Ltd. would be liable to penalty @ 1% on ₹ 14,50,000 for 3 months. The penalty leviable would be ₹ 43,500.

5. (a) The said statement is not correct. With effect from 01.03.2015, a new sub-rule (8) has been inserted in rule 11 of Central Excise Rules, 2002 vide *Notification No. 8/2015 CE (NT) dated 01.03.2015* to provide for authentication of invoices by digital signatures. It has been provided that an invoice issued under this rule by a manufacturer may be authenticated by means of a digital signature.

(b) The said statement is correct. Prior to 01.03.2015, the provisions of rule 25 of Central Excise Rules, 2002 relating to confiscation and penalty for specified contraventions were applicable to a producer, manufacturer, registered person of a warehouse and a registered dealer. However, with effect from 01.03.2015, the

scope of applicability of rule 25 has been extended vide *Notification No. 8/2015 CE (NT) dated 01.03.2015* to an importer who issues an invoice on which CENVAT credit can be taken. Further, it may be noted that non-accountal of excisable goods stored in the warehouse is a specified contravention under rule 25 of Central Excise Rules, 2002.

6. Renting of immovable property (whether residential or commercial) is a declared service under section 66E(a) of Finance Act, 1994. However, services by way of renting of residential dwelling for use as residence are covered in negative list of services and are thus, not liable to service tax.

Since, Mr. X has let out different floors of his residential building to different tenants and separate rent/lease deeds have been executed in respect of each floor of such building and vacant land given on rent/lease, principle of bundled service will not apply. In this backdrop, the taxability of each of the floor of the building and vacant land owned by Mr. X is computed as under:

Computation of service tax liability of Mr. X for the quarter April-June, 2014

Particulars	**(₹)**
Rent received for basement-commercial use [Note 1]	2,40,000
Rent received for ground floor-residential use [Note 2]	-
First floor occupied for personal use [Note 3]	-
Rent received for large vacant land in the backyard used for parking facility [Note 4]	5,40,000
Rent received for terrace given on lease [Note 5]	5,20,000
Gross value of taxable services	13,00,000
Less: Small service provider's exemption	10,00,000
Value of taxable services (inclusive of service tax)	3,00,000
Service tax liability (₹ 3,00,000x12.36/112.36) (rounded off)	**33,001**

Notes:

(1) As per section 65B(41) of the Act, renting includes letting, leasing, licensing or other similar arrangements in respect of immovable property. Therefore, leasing out of the basement of the building to Mr. B would not be covered under negative list of services as Mr. B uses the basement for commercial purpose. Thus, it would be liable to service tax as declared service.

(2) Renting of ground floor of the building to Mr. C for being used as a residence would not be chargeable to service tax as it is covered in negative list of services under section 66D(m) of Finance Act, 1994.

(3) Since Mr. X uses the first floor of the building himself, it would not be a service and thus, would not be liable to service tax.

(4) Renting of vacant land, an immovable property, to Mr. E, a parking contractor, would be liable to service tax as declared service since Mr. E uses it for commercial purpose.

(5) Leasing of terrace for erecting and maintaining a mobile communication tower is liable to service tax as a declared service.

7. In the given case, since the invoice is issued within the prescribed period of 30 days from the date of completion of provision of service, the point of taxation, as per rule 3 of the Point of Taxation Rules, 2011, shall be:

(a) Date of issuance of invoice (i.e. 21.11.2014)

or

(b) Date of receipt of payment (i.e. 16.11.2014) [Refer note below]

whichever is earlier, i.e. 16.11.2014.

Note: As per rule 2A of the Point of Taxation Rules, 2011, date of payment is:-

(a) date on which the payment is entered in the books of account (i.e. 16.11.2014)

or

(b) date on which the payment is credited to the bank account of the person liable to pay tax (i.e. 26.11.2014)

whichever is earlier, i.e. 16.11.2014.

8. Computation of value of taxable service and service tax liability of RWA of Blue Heaven Housing Society for the month of January, 2015

Particulars	**(₹)**
Monthly subscription charges [Note 1(i)]	5,50,000
Amount collected towards electricity charges levied by State Electricity Board on the members of RWA [Note 1(ii)]	-
Amount collected towards electricity charges levied by State Electricity Board on the RWA in respect of electricity consumed for common use of lifts and lights in common area [Note 1(iii)]	4,00,000
Proceeds from sale of entry tickets to cultural programme held in the park of the Housing Society [Note 2]	-
Proceeds from sale of space for advertisement in members' directory [Note 3]	3,00,000
Value of taxable service inclusive of service tax	12,50,000
Value of taxable service (₹ 12,50,000 x 100/112.36) (rounded off)	**11,12,496**
Service tax liability (₹ 12,50,000 x 12.36/112.36) (rounded off)	**1,37,504**

Notes:

1. Services provided by the RWA to its members will be liable to service tax as the RWA and its members shall be treated as distinct persons by virtue of Explanation 3(a) to the definition of 'service' as contained in section 65B(44) of the Finance Act, 1994.

   Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts the service provided by an unincorporated body or a non- profit entity registered under any law for the time being in force, to its own members by way of reimbursement of charges or share of contribution up to an amount of ₹ 5,000 per month per member for sourcing of goods or services from a third person for the common use of its members in a housing society or a residential complex.

   Circular No.175/01/2014 ST dated 10.01.2014 has, however, clarified the following in relation to exemption available to services provided by a Resident Welfare Association (RWA) to its own members:

   (i) If per month per member contribution of any or some members of a RWA exceeds ₹ 5,000, entire contribution of such members whose per month contribution exceeds ₹ 5,000 would be ineligible for the exemption under the said notification. Service tax would then be leviable on the aggregate amount of monthly contribution of such members.

   (ii) Services provided by a RWA in the name of its members, acting as a 'pure agent' of its members, are excluded from value of taxable service available for the purposes of exemption provided under mega exemption notification.

   (iii) However, in the case of electricity bills issued in the name of RWA, in respect of electricity consumed for common use of lifts and lights in common area, etc., the exclusion from the value of taxable service would not be available, since there is no agent involved in these transactions.

2. Entry to entertainment events is not taxable as the same is covered in the negative list of services under clause (j) of section 66D of the Finance Act, 1994.

3. Sale of space for advertisements in business directories would attract service tax as only selling of space for advertisement in print media is included in the negative list of services under clause (g) of section 66D of the Finance Act, 1994 and print media excludes business directories.

Note: *Since Mega Exemption Notification exempts the service provided by RWA to its own members by way of share of contribution per month per member up to an amount of ₹ 5,000, it is also possible to take a view that monthly contribution of a member in excess of ₹ 5,000, i.e. ₹ 500 (₹ 5,500 - ₹ 5,000) would be taxable. In that case, total monthly subscription charges liable to tax would be ₹ 50,000 and service tax liability would be computed accordingly.*

9. No, penalty cannot be imposed for the delay in payment of service tax arising on account of confusion regarding tax liability and divergent views due to conflicting court decisions. The facts of the given case are similar to the case of *Ankleshwar Taluka ONGC Land Loosers Travellers Co. OP. v. C.C.E., Surat-II 2013 (29) STR 352 (Guj.).* In the instant case, the High Court made the following three important observations:

(i) The levy was comparatively new and therefore, both unawareness and confusion were quite possible particularly when the members of the appellant society were essentially agriculturists.

(ii) There were divergent views of different benches of Tribunal, which may have added to such confusion.

(iii) The fact that the appellant had persuaded their right of reimbursement of payment of service tax with the service recipient by way of conciliation and arbitration cannot deprive them of the defence of bona fide belief of applicability of service tax.

The High Court held that even if the appellants were aware of the levy of service tax and were not paying the amount on the ground of dispute with the service recipient, there could be no justification in levying the penalty in absence of any fraud, misrepresentation, collusion or wilful mis-statement or suppression. Moreover, when the entire issue for levying of the tax was debatable, that also would surely provide legitimate ground not to impose the penalty.

10. Rule 2A(ii) of Service Tax (Determination of Value) Rules, 2006 *inter alia* provides that in case of works contracts entered into for execution of original works, service tax is payable on 40% of the total amount charged for the works contract. Further, as per Explanation 1(b) to rule 2A(ii), total amount means the sum total of the gross amount charged for the works contract and the fair market value of all goods and services supplied in or in relation to the execution of the works contract, whether or not supplied under the same contract or any other contract, after deducting -

(i) the amount charged for such goods or services, if any; and

(ii) the value added tax or sales tax, if any, levied thereon.

Thus, service tax liability of Skyline Builders would be computed in the following manner:-

Computation of service tax liability of Skyline Builders

Particulars	**(₹)**
Gross amount received excluding taxes **(A)**	95,00,000
Add: Fair market value of steel and cement supplied by M/s. P Enterprises (excluding taxes) **(B)**	10,00,000
Less: Amount charged by M/s. P Enterprises for steel and cement (excluding taxes) **(C)**	5,00,000
Total amount charged **[(A) + (B) - (C)]**	1,00,00,000

Value of service portion (40% of total amount charged in case of original works)	40,00,000
Service tax liability [₹40,00,000 × 12.36%]	**4,94,400**

However, in case of services provided in execution of works contract, when the service is provided by any individual/ HUF/ partnership firm (whether registered or not) including association of persons to a business entity registered as body corporate, 50% of the service tax is payable by the service provider and balance 50% by the service receiver under partial reverse charge in terms of *Notification No. 30/2012 ST dated 20.06.2012.* Therefore, in the given case, when Skyline Builders provide services to P Ltd. (a company) 50% of the service tax will be payable by the service provider (Skyline Builders) and balance 50% by the service receiver (P Ltd.). In that case, service tax liability of Skyline Builders would be 50% of the total service tax liability as computed above i.e. ₹ 2,47,200 [50% of ₹4,94,400].

11. (i) With effect from 01.10.2014, clause (o) of section 66D has been amended by Finance (No.) Act, 2014 to remove the service of transportation of passengers by radio taxis from the ambit of negative list of services. Thus, travel by radio taxis or radio cabs, whether or not air-conditioned, has been made liable to service tax w.e.f. 01.10.2014. However, an abatement of 60% has been extended to transport of passengers by a radio taxi from the same day by amending *Notification No. 26/2012 ST dated 20.06.2012*. The abatement would be available if CENVAT credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken under the provisions of CENVAT Credit Rules, 2004.

Thus, in the given case, since CENVAT credit on inputs, capital goods and input services is not being availed by Shree Cabs Pvt. Ltd., it can claim the abatement of 60% which will make the effective rate of service tax as 4.944% [40% × 12.36%]. Thus, service tax liability to be paid in cash will be ₹ 4,944 [₹ 1,00,000 × 4.944%]. In this case, entire service tax liability will have to be paid in cash as benefit of CENVAT credit cannot be availed.

(ii) With effect from 11.07.2014, *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012* has been amended to restrict the exemption available to transport of passengers by contract carriages for purposes other than tourism, conducted tour, charter or hire to transport of passengers by non air-conditioned contract carriages only.

In the given case, the buses are contract carriages since they are used for point to point travel and they do not stop to pick or drop the passengers during the journey. Thus, no service tax is payable by Surbhi Travels Ltd. running non air-conditioned buses (contract carriage) for point to point travel as the same are exempt.

12. Computation of net service tax liability (to be paid in cash) of LM Travels Pvt. Ltd. for December, 2014

Particulars	(₹)
Value of services	6,00,000
Less: Abatement @ 60% [Note 1]	3,60,000
Value of taxable service	2,40,000
Service tax @ 12.36%	29,664
Less: CENVAT credit [Note 2]	4,944
Net service tax liability to be paid in cash	**24,720**

Notes:

1. *Notification No. 26/2012 ST dated 20.06.2012* grants abatement of 60% in respect of services of renting of motorcab.
2. With effect from 01.10.2014, *Notification No. 26/2012 ST dated 20.06.2012* has been amended to provide that up to 40% CENVAT credit of input service of renting of a motorcab provided by a sub-contractor to the main contractor (providing service of renting of motorcab) could be availed by the main contractor, if the sub-contractor is paying service tax on full value i.e., no abatement is being availed by sub-contractor. This credit will be available even if the main contractor pays the service tax on abated value.

   Since ST Cabs Pvt. Ltd. has paid service tax on full value (₹ 1,00,000 x 12.36% = ₹ 12,360), LM Travels Pvt. Ltd. can avail credit upto ₹ 4,944 (40% of ₹ 12,360).
3. Since LM Travels Pvt. Ltd. is a company, reverse charge provisions will not apply in its case. Further, provisions of partial reverse charge will not apply in case of ST Cabs Pvt. Ltd. also, as in its case services are provided by a company and that too, to a recipient who is in similar line of business.

13. The action taken by Central Excise Officer is valid in law in view of the amendment made in section 87 of the Finance Act, 1994 vide the Finance (No.2) Act, 2014. Section 87 of the Finance Act, 1994 sets out the recovery provisions for service tax dues. With effect from 06.08.2014, a proviso has been inserted in clause (c) of section 87 to lay down that where the person (predecessor) from whom recovery is to be made

- transfers/disposes of his business/trade in whole or in part, or
- effects any change in the ownership thereof,

in consequence of which he is succeeded in such business or trade by any other person, then all goods, in the custody or possession of the successor may also be attached and sold for recovering the sums due from such predecessor at the time of such

transfer/disposal or change. Such attachment and sale could however be effected only after obtaining the written approval of the Commissioner of Central Excise.

Thus, Central Excise Officer's action of recovering the amount due from Mr. Piyush (predecessor), by attaching and selling the goods in the custody of Mr. Ankush (successor), is correct in law.

14. Section 90 of Finance Act, 1994 provides that offence involving collection of any amount as service tax but failure to pay the amount so collected to the credit of the Central Government beyond a period of six months from the date on which such payment becomes due is a cognizable offence, if the amount exceeds ₹50 lakh. Thus, by virtue of being a cognizable offence, the accused can be arrested without a warrant.

Since, in the given case amount involved exceeds ₹50 lakh (₹53 lakh) and the same has not been deposited within six months from the date on which such payment became due, Mr. Jagannath can be arrested for such an offence without an arrest warrant.

Section 91 of Finance Act, 1994, provides that the Principal Commissioner/ Commissioner of Central Excise by general or special order may authorize any officer of Central Excise, not below the rank of Superintendent of Central Excise, to arrest a person.

The maximum term of imprisonment in this case can be seven years in terms of section 89(1)(ii) of Finance Act, 1994. The proviso to clause (ii) of section 89(1), however, lays down that the punishment can be reduced to a term of less than six months, if there are special and adequate reasons, which would be recorded in the judgment of the Court, for granting lesser punishment. However, the fact that the accused has been convicted for the first time for an offence under Chapter V of Finance Act, 1994 is not considered as a special and adequate reason for awarding a sentence of imprisonment for a term of less than six months [Section 89(3)(i) of the Finance Act, 1994].

Thus, Mr. Jagannath cannot be imprisoned for a term of less than six months; his punishment could be anywhere between six months to seven years.

15. **The statement is not correct.** Recently, the Allahabad High Court addressed this issue in the case of *CCus & CEx & ST v. Indian Farmers Fertilizers Coop. Limited 2014 (35) STR 492 (All).*

In the instant case, the High Court relied on the case of *Mafatlal Industries Ltd. v. Union of India 1997 (89) ELT 247* wherein the Supreme Court held that "Where the burden of the duty has been passed on, the claimant cannot say that he has suffered any real loss or prejudice. The real loss or prejudice is suffered in such a case by the person who has ultimately borne the burden and it is only that person who can legitimately claim its refund."

The High Court, therefore, held that since the burden of tax had been borne by the service recipient themselves, the service recipient was entitled to claim refund of excess service tax paid consequent upon the downward revision of the charges payable by it.

It may be noted that section 11B of the Central Excise Act, 1944 is applicable to service tax vide section 83 of Finance Act, 1994.

16. Computation of export duty payable by Manchanda & Co.

Particulars	(US $)
Assessable value of the export goods (FOB price) [Note 1]	5,00,000
	(₹)
Value in Indian currency (US $ 5,00,000 x ₹ 60) [Note 2]	300,00,000
Export duty @ 8% [Note 3]	**24,00,000**

Notes:

1. As per section 14(1) of the Customs Act, 1962, assessable value of the export goods is the transaction value of such goods which is the price actually paid or payable for the goods when sold for export from India for delivery at the time and place of exportation.
2. As per third proviso to section 14(1) of the Customs Act, 1962, assessable value has to be calculated with reference to the rate of exchange notified by the CBEC on the date of presentation of shipping bill if goods are exported by aircraft.
3. As per section 16(1)(a) of the Customs Act, 1962, in case of goods entered for export, the rate of duty prevalent on the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation, is considered.

As per section 16(1)(a) of the Customs Act, 1962, when goods are entered for export under section 50 - which includes all three modes of export namely, vessel, aircraft and vehicle - the rate of duty prevalent on the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation, is considered. Further, as per third proviso to section 14(1) of the Customs Act, 1962, rate of exchange notified by the CBEC on the date of presentation of bill of export (in case of export by vehicle) has to be considered for computing assessable value of export goods.

Since the rate of exchange prevalent on 17.12.2014 (date of presentation of bill of export) is the same as on 12.12.2014 (date of presentation of shipping bill) and rate of duty also does not change (8% duty will be applicable for both export by aircraft and export by vehicle as rate of duty prevalent on the date of Let Export Order will only be considered in both the cases), the amount of export duty will remain same. Therefore, the answer will not change in the second case and the duty payable will be ₹ 24,00,000.

17. The issue involved in the given case is that whether the value of imported goods can be increased if Department fails to provide to the importer, the evidence of import of identical goods at higher prices. Recently, the Supreme Court addressed this issue in the case of *Gira Enterprises v. CCus. 2014 (307) ELT 209 (SC)*.

In the instant case, the Supreme Court observed that since Revenue did not supply the copy of computer printout, which formed the basis of the conclusion that the appellants under-valued the imported goods, the appellants obviously could not and did not have

any opportunity to demonstrate that the transactions relied upon by the Revenue were not comparable transactions.

The Supreme Court held that mere existence of alleged computer printout was not proof of existence of comparable imports. Even if assumed that such printout did exist and content thereof were true, such printout must have been supplied to the appellant and they should have been given reasonable opportunity to establish that the import transactions were not comparable.

Therefore, applying the ratio of the above mentioned decision to the given situation, it can be concluded that the contention of the Shine Enterprises is valid in law.

18. (a) The said statement is correct. Section 127B(1)(a) of Customs Act, 1962 has been amended with effect from 06.08.2014 vide the Finance (No. 2) Act, 2014 to provide that an application for settlement can also be filed in cases where bill of export, baggage declaration, label or declaration accompanying the goods imported/exported through post or courier have been filed and in relation to such document(s) a show cause notice has been issued.

(b) The said statement is incorrect. In case of seizure, erstwhile section 127B(2) of the Customs Act, 1962 prevented an assessee to make an application for settlement before the expiry of a period of 180 days from the date of seizure of his dutiable goods, books of account etc. However, with effect from 06.08.2014, sub-section (2) of section 127B of Customs Act, 1962 has been omitted vide the Finance (No. 2) Act, 2014. Thus, now settlement application can be made any time after the seizure of dutiable goods.

19. The said statement is not valid. Prior to 01.03.2015, public sector companies, resident public limited companies and resident private limited companies were notified under section 28E(c)(iii) of Customs Act, 1962 as the class or category of resident persons who can apply for advance ruling in case of specified matters relating to customs duty.

However, with effect from 01.03.2015, *Notification No. 27/2015 Cus (NT) dated 01.03.2015* has expanded the scope of advance ruling by additionally notifying resident firm as class or category of residents who can apply for advance ruling in case of specified matters relating to customs duty. Thus, now a resident firm will also be eligible to make an application for advance ruling in customs duty.

20. In order to be eligible for duty credit scrip entitlement under SEIS:

(a) Service provider must be located in India.

(b) It must provide only notified services in the specified manner.

(c) A service provider other than individual/sole proprietorship should have minimum net free foreign exchange earnings of US $15,000 in preceding financial year to be eligible for duty credit scrip.

(d) Service provider shall have to have an active IEC at the time of rendering such services for which rewards are claimed.

Since all the above conditions are fulfilled in the given case, ABC India Pvt. Ltd. is eligible for duty credit scrip entitlement under the Service Exports from India Scheme. However, while computing the duty credit scrip entitlement under said scheme, where the IEC holder is a manufacturer of goods as well as service provider, then the foreign exchange earnings and total expenses / payment / remittances shall be taken into account for service sector only. Therefore, export receipts of US $ 15,000 will not be taken into consideration while computing the duty credit scrip entitlement under the said scheme.

Thus, duty credit scrip entitlement of ABC India Pvt. Ltd. is 5% of US $ 50,000 i.e., US $ 2,500.

Further, if ABC India Pvt. Ltd. had provided telecom services to George Inc., it would not have been eligible for the duty credit scrip entitlement under said scheme as service providers in telecom sector are not eligible for the SEIS.

Applicability of Finance Act, Assessment Year etc. for November, 2015 – Final Examination

Paper 7 : Direct Tax Laws & Paper 8 : Indirect Tax Laws

The provisions of direct and indirect tax laws, as amended by the Finance (No.2) Act, 2014, including notifications and circulars issued up to 30th April, 2015, are applicable for November, 2015 examination. The relevant assessment year for Paper 7: Direct Tax Laws is A.Y.2015-16.

In Paper 7: Direct Tax Laws, the Wealth-tax Act, 1957 and Rules thereunder are **not** applicable for November 2015 examination.

Part II : Judicial Update – Direct Tax Laws

Significant Recent Legal Decisions

"Select Cases in Direct and Indirect Tax Laws – An Essential Reading for the Final Course" is a compilation of the significant decisions of Supreme Court, High Court and Authority for Advance Rulings. October, 2014 edition of the said publication is relevant for November, 2015 examination. Students may note that in addition to the cases reported in the said publication, following significant recent legal decisions are also relevant for November, 2015 examination:-

Basic Concepts

1. Can capital contribution of the individual partners credited to their accounts in the books of the firm be taxed as cash credit in the hands of the firm, where the partners have admitted their capital contribution but failed to explain satisfactorily the source of receipt in their individual hands?

CIT v. M.Venkateswara Rao (2015) 370 ITR 212 (T & AP)

Facts of the case: The assessee-firm was constituted in the year 1982 and its return for the assessment year 1993-94 was selected for scrutiny under section 143(3). The controversy was in relation to the capital contribution of ten partners aggregating to ₹ 76.57 lakhs. The assessee-firm's explanation that the partners have paid various amounts towards contribution of their share in the capital was not accepted since the source of income for the partners was not explained. The Commissioner (Appeals) observed that the amounts credited in the names of four partners were valid and that cash credits in the accounts of six other partners in the books of the firm were to be considered afresh by the Assessing Officer.

Issue under consideration: The issue before the High Court was whether the Assessing Officer was justified in treating the capital contribution of partners as income of the firm by invoking section 68?

High Court's Opinion: Section 68 directs that if an assessee fails to explain the nature and source of credit entered in the books of account of any previous year, the same can be treated as income. In this case, the amount sought to be treated as income of the firm is the contribution made by the partners to the capital. In a way, the amount so contributed constitutes the very substratum for the business of the firm and it is difficult to treat the pooling of such capital as credit. It is only when the entries are made during the course of business, they can be subjected to scrutiny under section 68.

Where the firm explains that the partners have contributed capital, section 68 cannot be pressed into service. At the most, the Assessing Officer can make an enquiry against the individual partners and not the firm when the partners have also admitted their capital contribution in the firm. The High Court made reference to decision in the case of *CIT v. Anupam Udyog 142 ITR 130 (Patna)* where it was held if there are cash credits in the books of the firm in the accounts of the individual partners and it is found as a fact that cash was received by the firm from its partner, then, in the absence of any material to

indicate that they are the profits of the firm, the cash credits cannot be assessed in the hands of the firm, though they may be assessed in the hands of individual partners.

High Court's Decision: The High Court, accordingly, held that the view taken by the Assessing Officer that the partnership firm has to explain the source of income of the partners as regards the amount contributed by them towards capital of the firm, in the absence of which the same would be treated as the income of the firm, was not tenable.

Charitable Trusts

2. In a case where properties bequeathed to a trust could not be transferred to it due to ongoing court litigation and pendency of probate proceedings, can violation of the provisions of section 11(5) be attracted?

DIT (Exemption) v. Khetri Trust (2014) 367 ITR 723 (Del)

Facts of the case: As per the 'will' of Late Raja Bahadur Sardar Singh, the entire property, including immovable property and shares in foreign companies, were bequeathed to the trust. However, the properties could not be transferred to or acquired by the trust because of ongoing litigation in the Court. In the probate proceedings, the 'will' was challenged and the probate proceedings are still pending.

The trustees paid ₹ 1,10,000 for raising a memorial for late Raja Bahadur Sardar Singh and the said amount was given to a business entity for this purpose, but due to the ongoing dispute, such project was not completed. The business entity, however, paid interest on the said amount. The Assessing Officer denied the benefit of exemption under section 11, on the ground that the asset held in the form of shares of foreign company and the advance given to business entity were contrary to the mandate of section 11(5) and thus, the condition specified in section 13(1)(d) has been violated.

Appellate Authorities' views: The Commissioner (Appeals) observed that the validity of the will has been challenged in the probate proceedings; therefore, till the 'will' is probated and affirmed as genuine, the trust would not acquire the legal right on the property for the purpose of Income-tax Act, 1961. In case the probate is denied, the properties would not devolve on the trust. The shares in foreign company were still in the name of the donor, Late Raja Bahadur Sardar Singh, and its acquisition by the trust is dependent upon the adjudication of the probate.

Further, with regard to the advance given to the business entity, the Commissioner (Appeals) found that the said amount cannot be treated as an investment which was covered and regulated by section 11(5), since the intent and purpose behind the payment was not investment.

These views of the Commissioner (Appeals) were confirmed by the Tribunal.

High Court's Decision: Based on the above factual findings, elucidated and affirmed by the Commissioner (Appeals) and the Tribunal, the High Court held that there was no violation of section 11(5) in this case.

3. Is the approval of Civil Court mandatory for amendment of trust deed, even in a case where the settler has given power to the trustees to alter the trust deed?

DIT (Exemptions) v. Ramoji Foundation (2014) 364 ITR 85 (AP)

Facts of the case: The settler gave power to the trustees to amend, alter, change or modify the objects of the trust deed with the approval of two-third majority. Such additional or altered object, however, must be of charitable nature falling within the definition thereof under the relevant provisions of the Income-tax Act, 1961. Based on these provisions of the trust deed and referring to the Supreme Court decision in *CIT v. Kamla Town Trust (1996) 217 ITR 699,* the Tribunal held that the trust deed can be amended without approaching the Civil Court. Therefore, the Tribunal directed the DIT (Exemptions) to grant registration to the assessee-trust under section 12AA on the basis of the amended trust deed.

Issue: The issue under consideration before the High Court is whether the Tribunal was correct in holding that the amendment to the trust deed can be made without approaching the Civil Court, on the basis of the decision in the case of *Kamla Town Trust (Supra)*.

High Court's Observations: The High Court observed that the power has been given to the trustees by the settler to amend the trust deed without approaching the Civil Court, provided all the conditions laid down by the settler are fulfilled. The sanction of Civil Court is required only when there is no such power. When the power has been specifically given to the trustees by the settler, no further power from the Civil Court is required.

The High Court made reference to the *Kamla Town Trust's* case and observed that it has not been stated anywhere in the Supreme Court's decision that in spite of the power given to them by settler to amend the trust deed, the trustees have to approach the Civil Court to get the trust deed rectified.

High Court's Decision: Accordingly, in this case, the High Court held that the Tribunal has correctly dealt with the matter and the trust deed amended by the trustees can be relied upon by the Revenue authorities for the purpose of granting registration under section 12AA.

Profits and gains from business or profession

4. Is the expenditure on replacement of dies and moulds, being parts of plant and machinery, deductible as current repairs?

CIT v. TVS Motors Ltd (2014) 364 ITR 1 (Mad)

Facts of the case: The assessee company, engaged in manufacture of motor cycles and spares, filed its return of income for the relevant assessment year. It later filed a revised return in which it claimed deduction under section 31 in respect of expenditure incurred on replacement of dies and moulds in the place of worn out dies and moulds. The claim

was rejected by the Assessing Officer on the ground that the assessee had claimed depreciation in respect of such expenditure in the earlier years.

Assessee's contention: The assessee contended that dies and moulds are not plant and machinery but are attachments to make plant and machinery function as per the requirements of the business. The assessee relied on the Madras High Court decision in the case of *Super Spinning Mill Ltd v. Asstt.CIT (2013) 357 ITR 720,* where expenditure on replacement of machinery parts was allowed as revenue expenditure.

High Court's Observations: The High Court referred to the Supreme Court ruling in *CIT v. Mahalakshmi Textile Mills Ltd. (1967) 66 ITR 710* and observed that as long as there was no change in the performance of the machinery and the parts that were replaced were performing precisely the same function, the expenditure has to be considered as current repairs of plant and machinery. In that case, the Supreme Court also observed that if grant of relief to an assessee is justified on another ground, the Revenue is bound to consider such claim of granting the relief. Accordingly, in this case, even though the assessee has claimed depreciation in the earlier years, the claim of the assessee for deduction of expenditure on replacement of moulds and dies as 'current repairs" is justified on the ground that there was no change in the performance of the machinery on account of such replacement.

The High Court also referred to its decision in the case of *CIT v. Machado Sons (2014) 2 ITR – OL 385* holding that **when the object of the expenditure was not for bringing into existence a new asset or to obtain a new advantage, the said expenditure qualifies as 'current repairs' under section 31.**

High Court's Decision: Applying the rationale of above decisions, the High Court held that "moulds & dies" are not independent of plant and machinery but are parts of plant and machinery. Once the dies are worn out, they had to be replaced so that the machine can produce the product according to business specifications. Thus, the expenditure incurred by the assessee towards replacement of parts of machinery to ensure its performance without bringing any new asset or advantage, is eligible for deduction as 'current repairs' under section 31.

5. Is guarantee commission paid by a company to its employee directors deductible as its business expenditure, where such guarantee was given by the employee directors to the bank for enabling credit facility to the company?

Controls & Switchgear Contractors Ltd v. Dy.CIT (2014) 365 ITR 312 (Del)

Facts of the case: The assessee, a listed company, wanted some credit facilities from the bank for its business purpose. The banker insisted on personal guarantee of the directors as a pre-condition for providing financial assistance to the company. The directors were employees of the company who were drawing salary from the company. A resolution was passed for paying commission to the directors and a sum of ₹ 24.37 lakhs each was paid as commission calculated at the rate of 1.5% of the principal sum, in respect of which personal guarantee was furnished by the directors to the bank.

Assessing Officer's Contention: The Assessing Officer applied section 36(1)(ii) and held that if the amount was not paid to them as commission, the same would have been payable as profits or dividend. Accordingly, the Assessing Officer contended that the assessee-company avoided dividend distribution tax under section 115-O which was otherwise payable. The appellate authorities also confirmed the disallowance of expenditure.

High Court's Observations and Decision: The High Court observed that the directors of the company are employees of the company and are entitled to remuneration for the services rendered as employees. The assessee-company passed a resolution resolving that the directors be paid commission for providing their personal guarantees for the financial assistance availed by the assessee-company from the bank. This act of providing personal guarantee was clearly beyond the scope of their services as employees of the company. The assessee-company, in its commercial wisdom, had agreed to pay a commission for furnishing of such guarantees by the director employees, which cannot be faulted. In such a case, the Assessing Officer only has to determine whether the transactions are real and genuine. It is not within his jurisdiction to impose his views as regards the necessity or the quantum of expenditure undertaken by the assessee. As regards section 36(1)(ii) the recipient directors were not entitled to receive the amount as commission in lieu of bonus or dividend. Dividend is paid to all the shareholders and the recipient directors were not the only shareholders of the company. The payment of commission, hence, cannot be taken as payment of dividend, since payment of dividend would result in payment to all the shareholders and not to select shareholders.

The High Court, therefore, set aside the Tribunal's order and directed rectification of the disallowance of amount paid as commission to directors.

6. Can employees contribution to Provident Fund and Employee's State Insurance be allowed as deduction where the assesssee-employer had not remitted the same on or before the "due date" under the relevant Act but remitted the same on or before the due date for filing of return of income under section 139(1)?

CIT v. Gujarat State Road Transport Corpn (2014) 366 ITR 170 (Guj)

Facts of the case: The assessee collected employees' contribution to Provident Fund and ESI which were remitted, after the due date under the relevant Acts but before the 'due date' for filing the return specified in section 139(1). The assessing authority held that the amount collected by way of employees' contribution to PF and ESI are income under section 2(24)(x) and their remittance is governed by section 36(1)(va). The time limit prescribed for remitting the contribution is the 'due date' prescribed under the Provident Funds Act, Employees' State Insurance Act, rule, order or notification issued thereunder or under any standing order, award, contract or service or otherwise.

Issue: The issue under consideration is whether extended time limit upto the due date of filing the return contained in section 43B would be available in respect of remittances which are governed by section 36(1)(va).

High Court's Observations: The High Court noted that section 43B(b) pertaining to employer's contribution cannot be applied with respect to employees' contribution which is governed by section 36(1)(va). So far as the employee's contribution is concerned, the *Explanation* to section 36(1)(va) continues to remain in the statute and there is no provision for applying the extended time limit provided under section 43B for remittance of employee's contribution. The amount of employee's contribution to PF and ESI is an income upon recovery from salary and its remittance within the 'due date' as specified in *Explanation* to section 36(1)(va) makes it eligible for deduction. Employees' contribution recovered by the employer is not eligible for extended time limit upto the due date of filing of return, which is available under section 43B in the case of employer's own contribution.

High Court's Decision: The High Court, accordingly, held that the delayed remittance of employees' contribution beyond the 'due date' prescribed in section 36(1)(va), is not deductible while computing the business income, even though such remittance has been made before the due date of filing of return of income under section 139(1).

Note: *A contrary view was expressed by Uttrakhand High Court in the case of CIT v. Kichha Sugar Co. Ltd. (2013) 356 ITR 351 holding that the employees' contribution to provident fund, deducted from the salaries of the employees of the assessee, shall be allowed as deduction from the income of the employer-assessee, if the same is deposited by the employer-assessee with the provident fund authority on or before the due date of filing the return for the relevant previous year.*

7. Is interest paid by the holding company as guarantor for the amount borrowed by the subsidiary company deductible under section 36(1)(iii)?

JK Synthetics Ltd v. CIT (2014) 369 ITR 310 (All)

Facts of the case: The assessee is a public limited company engaged in the manufacture and sale of synthetic yarn and cement. It stood as guarantor to the loans taken by its subsidiary company. The subsidiary company incurred heavy losses and as a result became a defaulter in paying its debts. The assessee was a guarantor to the loans taken by the subsidiary company for the purpose of protecting its own business interest. Since the subsidiary company could not adhere to the repayment of its liabilities, the assessee-holding company started repayment of loan installments on behalf of the subsidiary company and claimed ₹ 8 lakhs, being interest paid, as deduction under section 36(1)(iii). The claim of the assessee was rejected in assessment.

High Court's Opinion: To claim deduction under section 36(1)(iii) the following conditions are to be satisfied viz., (i) interest should have been payable; (ii) there should be a borrowing; and (iii) capital must have been borrowed or taken for business purposes. The High Court observed that if the capital borrowed is not utilized for the purposes of the business, the assessee will not be entitled to deduction under the clause.

It made reference to the Apex Court ruling in *Madhav Prasad Jatia v. CIT (1979) 118 ITR 200* where the expression '**for the purpose of business**' occurring in section

36(1)(iii) was held as wider in scope than the expression 'for the purpose of earning income, profits or gains'. The Apex Court observed that where a holding company has a deep interest in its subsidiary and advances money to the subsidiary and the same is used by the subsidiary for its business purposes, the lending-holding company would be entitled to deduction of interest on its borrowed loans.

High Court's Decision: Applying the rationale of the above Apex Court ruling to this case, the High Court observed that the assessee had deep business interest in the existence of subsidiary and therefore, repaid installments of loan to financial institutions. Such loans were given for the purpose of business. The High Court, thus, held that the claim for deduction of interest by the assessee-holding company is allowable.

8. Is expenditure incurred for construction of transmission lines by the assessee for supply of power to UPPCL by the assessee deductible as revenue expenditure?

Addtl. CIT v. Dharmpur Sugar Mill (P) Ltd (2015) 370 ITR 194 (All)

Facts of the case: The assessee was engaged in the business of manufacture and sale of sugar, chemicals and power and had a distillery. It paid ₹ 8.48 crores to Uttar Pradesh Power Corporation Ltd (UPPCL) for construction of transmission line and other supporting work for supply of power to UPPCL. The assessee generated power which was sold to UPPCL, its only customer. The agreement between the assessee and UPPCL stipulated that the entire expenditure for erection and installation of power transmission lines, towers and ancillaries from the point of power generation to sub-grid station would be incurred by the assessee. The UPPCL is to ensure quality control of the equipment and material and the work has to be carried out under its supervision and prior approval. The agreement stipulated that the entire power transmission line including towers and erection would be property of UPPCL which would provide for the subsequent supervision and maintenance. The assessee claimed the entire expenditure as a deduction under section 37(1). The claim of the assessee was disallowed by the Assessing Officer. However, the Commissioner (Appeals) deleted the disallowance by holding that by incurring the expenditure the assessee acquired right to make use of the asset for facilitating efficient conduct of its business and making it more profitable but without getting any advantage of enduring benefit to itself. The assessee did not acquire any asset to get covered by section 32 and hence, the expenditure incurred was revenue in nature. The Tribunal, too, confirmed the order of the Commissioner (Appeals).

High Court's Opinion: The High Court made reference to *Empire Jute Co Ltd v. CIT (1980) 124 ITR 1,* where the Supreme Court held that the true test is to consider the nature of the advantage in a commercial sense and it is only where the advantage is in the capital field that the expenditure would be disallowed. If the advantage consists in merely facilitating its trading operations or conducting its business while leaving the capital field untouched, the expenditure would be on revenue account.

A similar precedent in *CIT v. Gujarat Mineral Development Corpn. Ltd (1981) 132 ITR 377 (Guj)* was also cited to hold that the expenditure incurred in the laying of transmission lines was on revenue account.

The Allahabad High Court also made reference to the Rajasthan High Court ruling in *CIT v. Hindustan Zinc Ltd. (2009) 221 CTR (Raj) 637*, wherein it was observed that the erection of power lines by the assessee was for facilitating its routine operations and for smooth functioning of its business. The power lines remained the property of the Electricity Board. The High Court, therefore, held that the assessee had not acquired a capital asset or any enduring benefit or advantage.

High Court's Decision: Following the principle of law laid down by the Supreme Court in *Empire Jute Mills'* case, the Allahabad High Court, in this case, held that the expenditure which was incurred by the assessee in the laying of transmission lines was clearly on the revenue account. The transmission lines, upon erection, vested absolutely in UPPCL. The expenditure which was incurred by the assessee was for aiding efficient conduct of its business since the assessee had to supply electricity to its sole consumer UPPCL. This was not an advantage of a capital nature.

