Legal Decisions[1]

DIRECT TAXES

Income Tax

LD/66/64

Aayush NRI LEPL Health Care Pvt. Ltd.
vs.
Asst. Commissioner of Income Tax
18th October 2017

Even if the deductee had filed NIL return of income and had no tax liability, even after taking into account receipts from assessee, interest u/s. 201(1A) was still leviable.

The assessee had made payments without deducting tax u/s. 194J for A.Y. 2013-14 and A.Y. 2014-15. The AO treated the assessee as an assessee in default u/s. 201(1) and levied interest u/s. 201(1A). The CIT(A) noted that the deductee had filed return of income offering receipts from the assessee and thus held that assessee was not an assessee in default. However, the CIT(A) held that the assessee is liable for interest u/s. 201(1A) from the date on which such tax was deductible to the date of furnishing of return of income by the deductee.

Before ITAT, the assessee contended that the deductee had filed NIL return of income even after considering the amounts paid by the assessee. Further, since there was advance tax liability in the deductee's case and since the interest u/s. 201(1A) is compensatory in nature, there was no loss to the revenue and therefore, interest u/s. 201(1A) should not be levied.

ITAT observed that proviso to Section 201(1A) which was inserted w.e.f. July 1, 2012, makes it very clear that even though the assessee is not deemed to be an assessee in default under the first proviso to Section 201(1), the interest u/s. 201(1A) shall be payable from the date on which such tax is deductible to the date of furnishing of return of income by such a resident. ITAT held that the tax liability in the hands of the deductee has no relation or connection for charging the interest u/s. 201(1A).

ITAT held that the charging of interest from the date of the tax required to be deducted till the date of furnishing of return of income by the deductee was automatic and mandatory. ITAT noted that the interest paid u/s. 201(1A) was not compensatory but penal in nature.

Accordingly, ITAT upheld CIT(A)'s order regarding levy of interest.

LD/66/65

Commissioner of Income Tax
vs.
M/s Gemini Distilleries
12th October 2017

CBDT Instruction No. 3/2011 laying down monetary appeal filing limits for Revenue's Appeals, held to be not applicable to pending cases by SC; CBDT Instruction of 2011 held to be not retrospective in nature and shall not govern cases which have been filed before 2011.

The Karnataka HC had accepted assessee's stand that in view of Instruction No. 3 dated February 9, 2011 issued by the CBDT, the Revenue should not have filed an appeal before HC as the tax effect did not exceed the specified monetary limit of ₹10 lakh. Ruling in favour of assessee, the HC had held that CBDT Instruction No. 3/2011 which laid down monetary appeal filing limits for Revenue's appeals was applicable to pending cases also. Aggrieved, Revenue filed an appeal before the SC.

SC relied on co-ordinate bench ruling in *Suman Dhamija* [Civil Appeal Nos.4919-4920/2015] wherein it was held that Instruction/Circular dated 9.2.11 was not retrospective in nature and shall not govern cases which have been filed before 2011, and that, the same will govern only such cases which are filed after the issuance of the aforesaid instructions dated 9.2.2011.

SC opined that Central Board Of Direct Taxes [CBDT] cannot issue any circular having retrospective operation.

SC thus set aside Karnataka HC's ruling and remitted the matter back to the HC for re-adjudication on merits and in accordance with law.

LD/66/66

Jaya Balajee Real Media Pvt. Ltd.
vs.
Prin. Commissioner of Income Tax
11th October 2017

HC orders release of excess cash seized after adjustment towards payment of tax, surcharge and penalty under the Pradhan Mantri Garib Kalyan Yojana Scheme, 2016

[1] *Contributed by CA. Sahil Garud, CA. Mandar Telang, Indirect Taxes Committee, Committee on International Taxation, Insolvency and Bankruptcy Laws Group, Disciplinary Directorate and ICAI's Editorial Board Secretariat.*
Readers are invited to send their comments on the selection of cases and their utility at eboard@icai.in. For full judgment, write to eboard@icai.in

The assessee had deposited ₹40 crore during the demonetisation period into its current account with Canara Bank. Pursuant to search operation conducted, ₹36.97 crore lying in the current account of the assessee was seized. Subsequently, the assessee agreed to disclose ₹20 crore under the PMGKY Scheme.

The PMGKY Scheme mandated two conditions to be satisfied before a declaration in Form-I could be accepted from a person willing to come under the scheme: (i) payment of 30% of the income disclosed under the Act towards tax, payment of 10% of the undisclosed income as penalty and payment of 33% of the tax towards surcharge and (ii) the deposit of 25% of the declared income in RBI Bonds.

Subsequently, HC passed the interim order with the direction to the Revenue to appropriate 75% of the amount towards tax, surcharge and penalty and RBI bonds. Accordingly, Government adjusted ₹15 crore towards payment of taxes/penalty/RBI bonds investment under the PMGKY out of ₹20 crore income declared. Thereafter, the assessee filed a letter to the Revenue to release the balance 25% of the disclosed amount i.e. ₹5 crore on the ground that once the income was declared, there could be no claim on it by the Department. The Revenue rejected the assessee's claim on the ground that since the seizure was made u/s. 132B, the assessee was not entitled to the release of amount of ₹5 crore when the declaration was made under PMGKY scheme after seizure. Aggrieved, the assessee filed the Writ Petition before the HC.

HC observed that all the preconditions of PMGKY declaration were satisfied by assessee. HC observed that though the assessee should have filed a Miscellaneous Petition to the earlier Writ Petition instead of filing the new Writ Petition, in order to avoid the multiplicity of proceedings, the HC proceeded to decide the matter.

HC considered Revenue's contention that in view of Section 132B, assessee was not entitled to the release of ₹5 crore, especially when the declaration under the PMGKY Scheme was made after the seizure. However, it observed that if the declaration of the Petitioner was accepted under PMGKY Scheme, the department would have to release ₹5 crore and RBI bonds of ₹5 crore to the Petitioner. Further, even if the declaration was not accepted, the assessee would lose 70% of the amount seized but 30% would have to be returned. Thus, HC noted that no prejudice was caused to the Revenue, HC accepted the assessee's prayer for mercy on the ground that since the entire account was dried up, the assessee was not even in a position to pay salaries to their employees and release of feature films was also stuck.

Thus HC directed the Revenue to release an amount of ₹5 crore to the Petitioner within 2 weeks and to keep RBI bonds as security until the declaration filed under PMGKY scheme is accepted.

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LD/66/67

Prin. Commissioner of Income Tax

vs.

Nila Baurat Engineering Ltd.

11th October 2017

Section 80IA(4) deduction allowed to assessee company entrusted with the road project by Government on BOT basis, despite assessee assigning the task of maintenance and toll collection of the road to third party after completion of construction work.

The assessee is engaged in the business of civil construction and installation of various infrastructure projects. It was entrusted with a road project under build, operate and transfer ('BOT') basis by the State of Rajasthan. After completion of the construction work, the assessee assigned the task of operating and maintaining including collection of toll of the road for a period of one year to a third party. The third party was supposed to pay lump sum amount of ₹328 lakh to the assessee irrespective of actual toll collection. The third party claimed deduction on its profits arising out of toll collection activity under the provisions of Section 80IA(4). On its profit derived from the payment by RTIL, the assessee claimed deduction under Section 80IA(4) of the Act. The Tribunal by the impugned judgment allowed the claim.

Revenue had reopened the assessment of assessee u/s. 147 on the ground that as per proviso to Section 80IA(4), once the assessee had transferred the infrastructure facility for maintenance and operation, the assessee could not claim any deduction u/s. 80IA(4) and the third party which was maintaining and operating the infrastructure facility could claim the deduction. ITAT held that the assessee was eligible for deduction u/s. 80IA(4). Aggrieved, the Revenue appealed before Gujarat HC.

HC perused the provisions of Section 80IA and noted that deduction is allowed to any enterprise

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carrying on any business of developing, or operating and maintaining, or developing, operating and maintaining any infrastructure facility fulfilling the conditions specified therein. Admittedly, the assessee fulfilled the conditions u/s. 80IA(4).

HC observed that where any infrastructure facility is transferred to another enterprise for the purpose of operating and maintaining such facility in accordance with the agreement of the Central or State Government or the local or statutory authority, the section would apply to the transferee enterprise as if it were the enterprise to which this clause applies and the deduction from profits and gains would be available to such transferee enterprise for the unexpired period during which the transferor enterprise would be entitled to the deduction, had the transfer not taken place.

As per HC, proviso to Section 80IA(4) makes an enabling provision providing a deeming fiction whereby upon transfer of any infrastructure facility for the purpose of operating and maintaining, the transferee could claim the deduction for the remainder of the period. By virtue of the proviso, the transferee would step in the shoes of the transferor for the limited purpose of operation and maintenance and claim deduction on the profit element arising out of such activity. HC further observed that the provision of Section 80IA(4) itself envisages that in a given project, the developer and person who maintains and operates may be different.

HC held proviso to Section 80-IA(4) does not operate as to deprive the developer of the benefit of the deduction even after the facility is transferred for the purpose of maintenance and operation but would split the profit element into one derived from the development of the infrastructure and that derived from the activity of maintenance and operation thereof.

HC thus ruled in favour of assessee and held that the amount of ₹328 lakh per annum to be received by assessee from the third party would be relatable to infrastructure development activity and would qualify for deduction u/s. 80IA.

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LD/66/68

Virbhadra Singh (HUF)

vs.

Prin. Commissioner of Income Tax

5th October 2017

HC upheld revision u/s. 263 in case of HUF of Virbhadra Singh; noted that AO failed to apply his mind and conduct proper inquiry while accepting assessee's revised return declaring agricultural income 1872% higher than original return.

The assessee filed a return of income for disclosing agricultural income of ₹5 lakh which was enhanced to ₹2.81 crore by filing a revised return. The revised return was filed pursuant to notice u/s. 143(2) for assessment. Assessee's return was accepted in the scrutiny assessment proceedings u/s. 143(3). CIT held that AO erred in accepting the revised return regarding agricultural income and invoked provisions of Section 263. The agricultural income was thereafter treated as undisclosed income u/s. 68. CIT(A) and ITAT ruled in favour of Revenue.

Aggrieved, assessee filed an appeal against ITAT order before HC.

HC observed that assessee made investments in LIC policies which were in excess of income declared. HC noted that the AO did not examine as to whether gross mismatch in the income was on account of any bonafide omission or a mistake which caused the filing of revised income. The order was conspicuously silent on this aspect. The entire receipt of agriculture income of ₹2.81 crore was in cash. Agricultural income was disproportionately high only in the year under consideration and not in preceding and following years. The validity of the return, fulfilling the condition prescribed under Section 139(5) was not examined, more so in the factual backdrop when the revised return came to be filed only after issuance of notice for scrutiny.

HC held that order passed by AO was without application of mind and resulted in loss of revenue, thus was erroneous and prejudicial to the interest of Revenue. HC thus affirmed invoking of Section 263 by the CIT.