9. Where the assessee-company came into existence on bifurcation of a Joint Venture Company (JVC), can the amount paid by it to the JVC for use of customer database and transfer of trained personnel be claimed as revenue expenditure?

CIT v. IBM Global Services India P Ltd (2014) 366 ITR 293 (Karn)

Facts of the case: The assessee-company came into existence on the bifurcation of a joint venture company floated earlier by two other companies. The assessee-company paid ₹ 530 lakhs for use of domestic customer database to the joint venture company, which gave information about various customers who patronized the company in the past and who continued to have service maintenance contract. This enabled the assessee to provide maintenance support services and effectively run its software business. Also, certain skilled and trained employees of the joint venture company were transferred to the assessee-company for which it made a payment of ₹ 938.58 lakhs to the joint venture company. The assessee claimed both the payments viz. payment for use of domestic customer database and absorption of trained employees, as revenue expenditure. The claim of the assessee was disallowed by the Assessing Officer.

Assessing Officer's Contentions: The Assessing Officer contended that domestic customer database is a capital asset which provides an enduring advantage or benefit to the assessee, since by utilizing the same, the assessee can successfully run its business activities over a considerable period of time. Hence, he treated the payment made for acquisition of domestic customer database as the payment made towards acquisition of capital asset. The Assessing Officer also contended that compensation paid by the assessee to the joint venture company for transfer of human skill is a capital expenditure, since the expenditure incurred on recruitment and training of transferred personnel would provide an enduring benefit.

High Court's Observations and Decision: The High Court observed that the expenditure incurred for use of customer database did not result in acquisition of any capital asset. The assessee got the right to use the database and the company which

provided the database was not precluded from using such database. Therefore, the expenditure incurred was for use of data base and not for acquisition of such data base and, hence, is deductible as revenue expenditure.

As regards payment for obtaining trained and skilled employees, it was held that the joint venture company spent a lot of money to give training to employees who were transferred to the assessee-company. They were trained in the field of software. They have opted for employment with the assessee, and for their past services with the joint venture company, expenditure has been incurred. In effect, the payment made by the assessee-company was towards expenditure incurred for their training and recruitment. Such expenditure was in the revenue field, and therefore, the payment made by the assessee-company as per agreement to save such expenditure was also revenue in nature. Therefore, the expenditure incurred for obtaining trained and skilled employees cannot be termed as capital expenditure though the benefit may be of enduring nature. The High Court, thus, held that both the expenditures claimed were allowable as revenue expenditure.

10. Is release of retention money to the assessee-contractor on the basis of furnishing bank guarantee taxable as income of the assessee, where the assessee's right to receive retention money is subject to certain conditions including certification by the engineer in-charge?

Amarshiv Construction P Ltd v. Dy.CIT (2014) 367 ITR 659 (Guj

Facts of the case: The assessee-company was engaged in the business of civil construction. It was awarded a construction contract by Sardar Sarovar Narmada Nigam Ltd for construction of a part of the Sardar Sarovar Dam. Out of the bills raised by the assessee for such construction work, a certain portion was retained by the payer as retention money. This would be released only upon being certified by the engineer in-charge that the construction was carried out without any defects. The contract agreement was subsequently modified to permit greater liquidity to the assessee-contractor by allowing release of retention money where the contractor provides a matching bank guarantee for the sum to be released. Such bank guarantee would be encashed to the extent of dues or any defect found in the construction carried out or discharged at the end of the warranty period.

Issue: The issue before the High Court was whether the release of retention money based on bank guarantee results in accrual of income to the assessee-contractor.

High Court's Observations: The High Court observed that the crucial question is the point of time at which the assessee gets the right to receive such sum as his income. The High Court referred to the various decisions holding that **whenever the retention money of a contractor for performance of guarantee was held back by the employer of the contract, it cannot be taxed at that point of time and would accrue only when the release of retention money becomes an enforceable right to the contractor.** The moot point was a change in terms of the contract for release of retention money based on furnishing of bank guarantee by the contractor.

All the amounts received would not mean receipt of income. Whether income did accrue or not would depend on the fact of whether the right to receive the same had accrued to the payee or not. The fact that tax was deducted at source by the payer would also be of no consequence. The contractor i.e., the payee, has no control over tax deduction by the payer. Mere tax deduction will not decide the taxability of receipt. The manner in which the recipient has accounted the receipt in the books is also not a criterion for deciding the character of receipt. The amount was released based on furnishing of bank guarantee which cannot be equated or interpreted as conferring a right on the contractor-assessee to seek release of funds and to tax the same as income. The amount received is not a free entitlement and the bank guarantee could be invoked for recovery of dues for the defects in the work performed. Accordingly, the amount released based on bank guarantee with pending procedural formalities for approval of the work performed could not be taxed as income. This is because the income did not accrue when the funds were released as the release is based on bank guarantee and not on approval of performance appraisal.

There was no material change in the terms of contract, since both before and after the amendment of the agreement, the right to receive the amount was subject to the vital conditions of recoveries and adjustments against the amounts found due or defects in the work completed by the contractor. The right to receive the amount is also subject to certification by the engineer-in-charge that no liability was attached to the contractor. Therefore, the character of the amount received on furnishing of bank guarantee did not undergo any change. It still retained the character of retention money

High Court's Decision: The High Court, therefore, held that the release of retention money against furnishing of bank guarantee was a receipt not chargeable to tax.

11. Is interest income on margin money deposited with bank for obtaining bank guarantee to carry on business, taxable as business income?

CIT v. K and Co. (2014) 364 ITR 93 (Del)

Facts of the case: The assessee running a lottery, deposited certain funds with a bank in order to obtain bank guarantee to be furnished to the State Government of Sikkim. Such guarantee enabled the assessee to carry on the business of printing lottery tickets and for conducting lotteries on behalf of the State Government of Sikkim. The funds which were held as margin money, earned some interest.

Issue: The issue under consideration is whether such interest income would be taxable under the head 'Profits and Gains from Business or Profession' or under the head 'Income from other sources'.

High Court's Observations: The High Court noted that the interest income from the deposits made by the assessee is inextricably linked to the business of the assessee and such income, therefore, cannot be treated as income under the head 'Income from other sources'. The margin money requirement was an essential element for obtaining the bank guarantee which was necessary for the contract between the State Government of

Sikkim and the assessee. If the assessee had not furnished bank guarantee, it would not have got the contract for running the said lottery

High Court Decision: The High Court, accordingly, held that the interest income received on funds kept as margin money for obtaining the bank guarantee would be taxable under the head "Profits and gains of business or profession".

12. Under which head of income is franchise fee received by an assessee in tourism business, against special rights given to franchisees to undertake hotel business in assessee's property, taxable?

Tamil Nadu Tourism Development Corporation Ltd v. Dy. CIT (2014) 368 ITR 533 (Mad)

Facts of the case: The assessee-company, a wholly owned Government of Tamil Nadu Undertaking, was engaged in the business of development of tourism in the State. It leased some of its loss making hotel units to various franchisees for a consideration. The agreement envisaged leasing of hotels with attendant conditions including display of its name above the name of the franchisee in the name board, quality of food supplied, maintenance of rooms and buildings etc. to be followed by the franchisee. The assessee offered franchise fee as "Income from house property" and claimed deduction at 30% of Net Annual Value (NAV) under section 24, which was negatived in the assessment.

Appellate Authorities' Views: The Commissioner (Appeals) observed that the assessee was not engaged in any commercial or business activity to earn business income and thus, upheld the contention of the assessee that such income is taxable under the head "Income from house property". The Tribunal, however, observed that the assessee had not withdrawn from the business of carrying on tourism activities and it was only to earn more profits from its loss making units that it has let out the properties including business to franchisees. Thus, it held that the income arising from letting out of such properties is chargeable to tax as income from business. It negatived the claim for deduction of 30% of NAV made by the assessee.

High Court's Opinion: The issue before the High Court is whether the income by way of franchisee fee is taxable as income from business or as income from house property.

The High Court looked into the contract between the assessee and the franchisees which contained various conditions ranging from obtaining of permits and licences, maintenance of rooms, common area, garden maintenance, catering, Bar etc with 33 clauses. The assessee had not simply leased the land and building but had imposed further conditions as to how the business of franchisees' should be conducted with regard to the hotels given on lease.

The special conditions stipulated in the contract clearly indicated that the name of the assessee should be prominently indicated in the name board and that the name of the franchisee should be below the name of the assessee, thereby, making it clear that the assessee continued to operate the business through the franchisees. Thus, these special conditions were a clear indicator that the assessee continued to be in the business of tourism activities, though not directly but through the franchisees, and received income

as franchisee fee. The assessee received franchisee fee for giving a special right or privilege to the franchisees to undertake tourism business in the property.

High Court's Decision: The High Court, accordingly, held that the income earned by the assessee by way of franchisee fee is in the nature of business income and not income from house property.

13. Does payment of net present value of deferred sales tax liability result in remission of liability assessable under section 41(1)?

CIT v. Sulzer India Ltd (2014) 369 ITR 717 (Bom)

Facts of the case: The Government of Maharashtra, in order to grant incentives for establishing units in industrially backward or hilly areas, announced a sales tax deferral scheme. Under the scheme, the eligible units were permitted to collect sales tax and retain the same for a specified period of time. After the specified period, the amounts are to be remitted to the exchequer. The amount retained was treated as deemed payment of tax for which a certificate was given. Subsequently, the Government announced a scheme whereby the units could opt to prematurely pay the sales tax liability at net present value.

The assessee, in this case, had a deferred sales tax liability of ₹ 752.01 lakhs for which the payment at net present value was ₹ 337.13 lakhs. The assessee transferred the balance ₹ 414.88 lakhs to its capital reserve account.

The Assessing Officer made an addition of ₹ 414.88 lakhs to the income of the assessee, being remission of loan liability for premature payment of the amount of net present value by invoking section 41(1).

The Tribunal held that the amount credited to the capital reserve account in the books of the assessee and cannot be termed as remission / cessation of liability. Consequently, no benefit had arisen to the assessee in terms of section 41(1)(a). The issue before the High Court was regarding the taxability of the amount gained by the assessee by discharging the sales tax liability at net present value.

Revenue's contention *vis-à-vis* Assessee's contention: The Revenue argued that sales tax is always a trading receipt and the amount foregone by the State is a benefit by way of reduction in liability which is chargeable to tax under section 41(1).

The assessee contended that the sales tax liability in this case was not a liability in praesenti. The liability has been ascertained and determined in terms of the rules. The net present value is taken into consideration. Thus, the liability is not wiped out but its present value is ascertained and determined and that has been paid. There was no concession. There is absolutely no settlement negotiated or otherwise.

High Court's Opinion: The High Court observed that to apply section 41(1), the first requirement is that the allowance or deduction is made in respect of loss, expenditure or a trading liability incurred by the assessee and subsequently, the assessee obtained benefit in respect of such trading liability by way of remission or cessation thereof. In this

case, there was no evidence to show that there has been any remission or cessation of the liability by the State Government. Thus, one of the requirements of section 41(1)(a) has not been fulfilled in this case.

The Tribunal, while deciding the case, held that there was no remission or cessation of liability and the amount credited is a capital receipt. The High Court referred to Karnataka High Court decision in the case of *CIT v. Mcdowell & Co Ltd (2014) 369 ITR 684 (Karn)* and concurring with the reasoning of the Karnataka High Court, held that the amount retained under the deferral scheme was nothing but a loan given by the Government by way of incentive for setting up the industrial unit in a rural area. The said loan could have been retained for 15 years but an option for early repayment at net present value was given and on such payment, the entire liability to pay tax / loan stood discharged. It is not a benefit conferred on an assessee. Therefore section 41(1) is not attracted to facts of the case.

High Court's Decision: The High Court, accordingly, held that the remittance of deferred sales tax liability at net present value will not result in any income chargeable to tax under section 41(1).

Income from Other Sources

14. Does repair and renovation expenses incurred by a company in respect of premises leased out by a shareholder having substantial interest in the company, be treated as deemed dividend?

CIT v. Vir Vikram Vaid (2014) 367 ITR 365 (Bom)

Facts of the case: The assessee holds more than 75% of equity shares in a company and is the executive director of the company. In his personal capacity, he is the owner of certain premises in which he was carrying on a proprietary business. Subsequently, the assessee ceased to carry on the business of proprietary concern and hence, let out the premises to the company. The company incurred ₹ 2.51 crores towards construction and improvement of factory premises, which it continued to use otherwise than as the owner of the premises. The Assessing Officer held that the amounts spent by the company towards repair and renovation is taxable as deemed dividend in the hands of the assessee. In the alternative, the said amount was to be treated as a perquisite taxable in the hands of the assessee.

Appellate Authorities' Views: The Commissioner (Appeals) noted the assessee's submission that he had leased out the said premises for a rent lower than the prevailing market rate with an understanding that all expenditure for its upkeep and maintenance would be spent by the company on account of the assessee having stopped business activities. According to the Commissioner (Appeals), the assessee failed to substantiate his claim. The Commissioner (Appeals) was of the view that all the conditions provided under section 2(22)(e) for deemed dividend were satisfied. On the other hand, the Tribunal concluded that the payment was neither a deemed dividend nor a perquisite chargeable to tax.

High Court's Observations: The challenge before the High Court by the Revenue was only with regard to applicability of section 2(22)(e) in this case. The High Court observed that no money had been paid by way of advance or loan to the shareholder who has substantial interest in the company. Further, the amount spent was towards repairs and renovation of the premises owned by the assessee but occupied by the company as lessee. There is no dispute that the company had taken on rent the aforesaid premises.

The High Court observed that the expenditure incurred by virtue of repairs and renovation on the premises cannot be brought within the definition of advance or loan given to the shareholder having substantial interest in the company, though he is the owner of the premises. It cannot be treated as payment by the company on behalf of the shareholder or for the individual benefit of such shareholder. If held in such manner, it is a mere assumption not tenable in law.

High Court's Decision: The High Court, accordingly, held that the repair and renovation expenses in respect of premises occupied by the company cannot be treated as deemed dividend in the hands of shareholder being the owner of the building.

Assessment of various entities

15. Where land inherited by three brothers is compulsorily acquired by the State Government, whether the resultant capital gain would be assessed in the status of "Association of Persons" (AOP) or in their individual status?

CIT v. Govindbhai Mamaiya (2014) 367 ITR 498 (SC)

Facts of the case: Three brothers inherited a property consequent to demise of their father. A part of this bequeathed land was acquired by the State Government and compensation was paid for it. On appeal, compensation was enhanced and the enhanced compensation was paid with interest.

Issue: The issue under consideration is regarding the status in which capital gain arising on transfer of property would be assessed. The assessees' offered income in their status as "individual" but the Revenue sought to tax the same in their status as "Association of Persons" (AOP).

High Court's Observations: The High Court found that the parties inherited the property and there was no material on record to suggest consensus *ad idem* between the brothers for formation of AOP. It referred to *CWT v. Chander Sen (1986) 161 ITR 370 (SC)* to hold that as per section 4 of the Hindu Succession Act, 1956, income from the asset inherited by a son from his father has to be assessed as income of the son individually. Further, as per section 8 of the Hindu Succession Act, 1956, the property of the father devolves on his son in his individual capacity and not as karta of HUF. Thus, it was held that the income is chargeable to tax in their individual status and not as AOP.

Supreme Court's Observations: The Supreme Court referred to its earlier decision in the case of *Meera & Co v. CIT (1997) 224 ITR 635* in which the earlier precedent in the case of *CIT v. Indira Balakrishna (1960) 39 ITR 546 (SC)* was followed. The Apex Court

noted that "Association of Persons" means an association in which two or more persons join in a common purpose or common action.

The Supreme Court also referred to its judgment in *G. Murugesan & Bros. v. CIT (1973) 4 SCC 211*. In that case, it was held that an association of persons could be formed only when two or more persons voluntarily combined together for certain purposes.

In this case, the property in question came to the assessees' possession through inheritance i.e., by operation of law. It is not a case where any 'association of persons" was formed by volition of the parties. Further, even the income earned in the form of interest is not because of any business venture of the three assessees, but is the result of the act of the Government in compulsorily acquiring the said land. Thus, the basic test to be satisfied for making an assessment in the status of AOP is absent in this case.

Apex Court's Decision: The Apex Court, accordingly, held that the income from asset inherited by the legal heirs is taxable in their individual hands and not in the status of AOP.

Income-tax Authorities

16. Can the assessee's application, for adjustment of tax liability on income surrendered during search by sale of seized gold bars, be entertained, where assessment has not been completed?

Hemant Kumar Sindhi & Another v. CIT (2014) 364 ITR 555 (All)

Facts of the case: Consequent to a search in the premises of the assessee, some gold bars were seized from the locker. The assessee voluntarily disclosed some income during the course of search. The assessee filed an application for sale of the gold bars and adjustment of tax liability on undisclosed income out of the sale proceeds. This would obviate his liability to pay interest under sections 234B and 234C. The Assessing Officer dismissed the application on the reasoning that only when the assessment is completed and tax demand is crystallized, can recovery be initiated by the sale of gold bars. The assessee filed a writ contesting the dismissal of application by the Assessing Officer.

High Court's Observations: The High Court observed that section 132B(1)(i) uses the expression "the amount of any existing liability" and "the amount of the liability determined". The words "existing liability" postulates a liability that is crystallized by adjudication; Likewise, "a liability is determined" only on completion of the assessment. **Until the assessment is complete, it cannot be postulated that a liability has been crystallized.**

As per the first proviso to section 132B(1)(i), the assessee may make an application to the Assessing Officer for release of the assets seized. However, he has to explain the nature and source of acquisition of the asset to the satisfaction of the Assessing Officer. It is not the *ipse dixit* of the assessee but the satisfaction of the Assessing Officer on the basis of the explanation tendered by the assessee which is material.

High Court's Decision: The High Court, accordingly, held that the Assessing Officer was justified in his conclusion that it is only when the liability is determined on the completion of assessment that it would stand crystallized and in pursuance of which a demand can be raised and recovery can be initiated. Therefore, in the present case, the first proviso to section 132B(1)(i) would not be attracted. The High Court, thus, dismissed the writ petition.

Assessment Procedure

17. Can the Assessing Officer reassess the issues other than the issues in respect of which proceedings were initiated under section 147, when the original "reasons to believe" on the basis of which the notice was issued ceased to exist?

CIT v. Mehak Finvest P Ltd (2014) 367 ITR 769 (P&H)

Facts of the case: In the present case, reassessment proceedings were initiated against the assessee on the reason that various finance companies managed and controlled by certain persons were engaged in accommodation entries and the assessee-company was one among them. However, during the reassessment proceedings, the Assessing Officer noticed that fresh share application money amounting to ₹ 47 lakhs could not be explained by the assessee and hence invoked section 68 to bring to tax such sum. There was no addition on the basis of the original reason for which reassessment proceedings were initiated.

Issue: The issue under consideration is whether an addition can be made in reassessment when the original reasons on the basis of which notice for reassessment was issued did not survive.

Assessee's Contention vis-a-vis Revenue's Contention: The assessee contended that when the original reason prompting the initiation of reassessment proceedings did not survive, the question of making addition on some other fresh grounds was not possible. The basis of the assessee's contention was the Bombay High Court ruling in case of *CIT v. Jet Airways (I) Ltd (2011) 331 ITR 236 and Delhi High Court ruling in Ranbaxy Laboratories Ltd v. CIT (2011) 336 ITR 136*.

On the other hand, the Revenue placed reliance on the jurisdictional High Court decision in the case of *Majinder Singh Kang v. CIT (2012) 344 ITR 358* holding that reassessment can be made on the basis of additional grounds, even though the original reason forming the basis of issue of notice did not survive.

High Court's Observations: The High Court noted that *Explanation 3 to section 147* nowhere postulates or contemplates that the Assessing Officer cannot make any additions on any other ground unless some addition is made on the basis of the original ground for which reassessment proceeding was initiated. It cited the dismissal of special leave petition (SLP) against the High Court ruling in *Majinder Singh Kang's* case by the Supreme Court on 19.08.2011 as the binding precedent.

High Court's Decision: The High Court, accordingly, held that even though no addition is made on the original grounds which formed the basis of initiation of reassessment proceedings, the Assessing Officer is empowered to make additions on another ground for which reassessment notice might not have been issued but which came to his notice subsequently during the course of proceedings for reassessment.

Note : *A contrary view expressed by the Delhi High Court in Ranbaxy Laboratories Ltd.'s case has been reported in the October, 2014 edition of the publication "Select Cases in Direct and Indirect Tax Laws"*

18. Does the finding or direction in an appellate order that income relates to a different assessment year empower reopening of assessment for that assessment year, irrespective of the expiry of the six year time limit?

CIT v. PP Engineering Work (2014) 369 ITR 433 (Del)

Facts of the case: The Tribunal, in its order, directed that the cash credit of ₹ 32 lakhs found credited in the books of the assessee in the financial year 1999-2000 is chargeable to tax in the assessment year 2000-01 as against the assessment made by taxing the said amount in the assessment year 2001-02. In short, the Tribunal gave a finding that the cash credit under section 68 was assessable in a different assessment year than the assessment year in respect of which it heard the appeal. This prompted the Assessing Officer to issue a notice under section 148 in February, 2009 for reopening the proceedings for the A.Y.2000-01. The issue is validity of notice issued after a lapse of 6 years from the end of the relevant assessment year.

The Commissioner (Appeals) held that the reassessment is barred by time limitation and the Tribunal also upheld the order of the Commissioner (Appeals) without making reference to section 150 read with *Explanation 2* to section 153.

High Court's Opinion: The High Court made reference to section 150 which overrides the time limitation specified in section 149. Also, *Explanation 2* to section 153 makes it clear that when an order in appeal, revision or reference is made whereby any income is excluded from the total income of an assessee for an assessment year, an assessment of such income for another assessment year shall be deemed to be one made in consequence of or to give effect to any finding or direction contained in the said order for the purposes of section 150 and section 153.

The High Court made reference to the Delhi High Court ruling in the case of *Rural Electrification Corporation Ltd v. CIT (2013) 355 ITR 345* and opined that the findings of Commissioner (Appeals) and Tribunal on the question of limitation as legally untenable and incorrect.

High Court's Decision: The High Court observed that in view of the order of the Tribunal that the credit entries related to the earlier assessment year i.e., A.Y. 2000-01, the Assessing Officer initiated reassessment proceedings under section 147 by issue of notice under section 148 for the year and passed an order dated 29/12/2009 making an addition of ₹ 32 lakhs. The High Court held that by virtue of section 150 read with *Explanation 2* to section 153, the said order was not barred by limitation.

Note – *Under section 149(1)(b), the time limit for issue for notice under section 148 is six years from the end of the relevant assessment year, where the income chargeable to tax which has escaped assessment amounts to or is likely to amount to ₹ 1 lakh or more for that year.*

Section 150(1) states that notwithstanding anything contained in section 149, notice under section 148 may be issued at any time for the purpose of making an assessment or reassessment or recomputation in consequence of or to give effect to any finding or direction contained in an appellate or revisionary order.

Explanation 2 to section 153 provides that where by an order referred to in section 250, 254, 260, 262, 263 or 264, any income is excluded from the total income of the assessee for an assessment year, then, an assessment of such income for another assessment year shall, for the purposes of section 150 and section 153, be deemed to be one made in consequence of or to give effect to any finding or direction contained in the said order.

19. Is initiation of reassessment beyond a period of 4 years on the basis of subsequent Tribunal and High Court ruling valid, if there is no failure on the part of the assessee to disclose fully and truly all materials facts?

Allanasons Ltd v. Dy. CIT (2014) 369 ITR 648 (Bom)

Facts of the case: The assessee-company filed its return of income in which a claim for deduction under Chapter VI-A was made. The case was subjected to scrutiny assessment and order under section 143(3) was passed reducing the claim of deduction under Chapter VI-A. After 4 years from the end of the assessment year, a notice under section 148 was issued ascribing reasons such as subsequent tribunal and other court decisions which show that the deduction was excessively allowed in this case. The assessee challenged the reassessment proceedings by means of a writ before the court, contending that it is a settled position in law that the decision rendered by court subsequent to the assessment order does not by itself amount to failure on the part of the assessee to fully and truly disclose all material facts necessary for assessment.

High Court's Opinion: The High Court observed that it is well settled in terms of the proviso to section 147, that where any assessment is sought to be opened beyond a period of four years from the end of the relevant assessment year, two conditions have to be fulfilled cumulatively. The first condition is that there must be reason to believe that income chargeable to tax has escaped assessment. The second condition is that such escapement of income should have arisen due to failure on the assessee's part to fully and truly disclose all material facts required for the assessment.

Thus, escapement of income prompting reopening of assessment beyond the period of 4 years from the end of the assessment year is not possible unless it is due to the failure of the assessee to disclose fully and truly all material facts necessary for assessment.

Even a subsequent change of law cannot be taken as income escaping assessment for triggering reassessment provisions beyond 4 years from the end of the assessment year unless there was a failure on the part of the assessee to disclose fully and truly all material facts necessary for assessment. The High Court observed that in this case, the reasons recorded, when read as a whole did not indicate even remotely any failure on

the part of the assessee to disclose fully and truly any material fact necessary for assessment.

High Court's Decision: The High Court, accordingly, held that a subsequent decision of Tribunal or High Court by itself is not adequate for reopening the assessment completed earlier under section 143(3) unless there is a failure on the part of the assessee to disclose complete facts.

20. Is recording of satisfaction and quantification of escaped income a pre-condition for issuing notice under section 148 after 4 years from the end of the relevant assessment year?

Amarnath Agrawal v. CIT (2015) 371 ITR 183 (All)

Facts of the case: The assessee along with four others had obtained a lease of land and was in possession of the same from 1953. Subsequently, the State Government introduced a policy for conversion of lease-hold to free-hold. The assessee applied for conversion before the District Magistrate in 1997 and a sale deed was executed. The assessee deposited the necessary charges as demanded by the State Government and a freehold sale deed dated 25th March, 1998 was executed. The assessee sold a portion of the land during the F.Y. 1999-2000 and admitted the same as long-term capital gain taking into account the lease hold period also. In the assessment, the admission of income as long-term capital gain was accepted. However, after the expiry of four years from the end of the relevant assessment year, proceeding for reassessment of such income as short-term capital gains was resorted to by the Revenue on the ground that the lease hold period should not be considered for determining the period of holding of freehold land transferred. The assessee filed a writ challenging the validity of notice issued under section 148 stating that the requirements of section 149 read with section 151 were not considered by the Revenue.

High Court's Opinion and Decision: The High Court observed that two distinct conditions must be satisfied for assuming jurisdiction to issue a notice under section 148 after a period of 4 years viz. (i) escapement of income; and (ii) omission or failure on the part of the assessee to disclose fully and truly all material facts necessary for his assessment.

Under section 149(1)(b), it is imperative for the Assessing Officer, in his reasons, to state that the escaped income is likely to be ₹ 1 lakh or more. This is an essential ingredient for seeking approval and the basis on which satisfaction is to be recorded by the competent authority under section 151. If the condition precedent to substantiate the satisfaction of escapement of income is not made, the issuance of notice would be invalid.

In this case, since no reasons were recorded that the escaped income is likely to be ₹ 1 lakh or more so that the Chief Commissioner or Commissioner may record his satisfaction under section 151, the initiation of reassessment proceedings after four years was barred by time. The reasons recorded by the Assessing Officer were that the assessee had computed long-term capital gains tax liability, whereas he was liable to pay short-term capital gains tax, since he had sold a portion of the property within 3 years from the date of conversion of leasehold land into a freehold land.

The High Court observed that the property was held for more than 3 years and the conversion from leasehold to freehold being an improvement of the title did not have any effect on the taxability of profits. The reasons recorded by the Assessing Officer did not indicate any failure on the part of the assessee to disclose fully and truly all material facts at the time of assessment; it also did not indicate that the quantum of escapement of income exceeds ₹ 1 lakh. Accordingly, the High Court held that, in this case, the issue of notice under section 148 after the four year time period was not valid.

Appeals and Revision

21. Should the four year time limit for rectification of order by the Tribunal under section 254(2) be reckoned from the date of its order or from the date of receipt of order by the assessee?

Peterplast Synthetics P Ltd v. Asstt. CIT (2014) 364 ITR 16 (Guj)

Facts of the case: The assessee, dissatisfied with the order of Commissioner (Appeals), preferred an appeal before the Appellate Tribunal, which dismissed the appeal vide order dated February 20, 2007. The said order was, however, received by the assessee only on November 19, 2008. The assessee, after receipt of the order, preferred a rectification application against the same on May 9, 2012. The said rectification application was dismissed by the Tribunal on the ground that it is barred by law of limitation as provided under section 254(2) as the time limit of 4 years has to be reckoned from the date of order passed by the Tribunal i.e., from February 20, 2007. The assessee, being aggrieved with the dismissal of rectification application by the Tribunal, preferred a writ before the High Court.

Issue: The issue under consideration before the High Court is regarding the date to be reckoned for computing the period of limitation of four years under section 254(2) - whether the date of the Tribunal's order or the actual date of receipt of order by the assessee?

High Court's Observations: The High Court referred to the Bombay High Court ruling in *Petlad Bulakhidas Mills Co Ltd v. Raj Singh (1959) 37 ITR 264,* in which it was observed that the expression 'order' means an order, of which the affected party has actual or constructive notice. The right to make an application for revision is given to an assessee against an order, and that right can only be effectively exercised if the party affected had knowledge, either actual or constructive, of that order.

In that case, the Bombay High Court had observed that if the 'order' means a unilateral arriving at a decision by the appellate authority without the person affected having any knowledge of that decision, then, undoubtedly, the limitation would begin to run from the date when the authority chooses to pass the order. In such a case, the appellate authority may make the order, put it in a drawer, forget about it and if a year has passed after it, the right of the assessee to go for revision would be barred. Such contention is entirely untenable.

In this case, the Gujarat High Court observed that the effective right to appeal against the order or to seek rectification of the order could be exercised only when the affected party gets to know of the order. Thus, the right of appeal could be exercised only when the party affected by such order has knowledge of the order and hence, the limitation would start only from that date.

High Court's Decision: Applying the rationale of the above Bombay High Court ruling pronounced in relation to an application for revision, to the issue on hand pertaining to the date of reckoning the period of limitation for rectification under section 254(2), the Gujarat High Court held that the period of limitation has to be reckoned from the date of receipt of order by the assessee and not from the date of order. Therefore, the Tribunal had erred in dismissing the rectification application on the ground that it was barred by limitation by computing the time limit from the date of order instead of from the date of receipt of order by the assessee.

22. Is time limit under section 263 to be reckoned with reference to the date of assessment order or reassessment order, where the revision is in relation to an item which was not the subject matter of reassessment?

CIT v. Lark Chemicals Ltd (2014) 368 ITR 655 (Bom)

Facts of the case: The assessee-company, for the assessment year 2002-03, filed its return of income declaring a total income of ₹ 30.98 lakhs. This was accepted and the return was processed under section 143(1). Subsequently, it was reopened by issue of notice under section 148 and the order of reassessment was passed in June, 2006. The Commissioner assumed jurisdiction for revision of order by invoking section 263 in March, 2009. The subject matter of revision, however, was not related to any of the issues dealt with in the reassessment.

Issue under consideration: The issue before the High Court was whether the revision under section 263 is barred by limitation in view of the fact that the issues dealt with therein were not the subject matter of reassessment.

Tribunal's view: The Tribunal opined that jurisdiction under section 263 cannot be exercised in respect of those issues which were not the subject matter of consideration while passing the order of reassessment but were a part of the original assessment, the time limit for which had since expired. It relied on the Apex Court decision in the case of *CIT v. Alagendran Finance Ltd. (2007) 293 ITR 1,* wherein it was held that in such cases, the doctrine of merger would not apply and the period of limitation would commence from the date of original assessment and not from the date of reassessment.

High Court's Opinion: The High Court observed that if the revision happened to be in relation to issues dealt with in the reassessment proceedings, then, it would not be barred by limitation as the time limit would expire only on 31st March, 2009 i.e., two years from the end of the financial year in which the order sought to be revised under section 263, was passed. However, in this case, the revision proposed under section 263 was in respect of issues, other than the issues dealt with in the order of reassessment. The issues on which

the Commissioner sought to exercise jurisdiction under section 263 were concluded by virtue of intimation issued under section 143(1). The time period for revision under section 263 is two years from the end of the financial year in which order sought to be revised was passed [i.e., two years from the end of the financial year in which the intimation was issued under section 143(1)] and that time period has expired long ago.

High Court's Decision: The High Court, thus, held that the jurisdiction under section 263 could not be assumed on issues which were not the subject matter of issues dealt with in the order of reassessment but were part of the original assessment, for which the period of limitation expired long ago.

Penalties

23. Is concealment penalty leviable when the High Court admits the quantum appeal as involving substantial question of law?

CIT v. Nayan Builders & Developers (2014) 368 ITR 722 (Bom)

Facts of the case: In the assessment under section 143(3), the Assessing Officer made additions of (i) ₹ 104.76 lakhs towards income from a specified person; (ii) ₹ 10.79 lakhs towards disallowance of brokerage; and (iii) ₹ 2 lakhs towards disallowance of legal fee. The Tribunal upheld these additions in quantum proceedings. The Assessing Officer imposed penalty under section 271(1)(c) which was also confirmed by Commissioner (Appeals). The Tribunal was informed that the High Court had admitted substantial question of law with regard to those additions. Consequently, the Tribunal held that penalty was not leviable under section 271(1)(c).

Issue under consideration: The issue before the High Court was whether the Tribunal was correct in deleting the penalty under section 271(1)(c).

High Court's Opinion & Decision: The High Court observed that the issue of quantum addition was admitted by the High Court since it involved substantial question of law. When the High Court admits substantial question of law on an addition, it becomes apparent that the addition is certainly debatable. In such circumstances, penalty cannot be levied under section 271(1)(c). Thus, the High Court held that when the quantum proceeding is admitted by the High Court, it amounts to a debatable issue and hence, concealment penalty is not leviable.

24. Is penalty under section 271D imposable for cash loans/deposits received from partners?

CIT v. Muthoot Financiers (2015) 371 ITR 408 (Del)

Facts of the case: The assessee-firm, engaged in business of banking and money lending, had received huge amounts from the partners in the assessment years 1996-97 and 1998-99 by way of cash. The Assessing Officer levied penalty under section 271D. The Commissioner (Appeals) upheld the levy of penalty. The Tribunal observed that the advance made to the firm by the partners cannot be regarded as loan accepted by the

firm. It held that the amount advanced and accepted is capital of the firm and not loans which cannot be subjected to penalty under section 271D. The Revenue filed an appeal before High Court.

The assessee contended before the High Court that the amount advanced by the partners cannot be regarded as loan but is a capital of the firm. As the partnership firm has no separate legal entity, nor is there a separate identification between the firm and the partners, there is no violation of section 269SS in this case.

High Court's Opinion & Decision: The High Court referred to the case *CIT v. R.M. Chidambaram Pillai (1977) 106 ITR 292*, where the Apex Court was of the view that the firm is not a legal person even though it has some of the attributes of a personality. It held that the 'firm' is a collective noun, a compendious expression to designate an entity not a person. It also referred to *CIT v. Sivakumar. V (2013) 354 ITR 9 (Mad)*, where the High Court upheld the conclusion of the Tribunal to hold that there is no separate legal entity for the partnership firm and the partner is entitled to use the funds of the firm. In *CIT v. Lokhpat Film Exchange (Cinema) (2008) 304 ITR 172 (Raj)*, it was held that a partnership firm not being a juristic person, the *inter se* transaction between the firm and partners are not governed by the provisions of sections 269SS and 269T.

The High Court also noted the different view expressed by the Supreme Court in *CIT v. A.W. Figgies & Co. (1953) 24 ITR 405*, where it was held that the partners of the firm are distinct as civil entities while the firm as such is a separate and distinct unit for the purpose of assessment.

The High Court observed that the position that emerges is that there are three different Courts, which have held that section 269SS would not be violative when money is exchanged *inter se* between the partners and the firm.

The High Court further observed that, in this case, there was no dispute as regards the money brought in by the partners of the assessee-firm. The source of money was also not doubted. The transaction was bona fide and not aimed to avoid any tax liability. The credit worthiness of the partners and genuineness of the transactions coupled with relationship between the 'two persons' and two different legal interpretations put forward, could constitute a reasonable cause in a given case for not invoking sections 271D /271E read with section 273B.

The High Court held that the issue being a debatable one, there was reasonable cause for not levying penalty.

Miscellaneous Provisions

25. Can the Assessing Officer *suo moto* assume jurisdiction to declare sale of property as void under section 281?

Dr. Manoj Kabra v. ITO (2014) 364 ITR 541 (All)

Facts of the case: The assessee acquired a property for ₹ 7 lakhs though the stamp duty was paid in accordance with the circle rate which was ₹ 12 lakhs. Pursuant to the

sale deed, the assessee took possession of the property. Prior to the sale, the income tax assessment of vendor had been completed and a certain demand was raised against him in respect of the assessment year when the sale of the property was effected. The Assessing Officer issued a notice under section 281 to show cause as to why the sale deed executed in his favour (assessee-buyer) should not be treated as a void document. The assessee-buyer contended that he was a *bona fide* purchaser for adequate consideration and no notice of pendency of proceedings was to known him nor was it brought to his knowledge by the seller.

The assessee placed reliance on the decision of Supreme Court in the case of *TRO v. Gangadhar Vishwanath Ranade (Decd.) (1998) 234 ITR 188,* where it was held that section 281 of the Income-tax Act, 1961 is only a declaratory provision and not an adjudicatory provision entitling the income-tax authority to declare a document as a void document.

High Court's Observation: The High Court observed that the issue in this case was squarely covered by above Apex Court decision which held that the legislature had no intention to confer any exclusive power or jurisdiction upon the income-tax authority to decide any question arising under section 281. The Income-tax Act, 1961, does not prescribe any adjudicatory machinery for deciding any question which may arise under section 281. In order to declare a transfer as fraudulent under section 281, an appropriate proceeding in accordance with law was required to be taken under section 53 of the Transfer of Property Act, 1882. The Assessing Officer is required to file a suit for declaration to the effect that the transaction of transfer was void under section 281 of the Income-tax Act; but he himself cannot assume jurisdiction to declare the sale deed as void.

High Court's Decision: Applying the rationale of the Apex Court ruling, the High Court held that the Assessing Officer has no jurisdiction under section 281 to *suo moto* declare the sale as void.

Deduction, Collection and Recovery of Tax

26. Is section 194A applicable in respect of interest on fixed deposits in the name of Registrar General of High Court?

UCO Bank v. Dy. CIT (2014) 369 ITR 335 (Del)

Facts of the case: The assessee-bank accepted ₹ 707.46 lakhs as fixed deposit in the name of Registrar General of the High Court and issued a fixed deposit receipt in compliance with a direction passed by the court in relation to certain proceedings. Subsequently, the Assistant Commissioner of Income-tax issued a show cause notice to the bank for not deducting tax at source on the interest accrued and to show cause as to why it should not be treated as an assessee-in-default under section 201(1)/201(1A). The bank replied that the FDRs in the name of Registrar General of the Court was as a custodian because the actual beneficiary was unknown as the matter was sub judice and tax at source would be deducted when the payment is made to beneficiary as and when it is decided by the court. The Assistant Commissioner, however, passed an order treating the bank as assessee-in-default and raised a demand of ₹ 40.33 lakhs and ₹ 14.20 lakhs under sections 201(1) and 201(1A), respectively. Further, he initiated penalty

proceedings under section 271C. The assessee preferred a writ challenging the order passed imposing penal interest and initiation of penalty proceedings.

High Court's Opinion and Decision: The High Court opined that in the normal course, the bank is obliged to deduct tax at source in respect of any credit or payment of interest on deposits made with it. However, in this case, the actual payee is not ascertainable and the person in whose name the interest is credited is not a person liable to pay tax under the Act. The deposits kept with the bank under the orders of the court were, essentially, funds which were in custodia legis, that is, funds in the custody of the court. The interest on that account – although credited in the name of the Registrar General – was also part of funds under the custody of the Court. The Registrar General is not the recipient of the income represented by interest that accrues on the deposits made in his name. The credit of interest is not a credit to the account of a person who is liable to be assessed to tax.

The High Court observed that in the absence of a payee, the machinery provisions for deduction of tax to his credit are ineffective. The expression "payee" under section 194A would mean the recipient of income whose account is maintained by the person paying interest. The Registrar General is neither recipient of the amount credited to his account nor to interest accruing thereon. Therefore, he cannot be considered as a 'payee' for the purposes of section 194A. The credit by the bank in the name of the Registrar General would, thus, not attract the provisions of section 194A.

The High Court was of the view that *Circular No.8/2011 dated 14.10.2011* makes an assumption that the litigant depositing the money is the account holder with the bank or is the recipient of the income represented by the interest accruing thereon. This assumption is basically erroneous as the litigant who is asked to deposit the money in Court ceases to have any control or proprietary right over these funds. The person to whom the funds would be paid ultimately is determined by the court order and at that stage, tax would be required to be deducted at source to the credit of the recipient. However, the litigant who deposits the funds cannot be stated to be the recipient of income.

The High Court allowed the writ and set aside the orders passed by the tax authorities.

27. Is payment made for use of passive infrastructure facility such as mobile towers subject to tax deduction under section 194C or section 194-I?

Indus Towers Ltd v. CIT (2014) 364 ITR 114 (Del)

Facts of the case: The assessee owned a network of telecom towers and infrastructure services which were let out to major telecom operators in the country. Under section 197, the assessee sought for lower tax deduction under section 194C for the financial year 2013-14 at 0.5% and whereas the Assessing Officer issued a certificate under section 197 for lower tax deduction at 2.5% under section 194-I. The assessee filed a writ before the Delhi High Court. The Court directed the assessee to prefer a revision petition before the Commissioner of Income-tax.

The Commissioner of Income-tax rejected the contention of the assessee for applying section 194C and upheld the order of the Assessing Officer applying section 194-I, on the ground that

the mobile operators had the right to install the equipment on the tower owned by the assessee, which tantamounts to use of the land or telecommunication site and the tower owned by the assessee. The assessee once again preferred a writ before the High Court.

Assessee's Contentions: The assessee explained that its responsibility is to provide the entire passive infrastructure service with the aid of equipment belonging to it which is fully operated, controlled and managed by it. The customers do not have access, control or possession over the towers, sites or designated areas which are limited to rectification or maintenance of any defects in the equipments installed by them. The assessee, further, contended that its customers do not pay for any leasing rights but only for the services. Therefore, the provisions of section 194-I would not be attracted in this case.

High Court's Observations: The High Court observed that it was the intention of the parties to use the technical and specialized equipment maintained by the assessee. The infrastructure was given for the use of mobile operators. The towers were the neutral platform without which the mobile operators could not operate. Each mobile operator has to carry out this activity, by necessarily renting premises and installing the same equipment. The dominant intention was the use of equipment or plant or machinery and the use of premises was only incidental.

High Court's Decision: The High Court held that the submission of the assessee that the transaction is not "renting" is incorrect. Also, the Revenue's contention that the transaction is primarily "renting of land" is also incorrect. The underlying object of the arrangement was the use of machinery, plant or equipment i.e., the passive infrastructure and it is incidental that it was necessary to house the equipment in some premises. It directed that tax deduction be made at 2% as per section 194-I(a), the rate applicable for payment made for use of plant and machinery.

28. Is payment made to an overseas agent, who did not perform any service in India, liable for tax deduction at source?

DIT (International Taxation) v. Wizcraft International Entertainment (P) Ltd (2014) 364 ITR 227 (Bom)

Facts of the case: The assessee, an event management company, engaged the services of an agent to bring artistes to India. The assessee-company (i) paid commission to overseas agent; (ii) reimbursed the expenses in connection with the visit of the artistes in India; and (iii) paid fees to the artistes in India. The assessee-company deducted tax at source on the fees paid to the international artistes in India but did not deduct tax at source on the commission paid to the agent and on the reimbursement of expenses incurred in India by the artistes.

Assessing Officer's view *vis-à-vis* Commissioner (Appeals) view: The Assessing Officer contended that the payments made by the assessee including the payment made by way of commission to the agent and payment for reimbursement of expenses in connection with the visit of the artistes to India are liable for tax deduction at source. The Commissioner (Appeals) was of the view that expenses incurred and reimbursed do not

constitute income derived by the artistes from their personal activities, so as to be taxable under Article 18 of the Double Taxation Avoidance Agreement between India and UK; and hence, the same is not liable for deduction of tax at source.

Issue: The issue under consideration before the High Court was with regard to deduction of tax on commission paid to overseas agent who never took part in the events organized in India and amount paid as reimbursement of expenses incurred on travelling of artistes.

High court's Observations: The High Court observed that the assessee has deducted tax on the payments made to artistes for the services rendered in India. In so far as reimbursement of expenses is concerned, it has been verified with supporting documents that it was towards their air travel on which no tax was required to be deducted. With regard to the payment of commission, the agent did not act as a performing artist or entertainer. He was concerned only with the services rendered outside India. Thus, the Tribunal had recorded the finding of fact that the income of the agent did not arise from the personal activities in the contracting status of an entertainer or artist. He only contacted the artistes and negotiated with them for performance in India in terms of the authority given by the assessee. Hence, the commission paid to the overseas agent was not liable to tax in India. Consequently, there was no obligation for deducting tax at source at the time of making payment to the overseas agent.

High Court's Decision: The High Court, therefore, affirmed the decision of the Tribunal and Commissioner (Appeals) holding that the service rendered by the agent was outside India and hence, was not chargeable to tax in India. Thus, the requirement for deducting tax at source under section 195 on such payment does not arise.

29. Can incentives given to stockists and distributors by a manufacturing company be treated as "commission" to attract –

(i) the provisions for tax deduction at source under section 194H; and

(ii) consequent disallowance under section 40(a)(ia) for failure to deduct tax at source?

CIT v. Intervet India P Ltd (2014) 364 ITR 238 (Bom)

Facts of the case: The assessee-company engaged in manufacture of biological vaccines and animal health care pharmaceutical products, sold the same either through consignment or commission agents or directly through distributors or stockists. During the relevant financial year, it introduced a sales promotion scheme to boost sales by way of product discounts and product campaign. It passed on the incentives to distributors through consignment agents by way of sales credit notes. The Assessing Officer held that as the assessee was paying the stockists/distributors for the services rendered by them for buying and selling goods, on the basis of quantum of sales effected, such payment has to be considered as commission, on which tax was deductible at source under section 194H. Consequently, disallowance under section 40(a)(ia) was attracted for failure to deduct tax at source.

High Court's Observations: The High Court observed that the assessee had undertaken sales promotion by way of product discount scheme under which it offered incentive to the stockists / distributors and dealers. **The relationship between the assessee and the distributors / stockists was that of principal to principal.** The products were firstly sold to distributors / stockists who in turn resold the goods in the market. No service was offered by the assessee to them except a discount under the product discount scheme/product campaign scheme to buy the assessee's product.

High Court's Decision: The High Court, accordingly, held that the stockists and distributors were not acting on behalf of the assessee and most of the credit was by way of goods on meeting the sales target which could not be said to be a commission within the meaning of the *Explanation (i)* to section 194H. Accordingly, the High Court affirmed the order of the Tribunal which held that such payment does not attract deduction of tax at source. Consequently, disallowance under section 40(a)(ia) would not be attracted.

30. Can the Tax Recovery Officer (TRO) adjudicate disputes regarding quantum of liability between the garnishee (petitioner company, in this case) and the defaulting company, by exercising his powers under section 226(3)?

Uttar Pradesh Carbon & Chemicals Ltd v. TRO (2014) 368 ITR 384 (All.)

Facts of the case: The petitioner is a public limited company and is engaged in the business of financial services having registered office at Varanasi (shifted from Kanpur with effect from March 1, 2006). M/s Rich Capital and Financial services Ltd. became a defaulter of income-tax dues and demand to the extent of ₹ 3.20 crores was raised against it by the tax department. It was alleged by the said company that the petitioner company is a debtor and owed a sum of ₹ 1.55 crores to it. On the basis of this assertion made by the defaulting company, the Tax Recovery Officer (TRO) issued a notice under section 226(3) to the garnishee (petitioner company, in this case) requiring the garnishee to pay within the time specified in the notice so much of the amount as was sufficient to pay the amount due from the defaulting company in respect of arrears of tax. The notice, however, was purportedly sent at the address of the earlier registered office at Kanpur, which was not received by the petitioner company. Subsequently, when no reply was received from the petitioner company nor any amount was deposited, the TRO issued a notice, treating the petitioner as an assessee-in-default for the amount specified in the notice, holding that further proceedings would be taken against the petitioner for realization of the amount as if it were an arrears of tax due from it in the manner provided under sections 222 to 225. Thereafter, the TRO attached the equity shares in the demat account and also the balance in the savings bank account of the petitioner for recovery of tax due.

Petitioner's contentions: The petitioner filed an affidavit in terms of section 226(3)(vi) stating that it does not owe any sum to the defaulting company. Still the TRO issued summons and treated the petitioner as an assessee-in-default. The petitioner preferred a writ against such attachment of shares held in demat account and its bank account and prayed for quashing of the entire proceedings initiated under section 226(3). The petitioner contended that once it has denied its liability to pay any amount to the

defaulting company under law, the TRO cannot proceed further for recovery of tax arrears and the entire proceeding against it had to be quashed. It was also contended that the TRO does not hold jurisdiction to decide any dispute arising out of the business transaction between the defaulting company and the petitioner, which could be adjudicated only by the appropriate forum, such as the civil court.

Revenue's Contentions: The Revenue contended that a notice was sent by Speed Post under section 226(3) to the last known address of the petitioner and since there was no response, the petitioner was treated as an assessee-in-default and its demat account and bank account were attached. It further contended that the issue of technical breach arising due to non-service of notice on the debtor of the defaulting company had become infructuous in view of section 292B, since the petitioner participated in the proceedings subsequently.

High Court's Observations: The High Court observed that section 226(3) covers not only any sum of money due to the defaulting company being subjected to attachment but also any sum of money which may become due subsequently to the defaulting company being eligible for recovery by means of attachment. Thus, the provision covers not only persons owing but also those who may owe later to the defaulting company for the purpose of recovery of tax due. Further, since the petitioner has participated in the proceedings subsequently, the invalidity of the notice was cured and the defect, if any, was removed.

However, when the garnishee (i.e. debtor of the defaulting company) makes a statement on oath that the sum demanded or part thereof is not due from him or that it does not hold any money for or an account of the defaulting company, no further proceeding for recovery can be made.

The High Court observed that the powers under section 226(3) could not be invoked for effecting a recovery of a claim which is disputed. The condition precedent for exercising the power under section 226(3) is that the money is due and payable by the person concerned to the assessee.

The High Court opined that section 226(3) does not give any power to the Assessing Officer or the TRO to adjudicate disputes relating to the quantum of liability between the garnishee and the defaulting company, which is a matter within the purview of the Civil Courts.

High Court's Decision: The High Court referred to Apex Court decision in *Beharilal Ramcharan v. ITO (1981) 131 ITR 129* to hold that under section 226(3)(vi), a limited enquiry could only be conducted by the TRO and that too, by following the principles of natural justice. When the claim of amount is disputed by the debtor, the TRO cannot proceed to adjudicate the dispute between the parties i.e., the defaulting company and its debtor, for recovery of tax.

Thus, the High Court directed that the order of the TRO treating the petitioner as an assessee in default for the amount alleged to be owed by it to the defaulting company, cannot be sustained.

Part I : Statutory Update – Indirect Tax Laws

Significant Notifications and Circulars issued between 1st May, 2014 and 30th April, 2015

Study Material for Indirect Tax Laws [November, 2014 edition] contains all the relevant amendments made by the Finance (No.2) Act, 2014 and circulars/notifications issued up to 30.04.2014 as also the Budget 2014 notifications issued in July, 2014. However, for students appearing in November, 2015 examination, amendments made by notifications, circulars and other legislations made between 01.05.2014 and 30.04.2015 are also relevant. Such amendments (excluding Budget 2014 notifications) are given hereunder:-

SECTION A: CENTRAL EXCISE

Chapter 4: CENVAT Credit

1. Following amendments have been made in CENVAT Credit Rules, 2004 [CCR] vide ***Notification No. 6/2015 CE (NT) dated 01.03.2015*** **unless otherwise specified:**

(i) CENVAT credit allowed on inputs and capital goods received directly in the premises of the job worker [Rules 4(1) and 4(2)(a)]

Earlier, rule 4(1) allowed instant CENVAT credit on receipt of inputs into the factory of the manufacturer or in the premises of the output service provider or on the delivery of inputs to the output service provider. Likewise, rule 4(2)(a) allowed CENVAT credit on capital goods on receipt of the same in the factory or in the premises of the output service provider or outside the factory for generation of electricity for captive use within the factory or on the delivery of capital goods to the output service provider. Further, when goods were directly sent to job-worker's premises without bringing them in the manufacturer/output service provider's premises, CENVAT credit could be taken only when such goods were received back from the job-worker's premises in the premises of manufacturer/output service provider.

Rule 4(1) and rule 4(2)(a) have been amended to allow CENVAT credit in respect of inputs and capital goods immediately on receipt of the same in the premises of job worker where the same are sent directly to the job worker on the direction of the manufacturer or the provider of output service, as the case may be.

[Effective from 01.03.2015]

(ii) Time limit for availing credit on inputs and input services increased from 6 months to 1 year of the date of invoice [Rules 4(1) and 4(7)]

The time limit for availment of CENVAT credit on inputs and input services has been extended from six months to one year of the date of the issue of invoice/bill/challan etc. Amendments have been made in third proviso to rule 4(1) and the erstwhile sixth proviso (now fifth proviso) to rule 4(7) to enhance the time limit for availability of credit in respect of inputs and input services respectively.

The provisos lay down that the manufacturer and the provider of output service shall not take CENVAT credit after one year of the date of issue of any of the documents specified in rule 9(1).

[Effective from 01.03.2015]

(iii) Time limit for return of capital goods from a job worker to manufacturer/output service provider increased from 6 months to 2 years [Rule 4(5)]

Earlier, rule 4(5)(a) *inter alia* provided for a common time limit of 180 days for return of inputs and capital goods sent to a job-worker for the purpose of availing CENVAT credit.

Rule 4(5)(a) has now been amended to provide as follows:-

(a) CENVAT credit on inputs will be allowed even if any inputs as such or after being partially processed are sent to a job worker and from there subsequently sent to another job worker and likewise, for

- further processing,
- testing,
- repairing,
- re-conditioning or
- for the manufacture of intermediate goods necessary for the manufacture of final products or
- any other purpose.

Such credit will be allowed only if it is established from the records /challans/ memos/ or any other document produced by the manufacturer/ output service provider taking CENVAT credit that the inputs or the products produced therefrom are received back by the manufacturer/ output service provider within 180 days of their being sent from the factory/premises of output service provider, as the case may be.

(b) CENVAT credit on capital goods will be allowed even if any capital goods as such are sent to a job worker for

- further processing,
- testing,
- repair,
- re-conditioning or
- for the manufacture of intermediate goods necessary for the manufacture of final products or
- any other purpose.

Such credit will be allowed only if it is established from the records, challans or memos or any other document produced by the manufacturer /output service

provider taking the CENVAT credit that the capital goods are received back by the manufacturer /output service provider, as the case may be, within 2 years of their being so sent.

(c) Further, the credit will be allowed even if any inputs or capital goods are directly sent to a job worker without their being first brought to the premises of the manufacturer/ output service provider and in such a case, the period of 180 days or 2 years, as the case may be, will be counted from the date of receipt of such goods by the job worker.

(d) If the inputs or capital goods are not received back within 180 days and 2 years respectively, the manufacturer/ output service provider will have to pay an amount equivalent to the CENVAT credit attributable to the inputs or capital goods by debiting the CENVAT credit or otherwise. However, such credit may be retaken once the inputs or capital goods are received back in the factory/ premises of the output service provider.

[Effective from 01.03.2015]

(iv) Provisions relating to availment of CENVAT credit under partial and full reverse charge brought at par [Rule 4(7)]

Prior to 01.04.2015, there were separate provisions for availment of credit on input services in case of payment of service tax under full reverse charge and partial reverse charge. Whereas under full reverse charge, payment of service tax ensured availability of credit on input services; under partial reverse charge, payment to service provider (along with payment of service tax) was also a pre-requisite for availing credit.

The provisions for availing credit of service tax paid under partial reverse charge have now been aligned with the provisions applicable for full reverse charge. Thus, now CENVAT credit of service tax paid under partial reverse charge by the service receiver will also be allowed on payment of service tax alone without linking it to the payment to the service provider. The second proviso has been omitted and first proviso to rule 4(7) amended to give effect to this amendment.

Earlier, the third proviso to rule 4(7) laid down that CENVAT credit availed on input service ought to be reversed (except in case where service tax has been paid under full reverse charge) if value of input service and service tax is not paid within three months of the date of the invoice/bill/challan. The amount equivalent to the credit reversed could be taken back whenever the payment of value of input service and service tax is made.

The provisions contained in the erstwhile third proviso have now been set out in new second proviso to sub-rule (7). Cases where service tax is paid under reverse charge (both partial or full) have been excluded in the newly inserted second proviso.

[Effective from 01.04.2015]

(v) Explanations (I) and (II) to sub-rule (7) of rule 4 to apply to entire rule 4

Earlier, the below mentioned explanations were only applicable to sub-rule (7) of rule 4:

*"I. The amount mentioned in this **sub-rule** shall be paid by the manufacturer of goods or the provider of output service by debiting the CENVAT credit or otherwise on or before the 5th day of the following month except for the month of March, when such payment shall be made on or before the 31st day of the month of March.*

*II. If the manufacturer of goods or the provider of output service fails to pay the amount payable under this **sub-rule**, it shall be recovered, in the manner as provided in rule 14, for recovery of CENVAT credit wrongly taken."*

However, now the above-mentioned explanations have been made applicable to entire rule 4 by substituting the words **'sub-rule**' appearing therein with the word **'rule'**.

Thus, in effect, earlier the two explanations were applicable in respect of amount payable on non-payment of value of input service and service tax within three months of date of invoice as provided under sub-rule (7). However, now they will also apply in relation to amount payable on non-receipt of inputs and capital goods within 180 days and 2 years respectively under sub-rule (5)(a)(iii).

[Effective from 01.03.2015]

(vi) Export goods defined for the purpose of refund of CENVAT credit under rule 5 [Clause (1A) of Explanation 1 to rule 5]

Rule 5 provides for refund of CENVAT credit when a manufacturer clears export goods without payment of duty or a service provider exports an output service without payment of service tax. Refund is computed as per the formula prescribed in the rule and is subject to certain procedure, safeguards, conditions and limitations specified by the Board.

Though the term 'export service' has been defined in the rule to mean a service which is provided as per rule 6A of the Service Tax Rules, 1994, the term 'export goods' was not defined in the rule. The definition of 'export goods' has now been inserted in the rule to mean any goods which are to be taken out of India to a place outside India. Clause (1A) has been inserted in Explanation 1 to rule 5 to give effect to this amendment.

[Effective from 01.03.2015]

(vii) Inputs and input services used in the manufacture of non-excisable goods to attract reversal provisions under rule 6 [Explanations (1) and (2) to rule 6(1)]

(a) Rule 6 lays down the provisions for reversal of CENVAT credit when a manufacturer manufactures both dutiable and exempted final products or a service provider provides both taxable and exempted services.

(b) The rule sets out the various options to quantify the credit that needs to be reversed on inputs and input services which are used in manufacture of exempted goods or in provision of exempted services.

(c) Under rule 2(d) of CCR, **exempted goods are defined as excisable goods** which are exempt from the whole of the duty of excise leviable thereon, and includes goods which are chargeable to "Nil" rate of duty and goods in respect of which the benefit of an exemption under *Notification No. 1/2011 C.E. dated 01.03.2011* or under entries at serial numbers 67 and 128 of *Notification No. 12/2012 C.E. dated 17.03.2012* is availed.

(d) However, it has now been clarified vide Explanation 1 inserted after sub-rule (1) of rule 6 that **for the purposes of this rule, exempted goods or final products as defined in clauses (d) and (h) of rule 2 will include non-excisable goods cleared for a consideration from the factory**.

(e) It has been further clarified vide Explanation 2 that value of non –excisable goods for the purpose of this rule, will be the invoice value. Where such invoice value would not be available, the value will be determined by using reasonable means consistent with the principles of valuation contained in the Excise Act and the rules made thereunder.

(f) It is to be noted that the above explanations are applicable only to rule 6.

(g) The implication of the said amendment is that inputs and input services used in the manufacture of non-excisable goods will also attract the reversal provisions under rule 6. To illustrate, if a manufacturer manufactures dutiable and non-excisable goods, credit on input or input services used in the manufacture of non-excisable goods will have to be reversed in accordance with the provisions of rule 6.

(h) It is worthwhile to note here that since exempted service *inter alia* means services on which no service tax is leviable under section 66B of Finance Act, 1994, credit of inputs or input services used in provision of non-taxable services is required to be reversed under rule 6.

(i) Thus, now after the amendment in rule 6, there remains no difference with regard to reversal of credit by a manufacturer *vis-a-vis* a service provider. In other words, provisions for reversal of credit on exempted goods and exempted services have now been aligned.

[Effective from 01.03.2015]

(viii) Provisions applicable to first/second stage dealer regarding maintenance of records to be able to pass on the credit, to apply to an importer issuing CENVATable invoice [Rule 9(4)]

Rule 9(4) provides that CENVAT credit in respect of input or capital goods purchased from a first stage dealer or second stage dealer will be allowed only if such first stage dealer or second stage dealer has maintained records indicating the

fact that the input or capital goods was supplied from the stock on which duty was paid by the producer of such input or capital goods and only an amount of such duty on *pro rata* basis has been indicated in the invoice issued by him.

A proviso has been inserted in the sub-rule (4) which lays down that provisions of this sub-rule will apply *mutatis mutandis* to an importer who issues an invoice on which CENVAT credit can be taken.

[Effective from 01.03.2015]

(ix) Restrictions can also be imposed on a registered importer for misuse of CENVAT credit under rule 12AAA [Rule 12AAA]

Earlier, under rule 12AAA, the Central Government could impose restrictions on a manufacturer, first stage and second stage dealer, provider of a taxable service or an exporter, if there was a misuse of CENVAT credit.

Such restrictions can now be imposed in case of a registered importer also. Further, in the event of any misuse of CENVAT credit, registration of an importer can also be suspended like that of a dealer.

[Effective from 01.03.2015]

(x) Provisions introduced for recovery of CENVAT credit taken but NOT utilized and determining the manner of utilization of credit [Substituted rule 14]

Rule 14, which prescribes the provisions for recovery of CENVAT credit wrongly taken or erroneously refunded, has been substituted by a new rule to provide for recovery of CENVAT credit taken but NOT utilized. Further, the manner of determining utilization of credit has also now been provided in the rule itself. The provisions of the new rule are discussed hereunder:

(a) Where CENVAT credit has been taken wrongly but not utilised, the same will be recovered from the manufacturer/ output service provider in accordance with the provisions of section 11A of the Central Excise Act, 1944/ section 73 of the Finance Act, 1994 [Clause (i) of sub-rule (1)].

(b) Where CENVAT credit has been taken and utilised wrongly or has been erroneously refunded, the same will be recovered **along with interest** from the manufacturer/ output service provider in accordance with the provisions of sections 11A and 11AA (interest @ 18% for excise duty) of Central Excise Act, 1944/ sections 73 and 75 (graded interest ranging from 18% to 30% for service tax) of the Finance Act, 1994 [Clause (ii) of sub-rule (1)].

(c) For this purpose, all credits taken during a month will be deemed to have been taken on the last day of the month and the utilisation thereof will be deemed to have occurred in the following manner, namely: -

(i) the opening balance of the month has been utilised first;

(ii) credit admissible in terms of these rules taken during the month has been utilised next;

(iii) credit inadmissible in terms of these rules taken during the month has been utilized thereafter.

[Effective from 01.03.2015]

2. Clarification regarding availment of CENVAT credit after six months (now one year)

It has been clarified by CBEC that the limitation period of 6 months for availing CENVAT credit would not apply when re-credit is taken of amount reversed under:

(i) third proviso (now second proviso) to rule 4(7) of the CENVAT Credit Rules, 2004 (CCR)

(ii) rule 3(5B) of CCR

(iii) rule 4(5)(a) of CCR,

after meeting the conditions prescribed in these rules. The limitation period of 6 months applies only when the credit is taken for the first time on an eligible document.

[Circular No. 990/14/2014 CX dated 19.11.2014]

Note: *This Circular was issued during the period when the limitation period for availment of CENVAT credit was 6 months. However, the principle on the basis of which the clarification is issued will apply under new limitation period of 1 year also. Thus, the Circular may apply for amended provisions also.*

Third proviso to rule 4(7) (now second proviso), rule 3(5B) and rule 4(5)(a) of CCR stipulate as follows:

(i) Third proviso to rule 4(7) of CCR *(now second proviso) prescribes that if the payment of value of input service and service tax payable is not made within three months of date of invoice, bill or challan, then the CENVAT credit availed is required to be paid back by the manufacturer or service provider. Subsequently, when such payment of value of input service and service tax is made, the amount so paid back can be re-credited.*

(ii) Rule 3(5B) of CCR *stipulates that if the value of any input or capital goods before being put to use on which CENVAT credit has been taken, is written off or such provisions made in Books of Account, the manufacturer or service provider is required to pay an amount equal to credit so taken. However, when the inputs or capital goods are subsequently used, the amount so paid can be re-credited in the account.*

(iii) Rule 4(5)(a) of CCR *prescribes that in case inputs/capital goods sent to job worker are not received back within 180 days/ 2 years, the manufacturer or service provider is required to pay an amount equal to credit taken on such inputs/ capital goods in the first instance. However, when the inputs/ capital goods are subsequently received back from job worker, credit can be retaken of the amount so paid.*

3. Clarification regarding determination of place of removal in the case of exports for purposes of CENVAT credit of input services

While determining the eligibility of the input services to CENVAT credit, determination of place of removal is required. The following has been clarified in this regard:

(i) Place of removal in case of direct export of goods by the manufacturer exporter to his foreign buyer will be the port/ICD/CFS where the shipping bill is filed by the manufacturer exporter.

(ii) Place of removal in case of clearance of goods from the factory for export by a merchant exporter will be the factory gate. However, in isolated cases, it may extend further also depending on the facts of the case, but in no case, this place can be beyond the Port/ ICD/CFS where shipping bill is filed by the merchant exporter.

[Circular No. 999/6/2015 CX dated 28.02.2015]

Chapter-5: General Procedures Under Central Excise

1. Following amendments have been made in Central Excise Rules, 2002 [CER] vide ***Notification No. 8/2015 CE (NT) dated 01.03.2015:***

(i) Non/ short-payment of duty reflected in the periodic returns and penalty payable under rule 8(3A) to be recovered under section 11 [Rule 8(4)]

Rule 8 of the CER contains the provisions pertaining to manner of payment of excise duty. Sub-rule (4) of rule 8 laid down that the duty as assessed under rule 6 and the interest under sub-rule (3) of rule 8 would be recovered in accordance with the provisions of section 11 in the same manner as they are applicable for recovery of any duty or other sums payable to the Central Government.

The said sub-rule has been amended to provide that duty as assessed under rule 6 **and mentioned in the return filed under these rules,** the interest under sub-rule (3) **and penalty under sub-rule (3A)** will be recovered in accordance with the provisions of section 11.

[Effective from 01.03.2015]

(ii) Provisions introduced for preservation of records in electronic form with authentication by digital signatures [New sub-rules (4) & (5) of rule 10]

Rule 10 has been amended by inserting a new sub-rule (4) which provides that records under rule 10 may be preserved in electronic form and every page of the record so preserved shall be authenticated by means of a digital signature. The Board may notify the conditions, safeguards and procedure to be followed by an assessee preserving digitally signed records [Sub-rule (5)].

[Effective from 01.03.2015]

(iii) Invoice to contain details of job worker and the manufacturer/output service provider when goods are directly dispatched to job worker without first bringing them to the premises of the manufacturer/ output service provider [Second proviso to rule 11(2)]

Rule 11 contains the provisions relating to issuance of invoices. A second proviso has been inserted in rule 11(2) to lay down that if goods are directly sent to a job worker on the direction of a manufacturer or the provider of output service, the invoice will also contain the details of the manufacturer or the provider of output service, as the case may be, as buyer and contain the details of job worker as the consignee.

The above amendment has been made pursuant to the amendment made in rule 4 of CCR allowing CENVAT credit on receipt of inputs and capital goods in the premises of job worker without first bringing them to the premises of the manufacturer/output service provider.

[Effective from 01.03.2015]

(iv) Invoice to contain details of registered dealer and its customers when goods are directly dispatched to such customers without first bringing them to the premises of the registered dealer [Third proviso to rule 11(2)]

A third proviso has been inserted in rule 11(2) to lay down that if goods are directly sent to any person on the direction of the registered dealer, the invoice will also contain the details of the registered dealer as the buyer and the person as the consignee, and that person will take CENVAT credit on the basis of the registered dealer's invoice.

Further, if the goods imported under the cover of a bill of entry are sent directly to buyer's premises, the invoice issued by the importer should mention that goods are sent directly from the place or port of import to the buyer's premises [Fourth proviso].

[Effective from 01.03.2015]

(v) Provisions relating to issuance of an invoice under rule 11 to apply to an importer issuing CENVATable invoices [Rule 11(7)]

Earlier, sub-rule (7) provided that the provisions of rule 11 apply *mutatis mutandis* to goods supplied by a first stage dealer or a second stage dealer. The said sub-rule has been amended to also apply the provisions of rule 11 *mutatis mutandis* to goods supplied by an importer who issues an invoice on which CENVAT credit can be taken.

[Effective from 01.03.2015]

(vi) Provisions introduced for authentication of invoices by digital signatures [New sub-rules (8) and (9) of rule 11]

Authentication of invoices by means of digital signatures has been provided by inserting new sub-rule (8) in rule 11. New sub-rule (8) provides that an invoice issued under this rule by a manufacturer may be authenticated by means of a digital signature.

However, where the duplicate copy of the invoice meant for transporter is digitally signed, a hard copy of the duplicate copy of the invoice meant for transporter and self attested by the manufacturer would be used for transport of goods.

Under sub-rule (9), the Board may notify the conditions, safeguards and procedure to be followed by an assessee issuing digitally signed invoices.

It has been clarified that for the purposes of rule 10 and this rule, the expressions, "authenticate", "digital signature" and "electronic form" shall have the respective meanings as assigned to them in the Information Technology Act, 2000.

[Effective from 01.03.2015]

(vii) Belated filing of returns/ Annual Financial Information Statement/ Annual Installed Capacity Statement to attract late fee [New sub-rule (6) of rule 12 & new sub-rule (6) of rule 17]

Rule 12 prescribes the provisions relating to filing of various central excise returns. A new sub-rule (6) has been inserted in rule 12 to lay down that where any return [ER-1, ER-3, ER-8] or Annual Financial Information Statement [ER-4] or Annual Installed Capacity Statement [ER-7] is submitted by the assessee after the relevant due date, the assessee will be required to pay an amount calculated at the rate of ₹ 100 per day subject to a maximum of ₹ 20,000 for the period of delay in submission of each such return or statement.

Similarly new sub-rule (6) has been inserted in rule 17. Rule 17 governs the provisions in relation to removal of goods from 100% EOU to Domestic Tariff Area. Sub-rule (3) of rule 17 requires the 100% EOU unit to electronically submit a monthly return in form ER 2 within 10 days from the close of the month to which the return relates, in respect of excisable goods manufactured in, and receipt of inputs and capital goods in, the unit. Delay in filing of such return will now attract a late fee of ₹ 100 per day for each day of default subject to a maximum of ₹ 20,000 in terms of newly inserted sub-rule (6).

[Effective from 01.03.2015]

(viii) Restrictions can also be imposed on a registered importer for evasion of excise duty under rule 12CCC [Rule 12CCC]

Earlier, under rule 12CCC, Central Government could impose restrictions on a manufacturer, first stage and second stage dealer or an exporter, if there was evasion of excise duty.

Such restrictions can now be imposed in case of a registered importer also. Further, in the event of evasion of excise duty, registration of an importer can also be suspended like that of a dealer.

Consequential amendments have also been made in *Notification No. 16/2014 CE (NT) dated 21.03.2014 vide* ***Notification No. 10/2015 CE (NT) dated 01.03.2015*** so as to apply the provisions of the said notification to registered importer also. *Notification No. 16/2014 CE (NT) dated 21.03.2014* has been issued under 12CCC of Central Excise Rules, 2002 and rule 12AAA of CENVAT Credit Rules, 2004 to specify the nature of restrictions, types of facilities to be withdrawn and procedure for issue of such order in the event of evasion of excise duty or misuse of CENVAT credit.

[Effective from 01.03.2015]

(ix) Export under rule 18 to mean taking goods out of India to a place outside India [Explanation to rule 18]

Rule 18 governs the provisions relating to export of goods under a claim of rebate. The Explanation to the said rule has been amended to provide that 'export' means goods to be taken outside India or supplied as stores to foreign going vessels/aircraft. The amended explanation reads as under:

"Explanation – For the purposes of this rule, "export", with its grammatical variations and cognate expressions, means taking goods out of India to a place outside India and includes shipment of goods as provision or stores for use on board a ship proceeding to a foreign port or supplied to a foreign going aircraft."

Thus, rebate of excise duty will not be available on supply of goods to 100% EOU. As regards supply of goods to SEZ, it has been clarified vide CBEC ***Circular No.1001/8/2015-CX.8 dated 28.04.2015*** that since SEZ is deemed to be outside the Customs territory of India, any licit clearances of goods to an SEZ from the DTA will continue to be export. Therefore, such clearances will be entitled to the benefit of rebate under rule 18 and of refund of accumulated CENVAT credit under rule 5 of CCR, 2004, as the case may be.

[Effective from 01.03.2015]

(x) Registered importer to submit list of records and furnish required documents when called for under sub-rules (2) and (3) of rule 22 [Sub-rules (2) and (3) of rule 22]

Earlier, provisions of sub-rules (2) and (3) of rule 22 relating to submission of list of records and furnishing of the required documents on demand to the relevant authority for scrutiny were applicable to every assessee and first and second stage dealer.

The said sub-rules have been amended so as to apply these provisions to a registered importer issuing CENVATable invoices as well.

[Effective from 01.03.2015]

(xi) Registered importer liable to penal provisions under rule 25 [Rule 25]

Prior to 01.03.2015, the provisions of rule 25 relating to confiscation and penalty were applicable to a producer, manufacturer, registered person of a warehouse and a registered dealer. However, with effect from, 01.03.2015, the scope of applicability of rule 25 has now been extended to an importer who issues an invoice on which CENVAT credit can be taken.

[Effective from 01.03.2015]

2. Central excise registration to be granted online within 2 working days - verification of documents and premises to be carried out after the grant of the registration *[Notification No. 35/2001 CE (NT) dated 26.06.2001]*

Notification No. 35/2001 CE (NT) dated 26.06.2001 specifies the conditions, safeguards and procedures for registration of a person. ***Notification No. 7/2015 CE (NT) dated 01.03.2015*** has amended *Notification No. 35/2001 CE (NT)* to ensure that only an online application is made for registration and the same is granted within two working days of the receipt of a duly completed application form. Verification of documents and premises, as the case may be, can be carried out after the grant of the registration. The amended notification provides as under:

(i) Application for registration: Every person specified under rule 9(1) of CER, unless exempted from doing so by the Board under rule 9(2), shall get himself registered with the jurisdictional Deputy or Assistant Commissioner of Central Excise by applying in the form provided for registration in the website www.aces.gov.in

(ii) Registration of different premises of the same registered person: If the person has more than one premises requiring registration, separate registration certificate shall be obtained for each of such premises.

However, if a person manufactures or carries on trade in goods falling under Chapter 50 to 63 (textile articles) of First Schedule to the Central Excise Tariff Act, 1985 and has more than one premises requiring registration, he may obtain a single registration for all such premises, which fall within the jurisdiction of one Commissioner of Central Excise provided he declares the details of all such premises in the specified form.

Also, if a person manufactures Compressed Natural Gas (Tariff item 2711 of Central Excise Tariff) and has more than one premises requiring registration, which fall within the jurisdiction of one Chief Commissioner of Central Excise, he may obtain a single registration for all such premises with any of the Commissioner of Central Excise falling within the jurisdiction of the said Chief Commissioner. He will have to submit the details of all such premises along with the application for registration, subject to the condition that prior intimation shall be given before starting any additional premises subsequent to obtaining such registration.

(iii) Online filing of application: Application for registration or de-registration or amendment of the registration application shall be filed **only online** on the website www.aces.gov.in, in the forms provided in the website.

(iv) PAN based Registration: Applicant for registration shall mandatorily quote Permanent Account Number (PAN) of the proprietor or the legal entity being registered in the specified column in the application form, failing which registration will not be granted. Government Departments are exempt from the requirement of quoting the PAN in their online application.

(v) (a) Applicant to quote e-mail address and mobile number: Applicant shall quote his e-mail address and mobile number in the requisite column of the application form for communication with the Department.

(b) Business Transaction Numbers: Business transaction numbers obtained from other Government departments or agencies such as Customs Registration No (BIN No), Import Export Code (IEC) Number, State Sales Tax/ (VAT) Number, Central Sales Tax Number, Company Index Number (CIN), Service Tax Registration Number, which have been issued prior to the filing of Central Excise Registration application, shall be filled in the form and for the numbers subsequently obtained, the application shall be amended.

(vi) Registration Number and Certificate: Pending post-facto verification of premises and documents by the authorized Officers, registration application shall be approved by the Deputy or Assistant Commissioner within **2 days** of the receipt of duly completed online application form. A Registration Certificate containing registration number shall be issued online and a printed copy of such Registration Certificate shall be adequate proof of registration and the signature of the issuing authority is not required on the said Registration Certificate.