HC observed that ITAT didn't err in accepting the additional evidence placed on record by the Revenue. HC observed that CIT's powers u/s. 263 are wide enough to modify, cancel or direct fresh assessment in case of 'no inquiry' and that the AO should have conducted complete and proper inquiry of assessee's return which declared an income of 1872% higher than original income.

On the issue of whether the ITAT was right in accepting documents submitted by Revenue as additional evidence, HC observed that when the matter was being adjourned for about one and a half year, Revenue made certain submissions before ITAT which were accepted as additional evidence. HC noted that the additional evidence was accepted to support CIT's view. HC stated that additional

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X	100	1 Hr 15 Min	(I) Social Studies (Economics) (II) Mathematics (III) Business Awareness (IV) Aptitude	Online/Pen & Pencil	0.25	100	Objective - type (Multiple Choice) questions
XI	100	1 Hr 15 Min	(I) Business Studies (II) Accountancy (III) Economics (IV) Aptitude	Online/Pen & Pencil	0.25	100	
XII	100	1 Hr 15 Min	(I) Business Studies (II) Accountancy (III) Economics (IV) Aptitude	Online/Pen & Pencil	0.25	100	
B.Com/BBA /BMS/ Allied Subjects Part I, Part II & Part III Examination	100	1 Hr 15 Min	(I) Business Studies (II) Accountancy (III) Economics/ Financial Studies (IV) Aptitude	Online/Pen & Pencil	0.25	100	

Date Timings for the aforesaid test :

Class X/XI/XII & B.Com/BBA /BMS/Allied Subjects Part I, Part II & Part III	Level-I (Online test) 7th January, 2018 (Sunday)	Level-II Test : Online or Pen Pencil Mode in the designated test centre 21st January, 2018 (Sunday)
Part I	11.45 AM to 1.00 PM	**For Class X/XI/XII** 10:30 am. To 11.45 a.m.
Class XI /B.Com/BBA/BMS/Allied Subjects Part II	2.00 PM to 3.15 PM	**For B.Com/BBA/BMS/Allied Subjects Part I/Part II/Part III** 3.00 p.m. to 4.15 p.m.
Class XII/B.Com/BBA/BMS/Allied Subjects Part II	4.15 PM to 5.30 PM	

Prizes for Participants

Level-I Test

- All participants In Level-1 test will receive a Participation Certificate.

Level-I Test

- 1st Rank holder will be awarded with Rs 75,000/- for Class X, Class XI& Class XII, B.Com/BBA/BMS/Allied Subjects Part I, Part II & Part III separately, if multiple winners are there, the prize amount will be shared by them. If more than 50 joint rank holders for the same, the awardee will at least awarded with the cash prize of Rs 2,000/-.
- 2nd Rank will be awarded with Rs 50,000/-for Class X, Class XI & Class XII, B.Com/BBA/BMS/Allied Subjects Part I, Part II & Part III separately, if multiple winners are there, the prize amount will be shared by them. If several joint rank holders for the same are there, the awardee will at least awarded with the cash prize of Rs 1,500/-
- 3rd Rank will be awarded with Rs 25,000/-for Class X, Class XI& Class XII, B.Com/BBA/BMS/Allied Subjects Part I, Part II & Part III separately, if multiple winners are there, the prize amount will be shared by them. If several joint rank holders for the same are there, the awardee will at least awarded with the cash prize of Rs 1,000/-.
- Top 250 consolation prizes will be awarded worth Rs 500/- for Class X, Class XI & Class XII B.Com/BBA/BMS/Allied Subjects Part I, Part II & Part III separately.
- Appreciation certificate to the candidates who have secured 50% marks in the aforesaid online test.
- Participation Certificate will be given to each participant appeared for the Level-II Test.

Other Important Dates:

Award Ceremony: Award Ceremony will be held at Delhi NCR/Mumbai tentatively in the month of February, 2018

ICAI/Test Management Committee reserves the right to change in any of the modalities cited above.

Deputy Convener
Career Counseling sub-group under BoS, ICAI

Convener
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For any Query please contact :
Dr. Sambit Kumar Mishra, Secretary
Career Counselling sub-group under BoS, The Institute of Chartered Accountants of India
ICAI Bhawan, A-29, Sector 62, Noida (U.P.) - 201309
Telephone (O): 0120-3876871, 886 Email: ccc.events@icai.in, ccc.secretary@icai.in

evidence can be accepted on record in view of SC ruling in *K. Venkataramaiah* [AIR 1963 SC 1526], wherein it was held additional evidence can be taken on record in order to pronounce judgement in a more satisfactory manner.

HC concluded that CIT's powers u/s. 263 are wide enough to modify, cancel or direct fresh assessment in case of 'no inquiry'. HC stated that AO should have conducted complete and proper inquiry of assessee's return which declared an income of 1872% higher than original income.

HC further observed that the definition of term record u/s. 263(1)(b) is inclusive and it would include all records relating to any proceeding under the Act, be that of the Assessee or a third party, available at the time of examination by the Commissioner. The record need not pertain to the proceedings of the Assessee alone, be it for the relevant year or assessments pertaining to other years. It can also pertain to any other assessee. In fact, record of any proceedings under this Act available at the time of examination can be considered. Such record need not be placed by the parties. He has power to call for and examine the record of any proceedings under this Act.

Thus, HC ruled in favour of Revenue.

LD/66/69

Commissioner of Income Tax (TDS)
vs.
Vodafone Mobile Services Limited
18th September 2017

Proviso to Section 254(2A) requiring ITAT to dispose the appeal within 4 years is directory and not mandatory; Stay will not stand automatically vacated under the third proviso to Section 254(2A), unless ITAT records a finding that the assessee was responsible for the procrastination of the hearing of the appeal

Revenue had come up with the instant appeal, challenging the order of ITAT granting extension of stay beyond the period of 365 days.

Delhi HC in *Pepsi Foods Pvt. Ltd.* [CIT (2015) 57 Taxmann.com 337] struck down the third proviso to Section 254(2A) as unconstitutional. The matter was carried on appeal to the SC and by the time, the delay was condoned and the SLP was taken up for admission, the Tribunal disposed of the main appeal. Therefore, the SC in *Pepsi Foods (P) Ltd.*, closed the SLP leaving the question of law on the interpretation of the third proviso to Section 254 (2A) open to be decided in appropriate cases.

Section 254(2A) provides that ITAT should wherever possible, may hear and decide the appeal within the period of 4 years from the end of FY in which such appeal is filed. The first proviso to Section 254(2A) gives power to ITAT to grant stay for a period not exceeding 180 days from the date of stay order and states that ITAT shall dispose of the appeal within the stay period. Second proviso grants power to ITAT for extension of stay where the appeal is not disposed of within the period of stay while also stating that aggregate period of stay cannot exceed 365 days. Further, the third proviso states that if such appeal is not so disposed of within the period allowed under the first proviso or the period or periods extended or allowed under the second proviso, which shall not, in any case, exceed three hundred and sixty-five days, the order of stay shall stand vacated after the expiry of such period or periods, even if the delay in disposing of the appeal is not attributable to the assessee.

HC observed that after having imposed an obligation under sub-Section (2A) of Section 254 upon the Appellate Tribunal to decide an appeal within a period of four years, we do not know how the Parliament thought it fit to penalise the Assessee with the stay order getting vacated on account of the failure of the ITAT to dispose of the appeal within one year.

HC observed that the phrase used in the said provision is 'wherever it is possible' which implies that the Parliament had thought it fit not to make it mandatory for ITAT to dispose of the appeal within 4 years. Therefore, it was rightly held that obligation to dispose of an appeal within 4 years u/s. 254(2A) is only directory and not mandatory. If the obligation to dispose of an appeal within a time frame is only directory and not mandatory, the obligation under the proviso to dispose of an appeal within 1 year, cannot be said to be mandatory and the proviso will have to be read only as an exception to the main provision.

HC held that the applicability of the third proviso, has to be understood with two clear prescriptions on caveat which are: (1) that the third proviso has to be understood primarily as directory and not mandatory; (2) that in individual cases where the Tribunal finds that the Assessee is responsible for procrastinating the decision of the appeal, the Tribunal should vacate the stay at its discretion. HC held that stay will not stand automatically vacated under the third proviso to sub-Section (2A) of Section 254, unless the Tribunal records a finding that the Assessee was responsible for the procrastination of the hearing of the appeal.

Ruling as above, HC directed the ITAT to take up the appeals for disposal and dispose of the same within a period of three months from the date of receipt of this order. HC directed continuance of interim stay which was already granted.

LD/66/70
Vijay Vishin Meghani
vs.
DCIT
19th September, 2017

Bombay High Court condones delay of 2984 days in filing appeal to ITAT and also reprimands ITAT, Mumbai's unwarranted observations on chartered accountants

Background

The assessee, Mr. Vijay Vishin Meghani, was working with a German Bank as a Mumbai Representative. He was rendering his services from India to the foreign bank and, accordingly, he claimed deduction under Section 80-O of the Income-tax Act, 1961. The claim for deduction under Section 80-O was disallowed by the Assessing Officer for the A. Y. 1993-94 and the disallowance was confirmed by the Commissioner of income-tax (Appeals) [CIT(A)]. Against this order of the CIT(A), the assessee preferred an appeal before the Tribunal, i.e., ITAT, Mumbai.

In respect of the claim for deduction under Section 80-O for A.Y. 1994-95 and A.Y. 1996-97, which were disallowed by CIT(A) vide orders dated 01.02.2000, the assessee was advised by his chartered accountancy firm not to appeal before the Tribunal but to move a rectification application before the Assessing Officer, after adjudication of the appeal for the A.Y. 1993-94, in order to bring his assessment order for these years in conformity with the decision of the Tribunal relating to A.Y. 1993-94.

However, after continuous follow up with the department regarding the disposal of his rectification application, the same was finally rejected by the Assessing Officer, after a substantial period of time. Thereafter, the assessee was advised by another chartered accountant to file appeals before the Tribunal against the initial orders of the CIT(A) dated 01.02.2000 together with an application for condonation of delay of 2,984 days. The assessee supported the application for condonation of delay with an affidavit from his erstwhile chartered accountancy firm confirming that he was their client for the period from 1997 to 2006 and was advised by them to file a rectification application instead of appeal. It was this endorsement from the assessee's erstwhile chartered accountancy firm, which, according to the assessee, enabled him to seek condonation of delay. Every single aspect of the matter was highlighted, including the legal principles, before the ITAT, Mumbai, which, however, passed an order dated 20.08.2014 refusing to condone the delay of 2,984 days in filing the appeal.

Observations of the ITAT Mumbai

In the said order, the Tribunal noted that the question of rectification of assessment order for A.Y. 1994-95 does not arise since the Assessing Officer had allowed the deduction under Section 80-O and the deduction was disallowed in the order of CIT(A). Further, under the principle of doctrine of merger, an assessment order would merge with the order of CIT(A) in respect of the issues decided by the first appellate authority and hence, the question of rectification of assessment orders of both the years under consideration on the impugned issues, after receipt of the first appellate orders would not arise at all. In this background, the Tribunal remarked that chartered accountants are generally aware of these principles and proceeded to pass an order dated 20.08.2014 refusing to condone the delay in filing the appeal by 2,984 days.

In paras 9 to 9.6 of the said order, the Tribunal has made certain observations on chartered accountants, the scheme of education and training of ICAI, its CPE programs. While the Tribunal has initially lauded the strict training methodologies adopted by ICAI and its high standards, maintained through its vast and versatile curriculum, tough examination pattern and continuous updation of its curriculum, it has, in para 9.6, criticised the deteriorating standards of some chartered accountants in profession, and urged the ICAI to take note of these emerging alarming practices and take appropriate corrective steps to stop the same on war footing.

Filing of Miscellaneous Application by ICAI before ITAT Mumbai

The said matter was considered by the Council of ICAI at its meeting held on 15.09.2014. The Council unanimously felt that the comments made by ITAT, Mumbai on the profession and functioning of the ICAI were neither warranted as no facts relating to the profession were before the Tribunal nor was any opportunity of being heard given to ICAI in the said matter. The Council felt concerned that, on the basis of the opinion given by one of the members, general comments have been made by the Tribunal in respect of the standards of the entire profession. The Council deliberated on this matter and concluded that the sweeping observations made by ITAT, in its order, about the Institute and the profession of chartered accountancy in a matter relating to a particular tax payer, were not warranted and were totally out of context.

The Council underscored that the Institute is conscious of its responsibility to regulate the conduct of its members and whenever it comes across any lapse, the same is being appropriately dealt with under the disciplinary mechanism of the Chartered Accountants Act, 1949. The Council reiterated its respect for the judicial system in the country, including the ITATs. However, it was decided to take up the instant matter with appropriate authorities for expunging the aforesaid remarks made against the profession.

Accordingly, the ICAI filed Miscellaneous Application No. 72 and 73/Mum/2015 before the ITAT Mumbai submitting that certain observations made by it in its order dated 20.08.2014 in the case of the above assessee constituted a mistake apparent from record and hence, the order needed to be rectified under Section 254(2). In the said application, the ICAI has pointed out that the Tribunal had made certain observations about the chartered accountancy profession, the conduct of some of the students pursuing the chartered accountancy course and also about the ICAI in paragraphs 9 to 9.6 of its order, which were not warranted and did not relate to the issues to be addressed by the Tribunal in that case. The ICAI further contended that the Tribunal's observations were being interpreted by the public at large in a manner which affects its reputation.

Modification of para 9.6 of the order by the Tribunal to reflect the true intent

The ICAI was successful in getting the appropriate modification of the relevant para of the impugned judgement of ITAT Mumbai dated 20.08.2014. The Miscellaneous Application was disposed of by the Tribunal at its hearing on 04.09.2015 clarifying that none of the observations made by it in the said order was intended to criticise or should be construed as criticising the functioning of ICAI, further adding that the Tribunal had, in the said order, applauded the strict standards followed by the ICAI in imparting education and training. The Tribunal clarified that its observations on the later part of para 9.6 was intended to highlight or reiterate the importance of the articleship training and the self-study model conceived by ICAI. Such observations were intended only to give a wake-up call to the students pursuing chartered accountancy profession. The Tribunal, appreciating that its observations have not been conveyed as intended, modified para 9.6 of its order, by exercising its inherent powers of rectification under Section 254(2), as follows -

"9.6 However, if it is considered for a moment that the above said C.A. firm has really given such advice to the assessee herein and accordingly it has furnished the letter and affidavit, then it is a cause of concern to one and all. We have already noticed that the self study model coupled with 'on-site articled clerk training' embedded in the Chartered Accountancy course aims to achieve high quality education and training. The articled clerk training conceptualised in the C.A. education inculcate the habit of thinking, self-introspection, application of mind, analytical ability etc and they enable the C.A. students to have strong grip over the subjects and help achieving expertise in the domain fields. The commendable feature of the C.A. Course is that, as stated earlier, the C.A. students are given training by practicing Chartered Accountants during their articled clerk training program. Thus, the methodology adopted by the ICAI enables the C.A. students to become thorough professionals with versatile knowledge and innovative mind. The practical training given by the practising Chartered Accountants during the articled clerk period, in our view, is the fulcrum centre of the study module of the C.A. course and the students pursuing the C.A. course should and must utilise the opportunities provided to them or encountered by them during the articled clerk training period to the maximum possible extent. In the recent past, a number of coaching institutes have been established to give coaching to the students pursuing C.A. course. While the self-study model and articled clerk training may be supplemented with the coaching given by such institutes, any compromise on the practical training intended during articleship period or mere obtaining a C.A. degree without practical training would not make the students full-fledged chartered accountants and the same would go against the self-study model conceptualised by ICAI and there should not be any

doubt that it may have undesired results, which may affect the Country as a whole."

Filing of appeal before High Court by the assessee against order of the Tribunal refusing to condone delay

The assessee, on his part, preferred an appeal before the Bombay High Court against the order of ITAT, Mumbai refusing to condone the delay in filing appeals for A.Y. 1994-95 and A.Y. 1996-97. The substantial questions of law framed by the High Court in this case were two-fold, namely, whether the Tribunal was justified on facts and circumstances and in law in dismissing the two appeals as barred by limitation; and whether the discretion vesting in the Tribunal has been exercised by it reasonably and in accordance with the settled legal principles enabling condonation of delay in filing of statutory appeals.

The High Court observed that the assessee, in the said case, had relied upon the professional advice of a chartered accountant which is the reason for the delay of 2,984 days in filing the appeal. This reason, coupled with the fact that he has acted in a *bona fide* manner and has not been careless or negligent, constituted sufficient cause for condonation of delay.

In para 7 of its judgement, the High Court has criticised the Tribunal for not expressing itself in a manner befitting a judicial body or authority. The High Court opined that the Tribunal should not have departed from the principles of sobriety, restraint and reserve in criticising the conduct of those who are not before the Court or the Tribunal. The High Court further added that this elementary principle should have guided the Tribunal throughout and it is no good that such harsh, strong and adverse remarks have been deleted later on, since the damage was already done.

Furthermore, in para 14 of the said judgement, the High Court observed that the Tribunal had, unmindful of the legal principles which enable a liberal view to be taken of the lapse on the part of the litigant like the assessee, proceeded to pass a twenty-page order. The High Court, in para 15 of the said judgement, inferred that the Tribunal had, out of sheer desperation and frustration and agitated by the fact that the Revenue was not opposing the request for condonation of delay by the assessee, turned its attention towards the assessee's chartered accountant. The Court opined that it was unfortunate that, thereafter, paragraphs after paragraphs in the Tribunal's order were devoted to how a chartered accountant ought to have conducted himself while advising litigants in tax matters; and how he, as a professional, should have been aware that legal proceedings are to be filed in time; and how proper advice should have been given by him, in case there are adverse orders. The Court deduced that it was very unfortunate that the Tribunal had, apart from seeking to advice professionals, blamed not only individual chartered accountants but also the ICAI. The High Court concluded by stating that it was unfortunate that Courts of law or Tribunals, which are the last fact finding authorities in this case, had adopted such a course.

Order of High Court condoning the delay of 2,984 days in filing of appeal

The High Court, after perusing the entire order of the Tribunal wherein the conduct of the chartered accountant was questioned and the assessee was faulted for blindly accepting such an advice, remarked, in paras 17 & 18 of its order, that these were not relevant principles in the case on hand before the Tribunal. Relying upon the Apex Court judgement in *M/s. Concord of India Insurance Co. Ltd. vs. Smt. Nirmala Devi and Others AIR 1979 SC 1666* holding that legal advice tendered by a professional and the litigant acting upon it one way or the other could be a sufficient cause for seeking condonation of delay coupled with the other circumstances and factors for applying liberal principles, the High Court held that the said delay can be condoned. The High Court, eventually, felt that an overall view in the larger interest of justice has to be taken and no one should be deprived of an adjudication on merits unless the Court of law or the Tribunal/ Appellate Authority finds that the litigant has deliberately and intentionally delayed filing of the appeal, or that he is careless, negligent and his conduct is lacking in *bona fides*.

The High Court observed that, though the Tribunal was aware of these principles, it was possibly carried away by the fact that the delay of 2,984 days is incapable of condonation, which is not, however, the correct manner of approaching a matter of this nature. In the process, the Tribunal had proceeded to blame the assessee and the professionals and equally the Department. The High Court firmly opined that the Tribunal's order did not meet the requirement set out in law and that the Tribunal had completely misdirected itself and taken into account factors, tests and considerations which had no bearing or nexus with the issue at hand.

The High Court finally concluded that the Tribunal had erred in law and on facts in refusing to condone the delay, since in this case, the assessee had not been at fault as he had not intentionally and deliberately delayed the matter and had a *bona fide* explanation for the delay in filing the proceedings. Accordingly, the High Court, vide its order dated 19.09.2017, held that the delay of 2,984 days in filing the appeal is condonable, subject to payment of costs.

Service Tax

LD/66/71

Roma Henny Security Service Private Limited

vs.

Commissioner of Service Tax

17th October 2017

Service tax demand on sale of airport entry tickets quashed by HC, the levy of which was confirmed by CESTAT by invoking extended period limitation in terms of proviso to Section 73(1).

The assessee was granted licenses by the Airports Authority of India ('AAI') for sale of airport entry tickets to visitors. The assessee was not allowed by the AAI to collect service tax on the entry tickets during the period from 20.09.2004 to 01.03.2005. It was only after grant of such authority that assessee started collecting and depositing service tax from 02.03.2005 onwards.

A show cause notice dated 04.03.2008 was issued to the assessee for its failure to collect service tax during the period from 10.09.2004 to 01.03.2005 by invoking the extended period of limitation under clause (d) of the proviso to Section 73(1) of Finance Act. An adjudication order was passed on 06.05.2009 wherein it was held that failure of the assessee to pay service tax for the concerned period amounted to non-disclosure of facts, resulting into contravention of various provisions of the Act and said Rules aforesaid with intent to evade payment of service tax and education cess as applicable. CIT(A) confirmed Revenue's demand. CESTAT passed a detailed interim order dated 16.12.2014 while waiving the pre-deposit and stayed the recovery of adjudicated liability during pendency of appeal on ground of contrary views. The CESTAT however passed the final order upholding invocation of extended period of limitation u/s. 73(1) of Finance Act.

HC observed that CESTAT had committed errors. The CESTAT purported to set out para 5 of SC ruling in *P. C. Paulose, Sparkway Enterprises vs. Commissioner of Central Excise & Customs* [(2011) 21 STR 353] whereas it had in fact set out para 5 of the CESTAT's order which was in favour of the assessee. As per HC, there was non-application of mind by CESTAT. Further, HC found that CESTAT had failed to note certain important dates and therefore came to the erroneous conclusion that the invocation of extended period of limitation by the Revenue was justified.