(vii) Submission of documents: The applicant shall tender self attested copies of the following documents at the time of verification of the premises:

(a) Plan of the factory premises;

(b) Copy of the PAN Card of the proprietor or the legal entity registered;

(c) Photograph and Proof of the identity of the applicant;

(d) Documents to establish possession of the premises to be registered;

(e) Bank account details;

(f) Memorandum or Articles of Association and List of Directors; and

(g) Authorization by the Board of Directors or Partners or Proprietor for filing the application by a third party.

(viii) Physical verification:

(a) The authorized officer shall verify the premises physically within 7 days from the date of receipt of application through online. Where errors are noticed during the verification process or any clarification is required, the authorized

Officer shall immediately intimate the same to the assessee for rectification of the error within **15 days** of the receipt of intimation failing which the registration shall stand cancelled. The assessee shall be given a reasonable opportunity to represent his case against the proposed cancellation, and if it is found that the reasons given by the assessee are reasonable, the authorized Officer shall not cancel the registration to the premises.

(b) On the physical verification of the premises, if it is found to be non-existent, the registration shall stand cancelled. The assessee shall be given a reason opportunity to represent his case against the proposed cancellation, and if it is found that the reasons given by the assessee are reasonable, the authorized Officer shall not cancel the registration to the premises recording the complete and correct address.

(ix) Transfer of Business or acquisition of factory: Where a registered person transfers his business to another person, the transferee shall get himself registered afresh. Where an applicant has acquired an old factory from a Bank or a Financial Institution, he shall get himself registered afresh.

(x) Change in the Constitution: Where a registered person is a firm or a company or association of persons, then in the event of any change in the constitution of the firm leading to change in PAN, he shall get himself registered afresh. In other cases of change in constitution of business, where there is no change in PAN, the same shall be intimated to the jurisdictional Central Excise Officer within **30 days** of such change by way of amendment to the registration details to be carried out online and this will not result in any change in the registration number.

(xi) De-registration: Every registered person, who ceases to carry on the business for which he is registered, shall de-register himself by making an online application. Where there are no dues pending recovery from the assessee, application for de-registration shall be approved within **30 days** from the date of filing of online declaration and the assessee shall be informed, accordingly.

(xii) Cancellation of registration: A registration certificate granted under rule 9 may be cancelled after giving a reasonable opportunity to the assessee to represent his case against the proposed cancellation by the Deputy or Assistant Commissioner of Central Excise, in any of the following situations, namely:—

(a) where on verification , the premises proposed to be registered is found to be non-existent;

(b) where the assessee does not respond to request for rectification of error noticed during the verification of the premises within 15 days of intimation;

(c) where there is substantial mis-declaration in the application form; and

(d) where the factory has closed and there are no dues pending against the assessee

[Effective from 01.03.2015]

3. Manufacturer receiving excisable goods for specified use at concessional rate of duty allowed to furnish letter of undertaking, instead of executing a bond, on fulfilment of specified conditions [Rule 3(3) of Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001]

Rule 3 of Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001 required a manufacturer who intended to receive excisable goods for specified use at concessional rate of duty to make an application in quadruplicate and execute a general bond with surety or security.

With effect from 01.03.2015, rule 3 has been amended vide ***Notification No. 9/2015 CE (NT) dated 01.03.2015*** to provide that it would be sufficient if the manufacturer furnishes a letter of undertaking. However, such a relaxation would be available only to that manufacturer against whom no show cause notice has been issued under section 11A(4) or 11A(5) of Central Excise Act, 1944 or no action is proposed under any notification issued in pursuance of rule 12CCC of Central Excise Rules, 2002 or rule 12AAA of CENVAT Credit Rules, 2004.

[Effective from 01.03.2015]

Chapter 15: Advance Ruling

Benefit of advance ruling extended to resident firms [Section 23A(c)(iii)]

Earlier, *public sector companies*, *resident public limited companies* and *resident private limited companies* were notified under section 23A(c)(iii) of Central Excise Act, 1944 as the class or category of resident persons who can apply for advance ruling in case of specified matters relating to central excise duty.

Notification No. 11/2015 CE (NT) dated 01.03.2015 has expanded the scope of advance ruling by additionally notifying **resident firm** as class or category of residents who can apply for advance ruling in case of specified matters relating to excise duty. Thus, now a resident firm will also be eligible to make an application for advance ruling in excise duty.

Meaning of important terms

(a) **firm** shall have the meaning assigned to it in section 4 of the Indian Partnership Act, 1932 and includes-

- (i) the limited liability partnership as defined in section 2(1)(n) of the Limited Liability Partnership Act, 2008; or
- (ii) limited liability partnership which has no company as its partner; or
- (iii) the sole proprietorship; or
- (iv) one Person Company.

(b) (i) **sole proprietorship** means an individual who engages himself in an activity as defined in section 23A(a) of the Central Excise Act, 1944.

(ii) **One Person Company** means as defined in section 2(62) of the Companies Act, 2013.

(c) **resident** shall have the meaning assigned to it in section 2(42) of the Income-tax Act, 1961 in so far as it applies to a resident firm.

[Effective from 01.03.2015]

SECTION B: SERVICE TAX

Chapter 1: Basic Concepts of Service Tax

Clarification regarding levy of service tax on joint venture

CBEC has issued following clarification regarding levy of service tax on joint venture:

(i) **Services provided by the members of the Joint Venture (JV) to the JV and *vice versa* or between the members of the JV:** In accordance with Explanation 3(a) of the definition of service under section 65B(44) of the Finance Act, 1994, JV (an unincorporated temporary association constituted for the limited purpose of carrying out a specified project) and the members of the JV are treated as distinct persons and therefore, taxable services provided for consideration, by the JV to its members or *vice versa* and between the members of the JV are taxable.

(ii) **Cash calls (capital contributions) made by the members to the JV:** If cash calls are merely a transaction in money, they are excluded from the definition of service provided in section 65B(44) of the Finance Act, 1994. Whether a 'cash call' is 'merely…. a transaction in money' [in terms of section 65B(44) of the Finance Act, 1994] and hence not in the nature of consideration for taxable service, would depend on the comprehensive examination of the Joint Venture Agreement, which may vary from case to case. Detailed and close scrutiny of the terms of JV agreement may be required in each case, to determine the service tax treatment of cash calls.

[Circular No. 179/5/2014 ST dated 24.09.2014]

Chapter 2: Place of Provision of Service

Clarification regarding levy of service tax on activities involved in relation to inward remittances from abroad to beneficiaries in India through MTSOs

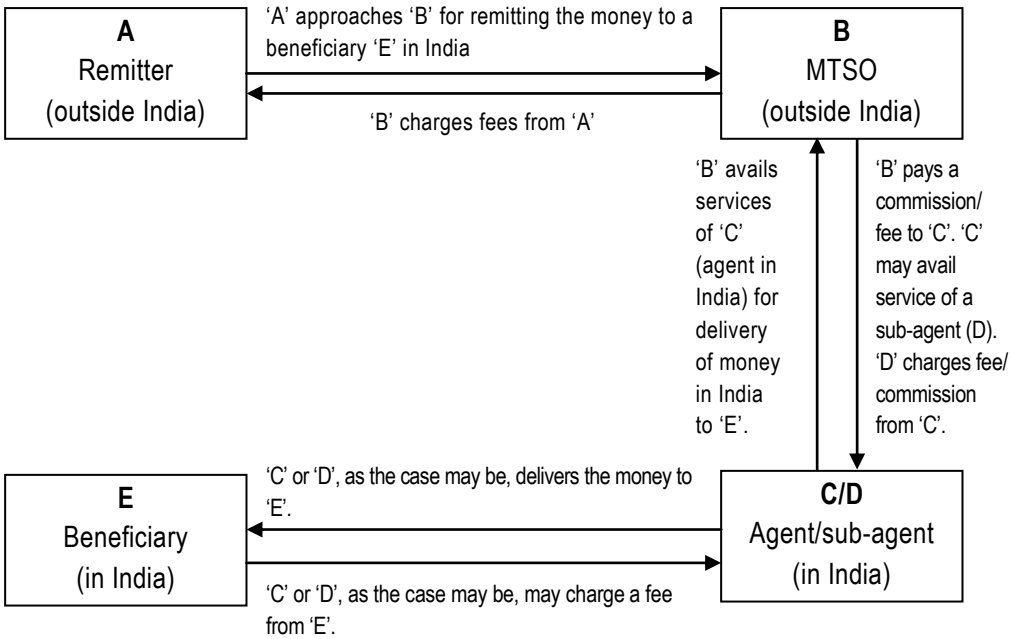
The remittances of money from overseas through the Money Transfer Service Operator (MTSO) route involves the following sequence of transactions:

Step 1: Remitter located outside India (say 'A') approaches a MTSO/bank (say B) located outside India for remitting the money to a beneficiary in India; 'B' charges a fee from 'A'.

Step 2: 'B' avails the services of an Indian entity (agent) (say 'C') for delivery of money to the ultimate recipient of money in India (say 'E'); 'C' is paid a commission/fee by 'B'.

Step 3: 'C' may avail service of a sub-agent (D). 'D' charges fee/commission from 'C'.

Step 4: 'C' or 'D', as the case may be, delivers the money to 'E' and may charge a fee from 'E'.



Circular No. 180/06/2014 ST dated 14.10.2014 has clarified the following issues in this regard:

S. No.	Issues	Clarification
1.	Whether service tax is payable on remittance received in India from abroad?	No service tax is payable *per se* on the amount of foreign currency remitted to India from overseas. As the remittance comprises money, it does not in itself constitute any service in terms of the definition of 'service' [Section 65B(44)].
2.	Whether the service of an agent or the representation service provided by an Indian entity/ bank to a foreign MTSO in relation to money transfer falls in the category of intermediary service?	Yes. The Indian bank or other entity acting as an agent to MTSO in relation to money transfer, facilitates in the delivery of the remittance to the beneficiary in India. In performing this service, the Indian Bank/entity facilitates the provision of money transfer service by the MTSO to a beneficiary in India. For their service, agent receives commission or fee. Hence, the agent falls in the category of intermediary as defined in rule 2(f) of the Place of Provision of Service Rules, 2012.
3.	Whether service tax is leviable on the service provided, as mentioned in point 2 above, by an intermediary/ agent located	Service provided by an intermediary is covered by rule 9(c) of the Place of Provision of Service Rules, 2012. As per this rule, the place of provision of service is the location of

	in India (in taxable territory) to MTSOs located outside India?	service provider. Hence, service provided by an agent, located in India (in taxable territory), to MTSO is liable to service tax. The value of intermediary service provided by the agent to MTSO is the commission or fee or any similar amount, by whatever name called, received by it from MTSO and service tax is payable on such commission or fee.
4.	Whether service tax would apply on the amount charged separately, if any, by the Indian bank/entity/agent/sub-agent from the person who receives remittance in the taxable territory, for the service provided by such Indian bank/entity/agent/sub-agent.	Yes. As the service is provided by Indian bank/entity/agent/sub-agent to a person located in taxable territory, the place of provision is in the taxable territory. Therefore, service tax is payable on amount charged separately, if any.
5.	Whether service tax would apply on the services provided by way of currency conversion by a bank/entity located in India (in the taxable territory) to the recipient of remittance in India?	Any activity of money changing comprises an independent taxable activity. Therefore, service tax applies on currency conversion in such cases in terms of the Service Tax (Determination of Value) Rules. Service provider has an option to pay service tax at prescribed rates in terms of Rule 6(7B) of the Service Tax Rules 1994.
6.	Whether services provided by sub-agents to such Indian Bank/entity located in the taxable territory in relation to money transfer is leviable to service tax?	Sub-agents also fall in the category of intermediary. Therefore, service tax is payable on commission received by sub-agents from Indian bank/entity.

Note: Circular No. 163/14/2012–ST dated 10.07.2012, issued earlier on the aforesaid subject, stands superseded.

Chapter 5: Exemptions And Abatements

1. Mega Exemption Notification amended

Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* has been amended vide ***Notification No. 6/2015 ST dated 01.03.2015, unless specified otherwise.*** The amendments are discussed in the following two broad categories:

(A) New exemptions

(B) Exemptions withdrawn/restricted

(A) NEW EXEMPTIONS

(i) Ambulance services provided by all service providers (whether or not by clinical establishment or an authorised medical practitioner or paramedics) exempted

Earlier, entry 2 exempted any service provided by way of transportation of a patient to and from a clinical establishment from service tax only when the said service was provided by a clinical establishment or an authorised medical practitioner or paramedics.

The scope of this exemption has now been widened to extend the said exemption to ambulance services provided by all service providers. Therefore, now the ambulance services provided by an entity which is not a clinical establishment or an authorised medical practitioner or paramedics would also be exempt from service tax. The above amendment has been made by substituting entry 2 with a new entry.

[Effective from 01.04.2015]

(ii) General insurance provided under Pradhan Mantri Suraksha Bima Yojna exempted

Entry 26 exempts services of general insurance business provided under specified schemes. A new clause (p) has been inserted vide ***Notification No. 12/2015 ST dated 30.04.2015*** in the said entry to exempt services of general insurance business provided under Pradhan Mantri Suraksha Bima Yojna.

[Effective from 30.04.2015]

(iii) Life insurance provided under Varishtha Pension Bima Yojna, Pradhan Mantri Jeevan Jyoti Bima Yojna and Pradhan Mantri Jan Dhan Yojna exempted

Entry 26A exempts services of life insurance business provided under specified schemes. Clauses (d), (e) and (f) have been inserted in the said entry to exempt services of life insurance business provided in respect of the following additional schemes:

Clause (d) Varishtha Pension Bima Yojna - ***[Effective from 01.04.2015]***

Clause (e) Pradhan Mantri Jeevan Jyoti Bima Yojna – ***[Effective from 30.04.2015 vide Notification No. 12/2015 ST dated 30.04.2015]***

Clause (f) Pradhan Mantri Jan Dhan Yojna - ***[Effective from 30.04.2015 vide Notification No. 12/2015 ST dated 30.04.2015]***

(iv) Collection of contribution under Atal Pension Yojna (APY) exempted

A new entry 26B has been inserted in the notification vide ***Notification No. 12/2015 ST dated 30.04.2015*** to exempt the services by way of collection of contribution under Atal Pension Yojna.

[Effective from 30.04.2015]

(v) Treatment of effluent by Common Effluent Treatment Plant operator exempted

A new entry 43 has been inserted in the notification to exempt the services by operator of Common Effluent Treatment Plant by way of treatment of effluent.

[Effective from 01.04.2015]

(vi) Pre-conditioning, pre-cooling, ripening, waxing, retail packing, labelling of fruits and vegetables exempted

A new entry 44 has been inserted in the notification to exempt the services by way of pre-conditioning, pre-cooling, ripening, waxing, retail packing, labelling of fruits and vegetables which do not change or alter the essential characteristics of the said fruits or vegetables.

[Effective from 01.04.2015]

(vii) Admission to a museum, national park, wildlife sanctuary, tiger reserve or zoo exempted

Services provided by way of admission to a museum, zoo, national park, wild life sanctuary and a tiger reserve have been exempted. A new entry 45 has been inserted in the notification to give effect to this exemption.

Following definitions have been also been inserted in the notification pursuant to the said exemption:

1. *National park has the meaning assigned to it in the clause (21) of the section 2 of The Wild Life (Protection) Act, 1972 [Clause (xaa)].*
2. *Wildlife sanctuary means sanctuary as defined in the clause (26) of the section 2 of The Wild Life (Protection) Act, 1972 [Clause (zk)].*
3. *Zoo has the meaning assigned to it in the clause (39) of the section 2 of the Wild Life (Protection) Act, 1972 [Clause (zl)].*

   Section 2(39) of the Wild Life (Protection) Act, 1972 provides that "Zoo" means an establishment, whether stationary or mobile, where captive animals are kept for exhibition to the public but does not include a circus and an establishment of a licenced dealer in captive animals.
4. *Tiger reserve has the meaning assigned to it in clause (e) of section 38K of the Wild Life (Protection) Act, 1972 [Clause (zi)].*

[Effective from 01.04.2015]

(viii) Exhibition of movie by exhibitor to distributor/ association of persons consisting of such exhibitor as one of its members exempted

Service provided by way of exhibition of movie by an exhibitor to the distributor or an association of persons consisting of the exhibitor as one of its members has been exempted. A new entry 46 has been inserted in the notification to give effect to this exemption.

[Effective from 01.04.2015]

(ix) Service provided with respect to Kailash Mansarovar and Haj pilgrimage exempted

Services provided by a specified organisation in respect of a religious pilgrimage facilitated by the Ministry of External Affairs of the Government of India, under bilateral arrangement, have been exempted from service tax vide ***Notification No. 17/2014 ST dated 20.08.2014.***

Specified organisation means:

(a) Kumaon Mandal Vikas Nigam Limited, a Government of Uttarakhand Undertaking; or

(b) Haj Committee of India and State Haj Committees constituted under the Haj Committee Act, 2002, for making arrangements for the pilgrimage of Muslims of India for Haj.

Thus, the religious pilgrimage organized by the Haj Committee and Kumaon Mandal Vikas Nigam Ltd. are not liable to service tax.

[Effective from 20.08.2014]

(B) EXEMPTIONS WITHDRAWN/RESTRICTED

(i) Scope of exemption available on specified services of construction, repair, maintenance etc. (when provided to the Government/ local authority/ Governmental authority) restricted

Earlier, entry 12 of the notification exempted six specified services of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation or alteration when provided to the Government, a local authority, or a Governmental authority.

The said entry has been amended to withdraw the above exemption in respect of the following construction, erection etc:

(a) a civil structure or any other original works meant predominantly for use other than for commerce, industry, or any other business or profession;

(b) a structure meant predominantly for use as

  (i) an educational,

  (ii) a clinical, or

  (iii) an art or cultural establishment;

(c) a residential complex predominantly meant for self-use or the use of their employees or other persons specified in the *Explanation* 1 to clause (44) of section 65B of the said Act.

Therefore, now the exemption under entry 12 is available only in respect of the following three types of construction, erection etc:

(a) a historical monument, archaeological site or remains of national importance,

archeological, excavation or antiquity or antiquity specified under the Ancient Monuments and Archaeological Sites and Remains Act, 1958;

(b) canal, dam or other irrigation work; and

(c) pipeline, conduit or plant for (i) water supply (ii) water treatment, or (iii) sewerage treatment or disposal.

[Effective from 01.04.2015]

(ii) Exemption to construction, erection, commissioning or installation of original works pertaining to an airport or port withdrawn

Earlier, services by way of construction, erection, commissioning or installation of original works pertaining to an airport, port or railways, including monorail or metro were exempt from service tax under entry 14(a) of the notification.

Entry 14(a) has now been amended to **withdraw such exemption in respect of an airport or port.** Thus, service tax will be payable on construction, erection, commissioning or installation of original works pertaining to an airport or port. The other exemptions covered under entry 14 of the notification are, however, not changed.

[Effective from 01.04.2015]

(iii) Service tax payable on a performance in folk or classical art forms of music/ dance/ theatre if the consideration therefor exceeds ₹ 1,00,000

Earlier, services by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, excluding services provided by such artist as a brand ambassador was exempt from service tax under entry 16 of the notification.

The scope of the said exemption has now been restricted by fixing a monetary limit of ₹ 1,00,000 in respect of a performance. Thus, now exemption to services provided by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, will be limited only to such cases where amount charged is upto ₹ 1,00,000 for a performance. However, services provided by an artist as brand ambassador will continue to remain taxable.

[Effective from 01.04.2015]

(iv) Exemption to transportation of food stuff by rail or vessels or road limited to milk, salt and food grain including flours, pulses and rice

Earlier, transportation of foodstuff - including flours, tea, coffee, jaggery, sugar, milk products, salt and edible oil, excluding alcoholic beverages - by rail/ vessel and by goods carriage was exempt from service tax under entry 20(i) and entry 21(d) of the notification respectively.

Entry 20(i) and entry 21(d) have been amended to restrict such exemption to transportation of only **milk, salt and food grain including flours, pulses and rice** by rail/ vessel and by goods carriage. Transportation of agricultural produce by rail

or a vessel and by goods carriage is separately exempt vide entry 20(h) and entry 21(a) respectively, and this exemption would continue.

[Effective from 01.04.2015]

(v) Exemption to services by (i) mutual fund agent/distributor to a mutual fund or asset management company and (ii) selling/ marketing agent of lottery tickets to a distributor/selling agent, withdrawn

Earlier, services by the following persons in their respective capacities were exempt from service tax under entry 29 of the notification:-

(i) mutual fund agent to a mutual fund or asset management company

(ii) distributor to a mutual fund or asset management company

(iii) selling or marketing agent of lottery tickets to a distributor or a selling agent.

The said exemption has now been withdrawn by omitting clause (c), (d) and (e) of entry 29 from the notification. Thus, service tax will be payable on these services.

[Effective from 01.04.2015]

(vi) Exemption withdrawn for services by way of making telephone calls from departmentally run public telephone etc.

Exemption has been withdrawn in respect of services by way of making telephone calls from-

(a) departmentally run public telephone;

(b) guaranteed public telephone operating only for local calls; or

(c) free telephone at airport and hospital where no bills has been issued.

Entry 32 of the notification has been omitted to give effect to this amendment.

[Effective from 01.04.2015]

2. Abatement Notification amended

Abatement *Notification No. 26/2012 ST dated 20.06.2012* has been amended vide ***Notification No. 8/2015 ST dated 01.03.2015*** as under:

(i) Uniform abatement of 70% prescribed for (i) goods and passenger transport by rail and (ii) goods transport by road and vessel, subject to uniform condition of non-availment of CENVAT credit on inputs, capital goods and input services

Earlier, service tax was payable on 30% of the value of rail transport for goods and passengers, 25% of the value of goods transport by road by a goods transport agency (GTA) and 40% for goods transport by vessels. The conditions prescribed also varied.

A uniform abatement of 70% has now been prescribed for (i) transport of goods and passengers by rail and (ii) transport of goods by road by a GTA and vessel

alongwith a uniform condition of non-availment of CENVAT credit on inputs, capital goods and input services, used for providing the taxable service. In case of goods transport by road by a GTA, the condition for non-availment of CENVAT is for service provider.

Thus, in effect, the abatement percentage has increased from 60 to 70 in case of goods transport by vessel and reduced from 75 to 70 in case of goods transport by road by a goods transport agency. The percentage of abatement however, has remained unaffected in case of rail transport of goods and passengers (70%). Further, while the condition of non-availment of CENVAT credit was present in the case of road and vessel transport of goods earlier also, the same has been introduced newly in case of rail transport of goods and passengers.

[Effective from 01.04.2015]

(ii) Abatement in case of passenger transportation by air in non-economy class reduced from 60% to 40%

Earlier, service tax was payable on 40% of the value of air transport of passengers for economy as well as higher classes, like business class.

Such abatement has now been bifurcated into two categories:-

(a) Abatement for transport of passengers by air, with or without accompanied belongings in economy class - 60%

(b) Abatement for transport of passengers by air, with or without accompanied belongings in other than economy class - 40%

Thus, in effect, abatement for classes other than economy has been reduced by 20% and therefore, service tax would be payable on 60% of the value of air travel in such higher classes.

[Effective from 01.04.2015]

(iii) No abatement for services provided in relation to chit

Earlier, in respect of services provided in relation to chit, service tax was payable on 30% of the value of taxable service under entry 8 of the notification.

However, the abatement of 70% has now been withdrawn from services provided in relation to chit by omitting entry 8. Consequently, service tax would be paid by the chit fund foremen on the full consideration received by way of fee, commission or any such amount. They would be entitled to take CENVAT credit.

[Effective from 01.04.2015]

3. GTA service provided for transport of export goods by road from place of removal/ CFS/ICD to land customs station exempted

Earlier, *Notification No. 31/2012 ST dated 20.06.2012* exempted the goods transport agency service provided for transport of export goods by road from -

- the place of removal to an inland container depot (ICD), a container freight station (CFS), a port or airport;
- any CFS or ICD to the port or airport.

Scope of this exemption has been widened vide ***Notification No. 4/2015 ST dated 01.03.2015*** to exempt such services when provided for transport of export goods by road from the place of removal or from any CFS/ICD to a land customs station (LCS) also.

[Effective from 01.04.2015]

4. Notification exempting services provided by a foreign commission agent to an Indian exporter rescinded consequent to amendment in the definition of intermediary in Place of Provision of Services Rules, 2012 ***[Notification No. 42/2012 ST dated 29.6.2012 rescinded]***

Services provided by a commission agent located outside India to an exporter of goods located in India were exempted vide *Notification No. 42/*2012 *ST dated 29.6.2012.* However, with effect from 01.10.2014, this exemption became redundant when the definition of "intermediary" in the Place of Provision of Services Rules, 2012 was amended vide *Notification No.14/2014 ST dated 11.07.2014* to include the intermediary of goods in its scope. By virtue of the said amendment, the place of provision of service provided by such foreign commission agents to Indian exporters of goods shifted from taxable territory (location of service receiver – Indian exporter) to non-taxable territory (location of service provider – foreign commission agent). Consequently, there remained no need of any exemption for the said service.

Therefore, since this exemption became redundant, *Notification No. 42/2012 ST dated 29.6.2012* has been rescinded vide ***Notification No. 3/2015 ST dated 01.03.2015***.

[Effective from 01.03.2015]

5. Taxable services provided by a person located in taxable territory against duty credit scrips [MEIS and SEIS] exempted from service tax

Notification Nos. 10 & 11/2015 ST dated 08.04.2015 have exempted the taxable services provided/agreed to be provided by a person located in the taxable territory against Merchandise Exports from India Scheme (MEIS) duty credit scrips and Service Exports from India Scheme (SEIS) duty credit scrips, issued to an exporter subject to the fulfillment of the following major conditions:

(a) Conditions prescribed for claiming exemption from basic customs duty, CVD and special CVD on goods imported into India against SEIS and MEIS duty credit scrips are complied with and the said scrips have been registered with the Customs Authority.

(b) Holder of the scrip, to whom taxable services are provided or agreed to be provided is located in the taxable territory.

(c) Holder of the scrip presents the scrip to the Customs Authority along with a letter and an invoice, challan etc. issued by the service provider indicating details of his

jurisdictional Central Excise Officer (hereinafter referred to as the said Officer) and the description, value of the taxable service provided or agreed to be provided and service tax leviable thereon.

(d) Customs Authority shall debit the service tax leviable, but for this exemption, in or on reverse of the scrip and send a written advice of the action taken to the said officer. The date of debit of service tax leviable, in the scrip, shall be taken as the date of payment of service tax.

(e) Holder of the scrip presents the scrip debited by the said Customs Authority within 30 days to the said Officer, along with an undertaking addressed to the said Officer, that in case of any service tax short debited in the scrip, he shall pay such service tax along with applicable interest.

(f) Based on the said written advice and undertaking the said Officer shall verify and validate on the reverse of the scrip, the details of the service tax leviable, which were debited by the said Customs Authority, and keep a record of payment of such service tax and interest, if any.

(g) Service provider retains a copy of the scrip, debited by the said Customs Authority and verified by the said Officer and duly attested by the holder of the scrip, in support of the provision of taxable services under this notification.

(h) Holder of the scrip, to whom the taxable services were provided/agreed to be provided shall be entitled to avail drawback or CENVAT credit of the service tax leviable under section 66B of the said Act, against the service tax debited in the scrip and validated by the said Officer.

[Effective from 08.04.2015]

Chapter-6: Service Tax Procedures

1. Following amendments have been made in Service Tax Rules, 1994 vide ***Notification No. 5/2015 ST dated 01.03.2015, unless specified otherwise:***

(i) Concept of aggregator introduced in service tax

The word 'aggregate' literally means a whole formed by combining several elements, formed by the combination of many separate items or units. The aggregator is one, who therefore aggregates or causes aggregation of units, items, things or services.

There are also many online websites that follow 'aggregator' model. Under this model, an entity collects or aggregates information on a particular service from several sources on a single platform and draws customers to its platform to connect them with the service provider. It may also facilitate the customers in comparing the prices and specifications of a particular service offered by multiple service providers.

Therefore, companies which act as aggregator for service providers like travel portals, food portals or cab services will now be liable to pay service tax.

(a) Definition of aggregator and brand name inserted in rule 2 [Rule 2(1)]

Amendments have been made in Service Tax Rules to bring such aggregator within the service tax net. The definition of "aggregator" has been provided by inserting clause (aa) in rule 2(1) as under-

"Aggregator means a person, who owns and manages a web based software application, and by means of the application and a communication device, enables a potential customer to connect with persons providing service of a particular kind under the brand name or trade name of the aggregator" ***[Rule 2(1)(aa)]***

Accordingly, "brand name or trade name" has also been defined by inserting clause (bca) in rule 2(1) as under:

"Brand name or trade means a brand name or a trade name whether registered or not, that is to say, a name or a mark, such as an –

- *invented word or writing,*
- *or a symbol,*
- *monogram,*
- *logo,*
- *label,*
- *signature,*

which is used for the purpose of indicating, or so as to indicate a connection, in the course of trade, between a service and some person using the name or mark with or without any indication of the identity of that person" ***[Rule 2(1)(bca)].***

[Effective from 01.03.2015]

(b) Aggregator to pay service tax under reverse charge [Rule 2(1)(d)(i)(AAA)]

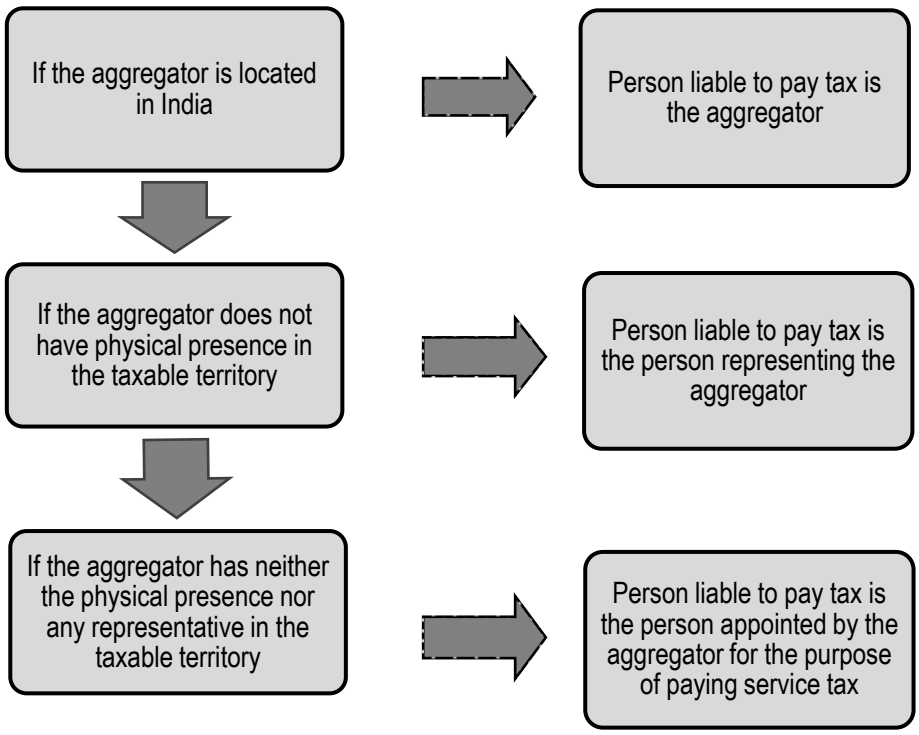
Rule 2(1)(d)(i) defines the term "person liable for paying service tax" in respect of the taxable services notified under section 68(2) of Finance Act, 1994. A new clause (AAA) has been inserted in the said rule to provide that in relation to service provided or agreed to be provided by a person involving an aggregator in any manner, the aggregator of the service would be the person liable for paying service tax.

In case, the aggregator does not have a physical presence in the taxable territory, any person representing the aggregator for any purpose in the taxable territory will be liable for paying service tax.

However, if the aggregator neither has a physical presence nor does it have a representative for any purpose in the taxable territory, it will have to appoint a person in the taxable territory for the purpose of paying service tax and such person will be the person liable for paying service tax.

The above has been represented in the diagram given in the next page.

[Effective from 01.03.2015]



(ii) Service tax to be payable by recipient of service in case of service provided by (a) mutual fund agent/ distributor to mutual fund/ asset management company, (b) selling/marketing agent of lottery tickets to lottery distributor/selling agent [Rule 2(1)(d)(i)(EEA) & Rule 2(1)(d)(i)(EEB)]

A new clause (EEA) has been inserted in the rule 2(1)(d)(i) to provide that in relation to service provided or agreed to be provided by a mutual fund agent or distributor to a mutual fund or asset management company, the recipient of the service would be the person liable for paying service tax.

A new clause (EEB) has been inserted in the rule 2(1)(d)(i) to provide that in relation to service provided or agreed to be provided by a selling or marketing agent of lottery tickets to a lottery distributor or selling agent, the recipient of the service would be the person liable for paying service tax.

[Effective from 01.04.2015]

(iii) CBEC to specify conditions, safeguards and procedure for registration in service tax [New sub-rule (9) inserted and sub-rule (1A) omitted in rule 4]

CBEC had specified certain documents which were to be submitted by the assessee within a period of 15 days from the date of filing of the application for registration vide the powers given under rule 4(1A).

Sub-rule (1A) has been omitted and a new sub rule (9) inserted to provide that CBEC will, by way of an order, specify the conditions, safeguards and procedure for registration in service tax.

In this regard, ***Order No. 1/15 ST dated 28.02.2015, effective from 01.03.2015*** has been issued, prescribing documentation, time limits and procedure for registration. It has also been prescribed that henceforth registration for **single premises will be granted within two days of filing the application.** The Order provides the documentation, time limits and procedure for registration as under:

General procedure

1. Applicants seeking registration for **single premises** shall file an online application for registration on ACES website in Form ST-1.
2. Following details are to be mandatorily furnished in the application form:
   (a) Permanent Account Number (PAN) of the proprietor or the legal entity being registered (except Government Departments)
   (b) E-mail and mobile number
3. Registration would be granted online within 2 days of filing the complete application form. On grant of registration, the applicant would be enabled to electronically pay service tax.
4. Registration Certificate downloaded from the ACES website would be accepted as proof of registration and there would be no need for a signed copy.

Documentation required

A self attested copy of the following documents will have to be submitted by registered post/ speed post to the concerned Division, within 7 days of filing the Form ST-1 online, for the purposes of verification:

1. Copy of the PAN Card of the proprietor or the legal entity registered
2. Photograph and proof of identity of the person filling the application
3. Document to establish possession of the premises to be registered such as proof of ownership, lease or rent agreement, allotment letter from Government, No Objection Certificate from the legal owner
4. Details of the main Bank Account
5. Memorandum/Articles of Association/List of Directors
6. Authorisation by the Board of Directors/Partners/Proprietor for the person filing the application
7. Business transaction numbers obtained from other Government departments or agencies such as Customs Registration No. (BIN No), Import Export Code (IEC) number, State Sales Tax Number (VAT), Central Sales Tax Number, Company Index Number (CIN) which have been issued prior to the filing of the

service tax registration application

Verification of premises, if there arises any need for the same, will have to be authorised by an officer not below the rank of Additional/Joint Commissioner.

Revocation of registration certificate

The registration certificate may be revoked by the Deputy/Assistant Commissioner in any of the following situations, after giving the assessee an opportunity to represent against the proposed revocation and taking into consideration the reply received, if any:

1. the premises are found to be non existent or not in possession of the assessee.
2. no documents are received within 15 days of the date of filing the registration application.
3. the documents are found to be incomplete or incorrect in any respect.

[Effective from 01.03.2015]

(iv) Provisions introduced for authentication of invoices by digital signatures [New rule 4C]

A provision has been added for authentication of invoices by means of digital signatures by inserting new rule 4C. New rule 4C provides that any invoice, bill or challan issued under rule 4A or consignment note issued under rule 4B may be authenticated by means of a digital signature. The Board may specify the conditions, safeguards and procedure to be followed by any person issuing digitally signed invoices, by way of a notification.

[Effective from 01.03.2015]

(v) Provisions introduced for preservation of records in electronic form with authentication by digital signatures [New sub-rules (4) and (5) inserted in rule 5]

Rule 5 has been amended by inserting a new sub-rule (4), which provides that records under rule 5 may be preserved in electronic form and every page of the record so preserved would be authenticated by means of a digital signature.

The Board may specify the conditions, safeguards and procedure to be followed by an assessee preserving digitally signed records [Sub-rule (5)].

For the purpose of rule 4C and sub-rule (4) and (5) of rule 5:

(i) The expression **"authenticate"** shall have the same meaning as assigned in the Information Technology Act, 2000.

(ii) The expression **"digital signature"** shall have the meaning as defined in the Information Technology Act, 2000 and the expression "digitally signed" shall be construed accordingly."

[Effective from 01.03.2015]

(vi) Cost Accountant/ Chartered Accountant nominated under section 72A also empowered to call for records and audit reports for scrutiny purposes [Rule 5A(2)]

Rule 5A(2) was quashed by the Delhi High Court in the case of *M/s. Travelite (India) 2014 (35) STR 653 (Del.)*[1] on the ground that the powers to conduct audit envisaged in the rule did not have appropriate statutory backing.

The said rule has been substituted with a new rule vide ***Notification No. 23/2014 ST dated 05.12.2014*** whereby authorized officers, audit party deputed by Commissioner or the C&AG, Cost Accountant or Chartered Accountant nominated under section 72A of the Finance Act, 1994 have been empowered to call for the specified records for scrutiny purposes and the assessee will be obliged to provide these documents within the time period as prescribed by the above mentioned persons.

In addition, ***Circular No. 181/7/2014 ST dated 10.12.2014*** issued thereafter clarified that the said new rule is within the scope of rule making powers under section 94(2)(k) as amended by the Finance (No.2) Act, 2014*. The said amended section provides a clear statutory backing for rule 5A(2). The expression "verified" used in section 94(2)(k) is of wide import and would include within its scope, audit by the departmental officers, as the procedure prescribed for audit is essentially a procedure for verification mandated in the statute.

New rule 5A(2) provides as follows:

"Every assessee, shall, on demand make available to the officer so empowered or the audit party deputed by the Commissioner or the Comptroller and Auditor General of India, or a cost accountant or chartered accountant nominated under section 72A of the Finance Act, 1994,-

(i) the records maintained or prepared by him in terms of rule 5(2);

(ii) the cost audit reports, if any, under section 148 of the Companies Act, 2013; and

(iii) the income-tax audit report, if any, under section 44AB of the Income-tax Act, 1961,

for the scrutiny of the officer or the audit party, or the cost accountant or chartered accountant, within the time limit specified by the said officer or the audit party or the cost accountant or chartered accountant, as the case may be."

Note:** Section 94(2) of the Finance Act, 1994 was amended by the Finance (No.2) Act, 2014 and clause (k) was inserted in said sub-section to empower Central Government to make rules in respect of ***imposition, on persons liable to pay service tax, for the proper levy and collection of the tax, of duty of furnishing information, keeping records and the manner in which such records shall be verified.