HC observed that the period in dispute was September 2004 to March 2005. Under Section 73(1), the assessee had to be served with a notice within 1 year from March 2005, i.e. by February 2006. Within this limitation period, a series of events took place viz., assessee obtained registration and commenced collecting and depositing service tax, assessee replied to the summons in November 2005. Thus as per HC, this was indicative that Revenue ought to have proceeded u/s. 73(1) within the period of 1 year. As per HC, there was no question of the assessee suppressing any material facts regarding the sale of entry tickets and its failure to collect service tax thereon. HC remarked that the assessee was right in questioning the invocation of the extended limitation period since the facts were known to the Revenue before 1 year period from March 1, 2005 expired.

Thus, HC ruled in favour of assessee and held that order of CESTAT was without application of mind. HC also set aside the orders and show cause notice of lower authorities.

LD/66/72

Commissioner of Central Excise and Service Tax vs. Karnataka Soaps & Detergents Ltd.

12th October 2017

Agarbathi perfumes (odoriferous compound applied to complete agarbathi manufacture) held to be excisable by Supreme Court; Actual marketing of goods is irrelevant to hold a product excisable/dutiable.

Assessee manufactures agarbathi perfumes in its Bangalore factory and then transferred to their Mysore factory where finally it is applied on raw agarbathis. Till the year 2001, the assessee paid excise duty on odoriferous compounds as this substance was covered under Chapter sub-heading 3302.90 of the First Schedule to the Central Excise Tariff Act, 1985. The Central Government vide its Circular No. 495/61/99-CX.3 dated 22.11.1999 clarified that odoriferous substance, not capable of being bought and sold in the market in the normal course of trade, is not excisable. Consequently, the assessee transferred the odoriferous compounds to its Mysore unit on stock transfer basis and some of the compound was sold to M/s Tibetan Handicrafts Centre.

As per Revenue, the assessee was liable to pay excise duty along with penalty and interest on goods transferred. CESTAT ruled in favour of assessee and set aside the said orders to the extent of the demand of duty, interest thereon and the penalty imposed on the assessee for which there was no evidence of sale. Being aggrieved by this, Revenue filed an appeal before SC.

SC observed that the concerned Circular was issued in the context of dispute with regard to dutiability/excisability of mixture, viz. aromatic chemicals (perfumes) which is also classifiable as odoriferous compound, under Central Excise Tariff and comes into existence during the course of manufacture of agarbathis, in a continuous process, as an intermediate product. The Circular clarifies that odoriferous substances are not marketable because these products are not sold by manufacturers in order to protect their trade secret. SC observed that Circular by way of illustration also clarified that the whole process of manufacturing Agarbathi is normally carried out in a continuous manner and since the whole process is continuous and these odoriferous substances do not remain with the manufacturer to be sold in the market.

SC observed that assessee does not manufacture Agarbathi as per general practice. The perfumery compound manufactured in its Bangalore unit was transported to its Mysore unit where it is finally applied to raw Agarbathis to complete the manufacturing process of Agarbatti and this process of manufacturing the perfumery compound is capable of being sold in the open market.

SC observed that the concerned circular cannot be equated with that of an exemption notification but is required to be read within the limited scope of its context in which it was issued. SC further observed that marketability is decisive test for dutiability and that whether the goods are marketed or not is of no relevance and even if the goods are available from only one source or from a specified market, makes no difference so long as they are available for purchasers. As per SC, the fact that goods are not in fact marketed is of no relevance. So long as the goods are marketable, they are goods for the purposes of Section 3 of the Act. Further, it is also not necessary that the goods in question should be generally available in the market. The marketability of articles does not depend upon the number of purchasers or on issue of whether the market confined to the territorial limits of this country.

SC observed that for excise duty to be chargeable under the constitutional entry read with Section 3 of the Central Excise Act, two prerequisites are necessary viz., (1) there must be “manufacture” which is understood to mean the bringing into existence of a new substance; (2) The word “goods” necessarily means that such manufacture must bring into existence a new substance known to the market as such which brings in the concept of marketability in addition to manufacture.

SC observed that perfumery compounds are capable of being sold in the open market and the odoriferous compound [Agarbatti perfumes] has got a shelf life and capable of being stored/transported/ sold and bought by agarbathi industries. It was also observed that assessee was also selling the same to a third party M/s Tibetan Handicrafts Centre Bylkuppe, Mysore District.

SC thus ruled in favour of Revenue holding Agarbatti perfumes to be excisable.

LD/66/73

M/s Historic Resort Hotels Pvt. Ltd.

vs.

Commissioner of Central Excise, Jaipur-II

Where services are procured on behalf of group companies and expenditure is incurred by one which is thereafter shared with other group companies; such arrangement cannot be said to be taxable under the category “Business Auxiliary Service”.

Facts:

The appellant and group companies are engaged in the hotel business. As per the terms of Memorandum of Arrangement amongst the group companies, the appellant incurred general business promotion expenditure for all the group companies which were later shared in proportion of their respective turnover. Revenue alleged that the appellant acted as the procurer of various services that promoted the business for the group companies and merely because the expenditure was shared by the appellant without profit the relationship between the appellant and the group companies of service provider and service recipient cannot be denied. It was submitted by the appellant that the services provided by third parties were actually availed by the group companies and the appellant only incurred the expenditure on behalf of them which was later recovered. It was further contended that the expenditure was recovered without any profit element and such sharing of expenditure will not attract service tax liability.

Held:

Tribunal observed that the appellant per se is not engaged in the business of sales promotion of its group companies. There is no scope for tax liability in the present arrangement where the expenditure is borne by the appellant and thereafter shared with the other group companies for services provided by third parties. In this regard, reference was made to the decision of the Apex Court in the case of *Gujarat State Fertilizers and Chemicals Ltd. and Anr. vs. CCE* wherein it was held that sharing of expenditure for common facilities cannot be treated as service by one to another. Reference was also made to the decisions of *Old World Hospitality Limited vs. CST, New Delhi* wherein it was held that the intent of the agreement was to create a common pool of resources for running and maintaining common facilities and therefore, no service provider service recipient relationship exists. Further in the case of *Reliance ADA Group Pvt. Ltd. vs. CST, Mumbai-IV,* it was held that in terms of the agreement among the group companies, the appellant acted as a manager based on the understanding that the cost would be distributed and borne by the group companies. It was further observed by the Tribunal that exact description of the service sought to be taxed has not been identified in the original order. The decision of *Ruchi Strips & Alloys Ltd. vs. CCE, Indore* was referred to in this regard wherein it was held that the impugned order is not sustainable as it did not discuss the legal scope of tax entry applicable.

Accordingly, it was held that there is no taxable service in the arrangement of sharing of business promotion expenditure among the companies.

LD/66/74

Arafaath Travels Pvt. Ltd.

vs.

Commissioner of Service Tax, Chennai

Tribunal held that saving of foreign exchange outflow is akin to receipt of monies in convertible foreign exchange and therefore, the amount which is receivable as commission retained out of the sale proceeds to be remitted to the principal shall be considered as payments received in convertible foreign exchange.

Facts:

In this case, the question before the Tribunal was whether the service rendered by the Appellant can be treated as 'Export of Service' in light of the condition that the receipt of payment should be in convertible foreign exchange. The facts of the case are as follows:

The Appellant provided services as a General Sales Agent to Saudi Arabian Airline Limited (Saudia) in terms of an agreement executed in Saudi Arabia for which it received normal as well as overriding commission. The scope of the services included *inter alia* soliciting, promoting, selling passenger air transportation for Saudia and assistance in all transactions likely to encourage air traffic contracted for a limited territory within India. It was alleged by the Department that such overriding commission received was taxable under the category 'Business Auxiliary Service' and cannot be considered as export of service in light of the provisions of Rule 3(3) of the erstwhile Export of Service Rules, 2005 as the services are provided within a limited territory in India. It was further contended that the overriding commission that was deducted in INRs out of the entire proceeds remittable was in violation of the condition that receipt should be in foreign currency stipulated by the said Rules. Appellant rebutted the claim of the Department by contending that the services are covered under the category "Business Auxiliary Services" and in view of the Export of Service Rules, 2005 it shall be considered as export of services as the recipient is located outside India and the services are 'used' outside India since the principal enjoys the growth of business outside India. The appellant placed reliance on the decision of the Apex Court in the case of *JB Boda & Co. (P.) vs. CBDT – AIR 1987 (SC) 1543* in support of the contention that even though the commission received is received in Indian Rupees, it should be considered as receipt in convertible foreign exchange.

Held:

In accordance with the conditions in Rule 3(3) of Export of Services Rules, 2005, the Tribunal held that although the appellant has contracted for a limited territory in India the benefits by way of increase in business are received by Saudia Airlines outside India. Reference was made to Circular No. 111/05/2009-ST dated 24.02.2009 which states that for the purpose of Business Auxiliary Services the relevant factor is the location of the service recipient and not the place of performance. In respect of the condition that the payment be received in foreign exchange, reliance was placed on the decision of Hon'ble Supreme Court in the case of *JB Boda & Co. (P.) (supra)* wherein it was held that when the total payment to be remitted in foreign exchange was reduced by the amount of brokerage, it shall be deemed to be received in convertible exchange. Reliance was also placed on the decision of the Hon'ble Madras High Court in the case of *Suprasesh General Insurance Services & Brokers (P) Ltd.* wherein it was held that even though the payments are received in Indian Rupees, there is a saving in outflow of foreign exchange and to that extent it can be considered as receipt in convertible foreign exchange. Tribunal also observed that retaining the amount of commission instead of remitting the entire proceeds and receiving the commission in convertible foreign exchange shall have the same end-effect.

Accordingly, it was held that retaining the amount of overriding commission while remitting the proceeds to foreign client and not receiving the same in convertible foreign exchange shall be considered as satisfying the condition that payments should be received in convertible foreign exchange.

Note:

Readers may note that, similar view has been taken by the Hon'ble Bombay Tribunal in the case of *Tristar Shipping Pvt. Ltd. vs. CST.*

LD/66/75

Bentley Systems (I) Pvt. Ltd.

vs.

Commissioner of Service Tax, New Delhi

Assistance/Training provided to the customer/ client of the software would be construed as incidental and ancillary to the sale of software.

Facts:

Appellant is an Information Technology Company engaged in providing IT services. Certain services were provided by the appellant for imparting skill and knowledge to clients/customers to whom the software is sold. It was the contention of the Department that training services provided by the appellant shall be covered within the meaning of "Commercial Training or Coaching Centre Service". On the other hand, the appellant submitted that the training services are provided to educate the client/customer or for assisting in smooth functioning of the software. It is incidental to the sale of software. Reference was made to the decision of the Tribunal in the case of *Commissioner of Central Excise, Chandigarh vs. Punjab Communication Ltd.*

Held:

The Tribunal observed that software provided by the appellant cannot be used by the customer/client unless assistance/training is provided. The decision of the Tribunal in the case of *Punjab Communication Ltd. (supra)* was referred and it was held that such assistance/training would be construed as incidental /ancillary to the sale of software. It shall not be taxed under "Commercial Training or Coaching Services".

International Taxation

LD/66/76

ADIT

vs.

E-Funds IT Solutions Inc.

Supreme Court

Merely having a subsidiary in India which provides services to the foreign principal does not form a Permanent Establishment in India

Facts and background of the case

E-Funds IT Solutions Inc. ('the assessee') is a company incorporated in the USA and the group is involved into the business of ATM management services, electronic payment management, decision support services and risk management and global outsourcing and professional services.

The assessee along with it's another group company E-Funds Corporation entered into service contracts with their customers for the provision of IT Enabled Services. This work was further subcontracted to E-Funds International India Private Limited ('E-Funds India').

As a result of this arrangement, E-Funds India provided back office support services to the US entities. The US entities used the services received from E-Funds India to provide the ITES to their ultimate customers. Accordingly, the transactions entered between the US entities and E-Funds India were in the nature of international transaction and were at arm's length.

However, during the assessment proceedings, the AO observed from the Functions, Assets and Risk ('FAR') analysis that the US entities conducted their business through E-Funds India and hence based on this E-Funds India formed a Fixed Place Permanent Establishment ('PE') of the US entities in India. Consequently the AO determined that the portion of income of the US entities which was not attributable to E-Funds India would be taxed in India.

The Commissioner of Income Tax (Appeals) ('CIT(A)') also upheld the view of the AO. However, he went a step further and concluded that in addition to the fixed place PE, the US entities also had a Service PE and Agency PE in India as per the terms of Article 5 of the India – USA Double Taxation Avoidance Agreement ('DTAA').

The ITAT upheld the CIT(A)'s order and concluded that the E-Funds India formed a Fixed Place PE and Service PE of US entities in India. However, it did not provide its decision on the Agency PE.

The Delhi High Court set aside the ruling of the ITAT and held that the E-funds India did not constitute PE for the US entities in India.

Issues involved in the ruling

1. Whether E-Funds India constituted a Fixed Place PE of the US entities in India?
2. Whether E-Funds India constituted a Service PE and Agency PE of the US entities in India?
3. Whether the representations made in the course of Mutual Agreement Procedure ('MAP') under the India–USA DTAA could be used to justify the creation of the PE in India?

Held

The Hon'ble Supreme Court ('SC') on the various issues held as under:

a. Fixed Place PE

The Hon'ble SC held that the burden to prove that the foreign entities had a PE in India lied on the Income Tax Department. While relying upon its another landmark judgement in the case of the *Formula One Championship Ltd. vs. CIT (Civil Appeal No. 3849 of 2017)* the SC held that a foreign entity would qualify for the fixed place PE in India as per Article 5 of the treaty only if the foreign entity has a place of business at its disposal in India.

In the present case, none of the US entities had any place of business at its disposal in India. The premises in India were not under the disposal or control of the US entities. These entities only had access to the premises in India. Further, the US entities also did not have any physical place of business in India.

The SC further commented that merely because of the fact that there were close transactions with the entity in India, it would not automatically create a fixed place of business for the US entities in India as per Article 5(1) of the India-USA DTAA. Further, the SC also held that the allegation of the AO that since E-Funds India did not bear any significant risk in India, it would form a fixed place PE in India was not tenable as per the provisions of the Act.

The SC further concluded that none of the business activities of the US entities were carried through the subsidiary in India. E-Funds India only provided the back office support services which enabled the US entities to render their services. Accordingly, under this situation it cannot be held that the business of the US entities is being conducted through E-Funds India. Accordingly, the Delhi High Court's ruling that E-Funds India does not form a fixed place PE for the US entities was upheld by the SC.

b. Service PE

The SC in the case of *DIT vs. Morgan Stanley and Co. Inc. (292 ITR 416)* had held that a foreign entity forms a service PE in India only if that entity provides services in India through its employees in India. In other words, the foreign entity forms a Service PE in India if the employees are sent on deputation to India and they remain on the payroll of the foreign entity or they continue to have a lien on their jobs with the foreign entity.

In the present case, the SC observed that one of the requirements of Article 5(2)(l) of the India US DTAA is that the foreign entity must furnish its services within India through its employees or other personnel. In this case, all the customers of the US entities were located in the US itself and none of the customers were in India. Hence, the precondition led down by Article 5(2)(l) of the India-USA DTAA was not fulfilled and accordingly, this did not give any rise to service PE of the foreign entities in India.

Further, for the employees deputed to India, 75% of their salaries were paid by the E-Funds USA, however, the same were reimbursed from the E-Funds India and also seconded employees worked under the control and supervision of E-Funds India. Accordingly, this did not form a Service PE of the US entities in India.

c. Agency PE

The assessee argued that since the Agency PE issue was not touched upon by the ITAT, the SC should not take up the same for its consideration. However, for the sake of completeness, the SC held that under the terms of the agreements entered between the US entities and E-Funds India, the Indian entity was never authorised to conclude any contracts on behalf of the US entities. Also the conditions of agency PE provided under Article 5(4) were not fulfilled and hence, the US entities also did not form Agency PE in India.

d. Mutual Agreement Procedure

The competent authorities of India and the US had initiated proceedings under the MAP article of the India–US Tax Treaty and had entered into an agreement as to attribution of profits between the US entities and E-Funds India.

The Department contended that the PE issue stood determined owing to certain statements made in the MAP Settlement Agreement to the effect that the US entities had PEs in India. It was argued that these statements should continue to remain applicable to the E-Funds Group as there had been no subsequent change in the factual position of the Group.

On this point, the High Court had concluded that MAP proceedings had been initiated on a without prejudice basis and that the existence of a PE was a question of law that needed to be determined purely on merits. Referring to Paragraph 3.6 of the OECD Manual on MAP Procedure, the Supreme Court observed that it was "very clear" that a MAP Settlement Agreement was time and case specific and could not be considered precedent for subsequent years. Thus, statements made in a MAP Settlement Agreement for a previous year could not be used in determining PE status for a subsequent year.

LD/66/77
Sedco Forex International Inc.
vs.
CIT
(Supreme Court)

SC explains interplay between the charging provisions and the presumptive taxation scheme.

Facts and Background of the case

The assessee was a non-resident ('NR') entity who had entered into contract with Indian oil exploration companies for supply of drilling unit for carrying out oil exploration activities in India.

Under the contract, the assessee apart from payment for supply of drilling units/rigs on hire, operating charges and other services, also earned mobilisation fees for movement of drilling unit from a foreign country to an offshore site in India.

The assessee opted to be governed by the presumptive taxation regime under Section 44BB of the Income Tax Act, 1961 ('the Act'). While computing the gross revenue to be taxed as per Section 44BB, the assessee declared the taxable income without considering the mobilisation fees for the movement of the rigs.

The assessee was of the impression that the mobilisation fees received were in the nature of the reimbursement of expenses and as the services were rendered outside India and the payment was also received outside India, the said payment was not taxable in India.

During the scrutiny assessment, the AO and the CIT(A) in the appellate proceedings included the mobilisation fees as a part of the gross revenue for determining the taxable profits and gains under Section 44BB of the Act. Further, the ITAT also confirmed the action of the AO and the CIT(A).

During the High Court appeal, the assessee relied upon the ruling of the Supreme Court in the case of *Ishikawajma-Harima Heavy Industries Limited* and argued that the offshore services rendered by the NRs are not taxable in India in absence of a sufficient territorial nexus of such services in India. The High Court distinguished the said decision and held that this decision dealt with the determination of income of the NR in accordance with the charging provisions of the Act whereas in the present case, the mobilisation fees were solely governed by the presumptive taxation system and hence the argument of the assessee was not accepted.

Issue involved in the case

The issue before the SC was whether such mobilisation fees was to be included in the profits while computing the profits and gains as per presumptive basis as per Section 44BB of the Act.

Held

On the charging provisions

The SC held that the HC was not correct in excluding the charging provisions while dealing with the presumptive scheme of taxation.

The charging provisions bring a particular income within the net of income tax. Accordingly, the income can be subject to tax only when the income falls within the scope of charging provisions of the Act.

Under the presumptive scheme, a special provisions/methodology for computation of income is provided to the assessee. However, this does not mean that the charging provisions are not applicable to that income. The presumptive taxation provisions are to be read in conjunction with the charging provisions and not in isolation.

On the mobilisation fees and the objective of the presumptive taxation provisions

The SC held that provisions for Section 44BB were a special provision to simplify the computation of profits and gains of the Taxpayers engaged in the provision of specified services. This scheme overrode the general scheme of computation of income. Section 44BB deems certain receipts to be "profits and gains of business" and hence, it has to be read in conjunction with charging provisions in a manner that a receipt coming within the scope of Section 44BB can be considered to be within the scope of charging provision.

The mobilisation fees was taxable under Section 44BB since it formed part of indivisible contract wherein the assessee received a fixed amount as fees regardless of actual expenses. The mobilisation fees were covered within the scope of Section 44BB since they represent amount paid or payable on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for or extraction or production of mineral oils in India.

As per the SC, the precondition for any kind of receipt is that whether it qualifies to be an "income" within the meaning of charging provisions of the Act. Once the amount under consideration is deemed to be 'profits and gains from business', it becomes income under the charging provisions and Section 44BB also treats the income as earned in India, satisfying the test of deeming charging provisions.

When it is found that the amount paid or payable (whether in or out of India) is covered under Section 44BB, the fiction created under Section 44BB becomes income under the charging provision also.

Hence, such receipt of mobilisation fees was also covered by charging provisions and hence fell within the purview of Section 44BB. Accordingly, the SC held mobilisation fees to be taxable u/s. 44BB which deems 10% of gross amount as "profits and gains of business".

LD/66/78

Black Duck Software Inc.

vs.

DCIT

(Delhi ITAT)

Payment received by the assessee as royalty for granting a non-exclusive, non-transferable software license to Indian customer for a specific time period is not liable to tax in India as Royalty since copyright in said software programme was retained by assessee

Facts and Background:

Black Duck Software Inc. was incorporated under the laws of USA. It was provider of products and services for automating the management, compliance and secure use of open source software in multi-source development at enterprise scale. During the year under consideration, the assessee had sold software under a 'Master License and Subscription Agreement' with two entities in India, namely, (a) Infosys Limited; and (b) Robert Bosch Engineering.

In course of assessment, the Assessing Officer ('AO') concluded that receipts of assessee pertaining to licensing of software were taxable as royalty under Section 9(1)(vi). Thereafter, he proceeded to hold that even under the treaty, the payment received by the assessee was in the nature of royalty within the terms of Article 12(3) of India-USA DTAA.

The DRP upheld the action of the AO.

Issue:

Whether the receipts of the assessee towards the licensing of the software were taxable in India as royalty in India?

Held:

The sole issue involved in this appeal was, whether the payment received by the assessee from supply of software, is taxable in India as royalty in India or not; either under Section 9(1)(vi); or under Article 12(3) of India-USA DTAA or both.

However, the revenue had not taken any stand that if it is not taxed as royalty, then can it be taxed as business income in India and if it is business income then whether there is any PE of assessee in India. There is no rebuttal of assessee's contention that it does not have any permanent establishment in India, therefore, receipts from sale of software will not be taxed as business income in terms of Article 7 of India-USA DTAA. Further, the assessee-company was a tax resident of USA and had sought shelter under India-USA DTAA, therefore, receipts in question had to be seen from the angle, whether such receipts could be held to be taxable, especially as royalty in terms and scope of para (3) of Article 12.