[Effective from 05.12.2014]

[1] The order of the High Court has been stayed by the Supreme Court in *2014-TIOL-101-SC-ST-LB.*

2. Amendments in Reverse Charge Notification

Taxable services in respect of which service tax is payable under section 68(2) of Finance Act, 1994, i.e., under reverse charge are notified under *Notification No. 30/2012 ST dated 20.06.2012.* The said notification has been amended vide ***Notification No. 7/2015 ST dated 01.03.2015*** as under:

(i) 100% service tax to be paid under reverse charge in case of service provided by (a) mutual fund agent/ distributor to mutual fund/ asset management company, (b) selling/marketing agent of lottery tickets to lottery distributor/selling agent and (c) person involving an aggregator

Following services have been added in the list of services on which service tax is payable under full reverse charge (100% service tax to be paid by the person liable for paying service tax other than the service provider):

(a) Taxable services provided or agreed to be provided by a mutual fund agent or distributor, to a mutual fund or asset management company - ***Effective from 01.04.2015***

(b) Taxable services provided or agreed to be provided by a selling or marketing agent of lottery tickets to a lottery distributor or selling agent - ***Effective from 01.04.2015***

(c) Taxable services provided or agreed to be provided by a person involving an aggregator in any manner - ***Effective from 01.03.2015***

(ii) Scope of reverse charge widened

The scope of reverse charge provisions has been widened with the introduction of concept of aggregator under service tax. Earlier, service tax was payable either by the service provider (normal charge) or the service receiver (reverse charge – full or partial). However, now under reverse charge provisions, service tax may be payable by any other person (who is liable for paying service tax) who may or may not be the service receiver (e.g., an aggregator). Thus, an amendment has been made in paragraph II of the notification to give effect to this amendment.

Further, in the Table in column (4), the column heading **"percentage of service tax payable by the person receiving the service"** has been substituted with **"percentage of service tax payable by any person liable for paying service tax other than the service provider"** as person liable to pay service tax may not necessarily be service receiver.

[Effective from 01.03.2015]

(iii) Entire service tax to be paid under reverse charge in case of manpower supply and security services

Earlier, in respect of services provided or agreed to be provided by way of supply of manpower for any purpose or security services by any individual, HUF or partnership firm including association of persons to a business entity registered as body corporate, 25% of service tax was payable by the person providing the service and remaining 75% by the service receiver.

However, now the entire service tax i.e., 100% service tax would be payable by the person liable for paying service tax other than the service provider (service recipient in this case).

[Effective from 01.04.2015]

Chapter-8: Other Provisions

1. Board/Chief Commissioner empowered to issue supplementary instructions [New rule 12 inserted in the Service Tax Rules, 1994]

With effect from 01.10.2014, ***Notification No. 19/2014 ST dated 25.08.2014*** has inserted new rule 12 in Service Tax Rules, 1994 to provide that Board or the Chief Commissioners of Central Excise may issue instructions for any incidental or supplemental matters for the implementation of the provisions of the Finance Act, 1994.

[Effective from 01.10.2014]

2. Benefit of advance ruling extended to resident firms [Section 96A(b)(iii)]

Earlier, *public sector companies*, *resident public limited companies* and *resident private limited companies* were notified under section 96A(b)(iii) of Finance Act, 1994 as the class or category of resident persons who can apply for advance ruling in case of specified matters relating to service tax.

Notification No. 9/2015 ST dated 01.03.2015 has expanded the scope of advance ruling by additionally notifying **resident firm** as class or category of residents who can apply for advance ruling in case of specified matters relating to service tax. Thus, now a resident firm will also be eligible to make an application for advance ruling in service tax.

Meaning of important terms

(a) **firm** shall have the meaning assigned to it in section 4 of the Indian Partnership Act, 1932 and includes-

- (i) the limited liability partnership as defined in section 2(1)(n) of the Limited Liability Partnership Act, 2008; or
- (ii) limited liability partnership which has no company as its partner; or
- (iii) the sole proprietorship; or
- (iv) one Person Company.

(b) (i) **sole proprietorship** means an individual who engages himself in an activity as defined in section 96A(a) of the Finance Act, 1994.

(ii) **One Person Company** means as defined in section 2(62) of the Companies Act, 2013.

(c) **resident** shall have the meaning assigned to it in section 2(42) of the Income-tax Act, 1961 in so far as it applies to a resident firm.

[Effective from 01.03.2015]

SECTION C: CUSTOMS AND FOREIGN TRADE POLICY

Chapter-9: Demand and Appeals

Clarification on applicability of pre-deposit provisions under section 129E of the Customs Act, 1962 to first stage appeal in matters relating to drawback

CBEC has clarified that mandatory pre-deposit would be payable in cases of demand of drawback when the appeal is filed before Commissioner (Appeals) as the new section 129E of Customs Act, 1962 would apply to such cases. However, the ambit of section 129E does not extend to appeals under section 129DD before Joint Secretary (Revision Application).

Therefore, while mandatory pre-deposit would be required to be paid in cases of drawback, rebate and baggage at the first stage appeal before Commissioner(Appeals), no pre-deposit would be payable in such cases while filing appeal before the JS(RA).

[Circular No. 993/17/2014-CX dated 05.1.2015]

Chapter-11: Duty Drawback

Following amendments have been made in Customs, Central Excise Duties and Service Tax Drawback Rules, 1995:

1. Duty drawback on rice allowed [Rule 3]

Earlier, no drawback was allowed on **rice falling under heading 1006** of the Customs Tariff. However, **with effect from 13.02.2015**, drawback will be allowed in respect of rice falling under heading 1006.

Rule 3 has been amended vide ***Notification No. 20/2015 Cus (NT) dated 10.02.2015*** to give effect to this amendment. Consequential amendments have been made in rule 6(4) and rule 7(5) of the said rules.

[Effective from 13.02.2015]

2. Application for Special Brand Rate cannot be made if a claim has been made under rule 3 or rule 4 [Rule 7]

Under rule 7, when the rate of duty drawback is lower than 4/5th of the duty/taxes paid, a Special Brand Rate may be applied. The said rule has been amended vide ***Notification No.109/2014 Cus (NT) dated 17.11.2014*** to provide that application for Special Brand Rate cannot be made where a claim for drawback under rule 3 or rule 4 has been made.

In other words, where the exporter has already filed a duty drawback claim under All Industry Rates (AIR) Schedule, he cannot request for fixation of Special Brand Rate of drawback. Thus, the exporter should determine prior to export of goods, whether to claim drawback under AIR or Special Brand Rate.

[Effective from 22.11.2014]

Chapter-14: Advance Ruling

Benefit of advance ruling extended to resident firms [Section 28E(c)(iii)]

Earlier, *public sector companies*, *resident public limited companies* and *resident private limited companies* were notified under section 28E(c)(iii) of Customs Act, 1962 as the class or category of resident persons who can apply for advance ruling in case of specified matters relating to customs duty.

Notification No. 27/2015 Cus (NT) dated 01.03.2015 has expanded the scope of advance ruling by additionally notifying **resident firm** as class or category of residents who can apply for advance ruling in case of specified matters relating to customs duty. Thus, now a resident firm will also be eligible to make an application for advance ruling in matters relating to customs duty.

Meaning of important terms

(a) **firm** shall have the meaning assigned to it in section 4 of the Indian Partnership Act, 1932 and includes-

(i) the limited liability partnership as defined in section 2(1)(n) of the Limited Liability Partnership Act, 2008; or

(ii) limited liability partnership which has no company as its partner; or

(iii) the sole proprietorship; or

(iv) one Person Company.

(b) (i) **sole proprietorship** means an individual who engages himself in an activity as defined in section 23A(a) of the Central Excise Act, 1944.

(ii) **One Person Company** means as defined in section 2(62) of the Companies Act, 2013.

(c) **resident** shall have the meaning assigned to it in section 2(42) of the Income-tax Act, 1961 in so far as it applies to a resident firm.

[Effective from 01.03.2015]

Chapter-16: Foreign Trade Policy

New Foreign Trade Policy 2015-2020 has come into effect from April 1, 2015. The salient features of the new policy are discussed hereunder[2]:

16.1. Introduction

Foreign Trade Policy is a set of guidelines or instructions issued by the Central Government in matters related to import and export of goods in India viz., **foreign trade**. In the era of globalization, foreign trade has become the lifeline of any economy. Its primary purpose is not merely to earn foreign exchange, but also to stimulate greater economic activity. International

[2] Students are advised to read this Chapter on Foreign Trade Policy in place of Chapter 16 of Section C: Customs & FTP of Study Material on Paper 8: Indirect Tax Laws [November, 2014 Edition]

trade not only enables a nation to specialize in the goods which it can produce most cheaply and efficiently, but also to consume more than it would be able to produce with its own resources. International trade enlarges the potential markets for the goods of a particular economy.

Legislation governing foreign trade: In India, Ministry of Commerce and Industry governs the affairs relating to the promotion and regulation of foreign trade. The main legislation concerning foreign trade is the **Foreign Trade (Development and Regulation) Act, 1992 FT(D&R) Act**. The FT(D&R) Act provides for the development and regulation of foreign trade by facilitating imports into, and augmenting exports from, India and for matters connected therewith or incidental thereto. As per the provisions of the Act, the Government:-

(i) may make provisions for facilitating and controlling foreign trade;

(ii) may prohibit, restrict and regulate exports and imports, in all or specified cases as well as subject them to exemptions;

(iii) is authorised to formulate and announce an export and import policy and also amend the same from time to time, by notification in the Official Gazette;

(iv) is also authorised to appoint a 'Director General of Foreign Trade' for the purpose of the Act, including formulation and implementation of the export-import policy.

Foreign Trade Policy: In exercise of the powers conferred by the FT(D&R) Act , the Union Ministry of Commerce and Industry, Government of India generally announces the integrated **Foreign Trade Policy (FTP)** every five years with certain underlined objectives. The Foreign Trade Policy was earlier called as Export Import policy i.e., EXIM Policy. However, export import policy is now referred to as Foreign Trade Policy (FTP) of the country as it covers areas much beyond export and import. This policy is updated every year, in addition to changes that are made throughout the year.

The FTP, in general, aims at developing export potential, improving export performance, encouraging foreign trade and creating favorable balance of payments position. The policies are driven by factors like export led growth, improving efficiency and competitiveness of the Indian industries, ease of doing business etc.

Salient Features of an FTP: The following are some of the key attributes of the FTP:

- Export-Import of goods and services is generally free unless specifically regulated by the provisions of the Policy or any other law for the time being in force.
- Export and import goods are broadly categorized as – (a) Free (b) Restricted (c) Prohibited.
- Some goods are 'free' for import and export but can be imported/exported only through State Trading Enterprises (STE).
- There are restrictions on exports and imports for various strategic, health, defence, environment, and other reasons. If the goods are restricted for import/export but not prohibited, the Government can give a permission/license for specific reasons.
- Exports are promoted through various promotional schemes.

- Goods and services are to be exported and not taxes. Hence, the taxes on exports are either exempted or adjusted or refunded on both outputs and inputs, through schemes of Duty Exemption, Duty Refund (Drawbacks and Rebates).
- Capital goods can be imported at NIL duty for the purpose of exports under the scheme of EPCG.
- For units undertaking to export all their production, there are special schemes so that they can avoid taxes at every stage under the scheme of EOU/SEZ.
- In certain cases imports get duty exemption/concession for certain special purposes. In such cases, to enable domestic suppliers compete with the international suppliers, the supplies of domestic suppliers are treated as deemed exports.
- Duty credit scrips Schemes are designed to promote exports of some specified goods to specified markets and to promote export of specified services.

Foreign Trade Policy 2015-2020 - The present Foreign Trade Policy, which was announced on 01.04.2015, is an integrated policy for the period between 01.04.2015 and 31.03.2020.

Guiding principles: The guiding principles of FTP 2015-2020 are as follows –

- Generation of employment and increasing value addition in country, in keeping with 'Make in India' vision.
- Focus on improving 'ease of doing business' and 'trade facilitation' by simplifying procedures and extensive use of e-governance – move towards paperless working.
- Encouraging e-commerce exports of specified products.
- Steps to encourage manufacture and export by SEZ, EOU, STP, EHTP and BTP.
- Duty credit scrips to (a) encourage exports of specified products to specified markets (b) export of services.
- Special efforts to resolve quality complaints and trade disputes.

The various measures taken in said direction include:

- The number of mandatory documents required for exports and imports of goods from/into India have been reduced to 3 each (discussed in detail in subsequent pages).
- The facility of 24 X 7 Customs clearance for specified imports has been made available at the 18 specified sea ports. The facility of 24 X 7 Customs clearance for specified imports has also been made available at the 17 specified air cargo complexes.
- Single window scheme has been introduced to enable importer and exporter to lodge their clearance documents at a single point thereby providing a common platform to trade to meet requirements of all regulatory agencies involved in exim trade.
- To facilitate processing of shipping bills before actual shipment, prior online filing facility for shipping bills has been provided by the Customs - 7 days for air shipments & ICDs and 14 days for shipments by sea.

- DGFT under the EDI initiatives has provided the facility of on line filing of applications to obtain Importer Exporter Code and various authorizations /scrips.

Exports from and imports in India, need a lot of regulatory requirements to be complied with at various stages. Yet if properly planned, exports and imports can utilize a lot benefits that are available under various provisions of the FTP. The policy not only prescribes the guidelines as to which goods and services can be imported/exported and the relevant procedures thereto but also provides a lot of benefits if properly planned.

Schemes like Duty Exemption Schemes, EPCG Schemes, Deemed Exports, etc., benefit exporters, importers and even defined domestic businesses thereby assisting all businesses to reduce costs at every stage in the value chain. In addition, exporters can avail other benefits under promotional schemes.

Administration of the FTP: The FTP is formulated, controlled and supervised by the office of the Director General of Foreign Trade (DGFT), an attached office of the Ministry of Commerce & Industry, Government of India. DGFT has several offices in various parts of the country which work on the basis of the policy formed by the headquarters at Delhi.

DGFT issues **authorization** (earlier called as licence) for import/export. 'Authorization' means a permission in terms of the FT(D&R) Act to import or export. It also grants **Importer Exporter Code** (IEC) Number to importers and exporters. Import and Export without IEC number is not permitted, unless specifically exempted.

Decision of DGFT is final and binding in respect of interpretation of any provision of foreign trade policy, classification of any item in ITC(HS), content scope or issue of any authorization issued under the FTP.

Other authorities involved: Though the FTP is formulated by DGFT, it is administered in close coordination with other agencies. Other important authorities dealing with FTP are:

(1) Central Board of Excise and Customs (CBEC): CBEC comes under Ministry of Finance and its two Departments namely, Customs and Central Excise facilitate in implementing the provisions of the FTP.

Customs Department is responsible for clearance of export and import goods after their valuation and examination. Customs authorities follow the policy formed by the DGFT while clearing the goods. Since there is a central excise duty on almost all the manufactured products, Central Excise authorities need to be involved for all matters of exports, where goods have to be cleared without duty. Central Excise Department works as Customs Departments at various required places, and has a crucial role in the procedural aspects.

(2) Reserve Bank of India (RBI): RBI is the nodal bank in the country which formulates the policies related to management of money, including payments and receipts of foreign exchange. It also monitors the receipt and payments for exports and imports. RBI works under the Ministry of Finance.

(3) State VAT Departments: Since VAT is payable on domestic goods but not on export goods, formalities with State VAT departments assume importance in ensuring tax free exports.

Contents of Foreign Trade Policy:

The contents of the FTP 2015-2020 are as follows

(i) **FTP 2015-2020:** having 9 Chapters giving basic policy. This has been notified by the Central Government on 01.04.2015. The policy is amended normally in April every year and also during the year.

(ii) **Handbook of Procedures 2015-2020:** (HBP 2015-2020) containing 9 chapters, covering procedural aspects of policy. This has been notified by Director General of Foreign Trade on 01.04.2015. It is amended from time to time as per requirements.

(iii) **Appendices and Aayat Niryat Forms (AANF):** containing various appendices and forms relating to import and export.

(iv) **Standard Input-Output Norms:** Standard Input-Output Norms (SION) of various products are notified from time to time.. Based on SION, exporters are provided the facility to make duty-free import of inputs required for manufacture of export products under the Duty Exemption Schemes like Advance Authorisation and DFIA.

(v) **ITC(HS) Classification of Exports and Import Items:** The Export Import Policy regarding import or export of a specific item is given in the Indian Trade Classification Code based on Harmonized System of Coding [ITC(HS)]. ITC-HS Coding was adopted in India for import-export operations. Indian custom uses eight digit ITC-HS Codes to suit the national trade requirements.

ITC-HS codes are divided into two schedules. **ITC(HS) Import Schedule I** describe the rules and guidelines related to import policies where as **Schedule II** describe the rules and regulation related to export policies. Presently, most of the goods can be imported without any authorization. Schedule II contains very few products, where export is prohibited or restricted. Excluding those items, export of all other goods is free.

Any changes or formulation or addition of new codes in ITC-HS Codes are carried out by DGFT (Directorate General of Foreign Trade).

Foreign Trade Policy *vis a vis* tax laws: The Foreign Trade Policy is closely knit with the Customs and Excise laws of India. However, the policy provisions *per-se* do not override tax laws. The exemptions extended by FTP are given effect to by issue of notifications under respective tax laws (e.g., Customs Tariff Act). Thus, actual benefit of the exemption depends on the language of exemption notifications issued by the CBEC. In most of the cases the exemption notifications refer to policy provisions for detailed conditions. Ministry of Finance/ Tax Authorities cannot question the decision of authorities under the Ministry of Commerce (so far as the issue of authorization etc. is concerned).

FTP, Handbook of procedures under FTP, Central Excise Act and Customs Act and notifications issued hereunder form an integrated scheme of indirect taxation. All these

statues have to be read as a whole and not in isolation, since they are series of statues relating to same subject matter.

Scope of FTP: The FTP covers the policies and regulations with respect to the following matters:

(i) Legal framework and trade facilitation – Chapter 1

(ii) Policy for regulating import and export of goods and services – Chapter 2

(iii) Export Promotional Measures – Export from India Scheme – Chapter 3

(iv) Duty Remission and Duty Exemption Scheme for promotion of exports – AA and DFIA and duty drawback – Chapter 4

(v) Export promotion Capital Goods (EPCG) Scheme – Chapter 5

(vi) Export Oriented Undertakings (EOU) / Electronic Hardware Technology Park (EHTP) / Software Technology Park (STP) and Bio Technology Parks (BTU) Schemes – Chapter 6

(vii) Deemed Exports – Chapter 7

(viii) Quality Complaints and Trade Disputes – Chapter 8

(ix) Definitions – Chapter 9

Provisions relating to Special Economic Zone (SEZ) are contained in a separate Act and are not part of FTP. However, provisions of SEZ are closely related to Foreign Trade Policy.

Handbook of Procedures (HBP 2015-2020) has 9 corresponding chapters which mainly deal with procedural aspects of the foreign trade policy.

Special Focus Initiatives: The FTP provides certain special focus initiatives for Market Diversification, Technological Upgradation, Support to status holders, Agriculture, Handlooms, Handicraft, Gems & Jewellery, Leather, Marine, Electronics and IT Hardware Manufacturing Industries, Green products, Exports of products from North-East, Sports Goods and Toys sectors wherein the Government of India shall make concerted efforts to promote exports.

Board of Trade: Board of Trade (BOT) has been constituted to advise Government on Policy measures for increasing exports, review export performance, review policy and procedures for imports and exports and examine issues relevant for promotion of India's foreign trade. Commerce & Industry Minister will be the Chairman of the BOT. Government shall also nominate upto 25 persons, of whom at least 10 will be experts in trade policy. In addition, Chairmen of recognized Export Promotion Councils (EPCs) and President or Secretary-Generals of National Chambers of Commerce will be ex-officio members. BOT will meet at least once every quarter.

Trade facilitation through EDI initiatives: DGFT has put in place a robust EDI system for the purpose of export facilitation and good governance. DGFT has set up a secured EDI message exchange system for various documentation related activities including import and export authorizations established with other administrative departments, namely, Customs, Banks and EPCs. This has reduced the physical interface of exporters and importers with the Government Departments and is a significant measure in the direction of reduction of transaction cost. The

endeavour of DGFT has been to enlarge the scope of EDI to achieve higher level of integration with partner departments. E-BRC (Electronic Bank Realisation Certificate) has enabled DGFT to capture details of realisation of export proceeds directly from the banks through secured electronic mode. Further, an online complaint registration and monitoring system allows users to register complaint and receive status/ reply online.

DGCI&S Commercial Trade Data: DGCI&S has put in place a Data Suppression Policy. Transaction level data would not be made publically available to protect privacy. DGCI&S trade data shall be made available at aggregate level with a minimum possible time lag in a query based structured format on commercial criteria.

16.2 Provisions regarding imports and exports

A. GENERAL PROVISIONS APPLICABLE TO IMPORT AND EXPORT OF GOODS

1. **Exports and imports are free unless regulated:** Exports and Imports shall be free, except where regulated by FTP or any other law in force. The item wise export and import policy shall be specified in ITC(HS) notified by DGFT from time to time. These are classified as – (a) Free (b) Restricted (c) Prohibited (d) Exclusive trading through State Trading Enterprise (STEs).
2. **Compliance with laws:** Every exporter or importer shall comply with the provisions of the FT (D&R) Act, the rules and orders made there-under, the FTP and terms and conditions of any authorization granted to him. All imported goods shall also be subject to domestic laws, rules, orders, regulations, technical specifications, environmental and safety norms as applicable to domestically produced goods unless specifically exempted.
3. **Interpretation of policy:** If any question or doubt arises in respect of interpretation of any provision, said question or doubt shall be referred to DGFT whose decision thereon shall be final and binding.
4. **Procedure:** DGFT may specify procedure to be followed by an exporter or importer or by any licencing or any other competent authority for the purpose of implementing provisions of Foreign Trade Act, the rules and the orders made there-under and FTP. Such procedures shall be published in Hand Book of Procedures by means of a Public Notice, and may, in like manner, be amended from time to time.
5. **Exemption from Policy/Procedure:** DGFT may pass such orders or grant such relaxation or relief, as he may deem fit and proper, on grounds of genuine hardship and adverse impact on trade. DGFT may, in public interest, exempt any person or class or category of persons from any provision of FTP or any procedure and may, while granting such exemption, impose such conditions as he may deem fit.
6. **Principles of Restriction:** DGFT may, through a notification, adopt and enforce any measure necessary for:

   (a) **Protection** of:-

      (i) public morals.

      (ii) human, animal or plant life or health.

(iii) patents, trademarks and copyrights and the prevention of deceptive practices.

(iv) national treasures of artistic, historic or archaeological value

(v) trade of fissionable material or material from which they are derived

(b) **Prevention** of traffic in arms, ammunition and implements of war and use of prison labour.

(c) **Conservation** of exhaustible natural resources.

7. **Export/import of restricted goods/services:** Any goods/services, export or import of which is restricted under ITC(HS) may be exported or imported only in accordance with an Authorization or in terms of a public notice/notification issued in this regard.

8. **Terms and Conditions of an authorization:** Every Authorization shall be valid for prescribed period of validity and shall contain such terms and conditions as may be specified by Regional Authority (RA), which may include:

(a) Quantity, description and value of goods;

(b) Actual User condition;

(c) Export obligation;

(d) Minimum Value Addition to be achieved;

(e) Minimum export/ import price; and

(f) Bank Guarantee/ Legal Undertaking/ Bond with Customs Authority/ RA.

(g) Validity period of import/export as specified in Handbook of Procedures

9. **Authorization not a right:** No person may claim an Authorization as a right and DGFT or RA shall have power to refuse to grant or renew the same in accordance with provisions of FT(D&R) Act, rules made there under and FTP.

10. **Penalty:** If an authorization holder violates any condition of such authorization or fails to fulfill export obligation, he shall be liable for action in accordance with FT (D&R) Act, the Rules and Orders made there under, FTP and any other law for time being in force.

11. **State Trading Enterprises (STEs):** STEs are governmental and non-governmental enterprises, including marketing boards, which deal with goods for export and/or import. Any goods, import or export of which is governed through exclusive or special privileges granted to State Trading Enterprises [STE(s)], may be imported or exported by STE(s) as per conditions specified in ITC(HS). DGFT may, however, grant an authorization to any other person to import or export any of these goods.

12. **Importer-Exporter Code (IEC):** It is a unique 10 digit code issued by DGFT to a person. IEC is mandatory to export any goods out of India or to import any goods into India unless specifically exempt. Permanent Account Number (PAN) is pre-requisite for grant of an IEC. Only one IEC can be issued against a single PAN.

An application for IEC is to be made manually to the nearest RA (Regional Authority) of DGFT or alternatively, it can be filed online, in Form ANF 2A and shall be accompanied by prescribed documents. In case of STPI/ EHTP/ BTP units, the Regional Offices of the DGFT having jurisdiction over the district in which the Registered/ Head Office of the STPI unit is located shall issue or amend the IECs.

13. **Trade with neighbouring countries:** DGFT may issue instructions or frame schemes as may be required to promote trade and strengthen economic ties with neighbouring countries.

14. **Transit facility:** Transit of goods through India from/ or to countries adjacent to India shall be regulated in accordance with bilateral treaties between India and those countries and will be subject to such restrictions as may be specified by DGFT in accordance with international conventions.

15. **Mandatory documents for export/import of goods from/into India:**

(a) Mandatory documents required for export of goods from India:

1. Bill of Lading/Airway Bill
2. Commercial Invoice cum Packing List*
3. Shipping Bill/Bill of Export

(b) Mandatory documents required for import of goods into India

1. Bill of Lading/Airway Bill
2. Commercial Invoice cum Packing List*
3. Bill of Entry

***Note:** As per CBEC *Circular No. 01/15-Customs dated 12/01/2015*, separate Commercial Invoice and Packing List would also be accepted.

B. PROVISIONS RELATING TO IMPORT OF GOODS

1. **Actual user condition:** Goods which are importable without any restriction, may be imported by any person. However, if such imports require an Authorization, actual user alone may import such goods unless actual user condition is specifically dispensed with by DGFT.

2. **Second hand goods:** Import of second hand capital goods, including refurbished/ re-conditioned spares shall be allowed freely. However, second hand personal computers/ laptops, photocopier machines, air conditioners, diesel generating sets will only be allowed against authorisation. Second hand (used) goods, [except second hand capital goods], shall be restricted for imports and may be imported only against Authorization.

3. **Removal of scrap/ waste from SEZ:** Any waste or scrap or remnant including any form of metallic waste & scrap generated during manufacturing or processing activities of an SEZ Unit/ Developer/ Co-developer shall be allowed to be disposed in DTA (Domestic Tariff Area) freely, subject to payment of applicable customs duty.

4. **Import of gifts and samples:** Import of gifts shall be permitted where such goods are otherwise freely importable under ITC(HS). In other cases, a Customs Clearance Permit (CCP) shall be required from DGFT. Further, import of samples shall be governed by the prescribed procedures. Authorisation for import of samples is required only in case of vegetable seeds, bees and new drugs. Samples of tea upto ₹ 2,000 (CIF) per consignment will be allowed without authorization. Samples upto ₹ 3,00,000 can be imported by all exporters without duty.

5. **Passenger Baggage:**

   (a) Bonafide household goods and personal effects may be imported as part of passenger baggage as per limits, terms and conditions thereof in the Baggage Rules, 1998.

   (b) Samples of such items that are otherwise freely importable under FTP may also be imported as part of passenger baggage without an Authorization.

   (c) Exporters coming from abroad are also allowed to import drawings, patterns, labels, price tags, buttons, belts, trimming and embellishments required for export, as part of their passenger baggage without an Authorization.

   Note: Baggage provisions have been discussed in detail in Chapter-7- Importation, Exportation and Transportation of Goods.

6. **Re-import of goods repaired abroad:** Capital goods, equipments, components, parts and accessories, whether imported or indigenous, except those restricted under ITC(HS) may be sent abroad for repairs, testing, quality improvement or upgradation or standardization of technology and re-imported without an Authorization.

7. **Import of goods used in projects abroad:** After completion of projects abroad, project contractors may import, without an Authorization, goods including capital goods used in the project provided they have been used for at least one year.

8. **Sale on high seas:** Sale of goods on high seas for import into India may be made subject to FTP or any other law in force.

9. **Import under lease financing:** It is freely permitted. Permission of Regional Authority is not required for import of capital goods under lease financing. However, RBI approval is required in some cases.

10. **Clearance of goods from customs:** Goods already imported/ shipped/ arrived, in advance, but not cleared from customs may also be cleared against an Authorization issued subsequently. However, this facility will not be available to restricted items or items traded through STEs.

11. **Execution of BG/ LUT:** Whenever goods are imported duty free or otherwise specifically stated, importer shall execute prescribed LUT (Letter of Undertaking)/ BG (Bank Guarantee)/ Bond with Customs Authority before clearance of goods. In case of indigenous sourcing, Authorization holder shall furnish LUT/ BG/ Bond to RA concerned before sourcing material from indigenous supplier/ nominated agency as per the prescribed procedures.

12. **Private/ public bonded warehouses for imports:** Private/ public bonded warehouses may be set up in DTA (Domestic Tariff Area) as per terms and conditions of notification issued by DoR. Any person may import goods, except prohibited items, arms and ammunition, hazardous waste and chemicals and warehouse them in such bonded warehouses. Such goods may be cleared for home consumption against authorisation, whenever required. Customs duty as applicable shall be paid at the time of clearance of such goods. If such goods are not cleared for home consumption within a period of one year or such extended period as the custom authorities may permit, importer of such goods shall re-export the goods.

C. PROVISIONS RELATING TO EXPORT OF GOODS

1. **Free exports:** All goods may be exported without any restriction except to the extent that such export is regulated by ITC(HS) or any other provision of FTP or any other law for the time being in force. DGFT may however, specify through a public notice such terms and conditions according to which any goods, not included in ITC(HS), may be exported without an Authorization.
2. **Export of samples:** Export of samples and free of charge goods shall be governed by prescribed procedures. Export of bona fide trade and technical samples of freely exportable item shall be allowed without any limit. In case of restricted items, application should be made to DGFT. Such samples can be exported as part of passenger baggage without an Authorisation.
3. **Export of passenger baggage:** Bonafide personal baggage may be exported either along with passenger or, if unaccompanied, within one year before or after passenger's departure from India. However, items mentioned as restricted in ITC(HS) shall require an Authorization. Government of India officials proceeding abroad on official postings shall, however, be permitted to carry alongwith their personal baggage, food items (free, restricted or prohibited) strictly for their personal consumption. Samples of such items that are otherwise freely exportable under FTP may also be exported as part of passenger baggage without an Authorisation.
4. **Export of gifts:** Goods, including edible items, of value not exceeding ₹ 5,00,000 in a licensing year, may be exported as a gift. However, items mentioned as restricted for exports in ITC(HS) shall not be exported as a gift, without an Authorization. For export of samples/gifts/ spares/ replacement goods (other than SCOMET items) in excess of ceiling/period, application can be made to DGFT in form ANF-2Q.
5. **Export of spares:** Warranty spares (whether indigenous or imported) of plant, equipment, machinery, automobiles or any other goods, [except those restricted under ITC(HS)] may be exported along with main equipment or subsequently, but within contracted warranty period of such goods subject to approval of RBI.
6. **Third party exports:** Third-party exports means exports made by an exporter or manufacturer on behalf of another exporter(s). In such cases, export documents such as shipping bills shall indicate name of both manufacturing exporter/manufacturer and third

party exporter(s). BRC, GR declaration, export order and invoice should be in the name of third party exporter. Such third party exports shall be allowed under FTP.

7. **Export of imported goods:** Goods imported, in accordance with FTP, may be exported in same or substantially the same form without an Authorization, provided that an item to be imported or exported is not restricted for import or export in ITC(HS).

   Exports of such goods imported against payment in freely convertible currency would be permitted provided export proceeds are realized in freely convertible currency. However, export of such goods to notified countries will be permitted in Indian rupees subject to at least 15% value addition.

8. **Export of replacement goods:** Goods or parts thereof on being exported and found defective/ damaged may be replaced free of charge by the exporter and such goods shall be allowed clearance by customs authorities, provided that replacement goods are not mentioned as restricted items for exports in ITC(HS).

9. **Export of repaired goods:** Goods or parts exported and found defective, damaged or otherwise unfit for use may be imported for repair and subsequent re-export. Such goods shall be allowed clearance without an Authorization and in accordance with customs notification.

   However, re-export of such defective parts/spares by the Companies/firms and Original Equipment Manufacturers shall not be mandatory if they are imported exclusively for undertaking root cause analysis, testing and evaluation purpose.

10. **Private Bonded Warehouses for exports:** Private bonded warehouses, which are set up exclusively for exports shall be entitled to procure goods from domestic manufacturers without payment of duty. Supplies made by a domestic supplier to such notified warehouses shall be treated as physical exports provided payments are made in free foreign exchange.

11. **Denomination of export contracts:** All export contracts and invoices shall be denominated either in freely convertible currency or Indian rupees but export proceeds shall be realised in freely convertible currency. However, export proceeds against specific exports may also be realized in rupees, provided it is through a freely convertible Vostro account of a non resident bank situated in any country other than a member country of Asian Clearing Union (ACU) or Nepal or Bhutan. Additionally, rupee payment through Vostro account must be against payment in free foreign currency by buyer in his non-resident bank account.

    Free foreign exchange remitted by buyer to his non-resident bank (after deducting the bank service charges) on account of this transaction would be taken as export realization under export promotion schemes of FTP. Contracts for which payments are received through ACU shall be denominated in ACU Dollar. Central Government may relax provisions in this regard in appropriate cases. Export contracts and invoices can be denominated in Indian rupees against EXIM Bank/ Government of India line of credit.

12. **Non-realisation of export proceeds:** If an exporter fails to realise export proceeds within time specified by RBI, he shall, without prejudice to any liability or penalty under any law in force, be liable to action in accordance with provisions of FT(D&R) Act, rules and orders made thereunder and provisions of FTP.
13. **Free movement of export goods:** Consignments of items meant for exports shall not be withheld/ delayed for any reason by any agency of Central/ State Government. In case of any doubt, authorities concerned may ask for an undertaking from exporter and release such consignment.
14. **No seizure of export related stock:** No seizure of stock shall be made by any agency so as to disrupt manufacturing activity and delivery schedule of exports. In exceptional cases, concerned agency may seize the stock on basis of prima facie evidence of serious irregularity. However, such seizure should be lifted within 7 days unless the irregularities are substantiated.

D. Personal hearing by DGFT for Grievance Redressal:

Government is committed to easy and speedy redressal of grievances from Trade and Industry. As a last resort to redress grievances of Foreign Trade players, DGFT may provide an opportunity for Personal hearing before Policy Relaxation Committee (PRC) subject to fulfillment of certain conditions.

Export Promotion Councils: Basic objective of Export Promotion Councils (EPCs) is to promote and develop Indian exports. Each Council is responsible for promotion of a particular group of products, projects and services.

Registration-cum-Membership Certificate (RCMC): Any person, applying for an Authorization to import/ export, or any other benefit or concession under FTP shall be required to furnish on DGFT's website in the Importer Exporter profile, RCMC granted by competent authority. For instance, Certificate of Registration as Exporter of Spices (CRES) issued by Spices Board shall be treated as RCMC for the purposes under this Policy.

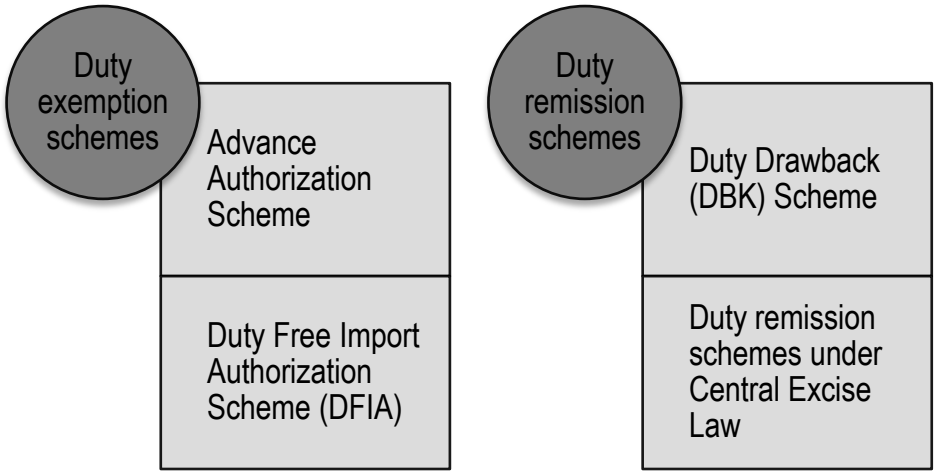
16.3 Export Promotion Schemes

Exports of a country play an important role in the economy. Government always endeavors to encourage exports by introducing various export promotion schemes. Consequently, there are various promotional measures under FTP and other schemes operated under Ministry of Commerce through various Export Promotion Councils.

As per WTO, export incentives cannot be given to the exporters as such otherwise there would be no free competition. Hence, all the export promotion schemes in India are directed towards ensuring that the inputs as well as final products are made tax-free.

(1) DUTY EXEMPTION & REMISSION SCHEMES

The Duty Exemption and Remission Schemes are the most important schemes in the Foreign Trade Policy, because they are most widely utilized and are largely compatible with the provisions of the Agreement on Subsidies and Countervailing Measures (ASCM) of the WTO.



(A) Duty exemption schemes: Under duty exemption schemes, exporter can import the inputs duty free for export production. The two duty exemption schemes are as follows:-

1. Advance Authorization Scheme
2. Duty Free Import Authorization Scheme (DFIA)

(B) Duty remission schemes: Under duty remission scheme, duty on inputs and input services used in the export product is either replenished or remitted. Duty Drawback (DBK) Scheme is designed for this purpose. Duty remission is also granted under central excise law, through CENVAT credit scheme and rules 18 and 19 of Central Excise Rules, 2002.

Duty exemption schemes

1. ADVANCE AUTHORIZATION SCHEME

- Under advance authorization scheme, **INPUTS** which are used in the export product can be imported without payment of customs duty.
- The goods imported are exempt from basic customs duty, additional customs duty, education cess, anti-dumping duty and safeguard duty, unless otherwise specified. The conditions for duty free imports against physical exports are provided in notification issued under the Customs law.
- Advance Authorisation shall be valid for 12 months from the date of issue of such Authorisation. Advance Authorisation for Deemed Export shall be co-terminus with contracted duration of project execution or 12 months from the date of issue of Authorisation, whichever is more.
- Period of fulfillment of export obligation under Advance Authorization is 18 months from the date of issue of Authorization or as notified by DGFT.
- Exports proceeds shall be realized in freely convertible currency except otherwise

specified.

(i) **Advance Authorisation on basis of SION:** Advance Authorization is issued for inputs in relation to the resultant product on the basis of SION. If SION for a particular item is not fixed, Advance Authorisation can be issued by RA based on self declaration by applicant, except certain specified products.