The ITAT observed that from a perusal of the scope of Master License Agreement, it was quite apparent that the assessee provided to its customers a non-exclusive; non-transferable license within the applicable subscription period. The clause dealing with license restriction clearly envisaged that it is not a perpetual license and customer had no right to retain or use the programme after termination of applicable subscription period for any reason. The customers were not permitted any access or use of the programmes for any users other than the user's license paid for by the customer. Though the customer was entitled to make reasonable number of copies of the programme for inactive back up; disaster recovery; failover or archival purposes, however, it has no right to rent; lease; assign; transfer; sub-license; display or otherwise distribute or make the programme available to any third party. The customer was further prohibited to modify; disassemble; decompile or otherwise reverse engineer the programme nor can permit any third party to do so. In other words, the assessee had all the rights not only on the copyright in the software, but also debarred its customers in several ways as highlighted above.

Further, the ITAT observed that the payment, which had been received by the assessee, was purely for copyrighted software product as against payment for giving any right to use any copyright in the software. The customers had a very limited right to access copyright software for its own business purpose and did not acquire any kind of right to exploit the copyright in the software. These facts were uncontroverted in the impugned order. The next question that arose was that based on these facts, whether such action of granting of license to customers can be reckoned as 'royalty' within the scope of Article 12(3) of the India-USA DTAA.

The ITAT was of the view that the main emphasis was on use of or the right to use of any copyright of a literary; artistic; or scientific work, which indicates that an exclusive right to use any copyright in an article (which is in the nature of literary; artistic; or scientific work) has to be given. Since the copyright had not been defined or explained in the treaty, therefore, meaning assigned of the copyright under the domestic law, i.e. Copyright Act, 1957 can be referred for understanding the true purport and meaning of copyright.

As per the ITAT, the definition of 'copyright' in Section 14 was an exhaustive definition and it referred to bundle of rights. In respect of computer programming, which was relevant for the issue under consideration, the copyright mainly consisted of rights as given in clause (b), that was, to do any of the act specified in clause (a) from (i) to (vii) as reproduced above. Thus, to fall within the realm and ambit of right to use copyright the computer software programme, various rights therein must be given and if the said rights are not given then there is no copyright in the computer programme or software.

Further, the ITAT observed that Section 52 of the Copyright Act also made it amply clear that private use including research or to utilise a computer programme for the purposes for which it was supplied or make back-up copies is purely for the temporary protection against loss; destruction or damage in order to utilise the computer programme for the purpose for which it was supplied. This doesn't enlarge the scope so as to reckon it as giving any copyright. Hence under the Copyright Act, no use or right to use of copyright has been given by the assessee to its customers in terms of its licensing agreement.

The ITAT was of the view that the issue whether consideration received for granting of license to use copyrighted software for licensee's own business and whether it can be brought to tax as 'royalty' under Article 12(3) of India-USA DTAA, is no longer *res integra.*

The revenue had tried to canvass a point that in the Supplement Agreement, there is a stipulation of unlimited number of users and unlimited size of managed code base; and also access has been granted to all companies within Robert Bosch group. It has also referred to corresponding managed code base as given in the Master License and Subscription Agreement. The managed code base has been defined in the agreement as code base owned or controlled by the customer, i.e., input into a programme by customer and managed using that programme over the course of the applicable subscription period. Since the software is to be run at an enterprise level, managed code base size has to be kept unlimited but within the organisation and is not meant for the outsiders.

It has been clarified by the assessee that software sold by the assessee was used as antivirus by the customers for entire organisation and access to such software is IP based and was given to the server installed at the customer's place, so that it could be used by the customer and all its employees. It was not the case of the revenue also that software is being commercially exploited by the customers albeit it has to be used only for private use within the organisation.

Based on the review of the agreement, an IP access was given to the Robert Bosch India at an enterprise level. All the employees in India could only use the antivirus software from the said server. If such an access to unlimited users, i.e., employees within the origination is not provided, then the secure software programme would be redundant and would not serve the purpose.

The ITAT observed that in view of the discussion made above, it was held that the payment received by the assessee did not fall within the ambit of 'royalty' under Article 12(3) of India-USA DTAA and hence, the same could be taxed under the terms of India USA Treaty. If the receipts could not be taxed under the treaty as royalty, then it cannot be taxed under the domestic law under Section 9(1)(vi) and accordingly, the ITAT allowed the appeal of the assessee.

LD/66/79
Electrical Material Center Co. Ltd.
vs.
DDIT
(Bangalore ITAT)

ITAT rejects the applicability of Virtual Permanent Establishment ('PE') in the absence of services actually rendered in India

Facts and background:

The assessee, a company resident of Saudi Arabia, received income from an Indian company by rendering certain services through four engineers sent to India. The engineers spent more than 360 man days individually, but their collective stay in India was 90 days only. The Indian company paid the assessee for services provided by the engineers in India.

While filing the return of income in India, the assessee claimed that income from services to the Indian company were in the nature of Fees for Technical Services ('FTS') and, in the absence of a provision on FTS under the Double Taxation Avoidance Agreement ('DTAA'), such income is not taxable in India.

Reliance was placed on the Madras High Court ruling in the case of *Bangkok Glass Industry Co. Ltd. vs. ACIT* in this regard. Furthermore, by placing reliance on the Mumbai ITAT's decision in the case of *Clifford Chance*, it was contended that only solar days should be considered for the purpose of determining the existence of a service PE. Accordingly, as the presence of engineers in India was less than 182 solar days, no service PE was created.

On the other hand, the Tax Authority was of the view that the assessee's income was taxable in India as "royalty" under the Indian-tax Act ('Act'), as well as the DTAA. Furthermore, a PE is created when aggregate man days (360) of stay of the engineers in India are considered.

Issue:

Whether the assessee formed a PE in India and whether the income received by the assessee was taxable in India?

Held:

The ITAT placed reliance on the Mumbai ITAT's decision in *Clifford Chance*, the ITAT held that only solar days are to be considered, and not man days. As the presence of the Taxpayer in India, through its engineers, was less than 182 days i.e., only 90 solar days, there was no service PE.

The previous decision of the Bangalore ITAT on virtual PE was distinguishable on facts as, in the present case, payment was made only for the services rendered through the engineers in India and no service was rendered through virtual modes like email, internet, video conferencing etc.

The ITAT observed that some countries like Saudi Arabia, Israel and Kuwait have come up with specific rules/guidelines on virtual PEs. Furthermore, the Bangalore Tribunal had recently upheld creation of a service PE even when services were rendered through virtual mode.

However, in the present ruling, the ITAT had distinguished its previous ruling on facts as, in the current case, no service was rendered through virtual modes like e-mail, internet, video conferencing etc.

The ITAT was of the view that the income was taxable as FTS, but it was of the view that FTS is general business income and that, in the absence of a specific FTS Article, the same should be covered within the purview of "business profits" and taxable only if attributable to PE in the source country. However, as there was no PE, the said profits could not be taxed as business profits.

Transfer Pricing

LD/66/80
Hyundai Motor India Limited
vs.
Dy. Commissioner of Income Tax
20th October 2017

DRP's order is binding on the AO; Assessment order is an order giving effect to the direction issued by DRP and against such order of assessment, the assessee has effective alternate remedy of filing appeal before ITAT.

The assessee is a wholly owned subsidiary of Hyundai Motor Company, South Korea, and is a manufacturer and exporter of cars. The assessee filed objections before DRP for AY 2012-13 against the draft assessment order. DRP had enhanced assessee's total income by enhancing transfer pricing adjustment. Assessee filed a writ Petition filed before Madras HC contending that TP-adjustment has to be limited to an international cross border transaction and to make any adjustment in any other area or category, which is not an international transaction, namely, imports from non-AE's, domestic sourcing and various other administrative costs is incorrect and not sustainable. The assessee contended that DRP, under the guise of exercising powers u/s. 144C(8), sought to enhance the adjustment by travelling beyond international transaction and making adjustments on non-international transaction including domestic procurement and administrative costs.

Before HC, the assessee submitted that Chennai ITAT in *Mobis India Ltd.* had held that the transfer pricing adjustment should have been restricted to controlled transactions. The Revenue submitted that the assessee is selling product manufactured with parts purchased from AE and the balance from non-AE and when the product is sold, overall profit margin is recorded without any data as to what would be the profit in relation to the purchases from its AE. The Revenue argued that any impact on the basis of calculation of ALP has to be considered as adjustment u/s. 92CA and the same cannot be proportionately reduced by considering that part of the purchases was from non-AE also.

HC observed that directions given by the DRP are binding on the Assessing Officer. Thus, the proceedings before the DRP is not an appeal over the draft assessment order, but an alternate mechanism provided to the assessee, a corrective mechanism. Prior to insertion of Section 144C, assessee could file an appeal to the CIT(A) challenging the assessment order. However, when the matter is referred to the DRP, its directions are binding on the AO. HC distinguished from assessee's reliance on Bombay HC decision in *Firestone International* [60 Taxman.com 235 (Bombay)] on facts. HC noted that in that case the assessee challenged the final assessment order giving effect to DRP directions before ITAT which examined the factual matrix and rendered a finding on how adjustment should be made after recording its finding of facts. HC thus opined that it is essential that the factual matrix has to be gone into before recording a finding as to whether the direction issued by the DRP is proper or not and how the ALP is to be determined.

As per HC, the important thing to be seen is whether the DRP has recorded any factual findings while disagreeing with the TPO with regard to computing quantum of adjustment. HC observed that the DRP considered the facts and gave a direction to TPO to not restrict the TP-adjustment to the proportion of international transactions to total operating costs. HC held that DRP's direction was output of examination of the facts, which is required to be implemented by the AO after which it ripens into an assessment order open to challenge in terms of the provision of the Act.

HC thus held that AO had to pass order of assessment giving effect to the DRP direction and such final assessment order can be challenged by the assessee before ITAT.

HC dismissed assessee's writ keeping open all the issues and noting that assessee can challenge the final assessment order before ITAT.

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LD/66/81

Commissioner of Income Tax

vs.

Jaipur Silver Jewels Private Limited

6th September 2017

Assessee-entity and another entity in which the wife of director of assessee was the sole shareholder, held to be not associated enterprises u/s. 92A; Premises of that other entity being owned by brother of assessee's director, also not a decisive factor.

One Anupama Singh was the sole shareholder of India Gems & Beads entity. She was the sister-in-law of one Shri Vinay Singh who was director of Assessee Company. AO invoked condition enumerated under Section 92A(2)(j) of the Act. Further, the premises of India Gems were owned by one Dharampal Singh who was the brother of Assessee Company's director and that Mr. Vinay Singh or India Bead did not pay anything to Dharampal Singh towards using his premises. The AO held that Assessee Company and India Beads were AEs u/s. 92A of the Act.

In order to ascertain ALP of international transactions, the assessee company was asked to work out the cost of material sold to the said associated concern *vis-a-vis* other concern. AO noted that since sale price of same goods to unconnected parties was available, CUP was the most suitable method of determining the ALP. AO observed that the average sale price of silver portion in the jewellery was the same as in the case of AE and in the cases of other concerns. However, in the case of stones, studded in said jewellery, AO observed that when it was sold to the other concern, the average sale price was shown at ₹40/- per gram, while in case of AE it was shown at ₹8.10 per gram. On this basis, the AO worked out such price of studded stone at ₹2.10 crore instead of ₹42.57 lakh shown by the assessee and worked out TP adjustment of ₹1.67 crore.

CIT(A) deleted the entire addition made by the AO stating that the transactions entered between assessee and India Gems & Beads Inc., USA were not covered u/s. 92A for the purpose of applying ALP.

However, ITAT in its order had upheld the findings of CIT(A) stating that he was justified in holding that transactions entered into between the assessee and India Gems & Beads Inc. (AE) were not international transaction for the purpose of adjustment under ALP. ITAT held that Anupama Singh is not a relative of the Director of the assessee company for the purpose of adjustment under ALP. ITAT concluded that the assessee and India Gems and Beads were not AEs u/s. 92A(2)(j).

Aggrieved, Revenue filed an appeal before HC.

HC held that since sister-in-law is not associated nor relative under the Income-tax Act, in that view of the matter, the provision of Section 92A(2)(m) was wrongly interpreted by the AO.

HC thus upheld ITAT's order and ruled in favour of assessee.

LD/66/82
Bechtel India (P.) Ltd.
vs.
ACIT
(Delhi ITAT)

Interest on delayed realisation of receivables is a separate international transaction and, therefore, requires separate benchmarking

Facts and Background

The assessee executed engineering design and drawing for various overseas Associated Enterprises ('AEs') to support the overseas offices in executing turnkey projects. During the year, the assessee had shown certain receivables from its AE.

The Transfer Pricing Officer ('TPO') noticed that payments against the invoices raised by the assessee were not received within the stipulated time. He further pointed out that the assessee had provided benefit to its AE by way of advancement of interest free loan in the garb of delayed receipt of receivables. He observed that these funds could have been otherwise deployed for at least earning interest income. Therefore, the assessee had incurred cost in connection with a benefit and services provided to the AE by way of delayed receipt of receivable. He pointed out that no payment terms have been specified as per service agreement or the invoice and, therefore, as per prudent estimate payment period of 30 days shall be allowed for payment of sales/service and any delay beyond the aforesaid period would be benchmarked accordingly.

On being called upon to furnish the time period for payment as per service agreement and why the delayed payments be not treated as unsecured loans advanced to the AEs, the assessee submitted that 'receivable was not an international transaction which warranted benchmarking.'

The TPO rejected this contention and held that interest was chargeable at arm's length level in respect of delayed receipt of invoice values. Accordingly, interest rate of 12.60 per cent was adopted for charging of deemed loan advanced for the period of receivables outstanding beyond the period stipulated in the service agreement/invoice. He, accordingly, directed for adjustment on account of Arm's Length Price ('ALP') of the receivables

The Dispute Resolution Panel ('DRP') affirmed the order of the TPO.

Issue:

Whether the interest was to be charged on the delayed receivables from the AEs?

Held:

The ITAT observed in the case of *Ameriprise India (P.) Ltd. vs. ACIT* that non-charging or under charging of interest on the excess period of credit allowed to the AE for the realisation of invoices amounts to an international transaction and the ALP of such an international transaction is required to be determined.

The ITAT observed in the above case that the working capital adjustment is in respect of international transaction of rendering services to the AE. Interest for credit period allowed as per the agreement is given in the price charged for rendering of services. Whereas the non-realisation of invoice value beyond the stipulated period is a separate international transaction whose ALP is required to be determined. Granting of working capital adjustment is confined to the international transaction of rendering of services, whose ALP is separately determinable.

Further, the ITAT was of the opinion that, the international transaction of interest receivable from its AEs for late realisation of invoices beyond such stipulated period is a separate international transaction. Allowing working capital adjustment in the international transaction of rendering of services can have no impact on the determination of ALP of the international transaction of interest on receivables from AEs beyond the stipulated period allowed as per agreement.

The ITAT ruled that in the case of *Mckinsey Knowledge Centre (P.) Ltd. vs. DCIT,* the Tribunal explained that if an invoice is raised during the year and the proceeds are realised within the year, but, beyond the stipulated period of agreement, then, the same will not come within the working capital adjustment because working capital adjustment is made with reference to the opening and closing balances as on 1st April and 31st March. Therefore, following the decision of the Tribunal in the said case, the assessee's contention that the interest on delayed payment of receivables get subsumed in the working capital adjustment allowed to the assessee is to be rejected. The assessee has also advanced an argument that since it was debt free fund company, which finding is not disputed, no interest could be attributable on the late realisation of receivables. This plea is to be rejected at the threshold because, as noted earlier, interest on delayed realisation of receivables is a separate international transaction and, therefore, requires separate benchmarking. It has nothing to do with the operations of the assessee company being with the debt free funds only.

Further the ITAT ruled that as far as the assessee's plea regarding selecting of ad hoc interest rate of LIBOR+400 bps while computing the addition is concerned, that the DRP has directed to compute the adjustment using the rates of six months LIBOR + 400 bps on receivables which are to be paid to the assessee in US $ in accordance with the decision in *Cotton Naturals (I.)(P.) Ltd.* of the Delhi High Court, wherein it has been held that it is the current year in which the loan is to be repaid which determines the rate of interest and, hence, the prime lending rate should not be considered for determining the interest rate.

Accordingly, the ITAT held that the interest on delayed trade receivables was a separate international transaction and hence, the same was to benchmarked separately.

LD/66/83
Elder Exim (P.) Ltd.
vs.
DCIT
(Mumbai ITAT)

Whether the transactions with foreign branch of Indian company were covered under the transfer pricing regime?

Facts and Background

The Assessee purchased raw material in the shape of spliced decorative veneer in flitch form from USA branch of an Indian company (Durian), and also made sale of its finished products to the said concern.

The stand of the assessee was that Durian was a company registered under the provisions of the Companies Act, 1956 and was indeed a tax resident of India and the assessee pointed out that the transaction with USA branch of Durian was a transaction with an Indian resident and that Durian was assessed in India on its worldwide income, being an Indian resident.

The Assessing Officer ('AO') treated the said transaction as 'international transaction' within the meaning of Section 92B. Accordingly, the AO sought to determine the arm's length price of the transaction in terms of Section 92(1).

The CIT(A) confirmed the order of the AO.

Issues

Whether the transactions with the branch of Indian Company were covered under the Transfer Pricing Regulations?

Held

The ITAT observed that the case put up by the assessee has been unjustly brushed aside by the lower authorities.

The ITAT was of the view that Section 92B(1) of the Act referred to an 'international transaction' to be a transaction between two or more associated enterprises, 'either or both of whom are non-residents'.

In the present case, the transactions had been entered by the assessee with the USA branch of Durian. Because the transactions have been entered into with the USA branch of Durian, it was sought to be treated as an 'international transaction' within the meaning of Section 92B(1) of the Act.

The ITAT observed that there was no denying the fact that Durian was an Indian tax resident, being a company incorporated under the provisions of the Companies Act, 1956 in India. As the assessee was also an Indian tax resident, therefore, neither the assessee and nor Durian are non-resident so as to include the transactions between them as 'international transaction' for the purposes of Section 92B(1) of the Act.

The ITAT therefore, held that the lower authorities erred in applying the provisions of Chapter X with respect to the impugned transactions and the transactions between the assessee and the branch of the Indian Company were not an eligible transaction to be covered under the Indian Transfer Pricing Regime.

Insolvency and Bankruptcy Code

Mobilox Innovations Private Limited vs. Kirusa Software Private Limited Supreme Court of India 21-09-2017

Section 9 read with Section 8 of the Insolvency and Bankruptcy Code, 2016–Application for initiation of corporate Insolvency resolution process by operational creditor-The expression "and" occurring in Section 8(2)(a) may be read as "or" in order to further the object of the statute and/or to avoid an anomalous situation-once the operational creditor has filed an application, which is otherwise complete, the adjudicating authority must reject the application under Section 9(5)(2)(d) if notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility - So long as a dispute truly exists in fact and is not spurious, hypothetical or illusory, the adjudicating authority has to reject the application-A "dispute" is said to exist, so long as there is a real dispute as to payment between the parties that would fall within the inclusive definition contained in Section 5(6)

In terms of purchase order issued by the Appellant/Corporate Debtor the Respondent/ Operational Creditor provided certain services and raised monthly invoices between December, 2013 and November, 2014. The bills so raised were payable within 30 days of receipt by the appellant. It is pertinent to note here that a non-disclosure agreement (NDA) was executed between the parties on 26th December, 2014 with effect from 1st November, 2013. In view of non-payment of dues, a demand notice dated 23rd December, 2016 was sent by the respondent under Section 8 of the Code. To this notice, the appellant responded that there exists serious and bona fide disputes between the parties and that nothing was payable as the respondent had been told on 30th January, 2015 that no amount would be paid to the respondent since it had breached the NDA.

The NCLT rejected the application filed under Section 9 of the Code on the ground that the default payment being disputed by the Corporate Debtor and that, the operational creditor has admitted that the notice of dispute has been received, the claim made is hit by Section (9)(5)(ii)(d) of the Code.

On appeal, the NCLAT set aside the order of the NCLT and remitted the case for consideration with the following observation:

"In the present case the adjudicating authority has acted mechanically and rejected the application under sub-section (5)(ii)(d) of Section 9 without examining and discussing the aforesaid issue. If the adjudicating authority would have noticed the provisions as discussed above and what constitutes 'dispute' in relation to services provided by operational creditors then it would have come to a conclusion that condition of demand notice under sub-section (2) of Section 8 has not been fulfilled by

the corporate debtor and defence claiming dispute was not only vague, got up and motivated to evade the liability."

On appeal, the Supreme Court held as follows:

The adjudicating authority, when examining an application under Section 9 of the Act will have to determine:

(i) Whether there is an "operational debt" as defined exceeding ₹1 lakh? (See Section 4 of the Act)

(ii) Whether the documentary evidence furnished with the application shows that the aforesaid debt is due and payable and has not yet been paid? and

(iii) Whether there is existence of a dispute between the parties or the record of the pendency of a suit or arbitration proceeding filed before the receipt of the demand notice of the unpaid operational debt in relation to such dispute?

If any one of the aforesaid conditions is lacking, the application would have to be rejected.

Apart from the above, the adjudicating authority must follow the mandate of Section 9, and in particular the mandate of Section 9(5) of the Act, and admit or reject the application, as the case may be, depending upon the factors mentioned in Section 9(5) of the Act.