Standard Input Output Norms (SION) are standard norms which define the amount of input(s) required to manufacture unit of output for export purpose. SION is notified by DGFT on basis of recommendation of Norms Committee.

(ii) **Items which can be imported duty free against advance authorization:**

- Inputs, which are physically incorporated in export product (making normal allowance for wastage).
- Fuel, oil, catalysts which are consumed/utilised to obtain export product.
- Mandatory spares which are required to be exported/supplied with resultant product permitted upto 10% of CIF value of Authorization.
- Specified spices only when used for activities like crushing/ grinding /sterilization/ manufacture of oils or oleoresins and not for simply cleaning, grading, re-packing etc.

However, items reserved for imports by STEs cannot be imported against advance authorization.

(iii) **Actual user condition for Advance Authorisation:** Advance Authorization and/ or materials imported thereunder will be with actual user condition. It will not be transferable even after completion of export obligation. However, Authorization holder will have an option to dispose off product manufactured out of duty free inputs once export obligation is completed.

In case where CENVAT credit facility on inputs has been availed for the exported goods, even after completion of export obligation, the goods imported against Advance Authorization shall be utilized only in the manufacture of dutiable goods whether within the same factory or outside (by a supporting manufacturer).

Waste/scrap arising out of manufacturing process, as allowed, can be disposed off on payment of applicable duty even before fulfillment of export obligation.

(iv) **Who are eligible for advance authorization:** Advance Authorization can be issued either to a manufacturer exporter or merchant exporter tied to supporting manufacturer(s).

Such Authorization can also be issued for:

(1) Physical exports

(2) Intermediate supply

(3) Supplies made to specified categories of deemed exports

(4) Supply of 'stores' on board of foreign going vessel/aircraft provided there is specific SION in respect of items supplied.

(v) Domestic sourcing of inputs: Holder of advance authorization has an option to procure the materials/ inputs from indigenous manufacturer/STE in lieu of direct import against Advance Release Order (ARO)/ Invalidation letter/ Back to Back Inland Letter of Credit. However, Advance Authorisation holder may obtain supplies from EOU/EHTP/BTP/STP/SEZ units, without obtaining ARO or Invalidation letter.

(vi) Conditions for redeeming authorisation: It is necessary to establish that inputs actually used in manufacture of the export product should only be imported under the authorization and inputs actually imported must be used in the export product, for redeeming the Authorisation. The name/description of the input in the Authorisation must match exactly with the name/description endorsed in the shipping bill.

Further, quantity of input to be allowed under Advance Authorisation shall be in proportion to the quantity of input actually used/ consumed in production. If goods are imported against advance authorization but export obligation is not fulfilled, duty and interest is payable.

Aforesaid provisions will also be applicable for supplies to SEZs and supplies made under deemed exports.

(vii) Annual Advance authorization: Advance Authorization can be issued for annual requirement also. Such authorization shall be issued for items specified in SION and is not available on self-declaration basis.

Exporters having past export performance (in at least preceding two financial years) shall be entitled for Advance Authorization for Annual Requirement.

Entitlement in terms of CIF value of imports shall be upto 300% of the FOB value of physical export and/ or FOR value of deemed export in preceding financial year or ₹ 1 crore, whichever is higher.

(viii) Value addition (VA): will be calculated as follows (except for gem and jewellery sector)–

VA = [(A-B) x 100]/B

A = FOB value of export realised/FOR value of supply received.

B = CIF value of inputs covered by authorisation plus any other imported materials used on which benefit of duty drawback (DBK) is claimed or intended to be claimed.

If some items are supplied free of cost by foreign buyer, its notional value will be added in the CIF value of import and FOB value of export for purpose of calculating value addition. Exports to SEZ Units/ supplies to Developers/ Co-developers, irrespective of currency of realization, would also be covered.

Minimum value addition required to be achieved under Advance Authorization is 15%, except for physical exports for which payments are not received in freely convertible currency and some other specified export products. For tea, minimum value addition required shall be 50%.

(ix) Admissibility of drawback: Drawback as per rate determined and fixed by Central Excise authority shall be available for duty paid inputs (both imported and indigenous) used in the export product.

2. DUTY FREE IMPORT AUTHORIZATION (DFIA) SCHEME

- Provisions applicable to Advanced Authorisation are broadly applicable in case of DFIA. However, these Authorizations shall be issued only for products for which Standard Input and Output Norms (SION) have been notified. Duty Free Import Authorisation (DFIA) is issued to allow duty free import of inputs. In addition, import of oil and catalyst which is consumed / utilised in the process of production of export product, may also be allowed.
- The goods imported are exempt ONLY from basic customs duty. Additional customs duty/excise duty, being not exempt, shall be adjusted as CENVAT credit as per DoR rules.
- DFIA shall be issued on post export basis for products for which SION have been notified. Separate DFIA shall be issued for each SION and each port.
- The applicant shall file an online application to RA concerned before starting exports under DFIA. Export shall be completed within 12 months from the date of online filing of application and generation of file number. While doing export/supply, applicant shall indicate file number on the export documents.
- After completion of exports and realization of export proceeds, request for issuance of transferable DFIA may be made to concerned RA within a period of:

  (a) 12 months from the date of export

  or

  (b) 6 months (or additional time allowed by RBI for realization) from the date of realization of export proceeds,

  whichever is later.
- RA shall issue transferable DFIA with a validity of 12 months from the date of issue.
- Exports proceeds shall be realized in freely convertible currency except otherwise specified.

(i) No DFIA for 'Actual Úser' condition inputs: No DFIA shall be issued for an export product where SION prescribes 'Actual User' condition for any input.

(ii) Domestic sourcing of inputs: Holder of DFIA has an option to procure the materials/ inputs from indigenous manufacturer/STE in lieu of direct import against Advance Release Order (ARO)/ Invalidation letter/ Back to Back Inland Letter of

Credit. However, DFIA holder may obtain supplies from EOU/EHTP/BTP/STP/SEZ units, without obtaining ARO or Invalidation letter.

(iii) Conditions for redeeming authorisation: It is necessary to establish that inputs actually used in manufacture of the export product should only be imported under the authorization and inputs actually imported must be used in the export product, for redeeming the DFIA. The name/description of the input in the DFIA must match exactly with the name/description endorsed in the shipping bill.

Further, quantity of input to be allowed under DFIA shall be in proportion to the quantity of input actually used/ consumed in production.

If goods are imported against advance authorization but export obligation is not fulfilled, duty and interest is payable.

Aforesaid provisions will also be applicable for supplies to SEZs and supplies made under deemed exports.

(iv) Value addition (VA): will be calculated as follows (except for gem and jewellery sector)–

VA = [(A-B) x 100]/B

A = FOB value of export realised/FOR value of supply received.

B = CIF value of inputs covered by authorisation plus any other imported materials used on which benefit of duty drawback (DBK) is claimed or intended to be claimed.

If some items are supplied free of cost by foreign buyer, its notional value will be added in the CIF value of import and FOB value of export for purpose of calculating value addition. Exports to SEZ Units/ supplies to Developers/ Co-developers, irrespective of currency of realization, would also be covered.

Minimum value addition required to be achieved under DFIA is 20%, except for physical exports for which payments are not received in freely convertible currency.

(v) Admissibility of drawback: Drawback as per rate determined and fixed by Central Excise authority shall be available for duty paid inputs, whether imported or indigenous, used in the export product.

Duty remission schemes

1. DUTY DRAWBACK (DBK) SCHEME

At present, this scheme is used to allow rebate of duties (central excise, customs and service tax) paid on inputs and input services used for exported final product. This scheme has been discussed in detail in Chapter-11-Duty Drawback.

2. DUTY REMISSION SCHEMES IN CENTRAL EXCISE LAW

Duty remission/exemption is also granted under central excise law, through CENVAT credit scheme and rules 18 and 19 of Central Excise Rules, 2002. These schemes are discussed in Section A: Central Excise.

(2) REWARD SCHEMES

Reward schemes are the schemes which entitle the exporters to duty credit scrips subject to various conditions. These scrips can be used for payment of customs duties on import of inputs/goods, payment of excise duties on domestic procurement of inputs/goods including capital goods, payment of service tax on procurement of services.

These scrips are transferable, i.e. they can be sold in market, if the holder of duty credit scrip does not intend to import goods against the scrips. Goods imported under the scrip are also freely transferable.

Following are two schemes for exports of merchandise and services:

(i) Merchandise Exports from India Scheme (MEIS)

(ii) Service Exports from India Scheme (SEIS)

1. MERCHANDISE EXPORTS FROM INDIA SCHEME (MEIS)

The objective of MEIS scheme is to compensate infrastructural inefficiencies and associated costs involved in export of goods/products, which are produced/manufactured in India, especially goods having high export intensity, employment potential and thereby enhancing India's export competitiveness.

(i) Reward under the scheme: Under MEIS, exports of notified goods/products to notified markets shall be eligible for reward at the specified rate(s). Unless otherwise specified, the basis of calculation of reward would be:

(i) on realised FOB value of exports in free foreign exchange,

or

(ii) on FOB value of exports as given in the Shipping Bills in free foreign exchange,

whichever is less.

(ii) Ineligible categories under MEIS: Some exports categories/sectors ineligible for Duty Credit Scrip entitlement under MEIS are listed below:

(1) EOUs / EHTPs / BTPs/ STPs who are availing direct tax benefits / exemption

(2) Supplies made from DTA units to SEZ units

(3) Exports through trans-shipment, i.e., exports that are originating in third country but trans-shipped through India

(4) Deemed Exports

(5) SEZ/EOU/EHTP/BPT/FTWZ products exported through DTA units

(6) Export products which are subject to Minimum export price or export duty

(7) Ores and concentrates of all types and in all formations

(8) Cereals of all types

(9) Sugar of all types and all forms

(10) Crude / petroleum oil and crude / primary and base products of all types and all formulations

(11) Export of milk and milk products and meat and meat products

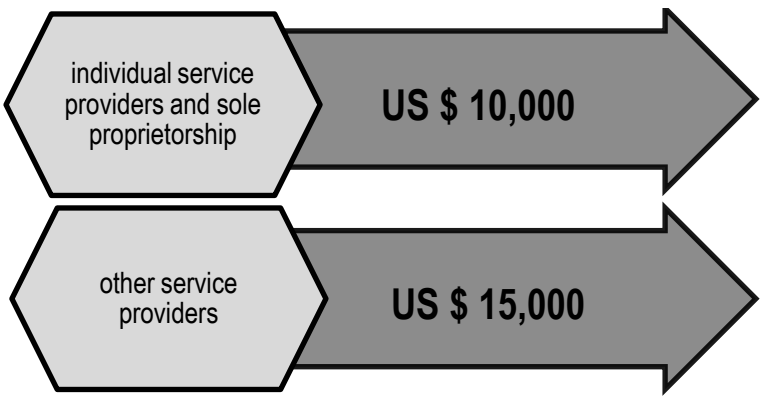
(12) Service Export

(iii) Export of goods through courier/foreign post offices using e-commerce: Exports of handicraft items, handloom products, books/periodicals, leather footwear, toys and tailor made fashion garments through courier or foreign post office using e-commerce of FOB value upto ₹ 25,000 per consignment shall be entitled for rewards under MEIS.

2. SERVICE EXPORTS FROM INDIA SCHEME (SEIS)

The objective of SEIS scheme is to encourage export of notified services from India. The scheme applies to export of services made on or after 01.04.2015.

(i) Eligible service providers: A service provider (with active IEC at the time of rendering services) located in India, providing notified services rendered in the specified manner* shall be eligible for reward at the notified rate(s) on net foreign exchange earned provided the minimum net free foreign exchange earnings of such service provider in preceding financial year is:



***Specified manner** is supply of a 'service' from India to any other country; (Mode 1-Cross border trade) and supply of a 'service' from India to service consumer(s) of any other country in India; (Mode 2-Consumption abroad).

Payment in Indian Rupees for service charges earned on specified services, shall be treated as receipt in deemed foreign exchange as per guidelines of Reserve Bank of India. The list of such services and the notified rates of rewards are as under:

Sl No	SECTORS	Admissible rate
1.	**BUSINESS SERVICES**	
A.	Professional services Legal services, Accounting, auditing and bookkeeping services, Taxation services, Architectural services, Engineering services, Integrated engineering services, Urban planning and landscape architectural services,	5%

	Medical and dental services, Veterinary services, Services provided by midwives, nurses, physiotherapists and paramedical personnel	
B.	Research and development services R&D services on natural sciences, R&D services on social sciences and humanities, Interdisciplinary R&D services	5%
C.	Rental/Leasing services without operators Relating to ships, Relating to aircraft, Relating to other transport equipment, Relating to other machinery and equipment	5%
D.	Other business services Advertising services, Market research and public opinion polling services Management consulting service, Services related to management consulting, Technical testing and analysis services, Services incidental to agricultural, hunting and forestry, Services incidental to fishing, Services incidental to mining, Services incidental to manufacturing, Services incidental to energy distribution, Placement and supply services of personnel, Investigation and security, Related scientific and technical consulting services, Maintenance and repair of equipment (not including maritime vessels, aircraft or other transport equipment), Building- cleaning services, Photographic services, Packaging services, Printing, publishing and Convention services	3%
2.	**COMMUNICATION SERVICES** Audiovisual services Motion picture and video tape production and distribution service, Motion picture projection service, Radio and television services, Radio and television transmission services, Sound recording.	5%
3.	**CONSTRUCTION AND RELATED ENGINEERING SERVICES** General Construction work for building, General Construction work for Civil Engineering, Installation and assembly work, Building completion and finishing work	5%
4.	**EDUCATIONAL SERVICES** (Please refer Note 1) Primary education services, Secondary education services, Higher education services, Adult education	5%

5.	**ENVIRONMENTAL SERVICES** Sewage services, Refuse disposal services, Sanitation and similar services	5%
6.	**HEALTH-RELATED AND SOCIAL SERVICES** Hospital services	5%
7.	**TOURISM AND TRAVEL-RELATED SERVICES**	
A.	Hotels and Restaurants (including catering)	
	a. Hotel	3%
	b. Restaurants (including catering)	3%
B.	Travel agencies and tour operators services	5%
C.	Tourist guides services	5%
8.	**RECREATIONAL, CULTURAL AND SPORTING SERVICES** (other than audiovisual services) Entertainment services (including theatre, live bands and circus services), News agency services, Libraries, archives, museums and other cultural services, Sporting and other recreational services	5%
9.	**TRANSPORT SERVICES** (Please refer Note 2)	
A.	Maritime Transport Services Passenger transportation*, Freight transportation*, Rental of vessels with crew*, Maintenance and repair of vessels, Pushing and towing services, Supporting services for maritime transport	5%
B.	Air transport services Rental of aircraft with crew, Maintenance and repair of aircraft, Airport Operations and ground handling	5%
C.	Road Transport Services Passenger transportation, Freight transportation, Rental of Commercial vehicles with operator, Maintenance and repair of road transport equipment, Supporting services for road transport services	5%
D.	Services Auxiliary To All Modes of Transport. Cargo-handling services, Storage and warehouse services, Freight transport agency services	5%

Notes:

(1) Under education services, SEIS shall not be available on Capitation fee.

(2) *Operations from India by Indian Flag Carriers only is allowed under Maritime transport services.

1. **Net Foreign exchange earnings**

   = Gross Earnings of Foreign Exchange **Minus** Total expenses/ payment/ remittances of Foreign Exchange by the IEC holder, relating to service sector in the financial year.

2. **'Services'** include all tradable services covered under General Agreement on Trade in Services (GATS) and earning foreign exchange.

3. **'Service Provider'** means a person providing:

   (i) Supply of a 'service' from India to any other country; *(Mode1- Cross border trade)*

   (ii) Supply of a 'service' from India to service consumer(s) of any other country; *(Mode 2- Consumption abroad)*

   (iii) Supply of a 'service' from India through commercial presence in any other country. *(Mode 3 – Commercial Presence)*

   (iv) Supply of a 'service' from India through the presence of natural persons in any other country *(Mode 4- Presence of natural persons)*.

(ii) Ineligible categories under SEIS:

(A) Foreign exchange remittances other than those earned for rendering of notified services would not be counted for entitlement. Thus, other sources of foreign exchange earnings such as equity or debt participation, donations, receipts of repayment of loans etc. and any other inflow of foreign exchange, unrelated to rendering of service, would be ineligible.

(B) Following shall not be taken into account for calculation of entitlement under the scheme:

(1) Foreign Exchange remittances

Related to Financial Services Sector:

- Raising of all types of foreign currency Loans
- Export proceeds realization of clients
- Issuance of Foreign Equity through ADRs/ GDRs or other similar instruments
- Issuance of foreign currency Bonds
- Sale of securities and other financial instruments
- Other receivables not connected with services rendered by financial institutions.

Earned through contract/ regular employment abroad (e.g. labour remittances)

(2) Payments for services received from EEFC Account

(3)	Foreign exchange turnover by Healthcare Institutions like equity participation, donations etc.
(4)	Foreign exchange turnover by Educational Institutions like equity participation, donations etc.
(5)	Export turnover relating to services of units operating under SEZ/ EOU/ EHTP/ STPI/ BTP Schemes or supplies of services made to such units
(6)	Clubbing of turnover of services rendered by SEZ/EOU/ EHTP/ STPI/ BTP units with turnover of DTA Service Providers
(7)	Exports of Goods
(8)	Foreign Exchange earnings for services provided by Airlines, Shipping lines service providers plying from any foreign country X to any foreign country Y routes not touching India at all
(9)	Service providers in Telecom Sector

Common Provisions for Exports from India Schemes (MEIS and SEIS)

(i) CENVAT/ Drawback:

- Additional Customs duty/excise duty/Service Tax paid in cash or through debit under Duty Credit scrip shall be adjusted as CENVAT Credit or Duty Drawback as per DoR rules or notifications.
- Basic Custom duty paid in cash or through debit under Duty Credit scrip shall be adjusted for Duty Drawback as per DoR rules or notifications.

Duty credit scrip shall be permitted to be utilized for payment of duty in case of import of capital goods under lease financing.

(ii) Transfer of export performance: Transfer of export performance from one IEC holder to another IEC holder shall not be permitted. Thus, a shipping bill containing name of applicant shall be counted in export performance / turnover of applicant only if export proceeds from overseas are realized in applicant's bank account and this shall be evidenced from e - BRC / FIRC.

However, MEIS rewards can be claimed either by the supporting manufacturer (along with disclaimer from the company / firm who has realized the foreign exchange directly from overseas) or by the company/ firm who has realized the foreign exchange directly from overseas.

(iii) Incentives of MEIS & SEIS are available to units located in SEZs also.

3. STATUS HOLDER

Status Holders are business leaders who have excelled in international trade and have successfully contributed to country's foreign trade. All exporters of goods, services and technology having an import-export code (IEC) number shall be eligible for recognition as a status holder. Status recognition depends upon export performance**.

An applicant shall be categorized as status holder upon achieving export performance during current and previous two financial years, as indicated below:

Status category	Export Performance [FOB/ FOR (as converted) Value (in US $ million)]
One Star Export House	3
Two Star Export House	25
Three Star Export House	100
Four Star Export House	500
Five Star Export House	2,000

****Points which merit consideration while computing export performance for grant of status:**

(a) Export performance will be counted on the basis of FOB value of export earnings in free foreign exchange.

(b) For deemed export, FOR value of exports in Indian Rupees shall be converted in US$ at the exchange rate notified by CBEC, as applicable on 1st April of each Financial Year.

(c) For granting status, export performance is necessary in at least 2 out of 3 years.

(d) For calculating export performance for grant of One Star Export House Status category, exports by IEC holders under the following categories shall be granted double weightage:

  (i) Micro, Small & Medium Enterprises (MSME)

  (ii) Manufacturing units having ISO/BIS

  (iii) Units located in North Eastern States and Jammu & Kashmir

  (iv) Units located in Agri Export Zones.

(e) Export performance of one IEC holder shall not be permitted to be transferred to another IEC holder. Hence, calculation of exports performance based on disclaimer shall not be allowed.

(f) Exports made on re-export basis shall not be counted for recognition.

(g) Export of items under authorization, including SCOMET items, would be included for calculation of export performance.

Privileges of Status Holders: Status holders are granted certain benefits like:

(a) Authorisation and custom clearances for both imports and exports on self-declaration basis.

(b) Fixation of Input Output Norms (SION) on priority i.e. within 60 days.

(c) Exemption from compulsory negotiation of documents through banks. The remittance receipts, however, would continue to be received through banking channels.

(d) Exemption from furnishing of Bank Guarantee in Schemes under FTP.

(e) Two Star Export Houses and above are permitted to establish export warehouses.

(f) Three Star and above Export House shall be entitled to get benefit of Accredited Clients Programme (ACP) as per the guidelines of CBEC.

(g) Status holders shall be entitled to export freely exportable items on free of cost basis for export promotion subject to an annual limit of ₹ 10 lakh or 2% of average annual export realization during preceding 3 licensing years, whichever is higher.

(3) EXPORT PROMOTION CAPITAL GOODS SCHEME (EPCG)

Export Promotion Capital Goods Scheme (EPCG) permits exporters to import capital goods for pre-production, production and post-production at zero customs duty or procure them indigenously without paying duty in the prescribed manner. In return, exporter is under an obligation to fulfill the export obligation.

Import under EPCG scheme shall be subject to an export obligation equivalent to 6 times of duty saved on capital goods to be fulfilled in 6 years reckoned from the date of issue of authorization. Authorisation shall be valid for 18 months from the date of issue of Authorisation. Import of capital goods shall be subject to 'Actual User' condition till export obligation is completed. After export obligation is completed, capital goods can be sold or transferred.

(i) Eligible exporters: Following are eligible for EPCG scheme:

- Manufacturer exporters with or without supporting manufacturer(s),
- Merchant exporters tied to supporting manufacturer(s), and
- Service providers including service providers designated as Common Service Provider (CSP) subject to prescribed conditions.

(ii) Eligible and ineligible capital goods:

<table>
<tr><th>Eligible capital goods include</th><th>Ineligible capital goods include</th></tr>
<tr><td>Capital Goods including capital goods in CKD/SKD condition</td><td>Second hand capital goods</td></tr>
<tr><td>Computer software systems</td><td rowspan="3">Any capital goods (including captive plants and Power Generator Sets of any kind) for:
• Export of electrical energy (power)
• Supply of electrical energy (power) under deemed exports
• Use of power (energy) in their own unit,</td></tr>
<tr><td>Spares, moulds, dies, jigs, fixtures, tools & refractories for initial lining and spare refractories</td></tr>
<tr><td>Catalysts for initial charge plus one subsequent charge</td></tr>
</table>

Capital goods for Project Imports notified by CBEC	and • Supply/export of electricity transmission services

(iii) Export Obligation: Export obligation means obligation to export product(s) covered by Authorisation/ permission in terms of quantity or value or both, as may be prescribed/specified by Regional or competent authority. Export obligation consists of average export obligation and specific export obligation.

Specific export obligation (Specific EO) under EPCG scheme is equivalent to 6 times of duty saved on capital goods imported under EPCG scheme, to be fulfilled in 6 years reckoned from Authorization issue-date. Specific EO is over and above the Average EO.

Note: In case countervailing duty (CVD) is paid in cash on imports under EPCG, incidence of CVD would not be taken for computation of net duty saved, provided CENVAT is not availed.

Average export obligation (Average EO) under EPCG scheme is the average level of exports made by the applicant in the preceding 3 licensing years for the same and similar products. It has to be achieved within the overall EO period (including extended period unless otherwise specified).

Conditions applicable to the fulfilment of the Export Obligation (EO):

(a) EO shall be fulfilled by the authorisation holder through export of goods which are manufactured by him or his supporting manufacturer / services rendered by him, for which the EPCG authorisation has been granted.

(b) In case of indigeneous sourcing of capital goods, specific EO shall be 25% less than the EO mentioned above, i.e. EO will be 4.5 times (75% of 6 times) of duty saved on such goods procured.

(c) Shipments under Advance Authorisation, DFIA, Drawback scheme, or reward schemes; would also be counted for fulfilment of EO under EPCG Scheme.

(d) EO can also be fulfilled by the supply of Information Technology Agreement (ITA-1) items to DTA, provided realization is in free foreign exchange.

(e) Both physical exports as well as specified deemed exports shall also be counted towards fulfilment of export obligation.

(iv) Incentives for early fulfillment of export obligation

In cases where Authorization holder has fulfilled 75% or more of specific export obligation and 100% of Average Export Obligation till date, if any, in half or less than half the original export obligation period specified, remaining export obligation shall be condoned and the Authorization redeemed.

(v) Post Export EPCG Duty Credit Scrip(s)

Under this scheme, capital goods are imported on full payment of applicable duties in cash. Later, basic customs duty paid on Capital Goods is remitted in the form of freely transferable duty credit scrip(s) [similar to the Reward schemes discussed earlier].

Salient features of the schemes are as follows:-

- Specific EO shall be 85% of the applicable specific EO stipulated under EPCG scheme. Average EO remains unchanged.
- Duty remission shall be in proportion to the EO fulfilled.
- These Duty Credit Scrip(s) can be utilized in the similar manner as the scrips issued under reward schemes can be utilised.

(4) EOU, EHTP, STP & BTP SCHEMES

Units under Export Oriented Unit (EOU) Scheme, Electronics Hardware Technology Park (EHTP) Scheme, Software Technology Park (STP) Scheme or Bio-Technology Park (BTP) Scheme export their entire production of goods and services (except permissible sales in DTA). They can import inputs and capital goods without payment of customs duty.

STP/EHTP/BTP schemes are similar to EOU schemes and provisions are more/ less identical. EOU scheme is administered by Ministry of Commerce and Industry, while STP/EHTP/BTP schemes are administered by their respective administrative ministries.

Software Technology Park (STP) is set up for development of software exports. Electronic Hardware Technology Park (EHTP) are for export of electronics hardware and software. STP/EHTP Scheme is administered by Ministry of Information Technology. Bio Technology Park (BTP) is established on the recommendation of Department of Biotechnology.

(I) ELIGIBILITY

- ❖ Such units may be set up for manufacture of goods, including repair, re-making, reconditioning, re-engineering, rendering of services, development of software, agriculture.
- ❖ Trading units are not covered under these schemes.
- ❖ Only projects having a minimum investment of ₹ 1 crore in plant & machinery shall be considered for establishment as EOUs. However, this shall not apply to units in EHTP/ STP/ BTP, Handicrafts/ Agriculture/ Floriculture/ Aquaculture/ Animal Husbandry/ Information Technology Services, Brass Hardware and Handmade jewellery sectors. Board of Approvals may also allow establishment of EOUs with a lower investment criteria.

(II) PROCEDURE FOR SETTING UP NEW EOU, EHTP, STP AND BTP

(a) Approval for setting up of units under EOU scheme shall be granted by the Units Approval Committee within 15 days as per prescribed criteria. In other cases, approval may be granted by Board of Approval set up for this purpose.

(b) On approval, concerned authority will issue a Letter of Permission (LoP)/ Letter of Intent (LoI) which will have initial validity of 2 years (extendable by 2 years and further extension, if necessary, by BoA), by which time unit should have commenced production.

(III) NET FOREIGN EXCHANGE EARNINGS

- EOU/ EHTP/ STP/ BTP unit must be a positive net foreign exchange earner. However, a higher value addition is specified for some sectors.
- **How to compute NFE earnings?:** NFE Earnings shall be calculated cumulatively in blocks of 5 years, starting from commencement of production.

In case unit is not able to achieve NFE due to:

(i) prohibition/ restriction imposed on export of any product, 5 years block period may be extended suitably by BoA.

(ii) adverse market condition or any grounds of genuine hardship having adverse impact on functioning of the unit, 5 year block is extendable upto 1 year.

Who monitors NFE?: Performance of EOU/ EHTP/ STP/ BTP units shall be monitored by Units Approval Committee as per prescribed guidelines.

Which supplies to DTA can be counted for positive NFE?: Following supplies effected from EOU/ EHTP/ STP/ BTP units to DTA (Domestic Tariff Area) will be counted for fulfillment of positive NFE:

(a) Supplies in DTA to holders of Advance Authorisation/ Advance Authorisation for annual requirement/ DFIA under duty exemption/ remission scheme/ EPCG scheme subject to certain exceptions.

(b) Supplies affected in DTA against foreign exchange remittance received from overseas.

(c) Supplies to other EOU/ EHTP/ STP/ BTP/ SEZ units, provided that such goods are permissible for procurement in terms of relevant provisions of FTP.

(d) Supplies made to bonded warehouses set up under FTP and/ or under section 65 of Customs Act and free trade and warehousing zones, where payment is received in foreign exchange.

(e) Supplies of goods and services to such organizations which are entitled for duty free import of such items in terms of general exemption notification issued by MoF.

(f) Supplies of Information Technology Agreement (ITA-1) items and notified zero duty telecom/ electronics items.

(g) Supplies of items like tags, labels, printed bags, stickers, belts, buttons or hangers to DTA unit for export.

(IV) ENTITLEMENTS TO UNITS UNDER EOU, EHTP, STP AND BTP SCHEMES

(a) Entitlements for supplies from DTA

- Supplies from DTA to EOU/ EHTP/ STP/ BTP units will be regarded as "deemed exports" and DTA supplier shall be eligible for relevant entitlements for deemed

exports, besides discharge of export obligation, if any, on the supplier.

- ❖ Notwithstanding the above, EOU/ EHTP/ STP/ BTP units shall, on production of a suitable disclaimer from DTA supplier, be eligible for obtaining entitlements specified under the provisions relating to deemed exports in FTP. For claiming deemed export duty drawback, they shall get brand rates fixed by DC wherever All Industry Rates of Drawback are not available.

In addition, EOU / EHTP / STP / BTP units shall be entitled to following:-

- ❖ Reimbursement of Central Sales Tax (CST) on goods manufactured in India. Interest @ 6% p.a. will be payable on delay refund of CST, if the case is not settled within 30 days of receipt of complete application.
- ❖ Exemption from payment of Central Excise Duty on goods procured from DTA on goods manufactured in India.
- ❖ Reimbursement of duty paid on fuel procured from domestic oil companies/ Depots of domestic oil Public Sector Undertakings as per drawback rate notified by DGFT from time to time. Reimbursement of additional duty of excise levied on fuel under the Finance Acts would also be admissible.
- ❖ CENVAT credit on service tax paid.

(b) Other Entitlements

- ❖ Exemption from industrial licensing for manufacture of items reserved for SSI sector.
- ❖ Export proceeds will be realized within 9 months.
- ❖ Units will be allowed to retain 100% of its export earnings in the EEFC account.
- ❖ Unit will not be required to furnish bank guarantee at the time of import or going for job work in DTA, subject to fulfillment of required conditions.
- ❖ 100% FDI investment permitted through automatic route similar to SEZ units.
- ❖ Units shall pay duty on the goods produced or manufactured and cleared into DTA on monthly basis in the manner prescribed in the Central Excise Rules.

(V) EXPORT AND IMPORT OF GOODS

Export : Following exports are permitted:

- ✓ all kinds of goods and services except items that are prohibited in ITC(HS),
- ✓ Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET) subject to fulfillment of the conditions indicated in ITC (HS).

Import : Following imports are permitted:

- * Export promotion material upto a maximum value limit of 1.5% of FOB value of previous years exports.
- * All types of goods, including capital goods, required for its activities, from DTA/ bonded warehouses in DTA/ International exhibition held in India, without payment

of duty subject to 'Actual User' condition, provided such goods are not prohibited items of import.

- Goods including capital goods (on a self certification basis) required for approved activity, free of cost or on loan/ lease from clients, subject to 'Actual User' condition.
- Certain specified goods from DTA, without payment of duty, for creating a central facility.
- Second hand capital goods, without any age limit, duty free.

Procurement and export of spares/ components, upto 5% of FOB value of exports, may be allowed to same consignee/ buyer of the export article, subject to the condition that it shall not count for NFE and direct tax benefits.

(VI) LEASING OF CAPITAL GOODS

An EOU/ EHTP/ STP/ BTP unit may:

- ✓ source capital goods from a domestic/ foreign leasing company without payment of excise/ customs duty, on the basis of a firm contract between parties.
- ✓ sell capital goods and lease back the same from a Non Banking Financial Company (NBFC) subject to fulfillment of specified conditions.

(VII) INTER UNIT TRANSFER

- ❖ Transfer of manufactured goods from one EOU/ EHTP/ STP/ BTP unit to another EOU/ EHTP/ STP/ BTP unit is allowed with prior intimation to concerned DC and Customs authorities, following procedure of in-bond movement of goods.
- ❖ Transfer of manufactured goods shall also be allowed from EOU/ EHTP/ STP/ BTP unit to a SEZ developer or unit following procedure prescribed in SEZ Rules, 2006.
- ❖ Capital goods may be transferred or given on loan to other EOU/ EHTP/ STP/ BTP/ SEZ units, with prior intimation to concerned DC and Customs authorities.

Note: Goods supplied by one unit of EOU/ EHTP/ STP/ BTP to another unit shall be treated as imported goods for second unit for payment of duty, on DTA sale by second unit.

(VIII) SALE OF UNUTILIZED MATERIAL

- ❖ In case an EOU/ EHTP/ STP/ BTP unit is unable to utilize goods (including capital goods) and services, imported or procured from DTA, it may be
  - ✓ transferred to another EOU/ EHTP/ STP/ BTP/ SEZ unit; or
  - ✓ disposed off in DTA with approval of Customs authorities on payment of applicable duties and submission of import authorization; or
  - ✓ exported.

  Such transfer from EOU/ EHTP/ STP/ BTP unit to another such unit would be treated as import for receiving unit.
- ❖ In case of capital goods, benefit of depreciation, as applicable, will be available in

case of disposal in DTA only when the unit has achieved positive NFE taking into consideration the depreciation allowed.

- ❖ No duty shall be payable in case capital goods, raw material, consumables, spares, goods manufactured, processed or packaged, and scrap/ waste/ remnants/ rejects are destroyed within unit after intimation to Customs authorities or destroyed outside unit with permission of Customs authorities.
- ❖ Disposal of used packing material will be allowed on payment of duty on transaction value.

(IX) DTA SALE OF FINISHED PRODUCTS/ REJECTS/ WASTE/ SCRAP/ REMNANTS AND BY-PRODUCTS

Entire production of EOU/ EHTP/ STP/ BTP units must be exported. However, following DTA sales are permissible:

(1) Sale of goods in DTA: Units* may sell goods in DTA

- ✓ **upto 50% of FOB value of exports** (including sales made to SEZ unit from Foreign Exchange Account of such unit),
- ✓ subject to fulfilment of positive NFE,
- ✓ on payment of concessional duties.

*other than gems and jewellery units

However, sale at concessional duty is not permitted:

(i) in respect of motor cars, alcoholic liquors, books, tea (except instant tea), pepper & pepper products, marble and other notified items or

(ii) to units engaged in activities of packaging/ labeling/ segregation/ refrigeration/ compacting/ micronisation/ pulverization/ granulation/ conversion of monohydrate form of chemical to anhydrous form or vice-versa.

An amount equal to Anti Dumping duty under section 9A of the Customs Tariff Act, 1975 leviable at the time of import, shall be payable on the goods used for the purpose of manufacture or processing of the goods cleared into DTA from the unit.

In case of units manufacturing and exporting more than one product, sale of any of these products into DTA, upto 90% of FOB value of export of the specific products is permitted, provided total DTA sales does not exceed the overall entitlement of 50% of FOB value of exports for the unit.

(2) Services provided in DTA: For services, sale in DTA shall also be permissible up to 50% of FOB value of exports and/ or 50% of foreign exchange earned, where payment of such services is received in foreign exchange.

(3) Sale of rejects in DTA: Rejects within an overall limit of 50% may be sold in DTA on payment of applicable duties (concessional or otherwise), on prior intimation to Customs authorities. Such sales shall be counted against DTA sale entitlement.

Sale of rejects upto 5% of FOB value of exports shall not be subject to achievement of NFE.

(4) Sale of scrap/ waste/ remnants, arising out of production, in DTA: Scrap/ waste/ remnants arising out of production process or in connection therewith may be sold in DTA, as per SION notified under Duty Exemption Scheme, on payment of concessional duties as applicable, within overall ceiling of 50% of FOB value of exports. Such sales of scrap/ waste/ remnants shall not be subject to achievement of positive NFE. Sale of waste/scraps/remnants by units not entitled to DTA sale or sales beyond DTA sales entitlement, shall be on payment of full duties. Scrap/waste/remnants may also be exported.

In case scrap/ waste/ remnants are destroyed with permission of Customs authorities, no duties/ taxes payable on same.

(5) Sale of by-products in DTA: By-products may also be sold in DTA subject to achievement of positive NFE, on payment of applicable duties, within the overall entitlement of 50% of FOB value of exports. Sale of by-products by units not entitled to DTA sales, or beyond entitlements shall also be permissible on payment of full duties.

(6) Procurement of spares/components, up to 2% of the value of manufactured articles, cleared into DTA, during the preceding year, may be allowed for supply to the same consignee / buyer for the purpose of after-sale-service.

Notes:

1. In case of DTA sale of goods manufactured by EOU/ EHTP/ STP/ BTP, where basic duty and CVD is nil, such goods may be considered as non-excisable for payment of duty.
2. In case of new EOUs, advance DTA sale will be allowed not exceeding 50% of its estimated exports for first year (2 years for pharmaceutical units).

(X) EXPORT THROUGH OTHER EXPORTERS

An EOU/ EHTP/ STP/ BTP unit may export goods manufactured/ software developed by it through another exporter or any other EOU/ EHTP/ STP/ SEZ unit subject to specified conditions

(XI) EXIT FROM EOU SCHEME

With approval of DC, an EOU may opt out of scheme. Such exit shall be subject to payment of excise and customs duties and industrial policy in force. If unit has not achieved obligations, it shall also be liable to penalty at the time of exit.

(XII) CONVERSION

Existing DTA units may also apply for conversion into an EOU/ EHTP/ STP/ BTP unit. Existing EHTP/ STP units may also apply for conversion/ merger to EOU unit and vice-versa. In such cases, units will remain in bond and avail exemptions in duties and taxes as applicable.

(5) DEEMED EXPORTS

Deemed Exports refer to those transactions in which goods manufactured in India are supplied to specified projects or to specific categories of consumers. In deemed exports, goods supplied do not leave the country and payment for such supplies is received either in Indian rupees or in free foreign exchange by the recipient of the goods.

The objective of deemed exports is to ensure that the domestic suppliers are not in disadvantageous position *vis-à-vis* foreign suppliers in terms of the fiscal concessions. The underlying theory is that foreign exchange saved must be treated at par with foreign exchange earned by placing Indian manufacturers at par with foreign suppliers. Deemed exports broadly cover three areas.

a. Supplies to domestic entities who can import their requirements duty free or at reduced rates of duty.

b. Supplies to projects/ purposes that involve international competitive bidding.

c. Supplies to infrastructure projects of national importance.

(I) CATEGORIES OF SUPPLIES CONSIDERED AS 'DEEMED EXPORT'

Supply by manufacturer	Supply by main/sub-contractors(s)
Supply of goods against Advance Authorisation/Advance Authorisation for Annual Requirement/ DFIA	Supply of goods to projects or turnkey contracts financed by multilateral or bilateral agencies/Funds notified by Department of Economic Affairs (DEA), under International Competitive Bidding.
Supply of goods to units located in EOU/ STP/BTP/EHTP	Supply of goods to any project where import is permitted at zero customs duty as per customs *Notification No. 12/2012-Cus dated 17.03.2012* and supply is made against International Competitive Bidding.
Supply of capital goods against EPCG authorisation	Supply of goods to mega power projects against International Competitive Bidding (even if customs duty on imports made by such project is not zero). The ICB procedures should be followed. Supplier is eligible for benefits as specified. International Competitive Bidding (ICB) is not mandatory for mega power projects if requisite quantum of power has been tied up through tariff based competitive bidding or if project has been awarded through tariff based competitive bidding.
Supply of marine freight containers by 100% EOU provided said containers are	Supply to goods to UN or international organisations for their official use or supplied

exported within 6 months	to projects financed by them.
	Supply of goods to nuclear projects through competitive bidding (need not be international competitive bidding).

(II) BENEFITS FOR DEEMED EXPORTS

Deemed exports shall be eligible for any / all of following benefits in respect of manufacture and supply of goods, qualifying as deemed exports, subject to specified terms and conditions:

a. Advance Authorisation/ Advance Authorisation for Annual requirement/ DFIA

b. Deemed Export Drawback

c. Refund of terminal excise duty if exemption is not available.

(III) ELIGIBILITY FOR REFUND OF TERMINAL EXCISE DUTY/ DEEMED EXPORT DRAWBACK

Refund of Terminal Excise duty or Central Excise duty paid on inputs/ components will be available only when CENVAT credit/ rebate of the same have not been availed by the recipient of such goods. Similarly, supplies will be eligible for deemed export drawback on Central Excise paid on inputs and service tax paid on input services, provided CENVAT credit facility/ rebate has not been availed by the applicant. However, in such cases, basic customs duty paid can be claimed as brand rate of duty drawback.

(IV) COMMON CONDITIONS FOR DEEMED EXPORT BENEFITS

(i) Supplies shall be made directly to entities listed in the point (I) above. Third party supply shall not be eligible for benefits/exemption.

(ii) In all cases, supplies shall be made directly to the designated Projects/Agencies/Units/ Advance Authorisation/ EPCG Authorisation holder. Sub-contractors may, however, make supplies to main contractor instead of supplying directly to designated Projects/ Agencies. Payments in such cases shall be made to sub-contractor by main-contractor and not by project Authority.

(iii) Supply of domestically manufactured goods by an Indian Sub-contractor to any Indian or foreign main contractor, directly at the designated project's/ Agency's site, shall also be eligible for deemed export benefit provided name of sub-contractor is indicated either originally or subsequently (but before the date of supply of such goods) in the main contract. In such cases payment shall be made directly to sub-contractor by the Project Authority.

16.4 Special Economic Zone (SEZ)

(a) Introduction

A Special Economic Zone (SEZ) is a geographically bound zone where the economic laws in matters related to export and import are more broadminded and liberal as compared to other parts of the country. **SEZ is considered to be a place outside India**

for all tax purposes. It is like a separate island within the territory of India and is deemed to be outside the customs territory of India. SEZs are projected as duty free area for the purpose of trade, operations, duty, and tariffs.

SEZ units are self-contained and integrated having their own infrastructure and support services. Within SEZs, a unit may be set-up for the manufacture of goods and other activities including processing, assembling, trading, repairing, reconditioning, making of gold/ silver, platinum jewellery etc.

Goods supplied to SEZs from DTA are treated as exports from India and goods supplied from the SEZ to the DTA are treated as imports into India.

The provisions relating to SEZ are contained in Special Economic Zone Act, 2005 and SEZ Rules, 2006.

State Governments are expected to play a very active role in the establishment of SEZ unit. Any proposal for setting up of SEZ unit in the Private/ Joint/ State Sector is routed through the concerned State government who in turn forwards the same to the Department of Commerce with its recommendations for consideration.

The main objectives of the SEZ Act are:

(a) Export of goods and services without taxes

(b) Generation of additional economic activity

(c) Promotion of exports of goods and services

(d) Promotion of investment from domestic and foreign sources

(e) Creation of employment opportunities

(f) Development of infrastructure facilities

(g) Providing exemption from duties and taxes on procurement

(h) Single window clearance: It is expected that this will trigger a large flow of foreign and domestic investment in SEZs, in infrastructure and productive capacity, leading to generation of additional economic activity and creation of employment opportunities.

The SEZ Rules provide for:

(a) Simplified procedures for development, operation, and maintenance of the Special Economic Zones and for setting up units and conducting business in SEZs.

(b) Single window clearance for setting up of an SEZ

(c) Single window clearance for setting up a unit in a Special Economic Zone

(d) Single Window clearance on matters relating to Central as well as State Governments

(e) Simplified compliance procedures

(f) Maintenance of documents with self-certification

(g) Simplified compliance procedures and documentation with an emphasis on self certification

The incentives and facilities offered to the units in SEZs for attracting investments into the SEZs, including foreign investment are:

(a) Duty free import/ domestic procurement of goods for development, operation and maintenance of SEZ units.

(b) Exemption from Central Sales Tax.

(c) Exemption from Service Tax.

(d) Single window clearance for Central and State level approvals.

(e) Exemption from State sales tax and other levies as extended by the respective State Governments.

16.5 Penalties

In case any exporter or importer in the country violates any provision of the Foreign Trade Policy or for that matter any other law in force, like Central Excise or Customs or Foreign Exchange, his IEC number can be cancelled by the office of DGFT and thereupon that exporter or importer would not be able to transact any business in export or import. The premises where any violation of the provisions of FTP has taken place or is expected to take place can be searched and the suspicious material seized.

Violations would cover situations when import or export has been made by unauthorized persons who are not legally allowed to carry out import or export or when any person carries out or admits to carry out any import or export in contravention of the basic FTP.

16.6 Glossary (Acronyms)

Acronym	Explanation
AA	Advance Authorisation
ACC	Assistant Commissioner of Customs
ANF	Aayaat Niryaat Form
BG	Bank Guarantee
BIFR	Board of Industrial and Financial Reconstruction
BoA	Board of Approval
BRC	Bank Realisation Certificate
BTP	Biotechnology Park
CBEC	Central Board of Excise and Customs
CCP	Customs Clearance Permit
CEA	Central Excise Authority
CEC	Chartered Engineer Certificate
CIF	Cost, Insurance & Freight

CVD	Countervailing Duty
DC	Development Commissioner
DFIA	Duty Free Import Authorisation
DGCI&S	Director General, Commercial Intelligence & Statistics.
DGFT	Director General of Foreign Trade
DoR	Department of Revenue
DTA	Domestic Tariff Area
EDI	Electronic Data Interchange
EEFC	Exchange Earners' Foreign Currency
EFC	Exim Facilitation Committee
EFT	Electronic Fund Transfer
EH	Export House
EHTP	Electronic Hardware Technology Park
EIC	Export Inspection Council
EO	Export Obligation
EOP	Export Obligation Period
EOU	Export Oriented Unit
EPC	Export Promotion Council
EPCG	Export Promotion Capital Goods
FDI	Foreign Direct Investment
FIEO	Federation of Indian Export Organisation
FOB	Free On Board
FT (D&R) Act	Foreign Trade (Development & Regulation) Act, 1992
FTP	Foreign Trade Policy
GATS	General Agreement on Trade in Services
ICD	Inland Container Depot
IEC	Importer Exporter Code
ISO	International Standards Organisation
ITC(HS)	Indian Trade Classification (Harmonised System)

Classification for Export & Import Items

ITPO	India Trade Promotion Organisation
LoC	Line of Credit
LoI	Letter of Intent
LoP	Letter of Permit

LUT	Legal Undertaking
MEA	Ministry of External Affairs
MoD	Ministry of Defence
MoF	Ministry of Finance
NC	Norms Committee
NFE	Net Foreign Exchange
NOC	No Objection Certificate
PSU	Public Sector Undertaking
R&D	Research and Development
RA	Regional Authority
RBI	Reserve Bank of India
RCMC	Registration-cum-Membership Certificate
S/B	Shipping Bill
SEZ	Special Economic Zone
SION	Standard Input Output Norms
SSI	Small Scale Industry
STE	State Trading Enterprise
STP	Software Technology Park
TEE	Towns of Export Excellence
VA	Value Addition

Part II : Judicial Update – Indirect Tax Laws

Significant Recent Legal Decisions

"Select Cases in Direct and Indirect Tax Laws – An Essential Reading for the Final Course" is a compilation of the significant decisions of Supreme Court, High Court and Larger Bench of Tribunal. October, 2014 edition of the said publication is relevant for November, 2015 examination. Students may note that in addition to the cases reported in the said publication, following significant recent legal decisions are also relevant for November, 2015 examination:-

SECTION A: CENTRAL EXCISE

Basic Concepts of Excise

1. Whether contaminated, under or over filled bottles or badly crowned bottles amount to manufactured finished goods which are required to be entered under R.G.-1 register, and which are exigible to payment of excise duty?

Amrit Bottlers Private Limited v. CCE 2014 (306) ELT 207 (All.)

Facts of the Case: The appellant was engaged in manufacturer of aerated water. Revenue alleged that the appellant was draining out manufactured aerated water on account of contaminated, under filled, over filled, badly crowned bottles, without entering them in R.G.1 register [daily stock account] and without payment of excise duty on the same. It issued a demand-cum show cause notice on the appellant for the recovery of said duty. Revenue was of the view that contaminated, under filled, over filled, badly crowned bottles were excisable goods. Further, if such goods were defective/non-marketable, the appellant should have sought remission of duty paid on such goods.

The appellant contended that such aerated water was drained out as certain bottles were found to be defective on account of contamination, under/over filling of the aerated water in bottles or such bottles were badly crowned. Under and over filling of the bottles make them unusable under the erstwhile Weights and Measures Act [now Legal Meteorology Act, 2009] as well as under the Prevention of Food Adulteration Act. Consequently, the aerated water which was drained out was not marketable. Thus, it was not required to be entered in R.G.-1 register. The appellant further submitted that excise duty could not levied on the goods which had not been manufactured and which were not marketable.

High Court's Observations: The Court observed that only a finished product can be entered in RG 1 register. A finished product is a product which is manufactured as well as which is marketable. The law required the appellant to provide a screening test before it could declare the manufactured product as a finished product, which was marketable. In other words, a finished product was required to be accounted for in R.G. 1 register only after undergoing the screening test and having found that they were fit for sale.

Under filled or over filled or badly crowned caps bottles could not be treated as being fully manufactured nor could they be treated as finished goods. Moreover, bottles filled

with less or more aerated water were not marketable under the erstwhile Weights and Measures Act [now Legal Meteorology Act, 2009]. Consequently, such goods could not be entered in R.G. 1 register.

High Court's Decision: The Court held that in the instant case, contaminated, under filled, over filled and badly crowned bottles found at the stage of production were not marketable goods. Thus, they were not required to be entered under R.G.-1 register and consequently, no excise duty was payable on them.

Note: *RG-1 register is a daily stock account required to be maintained under rule 10 of the Central Excise Rules, 2002. Rule 10 provides that every assessee shall maintain proper records, on a daily basis, in a legible manner indicating the particulars regarding:*

a. description of the goods produced or manufactured,

b. opening balance, quantity produced or manufactured,

c. inventory of goods,

d. quantity removed,

e. assessable value,

f. the amount of duty payable; and

g. particulars regarding amount of duty actually paid.

Valuation of Excisable Goods

2. Should a part of sales tax retained by the manufacturer from its customers under a tax concession granted to it, be included in the transaction value of such goods under section 4(3)(d) of the Central Excise Act, 1944?

CCE v. Maruti Suzuki India Limited 2014 (307) ELT 625 (SC)

Facts of the Case: The assessee was a prestigious unit manufacturing and selling vehicles in the State of Haryana. Being a prestigious unit, a tax concession was granted to the assessee considered by the High Powered Committee (HPC) under the erstwhile Haryana General Sales Tax Rules, 1975. Therefore, an entitlement certificate was issued to the assessee for implementation of the decision of HPC.

A show cause notice was issued by the Department on the ground that on the sale of its vehicles during the period in question, the assessee had deposited only 50% of the sales tax collected by it from its customers and retained balance 50% availing the tax concession granted to it. The retained sales tax was neither actually paid nor actually payable to the State Government. Therefore, the sales tax retained by the assessee constituted a part of the "transaction value" of the vehicles sold by the assessee to the customers in terms of its definition in section 4(3)(d) of the Central Excise Act, 1944 and excise duty was payable on the same.

The assessee contended that it was not actually exempted from payment of sales tax to the extent of 50% collected from the customers, but that the payment of sales tax was

deferred. The 50% sales tax retained for a period of 14 years had to be adjusted against the capital subsidy due to the assessee by the State Government. However, Revenue contended that decision of the HPC did not support the case of the assessee as the entitlement certificate did not mention anything to the effect that it was for the deferment of payment of any sales tax. Thus, the assessee was not supposed to return any amount of sales tax concession to the State Government nor this amount was to be adjusted towards any capital subsidy granted by the State Government.

Supreme Court's Observations: The Supreme Court concurred with the Revenue's contention that there was no mention in the decision of the HPC about adjustment of this amount of sales tax concession against any scheme or any capital subsidy. The entitlement certificate also did not give any indication of deferment of tax or capital subsidy.

Further, referring to CBEC *Circular dated 30th June, 2000,* the Apex Court opined that the assessee retained 50% of the sales tax collected from its customers and it was neither actually paid nor actually payable to the Government. Therefore, the transaction value under section 4(3)(d) shall be calculated by including the amount of sales tax retained by the assessee and they were liable to pay excise duty on such amount.

Supreme Court's Decision: The Apex Court, overruling the Tribunal's decision, held that since assessee retained 50% of the sales tax collected from customers which was neither actually paid to the exchequer nor actually payable to the exchequer, transaction value under section 4(3)(d) of the Central Excise Act,1944, would include the amount of such sales tax.

Notes:

(i) The definition of "transaction value" in Section 4(3)(d) of the Excise Act reads as follows:-

"transaction value" means the price actually paid or payable for the goods, when sold, and includes in addition to the amount charged as price, any amount that the buyer is liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale, whether payable at the time of the sale or at any other time, including, but not limited to, any amount charged for, or to make provision for, advertising or publicity, marketing and selling organization expenses, storage, outward handling, servicing, warranty, commission or any other matter; but does not include the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods.

(ii) The relevant paragraphs of the CBEC Circular No. 354/81/2000 TRU dated 30th June, 2000 read as follows:-

"As regards exclusion of taxes while working out assessable value, the definition of transaction value itself mentions that whatever amount is actually paid or actually payable to the Government or the relevant statutory authority by way of excise, sale

tax and other taxes, such amount shall be excluded from the transaction value. In other words, if any excise duty or other tax is paid at a concessional rate for a particular transaction, the amount of excise duty or tax actually paid at the concessional rate shall only be allowed to be deducted from price. The assessee cannot claim that the excise duty or tax payable at the "normal rate" should be allowed to be deducted. The words "actually paid" have, therefore, been used to (in) the definition of transaction value to reflect the legislative intention as explained above.

The words "actually payable" in the context of the amount of duty of excise, sales tax and other taxes would normally come into play only in those situations where the amount of excise, sales tax or other taxes is not paid at the time of transaction but paid subsequently, for example, sales tax payable under a deferment scheme."

CENVAT credit

3. Will rule 6 of the CENVAT Credit Rules, 2004 apply, if the assessee clears an exempted by-product and a dutiable final product?

UOI v Hindustan Zinc Limited. 2014 (303) ELT 321 (SC)

Facts of the Case: The respondent assessee was engaged in the manufacture of a dutiable product. During the manufacturing process, a by-product was also being produced which was exempted from the excise duty.

The Department denied CENVAT credit to the assessee saying that since the output products of the assessee were both dutiable and exempted, they were either required to maintain separate records for inputs used in taxable and exempted output or were to pay 8% [now 6%] of the sale price of by-product in terms of rule 6 of the CENVAT Credit Rules, 2004. It was submitted that language of the CENVAT Credit Rules, 2004 needs to be interpreted literally. Since, rule 6 does not provide any distinction between exempted final product and exempted by-product, its provisions would also be applicable to the by-product manufactured and therefore, the assessee was obliged to pay excise duty @ 8% [now 6%] in respect of clearance of exempted by-product.

Supreme Court's Decision: The Supreme Court held that since in rule 57CC of the erstwhile Central Excise Rules, 1944 [now rule 6 of the CENVAT Credit Rules, 2004], the term used is 'final product' and not 'by-product', said rule cannot be applied in case of 'by-product' when such by-product emerged as a technological necessity. If the Revenue's argument is accepted, it would amount to equating by-product with final product thereby obliterating the difference, though recognised by the legislation itself.

***Note**: The principle enunciated in the above case by the Supreme Court is that rule 6 of CCR would not apply when manufacture of dutiable final product results in emergence of exempted by-product on account of technological necessity.*

4. Whether CENVAT credit can be availed of service tax paid on customs house agents' (CHA) services, shipping agents' and container services and services of

overseas commission agents used by the manufacturer of final product for the purpose of export, when the export is on FOB basis?

Commissioner v. Dynamic Industries Limited 2014 (35) STR 674 (Guj.)

Facts of the Case: The assessee availed CENVAT credit of service tax paid by it on CHA services, shipping agent and container service and commission paid to overseas agents in respect of finished goods which were exported. The Revenue objected to the CENVAT credit claimed on these services.

Point of Dispute: The Revenue alleged that the CHA services, shipping agent's services, container services and services of overseas commission agent had been availed after the goods were cleared from the place of removal and they were not in relation to the manufacturing activities undertaken by the assessee nor these were pertaining to the activities of clearance of goods from the place of removal. These services, according to the Revenue, did not fall under the definition of the term "input service" and the related CENVAT credit availed was inadmissible.

The assessee contended that the issue was no more *res integra* and in a host of decisions the Tribunal had taken a view that where exports are FOB basis, the place of removal has to be taken as port and, therefore, the service availed by it till the goods reach the port would be admissible; that without the assistance of overseas agents, manufactured goods cannot be sold and, therefore, the services of overseas agents have to be treated as one relating to manufacture.

High Court's Observations: The High Court referred to definition of 'input service' as also placed reliance on various cases dealing with subject and made the following observations:

(i) In case of all three services in relation to which substantial question of law has been framed there is no specific inclusion of such services in the definition of input service.

(ii) Any service used by the manufacturer directly or indirectly in relation to manufacture of final products and clearing of final products upto the place of removal would certainly be covered within the definition of input service. In the present case, the place of removal would be the port.

(iii) Revenue has not disputed the fact that the services in relation to which the CENVAT credit is claimed by the assessee were availed for the purpose of clearing the goods for the purpose of export.

(iv) As regards customs house agent service and shipping agents and container services, the decision of this Court in *Cadila Healthcare Ltd. 2013 (30) STR 3 (Guj.)* would apply and the definition of input service would cover both these services, considering the nature of services and the place of removal being the 'port' in this case.

(v) With regard to the services of overseas commission agent also, the decision of this Court in *Cadila Healthcare Ltd. 2013 (30) STR 3 (Guj.)* would apply wherein it was held that the CENVAT credit on a service could be availed if that service is used directly or indirectly in the manufacture or clearance of final product. As the services of overseas commission agent have not been used for these purposes, the denial in the referred case shall apply to the present case also. *Consequently, CENVAT credit would not be admissible in respect of the commission paid to foreign agents.*

High Court's Decision: The High Court held that CENVAT credit in respect of (i) customs house agents services, (ii) shipping agents and container services and (iii) cargo handling services is admissible, but the CENVAT credit availed for the services of overseas commission agent is not allowed.

Notes:

1. *'Place of removal' is a significant concept in the CENVAT Credit Rules, 2004. The services relating to clearance upto place of removal are covered in the definition of input service and services beyond the place of removal are not so covered. The above judgment deals with this concept, and takes a view that in the present case since the property in the goods was passed at port, the port would be considered as place of removal and services of CHA etc. used till port are therefore covered in the definition of input service.*

   Further, CBEC vide Circular No. 999/6/2015 CX dated 28.02.2015 has also clarified that in case of export of goods by the manufacturer exporter to his foreign buyer, place of removal will be the port where the shipping bill is filed by the manufacturer exporter and accordingly, the eligibility to CENVAT credit is to be determined.

   In the light of said clarification, conclusion drawn by the Gujarat High Court in aforesaid case is reaffirmed that since services used in clearance of final product upto the place of removal are covered in the definition of input service, CENVAT credit would be admissible to the manufacturer exporter in the given case.

2. *Another position taken in this case by the High Court is that the services of 'overseas commission agents' are not covered in the definition of input service. This is highly disputable position and there are judgments where a different view has been taken e.g. the judgment of Punjab & Haryana High Court in the case of Ambika Overseas 2012 (25) STR 348 says that the services of commission agent are covered in the definition of input service.*

5. Can CENVAT credit availed on inputs (contained in the work-in-progress destroyed on account of fire) be ordered to be reversed under rule 3(5C) of the CENVAT Credit Rules, 2004?

CCE v. Fenner India Limited 2014 (307) ELT 516 (Mad.)

Facts of the Case: The respondent assessee was engaged in manufacturing of Oil Seals. On account of fire accident in the factory, the work in progress stocks were burnt and rendered unfit for usage. The assessee had availed CENVAT credit on the raw materials, which were to be used for production of Oil Seals.

A show cause notice was issued to the assessee demanding the CENVAT credit availed on raw materials destroyed along with the interest and penalty though Department did not dispute the fact that inputs on which CENVAT credit had been taken were destroyed by fire when work was in progress. The assessee contended that since inputs were put in use for the manufacture of final products, question of reversing the credit did not arise. However, Revenue, by relying upon rule 3(5C) of the CENVAT Credit Rules, 2004 submitted that the assessee was bound to reverse the credit taken on the inputs.

High Court's Observations: The High Court observed that, it was not in dispute that the inputs on which the CENVAT credit had been availed were destroyed in a fire accident when the work was in progress. Once the fact was not disputed, then the assessee could not be called upon to reverse the credit.

The High Court placed reliance upon the view taken by the Gujarat High Court in the case of *CCE v. Biopac India Corporation Limited 2010 (258) E.L.T.56 (Gujarat H.C.),* wherein it was held that the goods destroyed in fire after being used for many years cannot be said as not used in the manufacture of final product and the assessee need not reverse the credit availed on such inputs.

The High Court further noted that rule 3(5C) can be invoked where on any goods manufactured or produced by an assessee, the payment of duty is ordered to be remitted under rule 21 of the Central Excise Rules, 2002. Thus, only in such case, the CENVAT credit taken on the inputs used in the manufacture of production of said goods shall be reversed.

High Court's Decision: The High Court held that CENVAT credit would need to be reversed only when the payment of excise duty on final product is ordered to be remitted under rule 21 of the Central Excise Rules, 2002, which deals with the remission of duty. In the present case, the assessee has not claimed any remission and no final product has been removed, hence, assessee need not reverse the CENVAT credit taken on inputs (contained in the work-in-progress) destroyed in fire.

6. Is a cellular mobile service provider entitled to avail CENVAT credit on tower parts & pre-fabricated buildings (PFB)?

Bharti Airtel Ltd. v. CCEx. Pune III 2014 (35) STR 865 (Bom.)

Facts of the case: The appellant was engaged in providing cellular telephone services and was paying service tax on the same. The appellant availed CENVAT credit of excise duty paid on the Base Transreceiver Station (BTS) claiming to be a single integrated system consisting of tower, GSM or Microwave Antennas, Prefabricated building (PFB), isolation transformers, electrical equipments, generator sets, feeder cables etc. The

appellant treated these systems as "composite system" classifiable under Chapter 85.25 of the Central Excise Tariff Act [CETA].

Department's contentions: The Department allowed the credit on antenna but objected to availment of CENVAT credit on other items viz. the tower and parts thereof and the PFB on the following grounds:

(i) Each of the goods of the BTS had independent functions and hence, they could not be treated and classified as single unit.

(ii) Tower was fixed to the earth and after its installation became immovable and therefore, could not be said to be goods. Even in CKD or SKD condition, the tower and parts thereof would fall under Chapter heading 7308 of the Central Excise Tariff Act which is not specified in clause (i) of Rule 2(a)(A) of the Credit Rules, 2004 (CCR) as capital goods.

(iii) Tower and parts thereof were not directly utilised for output service as the same had been basically a structural support for certain equipment.

Appellant's contentions: The appellant contended that the goods in question were clearly covered within the ambit of the definition of "capital goods" under rule 2(a)(A) of the CCR. The appellant submitted that tower is an accessory of antenna and that without towers antennas cannot be installed and as such the antennas cannot function and hence, the tower should be treated as parts and components of the antenna.

Alternatively, the goods in question would fall within the definition of "input" under rule 2(k) of CCR. Since, the towers and shelters were received in knocked down condition (CKD) and were used for providing telecom services, the same qualified as "inputs" in terms of rule 2(k) of the CCR. The appellant submitted that since rule 2(k)(2) *[now 2(k)(iv)]* uses the words "all goods" which are "used for providing any "output service", these goods completely fell within the purview of rule 2(k) so as to mean inputs.

However, the Tribunal, when the matter was brought before it, rejected the appellant's plea that the towers and parts thereof and the PFB were capital goods under CCR as also the alternate plea of the appellant that the said goods were inputs falling under rule 2(k) of the CCR.

High Court's Observations: When the appellant moved the High Court, the High Court observed as under:

(i) A combined reading of rule 2(a)(A)(i), 2(a)(A)(iii) and 2(a)(2) indicates that only the category of goods in rule 2(a)(A) falling under clause (i) and (iii) and used for providing output services can qualify as capital goods in the relevant context. All capital goods are not eligible for credit and only those relatable to the output services would be eligible for credit.

(ii) The appellant's contention that they were entitled for credit of the duty paid on account of BTS being a single integrated/composite system classifiable under Chapter 85.25 of the CETA Tariff Act, is not acceptable. Since the various components of the BTS had independent functions, it could not be classified as

single integrated/composite system so as to be capital goods. In that case, tower and parts thereof and PFB would not fall under clause (i) of rule 2(A)(a) of CCR.

(iii) The other contention of the appellant of tower being an accessory of antenna is also without substance as the antenna can be installed irrespective of tower. It would be misconceived and absurd to accept that tower is a part of antenna. An accessory or a part of any goods would necessarily mean such accessory or part which would be utilized to make the goods a finished product or such articles which would go into the composition of another article. The towers are structures fastened to the earth on which the antennas are installed and hence, cannot be considered to be an accessory or part of the antenna.

(iv) Therefore, the goods in question namely the tower and part thereof and the PFB did not fall within the definition of capital goods and hence, the appellants could not claim the credit of duty paid on these items.

(v) The alternative contention of the appellant that the tower and parts thereof and the PFB would also fall under the definition of 'input' under rule 2(k), could also not be sustained.

(vi) Since the tower and parts thereof were fastened and were fixed to the earth and after their erection became immovable, they could not be termed as goods. The towers were admittedly immovable structures and non-marketable and non-excisable and hence, could neither be regarded as capital goods under rule 2(a) nor could be categorized as 'inputs' under rule 2(k) of the CCR.

(vii) Even in the CKD or SKD condition, the tower and parts thereof would fall under the Chapter heading 7308 of the Central Excise Tariff Act which is not specified in clause (i) of rule 2(a)(A) of CCR so as to be capital goods.

High Court's Decision: The High Court rejected the appeals of the appellant and upheld the findings of the Tribunal holding that the mobile towers and parts thereof and shelters / prefabricated buildings are neither capital goods under rule 2(a) nor 'inputs' under rule 2(k) of the CCR. Hence, CENVAT credit of the duty paid thereon by a cellular mobile service provider was not admissible.

7. Whether sales commission services are eligible input services for availment of CENVAT credit? If there is any conflict between the decision of the jurisdictional High Court and the CBEC circular, then which decision would be binding on the Department? Also, if there is a contradiction between the decision passed by jurisdiction High Court and another High Court, which decision will prevail?

Astik Dyestuff Private Limited v. CCEx. & Cus. 2014 (34) STR 814 (Guj.)

Facts of the Case: In the present case, the assessee availed CENVAT credit on sales commission services obtained by them. The Revenue, however, denied such credit on the contention that 'sales commission services' do not fit into the definition of 'input services' under rule 2(l) of CENVAT Credit Rules, 2004 in view of the Gujarat High Court decision in the case of *Commissioner v. M/s.Cadila Healthcare Ltd in 2013 (4) STR 3.*

Point of Dispute: The assessee submitted that in view of CBEC Circular dated 29-04-2011, they were entitled to CENVAT credit on sales commission services obtained by them and that the Department, bounded by the CBEC Circular, could not take a contrary decision. They further submitted that since the decision of the Gujarat High Court in case of *Cadila Healthcare Limited* referred by the Revenue is contrary to that of the Punjab & Haryana High court in the case of *Commissioner v. Ambika Overseas 2012 (25) STR 348 (P&H),* wherein the CENVAT credit on such input services was allowed to the assessee, hence the matter should be referred to the Larger bench.

High Court's Observations: The High Court observed that it is required to be noted that issue involved in the present appeal i.e. whether the appellant would be entitled to CENVAT credit on sales commission services obtained by them is now not *res integra* in view of the decision of this Court in the case of *Cadila Healthcare Limited*. It was elaborated by the High Court that in the case of *Cadila Healthcare Limited,* the jurisdictional High Court did not allow CENVAT credit on sales commission services after interpreting the relevant provisions of law. The High Court clarified that the decision of the jurisdictional High Court is binding to the Department rather than the Circular issued by the C.B.E. & C.

In regard to the request made by the assessee to refer the issue to the Larger Bench, the High Court rejected the same by saying that the appeal against the decision of the jurisdictional High Court (Gujarat H.C) in the case of *Cadila Healthcare Limited* was filed before the Hon'ble Supreme Court and the Apex Court had seized the matter and no stay order was granted in that case. Therefore, the High Court opined that it will not be proper on its part to refer the matter to the Larger Bench in the present case. Even otherwise, the High Court did not find any reason to take a contrary view than its decision in the case of *Cadila Healthcare Limited*.

High Court's Decision: The High Court held that –

(i) if there is any conflict between the decision of the jurisdictional High Court and the CBEC Circular, then decision of the jurisdictional High Court will be binding to the Department rather than CBEC Circular. Therefore, the assessee would not be entitled to CENVAT credit on sales commission services obtained by them.

(ii) merely because there might be a contrary decision of another High Court is no ground to refer the matter to the Larger Bench.

(iii) when there are two contrary decisions, one of jurisdictional High Court and another of the other High Court, then the decision of the jurisdictional High Court would be binding to the Department and not the decision of another High Court.

General Procedures under Central Excise

8. Is interest payable under rule 7(4) of the Central Excise Rules, 2002 if amount of differential duty paid in full before final assessment order is passed?

Ceat Limited v. CCE & C 2015 (317) ELT 192 (Bom.)

Facts of the Case: The appellants cleared the manufactured goods on provisional assessment basis under rule 7 of the Central Excise Rules, 2002. However, they did not wait for the passing of final assessment order by Deputy/ Assistant Commissioner finalizing the provisional assessment and paid the differential duty before the passing of said order.

The Department issued a show cause-cum-demand seeking to recover from the assessee the interest under rule 7(4) of the rule on the amount of differential duty paid by them. However, Revenue did not contend that the differential duty paid prior to finalization of the assessment was not correct, accurate or was not properly computed.

The assessee contended that interest liability under rule 7(4) of the rules arises only after passing of final assessment order. Interest is liable to be paid from the month following the month in which assessments were finalized. However, since the assessee had paid the differential duty well before the date of finalization of the assessment order, it was not liable to pay the interest on the same. Further, since the finalisation of provisional assessment had not resulted into any additional liability, rule 7(4) was not attracted and consequently, interest was not payable by the assessee.

High Court's Observations: The High Court observed that on finalization of provisional assessment, it is possible that duty liability determined is more than that recovered in the provisional assessment. Liability to pay interest under rule 7(4) arises on any such amount payable to Central Government consequent to order for final assessment under rule 7(3). The Court agreed that since in the assessee's case, final assessment resulted in nothing due and payable to the Government; later part of rule 7(4) was not attracted. Consequently, no interest was recoverable from them. Indeed, in case where assessee had paid the differential duty prior to finalization of the assessment, if the interest was to be recovered and was payable on such date, rule would have specifically said so.

High Court's Decision: The High Court held that provisions of rule 7(4) will not be applicable and hence, the interest is not payable, if amount of differential duty is paid in full before the final assessment order is passed.

Demand, Adjudication and Offences

9. In case the revenue authorities themselves have doubts about the dutiability of a product, can extended period of limitation be invoked alleging that assessee has suppressed the facts?

Sanjay Industrial Corporation v. CCE 2015 (318) ELT 15 (SC)

Facts of the Case: In this case, the appellant was engaged in the business of cutting larger steel plates into smaller sizes and shapes as per the requirement of the customers. After cutting the plates as per the customer's specifications, same were supplied to them. This process is known as profile cutting.

The appellant did not pay excise duty on the belief that the aforesaid process did not amount to manufacture as per section 2(f) of the Central Excise Act, 1944. Department issued a show cause notice demanding the excise duty and penalty alleging that the

activity carried out by the appellant amounts to "manufacture". It had invoked the extended period of limitation under section 11A holding that it was a case of suppression and misrepresentation facts by the appellant.

Point of Dispute: The primary contention of the appellant was that penalty could not be imposed invoking extended period of limitation as there was no suppression or misrepresentation of facts by them. It referred to order-in-original in case of *M/s Pioneer Profile Industries, Pune* involving the same process wherein although the Commissioner held that process of profile cutting amounted to manufacture, but did not impose the penalty because the question as to whether this process amounted to manufacture was in doubt earlier.

Supreme Court's Observations: Referring the order of the Commissioner in case of *M/s Pioneer Profile Industries, Pune,* the Apex Court inferred that even Department had the doubts relating to excisability of process of profile cutting. In view thereof, if the appellant also had nurtured the belief that the process carried out by him did not amount to manufacture and did not pay excise duty, this conduct of the appellant was a bonafide conduct and could not be treated as willful suppression of facts.

Supreme Court's Decision: The Supreme Court held that since Revenue authorities themselves had the doubts relating to excisability of process of profile cutting, the bonafides of the appellant could not be doubted. Hence, extended period of limitation could not be invoked and penalty was set aside.

Appeals

10. Can an appeal be filed before the Supreme Court against an order of the CESTAT relating to clandestine removal of manufactured goods and clandestine manufacture of goods?

CCE v. Fact Paper Mills Private Limited 2014 (308) ELT 442 (SC)

Supreme Court's Decision: The Supreme Court held that the appeals relating to clandestine removal of manufactured goods and clandestine manufacture of goods are not maintainable before the Apex Court under section 35L of the Central Excise Act, 1944.

11. Does the Commissioner (Appeals) have the power to review his own order of pre-deposit?

M/s Venus Rubbers v. The Additional Commissioner of Central Excise, Coimbatore 2014 (310) ELT 685 (Mad.)

High Court's Decision: The High Court held that there is no provision of law under the Central Excise Act, 1944 which gives power to the Commissioner (Appeals) to review his order. However, such a power is available to the Tribunal under section 35C(2) of the Central Excise Act, 1944 to rectify any mistake apparent on the record. The High Court elaborated that when there is no power under the statute, the Commissioner (Appeals) has no authority to entertain the application for review of the order.

SECTION B: SERVICE TAX

Basic Concepts of Service Tax

12. Does preparation of ready mix concrete (RMC) along with pouring, pumping and laying of concrete amount to provision of service?

Commissioner v. GMK Concrete Mixing Pvt. Ltd. 2015 (38) STR J113 (SC)

Facts of the case: In this case, the assessee was engaged in preparation of ready mix concrete (RMC). While carrying out such dominant objects, other ancillary and incidental activities like pouring, pumping and laying of concrete were also carried out. The Revenue contended that the whole activity carried out by the assessee was not a sale transaction, as it also included element of service in it. Hence, the assessee was liable to pay service tax. The Department was of the view that the activities like pouring, pumping and laying of concrete is a significant part of the transaction and not incidental to transaction of sale.

The Tribunal, when the matter was brought before it, held that agreement to supply RMC does not constitute any taxable service. Aggrieved by such an order, the Revenue, preferred an appeal before the Supreme Court.

Supreme Court's Decision: The Supreme Court upheld the decision of the Tribunal wherein it was held that the contract between the parties was to supply RMC and not to provide any taxable services. Therefore, since the Finance Act, 1994 is not a law relating to commodity taxation, the adjudication was made under mistake of fact and law fails. By this judgment, the Supreme Court dismissed the appeal filed by the Revenue.

13. Whether supply of food, edibles and beverages provided to the customers, employees and guests using canteen or guesthouse of the other person, results in outdoor caterer service?

Indian Coffee Workers' Co-operative Society Limited v. CCE & ST 2014 (34) STR 546 (All.)

Facts of the Case: The assessee entered into agreements with National Thermal Power Corporation Limited (NTPC) for running and maintenance of a guest house and with Lanco Infratech Limited (LANCO) for running and maintenance of catering services for its Township. The assessee charged amounts in cash from individual customers for food, eatables and beverages supplied according to rates stipulated in the menu card. The assessee did not pay any service tax as it was of the view that it did not provide any service to NTPC or LANCO but only sold goods in their canteens to individual customers (not to NTPC and LANCO). NTPC and LANCO just provided a place for running the canteen on rent and reimbursed certain expenses for maintenance and running. Thus, there should not be any service tax liability on this activity.

However, the Revenue demanded service tax from the assessee by treating the activity of the assessee as outdoor catering services since he was engaged in providing services in connection with catering at a place other than his own. The Revenue was of the opinion that the fact that food, beverages or edibles were consumed by employees of

NTPC and LANCO or by those who use the guest house or facility, made no difference to the position that the service was provided by the assessee to NTPC or LANCO, and attracted service tax.

High Court's Observations: The High Court opined that the assessee is a caterer. The assessee is a person who supplies food, edibles and beverages for a purpose. The purpose is to cater to persons who use the facility of a canteen which is provided by NTPC or by LANCO within their own establishments. NTPC and LANCO have engaged the services of the assessee as a caterer. Further, since the assessee provides the services as a caterer at a place other than his own, he is an outdoor caterer.

The High Court clarified that taxable catering service could not be confused with who had actually consumed the food, edibles and beverages which were supplied by the assessee. Taxability or the charge of tax does not depend on whether and to what extent the person engaging the service consumes the edibles and beverages supplied, wholly or in part. What is material is whether the service of an outdoor caterer is provided to another person and once it is, as in the present case, the charge of tax is attracted.

Further the High Court elaborated that the charge of tax in the cases of VAT is distinct from the charge of tax for service tax. The charge of service tax is not on the sale of goods but on a taxable service provided. Hence, the fact that the assessee had paid VAT on the sale of goods on the supply of food and beverages to those who consume them at the canteen, would not exclude the liability of the assessee for the payment of service tax in respect of the taxable service provided by the assessee as an outdoor caterer.

High Court's Decision: Based on the observation made above, the High Court held that the assessee was liable for payment of service tax as an outdoor caterer.

Note: *Though the above judgment is based on the definition of 'outdoor caterer' and taxable outdoor catering services as existing prior to 1st July 2012, the principle in the judgment will hold true even for the period beginning from 1st July 2012. Under the current position of law, service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as part of the activity, is liable to service tax as declared service.*

14. Whether the course completion certificate/training offered by approved Flying Training Institute and Aircraft Engineering Institutes is recognized by law (for being eligible for exemption from service tax) if the course completion certificate/ training/ is only for the purpose of eligibility for obtaining ultimate licence/approval for certifying repair/maintenance/airworthiness of aircrafts?

CCE & ST v. Garg Aviations Limited 2014 (35) STR 441 (All.)

Facts of the Case: The assessee was running a Flying Training Institute and Aircraft Maintenance Engineering Institute. It was engaged in providing training and coaching to individuals in the field of flying of aircraft for obtaining Commercial Pilot License from the

Director Civil Aviation (DGCA), New Delhi. It also provided training for obtaining Basic Aircraft Maintenance Engineering Licence.

Point of Dispute: The Department demanded service tax on this training activity. However, the assessee contended that since the services were leading to the grant of diploma/certificate recognised by the law, the services were exempt and thus, were not chargeable to service tax. The assessee cited the case of *Indian Institute of Aircraft Engineering v. Union of India 2013 (30) STR 689*, in which the Delhi High Court, in the similar matter held that such services were not chargeable to service tax being exempt.

High Court's Observations: The High Court referred to the judgment of the Delhi High Court in *Indian Institute of Aircraft Engineering v. Union of India,* wherein the Delhi High Court made the following observations:

(i) The expression 'recognized by law' is a very wide one. The legislature has not used the expression "conferred by law" or "conferred by statute". Thus, even if the certificate/degree/diploma/qualification is not the product of a statute but has approval of some kind in 'law', it would be exempt.

(ii) The Aircraft Act, 1934 (the Act) and the Aircraft Rules, 1937 (the Rules) and the Civil Aviation Requirements (CAR) issued by the DGCA under Rule 133B of the Rules, having provided for grant of approval to such institutes and having laid down conditions for grant of such approval and having further provided for relaxation of one year in the minimum practical training required for taking the DGCA examination, have recognized the course completion certificate and the qualification offered by such Institutes.

(iii) The certificate/training/qualification offered by Institutes which are without approval of DGCA would not confer the benefit of such relaxation. Thus, the certificate/training/qualification offered by approved Institutes, has by the Act, Rules and the CAR been conferred some value in the eyes of law, even if it be only for the purpose of eligibility for obtaining ultimate licence/approval for certifying repair/maintenance/airworthiness of aircrafts.

(iv) The Act, Rules and CAR distinguish an approved Institute from an unapproved one and a successful candidate from an approved institute would be entitled to enforce the right, conferred on him by the Act, Rules and CAR, to one year relaxation against the DGCA in a Court of law. The inference can only be one, that the course completion certificate/training offered by such Institutes is recognized by law.

(v) An educational qualification recognized by law will not cease to be recognized by law merely because for practicing in the field to which the qualification relates, a further examination held by a body regulating that field of practice is to be taken.

The Delhi High Court held that the recognition accorded by the Act, Rules and CAR supra to the course completion certificate issued by the institutes as the petitioner cannot be withered away or ignored merely because the same does not automatically allow the holder of such qualification to certify the repair, maintenance

or airworthiness of an aircraft and for which authorization a further examination to be conducted by the DGCA has to be passed/cleared.

High Court's Decision: The High Court upheld the decision of the Tribunal and held that the Revenue had not been able to persuade the Court to take a contrary view as taken by the Delhi High Court in *Indian Institute of Aircraft Engineering.* The appeal filed by the Revenue would not give rise to any substantial question of law. Hence, the appeal filed was dismissed and the assessee was held not to be liable to pay service tax.

Note: *The above case is in context of the taxable service category of 'commercial coaching or training services' and the related exemption as they stood prior to 1st July 2012. However, as the broad position of the taxable service and the related exemption (which is now covered under the negative list) remains the same, the principle in the judgment may hold true in the present position of law also.*

15. Whether deputation of some staff to subsidiaries/group of companies for stipulated work or for limited period results in supply of manpower service liable to service tax, even though the direction/control/supervision remained continuously with the provider of the staff and the actual cost incurred was reimbursed by the subsidiaries/group companies?

Commissioner of Service Tax v. Arvind Mills Limited 2014 (35) S.T.R. 496 (Guj.)

Facts of the Case: The assessee was engaged in manufacturing of fabrics and ready-made garments. In order to reduce its cost, they deputed some of their employees to their group company. The employees deputed did not work exclusively under the direction or supervision of the subsidiary company and upon completion of the work they were repatriated to the assessee company. The Revenue sought to recover service tax from the assessee for the reimbursement recovered by it from its group/subsidiary companies for the cost of such employees on deputation under the service category of 'manpower supply'.

High Court's Observations: The High Court observed that 'manpower supply services' would not cover the activity of the assessee. The assessee, in order to reduce its cost of manufacturing, deputed some of its staff to its subsidiaries or group companies for stipulated work or for limited period. All throughout, the control and supervision remained with the assessee. The assessee was not in the business of providing recruitment or supply of manpower. Actual cost incurred by the assessee in terms of salary, remuneration and perquisites was only reimbursed by the group companies. There was no element of profit or finance benefit. The subsidiary companies could not be said to be their clients. The High Court noted that the employee deputed did not exclusively work under the direction or supervision or control of subsidiary company.

High Court's Decision: The High Court rejected the contention of the Revenue and held that deputation of the employees by the respondent to its group companies was only for and in the interest of the assessee. There is no relation of agency and client. The

assessee company was not engaged in providing any services directly or indirectly in any manner for recruitment or supply of manpower temporarily or otherwise to a client. Therefore, they were not liable to pay service tax.

Note: *Though this judgment is rendered in the context of position of law as it stood prior to 01.07.2012 (pre-negative list regime), the principle enunciated in the above judgement will hold good under the current negative list regime as well.*

16. Whether section 66E(i) of the Finance Act, 1994 which levies service tax on the service portion of activity wherein goods being food or any other article for human consumption or any drink (whether or not intoxicating) is supplied in any manner as a part of activity, is *ultra vires* the Article 366(29A)(f) of the Constitution?

Hotel East Park v. UOI 2014 (35) STR 433 (Chhatisgarh)

Questions of Law: The substantial questions of law which arose before the High Court were:

(a) Whether any service tax can be charged on sale of an item or *vice versa*?

(b) Whether in view of Article 366(2A)(f) service is subsumed in sale of foods and drinks and whether such Article is violated by section 66E(i) of the Finance Act, 1994?

High Court's Observations: The High Court observed as under:

(i) With reference to question (a) above, the High Court observed that a tax on the sale and purchase of food and drinks within a State is in exclusive domain of the State. The Parliament cannot impose a tax upon the same. Similarly, there is no entry in List II or List III of the Seventh Schedule to the Constitution under which service tax can be imposed. There is no legislative competence with the States to impose a tax on any service.

(ii) With reference to question (b) above, the High Court observed that Article 366(29A)(f) of the Constitution does not indicate that the service part is subsumed in the sale of the food; it rather separates sale of food and drinks from service. Section 65B(44) as well as section 66E(i) of the Finance Act, 1994, charge service tax only on the service part and not on the sales part. It indicates that the sale of the food has been taken out from the service part.

(iii) The quantum of services to be taxed is explained under rule 2C of the Service Tax (Determination of Value) Rules, 2006 read with *Notification No. 25/2012 ST* notified by the Central Government. Rule 2C presumes a fixed percentage of bill value as the value of taxable service on which service tax should be charged. However, there is no provision in VAT Act to bifurcate the amount of bill into sale and service.

High Court's Decision: The High court held that section 66E (i) of the Finance Act, 1994 is *intra vires* the Article 366(29A)(f) of the Constitution of India.

Further, the High Court held that no VAT can be charged over the amount meant for service and that the amount over which service tax has been charged should not be subject to VAT. The High Court directed the State Government to frame such rules and

issue clarifications to this effect to ensure that the customers are not doubly taxed over the same amount. The rules may be in conformity with the bifurcation as provided under the Finance Act, 1994 or ensure that the Commercial Tax authorities do not charge VAT on that part of the value of the food and drink on which service tax is being assessed.

Notes:

(i) Clause 19 of the notification No. 25/2012 ST exempts the service tax in serving food or beverages by the restaurants other than the air-conditioned restaurant or having licence to serve alcoholic beverages i.e. service tax is levied only in those restaurants that have air-conditioning or licence to serve alcoholic beverages.

(ii) Rule 2C of the Service Tax (Determination of Value) Rules, 2006 clarifies that in case of a restaurant, service is presumed to be 40% of the bill value and in case of outdoor catering, it is presumed to be 60% of the bill value. It shows that the value of the food is taken to be 60% of the bill in the case of restaurant and 40% of the bill in case of catering service.

(iii) Article 366 (29A)(f) of the Constitution provides that "tax on the sale or purchase of goods" includes a tax on the 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 (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration.

Valuation of Taxable Service

17. Can the expression 'suppression of facts' be interpreted to include in its ambit, mere failure to disclose certain facts unintentionally?

Naresh Kumar & Co. Pvt. Ltd v. UOI 2014 (35) STR 506 (Cal.)

High Court's Decision: The High Court held that willful suppression cannot be assumed and/or presumed merely on failure to declare certain facts unless it is preceded by deliberate non-disclosure to evade the payment of tax. The extended period of limitation can be invoked on clear exposition that there has been a conscious act on the part of the assessee to evade the tax by non-disclosing the fact which, if disclosed, would attract service tax under sections 66 (now section 66B) & 67 of the Finance Act, 1994. The non-disclosure of the fact which, even if, disclosed would not have attracted the charging section cannot be brought within the ambit of suppression of fact for the purpose of extension of limitation period.

Exemptions and Abatements

18. Is exemption in relation to service provided to the developer of SEZ or units in SEZ available for a period prior to actual manufacture (which is the authorized operation) of final products considering these services as the services used in authorised operations of SEZ?

Commissioner of Service Tax v. Zydus Technologies Limited 2014 (35) STR 515 (Guj.)

Facts of the Case: The assessee had manufacturing operations in the SEZ. The Development Commissioner of SEZ granted an extension of one year to the assessee to start manufacturing operations (which were authorised operations of the SEZ). The assessee procured certain services (scientific and technical consultancy) during this period (before beginning of the manufacture) in order to enable it to undertake manufacturing activity.

Later, when the assessee applied for refund of service tax paid on such input services under *Notification No. 9/2009 ST dated 03.03.2009,* the refund was denied on the ground that since the services were received before the authorised operations (i.e., manufacturing) started, the said input services would not be considered to have been used in authorised operations of SEZ unit, and thus, would not get qualified for refund.

Point of Dispute: The Revenue submitted that as per sub-section (2) of section 4 and sub-section (9) of section 15 of the Special Economic Zones Act, 2005 meaning of "authorized operations" can be concluded as "such operation so authorized shall be mentioned in the letter of approval". Thus, since the manufacturing of the goods mentioned in the letter of approval had not started, it could not be said that the authorized operation of SEZ had started.

The assessee contended that it is necessary for SEZ to procure taxable services right from the budding stage and it is only after having obtained such support service of business that the unit would start functioning for production.

When the CESTAT held that the assessee shall be entitled to refund as claimed, the matter was brought before the High Court by the Department.

High Court's Observations: The High Court relied on its decision passed in the case of *Cadila Healthcare Ltd 2013 (30) STR 3 (Guj.)* and held that no error has been committed by the CESTAT in holding that the assessee shall be entitled to refund; as though the operations of the assessee did not reach to the commercial production stage, the input services of scientific and technical consultancy procured by them were in relation to the manufacture which would take place at a later date.

High Court's Decision: In the instant case, the High Court referring to their previous decision in case of *CCEx. v. Cadila Healthcare Ltd*. held that the services rendered for a period prior to actual manufacture of final product is commercial activity/production and assessee is entitled to exemption by way of refund claimed.

Note: *Though the above judgment is with reference to SEZ Exemption Notification No. 9/2009 ST, the principle discussed appears to be relevant in context of the present SEZ Exemption Notification No. 12/2013 ST also.*

19. Is 'hiring of cab' different from 'renting of cab' for service tax purposes?

CCus. & CEx. v. Sachin Malhotra 2015 (37) STR 684 (Uttarakhand)

High Court's Observations: The High Court opined that under 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 license informed of his movements from time to time. However, 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.

The High Court observed that though rent and hire may, in a different context, have the same connotation; in the context of rent-a-cab scheme and hiring, they signify two different transactions.

High Court's Decision: The High Court upheld the decision of the Tribunal wherein it was held that 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.

Note: *Though the above judgment relates to the pre-negative list regime, it is equally relevant for the existing regime as well.*

Demand, Adjudication and Offences

20. Whether the recipient of taxable service having borne the incidence of service tax is entitled to claim refund of excess service tax paid consequent upon the downward revision of charges already paid, and whether the question of unjust enrichment arises in such situation?

CCus CEx & ST v. Indian Farmers Fertilizers Coop. Limited 2014 (35) STR 492 (All)

The CESTAT answered the above question against the Revenue so this appeal was filed with the High Court by the Revenue. It was the contention of the Revenue that the respondent being recipient of service was not entitled to file a refund claim under section 11B as the expression "any person" in section 11B of the Central Excise Act, 1944 does not include the recipient of the service. The Revenue submitted before the High Court that the principles of unjust enrichment as provided in section 11B were not considered by the CESTAT while allowing the refund claim and that the refund claim filed was not within the period of limitation of one year under section 11B.

High Court's Observations: The High Court relied on the case of *Mafatlal Industries Ltd. v. Union of India 1997 (89) ELT 247* wherein the Supreme Court held that "*Where the burden of the duty has been passed on, the claimant cannot say that he has suffered any real loss or prejudice. The real loss or prejudice is suffered in such a case by the person who has ultimately borne the burden and it is only that person who can legitimately claim its refund."*

The High Court observed that since the respondent, being the recipient of taxable service, had borne the incidence of service tax themselves; there was no question of unjust enrichment. Hence, the respondent was entitled to claim refund of excess service tax paid consequent upon the downward revision of the charges payable by it.

Further, the High Court pointed out that the fact that respondent had not filed the refund claim with the period of limitation was not challenged by the Revenue in the grounds of appeal before the first appellate authority [Commissioner (Appeals)] or in the form of cross objections before the Tribunal. The High Court relied on the Supreme Court's decision in the case of *Commissioner of Customs* v. *Toyo Engineering India Limited 2006 (201) ELT 513 (SC)* wherein it was held that the Revenue could not be allowed to raise submissions for the first time in a second appeal before the Tribunal.

High Court's Decision: The High Court upheld the decision of the CESTAT that since the burden of tax has been borne by the respondent as a service recipient, question of unjust enrichment will not arise as per section 11B of the Central Excise Act 1944 (as applicable to service tax under section 83 of Finance Act,1994).

Further, the High Court held that once the finding of the adjudicating authority that the claim for refund was filed within the period of limitation was not challenged by the Revenue before the first appellate authority and CESTAT, Revenue could not assert to contrary and first time urge a point in an appeal before this Court which was not raised in grounds of appeal before authorities below.

21. Whether the amendment made by Finance Act, 2013 in section 37C(1)(a) of Central Excise Act,1944 to include speed post as an additional mode of delivery of notice is merely clarificatory in nature having retrospective effect or does it operate prospectively?

Jay Balaji Jyoti Steels Limited v. CESTAT Kolkata 2015 (37) STR 673 (Ori.)

Point of Dispute: The contention of the assessee was that the amendment made in section 37(C)(1)(a) of the Central Excise Act,1944 which added "speed post" as an additional mode of service of notice could only operate prospectively and not retrospectively.

High Court's Observations: The High Court observed that in view of section 28 of the Indian Post Office Act, 1898, any postal article which is registered at the post office from which it is posted, and a receipt has been issued in respect of such article, is to be treated as "registered post". The High Court pointed out that since for both "registered post" as well as "speed post", receipts are required to be issued when articles are delivered to the post offices, both "speed post" and "registered post" satisfy the requirement of section 28 of the Indian Post Office Act, 1898. The only difference between the two is that the charges payable for the "speed post" are higher as the same ensures delivery at an early date.

Consequently, the High Court was of the view that addition of the term "speed post" in section 37(C)(1)(a) was merely clarificatory. The High Court further stated that the said

amendment is clearly curative since various other High Courts have held that "communication of notices through speed post was in consonance with law".

The High Court reiterated that it is well settled in law that where an amendment which is brought about is "clarificatory in nature", the same would date back to the date on which the original provision was introduced*.

High Court's Decision: The High Court, therefore, held that insertion of words "or by speed post with proof of delivery" in section 37C(1)(a) of the Central Excise Act, 1944 is clarificatory and a procedural amendment and hence, would have retrospective effect.

Notes:

1. *Prior to 10.05.2013, a decision, order, summon or notice used to be served to the intended person either by tendering the same (physical delivery) or by sending it through registered post with acknowledgment due in terms of section 37C(1)(a) of the Central Excise Act, 1944. However, w.e.f. 10.05.2013, section 37C(1)(a) was amended vide the Finance Act, 2013 so as to include additional modes of delivery for decisions, orders, summons or notices namely, speed post with proof of delivery or courier approved by CBEC.*

*2. *The Supreme Court dealt with the issue of retrospective operation of clarificatory amendments in the case of R. Rajagopal Reddy (dead) by Lrs. & Ors. v. Padmini Chandrasekharan (dead) by Lrs., 1995 (2) SCC 630 as under:*

"Declaratory enactment declares and clarifies the real intention of the legislature in connection with an earlier existing transaction or enactment, it does not create new rights or obligations. If a statute is curative or merely declaratory of the previous law retrospective operation is generally intended. A clarificatory amendment of this nature will have retrospective effect and therefore, if the principal Act was existing law when the Constitution came into force the amending Act also will be part of the existing law. If a new Act is to explain an earlier Act, it would be without object unless construed retrospective. An explanatory Act is generally passed to supply an obvious omission or to clear up doubts as to the meaning of the previous Act."

The said judgement of the Apex Court was affirmed by the Full Bench of the Hon'ble Supreme Court in the case of Shyam Sunder and Others v. Ram Kumar and Another, 2001 (8) SCC 24.

Other Provisions under Service Tax

22. Can the Commissioner (Appeals) remand back a case to the adjudicating authority under section 85 of the Finance Act, 1994?

Commissioner of Service Tax v. Associated Hotels Ltd. 2015 (37) STR 723 (Guj.)

Point of Dispute: The question of law which was raised in this case was that whether the Commissioner (Appeals), exercising powers under section 85 of the Finance Act, 1994, has the power to remand the proceedings back to the adjudicating authority.

The Department contended that due to the amendment made in section 35A(3) of the Central Excise Act, 1944, in the year 2001*, the powers of remand which were previously specifically granted to the Commissioner (Appeals) were taken away. It was argued by the Department that since section 85(5) of the Finance Act, 1994 provides that the Commissioner (Appeals) while hearing the appeals under section 85 of the Act, follows the same procedure and exercises same powers which he does while hearing the appeals under the Central Excise Act, 1944, Commissioner (Appeals) does not have the power to remand the proceedings back to the adjudicating authority *in service tax matters also.*

High Court's Observation: The High Court observed that section 85(4) of the Finance Act, 1994 is worded widely and gives ample powers to the Commissioner while hearing and disposing of the appeals to pass such orders as he thinks fit including an order enhancing tax, interest or penalty. Such powers would, therefore, inherently contain the power to remand a proceeding for proper reasons to the adjudicating authority.

Further, the High Court rejected the Department's contention that by virtue of section 85(5) of the Finance Act, 1994, the limitation on power of Commissioner (Appeals) to remand a proceeding as contained in section 35A(3) of Central Excise Act, 1944 also applied to appeals under section 85 of Finance Act, 1994. This is so because, even though sub-section (5) of section 85 requires the Commissioner (Appeals) to follow the same procedure and exercise same powers in making orders under section 85, as he does while hearing the appeals under the Central Excise Act, 1944, sub-section (5) itself starts with the expression "subject to the provisions of this Chapter".

The High Court held that sub-section (4) of section 85 itself contains the width of the power of the Commissioner (Appeals) in hearing the proceedings of appeal under section 85. The scope of such powers flowing from sub-section (4), therefore, cannot be curtailed by any reference to sub-section (5) of section 85 of the Finance Act, 1994.

High Court's Decision: The High Court, therefore, held that section 85(4) of the Finance Act, 1994 gives ample powers to the Commissioner while hearing and disposing of the appeals and such powers inherently contain the power to remand a proceeding for proper reasons to the adjudicating authority.

Notes:

**1. Section 35A(3) of the Central Excise Act, 1944 was amended with effect from 11-5-2001. Prior to the amendment, the said provision read as under:*

"The Commissioner (Appeals) may, after making such further inquiry as may be necessary, pass such order as he thinks fit confirming, modifying or annulling the decision or order appealed against, or may refer the case back to the adjudicating authority with such directions as he may think fit for a fresh adjudication or decision, as the case may be, after taking additional evidence, if necessary."

After 11-5-2001, the amended section 35A(3) reads as under :

"The Commissioner (Appeals) shall, after making such further inquiry as may be necessary, pass such order, as he thinks just and proper, confirming, modifying or annulling the decision or order appealed against."

2. *The Delhi High Court in the case of Commissioner v. World Vision 2011 (24) STR 650 (Del.) has also held that under section 85(4) of Finance Act, 1994, the Commissioner (Appeals) has the power to remand back the case to the adjudicating authority for fresh consideration.*

23. Whether the period of limitation or the period within which delay in filing an appeal can be condoned, specified in terms of months in a statute, means a calendar month or number of days?

CCus & CEx. v. Ashok Kumar Tiwari 2015 (37) STR 727 (All.)

Facts of the case: The assessee received the adjudication order on 08.10.2011 and filed an appeal against the said order before Commissioner of Central Excise (Appeals) on 09.04.2012 along with an application for condonation of delay. However, the Commissioner dismissed the appeal as being time barred and declined to condone the delay. Tribunal, on appeal, decided that the delay should be condoned in assessee's case. It observed that period of limitation of 3 months prescribed under section 85(3) of the Finance Act, 1994 meant 3 calendar months and not 90 days and proviso to said sub-section empowered Commissioner to condone the delay for sufficient cause so as to allow the appeal to be presented within a further period of 3 months.

Point of dispute: The issue which came up for consideration before High Court was whether the period of limitation or the period within which delay in filing an appeal can be condoned, specified in terms of months in a statute, means a calendar month or number of days.

High Court's Observations: The High Court opined that where the legislature intends to define the period of limitation with regard to the number of days, it does so specifically. Section 85 of the Finance Act, 1994 has defined the period of limitation as well as the power to condone the delay with regard to a stipulation in terms of months and such a stipulation can only mean a calendar month. Once the legislature has used the expression "three months" both in the substantive part of sub-section (3) of section 85 as well as in its proviso*, it would not be open for the High Court to substitute the words "3 months" by the words "90 days" and if it does so, it would amount to rewriting the legislative provision, which is impermissible.

The High Court noted that section 3(35) of the General Clauses Act, 1897 also defines the expression "month" to mean a month reckoned according to the British calendar. Further, the day on which order was received by the assessee, i.e. 08.10.2011 had to be excluded while computing the period of limitation in view of section 9 of said Act**. Since the original period of limitation and the period within which delay could be condoned expired on a public holiday, i.e. 08.04.2012, the assessee filed the appeal on the next working day, i.e. 09.04.2012.

High Court's Decision: In the given case, the Commissioner of Central Excise (Appeals) had the jurisdiction to condone the delay in filing of appeal by the assessee as the same had been filed within the stipulated time prescribed for the same.

Notes:

**1. Sub-section (3) of section 85 of the Finance Act, 1994 stipulates the period of limitation for filing an appeal with Commissioner of Central Excise (Appeals). Further, proviso to said section stipulates the period within which delay in filing said appeal can be condoned. Provisions of section 85(3) and its proviso were applicable till 27.05.2012. However, with effect from 28.05.2012, sub-section (3) of section 85 and its proviso ceased to have effect and sub-section (3A) to said section and its proviso were inserted by the Finance Act, 2012.*

While sub-section (3) and its proviso stipulated the original period of limitation as three months and the extent to which delay could be condoned also as three months, as per sub-section (3A), the original period of limitation is two months and delay can be condoned within a further period of one month.

Although the aforesaid judgment is based on sub-section (3) of section 85, the principle derived in the said ruling i.e., where legislature specifies period of limitation as well as period within which delay in filing an appeal can be condoned in terms of months, such a stipulation can only mean a calendar month and not number of days, is applicable to sub-section (3A) of section 85 also.

***2. Supreme Court, in case of M/s. Econ Antri Ltd v. M/s. Rom Industries Ltd. & Anr, had also taken a similar view on this point and decided that while computing the period of limitation, the day on which the offence is committed/ date of cause of action has to be excluded.*

24. Can the appeal filed in time but to wrong authority be rejected by the appellate authority being time barred?

Chakiat Agencies v. UOI 2015 (37) STR 712 (Mad.)

Facts of the case: In the instant case, the assessee filed an appeal to Commissioner, but mistakenly gave it to the adjudicating officer who had passed the original order. The appellate authority rejected the appeal on the ground that the appeal was not received in time in his office.

Point of dispute: The Department contended that although appeal was received in time by the adjudicating officer, appellate authority rejected the appeal as the same was not received in its office in time.

High Court's Observations: The High Court noted that the appeal had been preferred in time, but reached different wing of the same building. Since the appeal was received by the adjudicating officer who has passed the original order, he ought to have sent it to the other wing of the same building, but he had not done the same. Therefore, the order

passed by the appellate authority cancelling the appeal on the ground that it was not received in time, could not be accepted.

The High Court, further, referred to Andhra Pradesh High Court judgment in *Radha Vinyl Pvt. Ltd. v. Commissioner of Income Tax and Another* case where in similar circumstances it was held that although the appeal had been addressed to the wrong officer, Department could not deny the fact that the appeal was pending before it. Either the Department should have returned the appeal papers to the assessee to enable him to file appeal before the appropriate authority or should have handed over the appeal papers to the competent authority. Consequently, now the Department could not say that the appeal was not filed with the competent authority.

High Court's Decision: In the light of the above discussion, the High Court directed the appellate authority to entertain the appeal of the assessee and to pass appropriate orders on merits and in accordance with law, after affording him an opportunity of being heard.

SECTION C: CUSTOMS

Levy and Exemption from the Customs Duty

25. Would countervailing duty (CVD) on an imported product be exempted if the excise duty on a like article produced or manufactured in India is exempt?

Aidek Tourism Services Pvt. Ltd. v. CCus. 2015 (318) ELT 3 (SC)

Supreme Court's Decision: Supreme Court held that rate of additional duty leviable under section 3(1) of the Customs Tariff Act, 1975 would be only that which is payable under the Central Excise Act, 1944 on a like article. Therefore, the importer would be entitled to payment of concessional/ reduced or nil rate of countervailing duty if any notification is issued providing exemption/ remission of excise duty with respect to a like article if produced/ manufactured in India.

Classification of goods

26. Whether the mobile battery charger is classifiable as an accessory of the cell phone or as an integral part of the same?

State of Punjab v. Nokia India Private Limited 2015 (315) ELT 162 (SC)

In this case, the assessee classified the mobile battery charger as an integral part of the main product i.e. Nokia mobile phone. It contended that cell phone could not be operated without the charger. Further, mobile battery chargers were provided free with the cell phone in a composite package. Therefore, it applied the concessional rate of tax on the mobile battery charger also, as applicable on the mobile phone. However, it also admitted that whenever it sold the chargers separately, tax was not charged at the concessional rate.

According to Department, a battery charger was not a part of the cell phone but merely an accessory thereof. Thus, concessional rate of tax applicable on cell phones was not applicable to the mobile battery chargers.

Supreme Court's Observations: The Supreme Court decided the case in favour of Revenue and against the assessee holding that the battery charger is not a part of the mobile/cell phone but an accessory to it, on the basis of the following observations:

(i) Had the charger been a part of cell phone, cell phone could not have been operated without using the battery charger. However, as a matter of fact, it is not required at the time of operation. Further, the battery in the cell phone can be charged directly from the other means also like laptop without employing the battery charger, implying thereby, that it is nothing but an accessory to the mobile phone.

(ii) As per the information available on the website of the assessee, it had invariably put the mobile battery charger in the category of an accessory which means that in the common parlance also, the mobile battery charger is understood as an accessory.

(iii) A particular model of Nokia make battery charger was compatible with many models of Nokia mobile phones and also many models of Nokia make battery chargers are compatible with a particular model of Nokia mobile phone, imparting various levels of effectiveness and convenience to the users.

(iv) Rule 3(b) of the General Rules for Interpretation of the First Schedule of the Customs Tariff Act, 1975 can also not be applied in the assessee's case as merely making a composite package of cell phone and mobile battery charger will not make it composite goods for the purpose of interpretation of the provisions.

Supreme Court's Decision: The Apex Court held that mobile battery charger is an accessory to mobile phone and not an integral part of it. Further, battery charger cannot be held to be a composite part of the cell phone, but is an independent product which can be sold separately without selling the cell phone.

Valuation under the Customs Act, 1962

27. Can the value of imported goods be increased if Department fails to provide to the importer, evidence of import of identical goods at higher prices?

Gira Enterprises v. CCus. 2014 (307) ELT 209 (SC)

Facts of the Case: The appellant imported some goods from China. On the basis of certain information obtained through a computer printout from the Customs House, Department alleged that during the period in question, large number of such goods were imported at a much higher price than the price declared by the appellant. Therefore, Department valued such goods on the basis of transaction value of identical goods as per erstwhile rule 5 [now rule 4 of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007] and demanded the differential duty alongwith penalty and interest from the appellant. However, Department did not provide these printouts to the appellant.

The appellant contended that Department's demand was without any basis in law, without any legally admissible evidence and opposed to the principles of natural justice as the computer printout which formed the basis of such demand had not been supplied to them. Resultantly, the appellant had no means of knowing as to whether any imports of comparable nature were made at the relevant point of time.

Supreme Court's Observations: Supreme Court observed that since Revenue did not supply the copy of computer printout, which formed the basis of the conclusion that the appellants under-valued the imported goods, the appellants obviously could not and did not have any opportunity to demonstrate that the transactions relied upon by the Revenue were not comparable transactions.

Supreme Court's Decision: The Supreme Court held that mere existence of alleged computer printout was not proof of existence of comparable imports. Even if assumed that such printout did exist and content thereof were true, such printout must have been supplied to the appellant and it should have been given reasonable opportunity to establish that the import transactions were not comparable.

Thus, in the given case, the value of imported goods could not be enhanced on the basis of value of identical goods as Department was not able to provide evidence of import of identical goods at higher prices.

***Note**: This case establishes the principle that the onus to prove that identical goods have been imported at a price higher than the value of the goods declared by the importer, lies with the Department.*

Demand and Appeals

28. Can a writ petition be filed before a High Court which does not have territorial jurisdiction over the matter?

Neeraj Jhanji v. CCE & Cus. 2014 (308) ELT 3 (SC)

Facts of the Case: In this case, the assessee filed a writ petition before the Delhi High Court *against the* order in original passed by the Commissioner of Customs of Kanpur. However, the jurisdictional High Court for the petitioner would have been Allahabad High Court. When the Revenue raised objection over the territorial jurisdiction of the High Court, the assessee withdrew the appeal from the Delhi High Court and filed the appeal with the Allahabad High Court with the application for condonation of delay. The Allahabad High Court, however, dismissed the application for condonation of delay and also dismissed the appeal as time barred. Then, the assessee filed a special leave petition with the Supreme Court.

Supreme Court's Decision: The Supreme Court observed that the very filing of writ petition by the petitioner in Delhi High Court against the order in original passed by the Commissioner of Customs, Kanpur indicated that the petitioner had taken chance in

approaching the High Court at Delhi which had no territorial jurisdiction in the matter. The filing of the writ petition before Delhi High Court was not at all bona fide.

***Note**: In the aforementioned case, the Apex Court has disapproved the practice of Forum Shopping as adopted by the petitioner. Forum Shopping is the practice adopted by the litigants to have their legal case heard in the Court which would provide most favourable decision.*

Refund

29. Is limitation period of one year applicable for claiming the refund of amount paid on account of wrong classification of the imported goods?

Parimal Ray v. CCus. 2015 (318) ELT 379 (Cal.)

Facts of the case: The petitioners imported tunnel boring machines which were otherwise fully exempt from customs duty. However, owing to erroneous classification of such machines, they paid large amount of customs duty.

After expiry of more than 3 years, the petitioners filed a writ petition claiming the refund of the amount so paid. The said refund claim was rejected on the ground that the petitioners failed to make a proper application of refund under section 27 of the Customs Act, 1962 within the stipulated period of 1 year of payment of duty.

High Court's Observations: The High Court observed that, the provisions of section 27 applies only when there is over payment of duty or interest under the Customs Act, 1962. When the petitioners' case is that tunnel boring machines imported by it were not exigible to any duty, and any sum paid into the exchequer by them was not duty or excess duty but simply money paid into the Government account. The Government could not have claimed or appropriated any part of this as duty or interest. The money received by Government could more appropriately be called money paid by mistake by one person to another, which the other person is under obligation to repay under section 72 of the Indian Contract Act, 1872. The obligation was a continuing obligation. When a wrong is continuing, there is no limitation for instituting a suit complaining about it

High Court's Decision: The High Court held that law of limitation under Customs Act is applicable to duty or interest paid under the Act. However, any sum paid into the exchequer by the assessee is not duty or excess duty but is simply money paid into the account of Government. Therefore, the assessee is entitled to refund of the sum paid by it to the customs authorities.

Provisions Relating to Illegal Import, Illegal Export, Confiscation, Penalty & Allied Provisions

30. Whether mere dispatch of a notice under section 124(a) would imply that the notice was "given" within the meaning of section 124(a) and section 110(2) of the said Customs Act, 1962?

Purushottam Jajodia v. Director of Revenue Intelligence 2014 (307) ELT 837 (Del.)

Facts of the Case: As per section 110(2) of the Customs Act, 1962, a notice under section 124(a) is required to be **"given"** to the person from whose possession they were seized informing him the grounds on which goods are proposed to be confiscated, within 6 months (extendable upto one year) of seizure of the goods. Otherwise, goods need be returned to such person.

However, in the present case, the notice under section 124(a) was dispatched by registered post on the date of expiry of stipulated period under section 110(2) and received by the petitioner after the expiry of such period.

The petitioner contended that since said notice had not been received before the expiry of the said period of six months (extendable upto one year), goods should be returned to him. Relying on Supreme Court's decision in case of *K. Narsimhiah v. H.C. Singri Gowda AIR 1966 SC 330* and Gujarat High Court's decision in case of *Ambalal Morarji Soni v. Union of India AIR 1972 GUJ 126*, it submitted that by the use of the word "given" used in section 110(2), the legislative intent was clear that the notice had to be received by the person concerned or the notice had to be offered/tendered and refused by the person concerned. Mere dispatch by post would not be covered by the word "given" as appearing in the above mentioned provisions of the said Act. Further the expression "given" was distinct and different from the word "issued" or "served".

Revenue, referring to section 153(a), submitted that the moment a notice is tendered or sent by registered post or by an approved courier, that amounts to service of the notice and the actual receipt by the noticee is not a relevant consideration. Since the notice had been sent by registered post within the stipulated period as prescribed under section 110(2) of the said Act, the goods were not liable to be released. They primarily placed reliance on decision of Calcutta High Court in case of *Kanti Tarafdar 1997 (91) ELT 51 (Cal.)* and Madhya Pradesh High Court in case of *Ram Kumar Aggarwal 2012 (280) ELT 13 (M.P.).*

High Court's Observations: The Delhi High Court observed that section 124(a) clearly stipulates that no order confiscating any goods or imposing any penalty on any person shall be made unless the owner of the goods or person from whom goods have been seized is "given a notice" in writing, "informing him of the grounds on which it is proposed to confiscate the goods or to impose a penalty". In case such notice is not given within the stipulated period of six months or the extended period of a further six months, seized goods have to be released.

The object of section 124(a) is that the person from whom the goods have been seized had to be informed of the grounds on which the confiscation of the goods is to be founded. This can happen only when such person receives the notice and is capable of reading and understanding the grounds of the proposed confiscation. On a conjoint reading of section 110(2) and section 124(a) of the said Act, the Court opined that the notice contemplated in these provisions can only be regarded as having been "given" when it is actually received or deemed to be received by the person from whom the goods have been seized.

The Delhi High Court was in complete agreement with the Supreme Court's decision in case of *K. Narsimhiah* as followed by Gujarat High Court in case of *Ambalal Morarji Soni.* However, it disagreed with the decision of Calcutta High Court in case of *Kanti Tarafdar.* The Delhi High Court pointed out that the decision in the said case was arrived at on the (wrong) premise that section 124 requires that a notice be "issued" as against a notice being "given" when the body of the provision of section 124 nowhere uses the expression "issue of show cause notice". The Delhi Court elaborated that it is only the heading of that section which uses that expression (**issue** of show notice) and the body of section 124(a), on the contrary, uses the exact same expression "given" as used in section 110(2) of the said Act. Therefore, the Delhi High Court was of the view that very basis of the Calcutta High Court's decision in *Kanti Tarafdar* is incorrect. The Delhi High Court also disagreed with the Calcutta High Court's observation that the word "given" used in section 110(2) and section 124(a) is in any manner controlled by section 153. The Delhi High Court opined that in the context of the present cases, section 153 would only define the mode and manner of service and not the time of service or when a notice can be said to have been "given".

Further, Delhi High Court was of the view that Madhya Pradesh High Court, in case of *Ram Kumar Aggarwal,* wrongly concluded that when the legislature had used the words "notice is given" it would "obviously mean that the notice must be issued within six months of the date of seizure". The Delhi High Court, on the other hand, opined that expression "notice is given" does not logically translate to the conclusion that "notice must be issued within the stipulated period".

High Court's Decision: The High Court held that since the petitioners did not receive the notice under section 124(a) within the time stipulated in section 110(2) of the Act, such notice will not considered to be "given" by the Department within the stipulated time, i.e. before the terminal date. Consequently, the Department was directed to release the goods seized.

Note: *Section 124(a) of the Customs Act, 1962, inter alia, stipulates that no order confiscating any goods or imposing any penalty on any person shall be made under this Chapter unless the owner of the goods or such person is* ***given*** *a notice in writing informing him of the grounds on which it is proposed to confiscate the goods or to impose a penalty.*

Further, section 110(2) of the Act stipulates that where no such notice is ***given*** *within six months of the seizure of the goods, the goods shall be returned to the person from whose possession they were seized.*