Another thing of importance is the timelines within which the insolvency resolution process is to be triggered. The corporate debtor is given 10 days from the date of receipt of demand notice or copy of invoice to either point out that a dispute exists between the parties or that he has since repaid the unpaid operational debt. If neither exists, then an application once filed has to be disposed of by the adjudicating authority within 14 days of its receipt, either by admitting it or rejecting it. An appeal can then be filed to the Appellate Tribunal under Section 61 of the Act within 30 days of the order of the Adjudicating Authority with an extension of 15 further days and no more.

Section 64 of the Code mandates that where these timelines are not adhered to, either by the Tribunal or by the Appellate Tribunal, they shall record reasons for not doing so within the period so specified and extend the period so specified for another period not exceeding 10 days. Even in appeals to the Supreme Court from the Appellate Tribunal under Section 62, 45 days' time is given from the date of receipt of the order of the Appellate Tribunal in which an appeal to the Supreme Court is to be made, with a further grace period not exceeding 15 days. The strict adherence of these timelines is of essence to both the triggering process and the insolvency resolution process. One of the principal reasons why the Code was enacted was because liquidation proceedings went on interminably, thereby damaging the interests of all stakeholders, except a recalcitrant management which would continue to hold on to the company without paying its debts. Both the Tribunal and the Appellate Tribunal will do well to keep in mind this principal objective sought to be achieved by the Code and will strictly adhere to the time frame within which they are to decide matters under the Code.

It is, thus, clear that so far as an operational creditor is concerned, a demand notice of an unpaid operational debt or copy of an invoice demanding payment of the amount involved must be delivered in the prescribed form. The corporate debtor is then given a period of 10 days from the receipt of the demand notice or copy of the invoice to bring to the notice of the operational creditor the existence of a dispute, if any. The notes on clauses annexed to the Insolvency and Bankruptcy Bill of 2015, in which "the existence of a dispute" alone is mentioned. Even otherwise, the word "and" occurring in Section 8(2)(a) must be read as "or" keeping in mind the legislative intent and the fact that an anomalous situation would arise if it is not read as "or". If read as "and", disputes would only stave off the bankruptcy process if they are already pending in a suit or arbitration proceedings and not otherwise. This would lead to great hardship; in that a dispute may arise a few days before triggering of the insolvency process, in which case, though a dispute may exist, there is no time to approach either an arbitral tribunal or a court. Further, given the fact that long limitation periods are allowed, where disputes may arise and do not reach an arbitral tribunal or a court for upto three years, such persons would be outside the purview of Section 8(2) leading to bankruptcy proceedings commencing against them. Such an anomaly cannot possibly have been intended by the legislature nor has it so been intended. One of the objects of the Code *qua* operational debts is to ensure that the amount of such debts, which is usually smaller than that of financial debts, does not enable operational creditors to put the corporate debtor into the insolvency resolution process prematurely or initiate the process for extraneous considerations. It is for this reason that it is enough that a dispute exists between the parties. It is settled law that the expression "and" may be read as "or" in order to further the object of the statute and/or to avoid an anomalous situation.

In the first Insolvency and Bankruptcy Bill, 2015 that was annexed to the Bankruptcy Law Reforms Committee Report, Section 5(4) defined "dispute" as meaning a "*bona fide* suit or arbitration proceedings…". In its present *avatar*, Section 5(6) excludes the expression "*bona fide*" which is of significance. Therefore, it is difficult to import the expression "*bona fide*" into Section 8(2)(a) in order to judge whether a dispute exists or not.

It is clear, therefore, that once the operational creditor has filed an application, which is otherwise complete, the adjudicating authority must reject the application under Section 9(5)(2)(d) if notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility. It is clear that such notice must bring to the notice of the operational creditor the "existence" of a dispute or the fact that a suit or arbitration proceeding relating to a dispute is pending between the parties. Therefore, all that the adjudicating authority is to see at this stage is whether there is a plausible contention which requires further investigation and that the "dispute" is not a patently feeble legal argument or an assertion of fact unsupported by evidence. It is important to separate the grain from the chaff and to reject a spurious defence which is mere bluster. However, in doing so, the Court does not need to be satisfied that the defence is likely to succeed. The Court does not at this stage examine the merits of the dispute except to the extent indicated above. So long as a dispute truly exists in fact and is not spurious, hypothetical or illusory, the adjudicating authority has to reject the application.

On Facts of the Case:

1. *According to the respondent, the definition of "dispute" would indicate that since the NDA does not fall within any of the three sub-clauses of Section 5(6), no "dispute" is there on the facts of this case.*

The Supreme Court held that:

First and foremost, the definition is an inclusive one, and that the word "includes" substituted the word "means" which occurred in the first Insolvency and Bankruptcy Bill. Secondly, the present is not a case of a suit or arbitration proceeding filed before receipt of notice–Section 5(6) only deals with suits or arbitration proceedings which must "relate to" one of the three sub clauses, either directly or indirectly. A "dispute" is said to exist, so long as there is a real dispute as to payment between the parties that would fall within the inclusive definition contained in Section 5(6). The correspondence between the parties would show that on 30th January, 2015, the appellant clearly informed the respondent that they had displayed the appellant's confidential client information and client campaign information on a public platform which constituted a breach of trust and a breach of the NDA between the parties. They were further told that all amounts that were due to them were withheld till the time the matter is resolved. On 10th February, 2015, the respondent referred to the NDA of 26th December, 2014 and denied that there was a breach of the NDA. The respondent went on to state that the appellant's claim is unfounded and untenable, and that the appellant is trying to avoid its financial obligations, and that a sum of ₹19,08,202.57 should be paid within one week, failing which the respondent would be forced to explore legal options and initiate legal process for recovery of the said amount. This email was refuted by the appellant by an e-mail dated 26th February, 2015 and the appellant went on to state that it had lost business from various clients as a result of the respondent's breaches. Curiously, after this date, the respondent remained silent, and thereafter, by an e-mail dated 20th June, 2016, the respondent wished to revive business relations and stated that it would like to follow up for payments which are long stuck up. This was followed by an e-mail dated 25th June, 2016 to finalise the time and place for a meeting. On 28th June, 2016, the appellant wrote to the respondent again to finalise the time and place. Apparently, nothing came of the aforesaid e-mails and the appellant then fired the last shot on 19th September, 2016, reiterating that no payments are due as the NDA was breached.

Going by the aforesaid test of "existence of a dispute", it is clear that without going into the merits of the dispute, the appellant has raised a plausible contention requiring further investigation which is not a patently feeble legal argument or an assertion of facts unsupported by evidence. The defence is not spurious, mere bluster, plainly frivolous or vexatious. A dispute does truly exist in fact between the parties, which may or may not ultimately succeed, and the Appellate Tribunal was wholly incorrect in characterising the defence as vague, got-up and motivated to evade liability.

2. *According to the respondent, the breach of the NDA is a claim for unliquidated damages which does not become crystallised until legal proceedings are filed, and none have been filed so far.*

The Supreme Court held that:
The period of limitation for filing such proceedings has admittedly not yet elapsed. Further, the appellant has withheld amounts that were due to the respondent under the NDA till the matter is resolved. Admittedly, the matter has never been resolved. Also, the respondent itself has not commenced any legal proceedings after the e-mail dated 30th January, 2015 except for the present insolvency application, which was filed almost 2 years after the said e-mail. All these circumstances go to show that it is right to have the matter tried out in the present case before the axe falls.

Therefore, the appeal was allowed and the judgment of the Appellate Tribunal was set aside.

Case Review: Order dated 24-05-2017 of NCLAT in *Kirusa Software Private Ltd. vs. Mobilox Innovations Private Ltd.*, Company Appeal (AT) (Insolvency) 6 of 2017, set aside. (Reported in IIIPI Update # 5 Part II July 2017_Case Updates)

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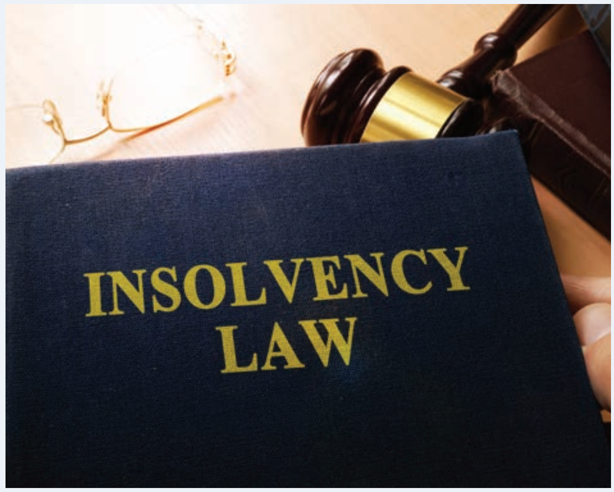
Black Pearl Hotels Pvt. Ltd.
vs.
Planet M Retail Ltd.
National Company Law Appellate Tribunal (NCLAT)
17-10-2017

Section 9 of the Insolvency and Bankruptcy Code, 2016 read with Article 137 of the Limitation Act, 1963–Application for Initiation of Corporate Insolvency Resolution Process by Operational Creditor-Insolvency and Bankruptcy Code, 2016 has come into force with effect from 1st December, 2016 and therefore, the right to apply under this Code accrues only on or after 1st December, 2016

The applicant/Operational Creditor filed an application under Section 9 of the Code before NCLT, Mumbai Bench on the ground that the respondent/Corporate Debtor (CD) had failed to pay its agreed dues. The Adjudicating Authority by



its impugned order dated 4th May 2017 dismissed the application on the ground that the application was barred by limitation.

On appeal, the NCLAT held as follows:
Insolvency and Bankruptcy Code, 2016 has come into force with effect from 1st December, 2016. Therefore, the right to apply under I&B Code accrues only on or after 1st December, 2016 and not before the said date (1st December, 2016). As the right to apply under Section 9 of I&B Code accrued to appellant since 1st December, 2016, the application filed much prior to three years, the said application cannot be held to be barred by limitation.

In so far as the application under Section 9 of the Arbitration and Conciliation Act, 1996 preferred by appellant, it has been specifically pleaded by the appellant and not disputed by the respondent that the appellant filed an application to withdraw the application under Section 9 of the Arbitration Act, expressly reserving liberty to institute fresh proceeding for interim relief. In such circumstances and as no arbitral dispute is pending, the application cannot be rejected.

The Adjudicating Authority, Mumbai Bench was not correct in holding that the application was barred by limitation. For the said reason the order rejecting the application cannot be sustained.

Case Review: Order dated 04.05.2017 passed by the NCLT, Mumbai Bench, in *Black Pearl Hotels Pvt. Ltd, Operational Creditor vs. Planet M. Retail Ltd.*, Corporate Debtor, (C.P. No.464/I&BP/NCLT/MAH/201), set aside.

Disciplinary Case

CA. ABC In re:

Facts of the case:

A letter dated 17th March 2009 was received from the Superintendent of Police, Central Bureau of Investigation (hereinafter referred to as the Informant) containing allegations against CA. ABC (hereinafter referred to as the Respondent). On receiving the aforesaid letter, which was not in prescribed Form 'I', the Informant was requested vide letter dated 25th March 2009 to file the complaint in prescribed Form 'I', but the same was not filed. On overall examination of the allegations and the documents received thereof, the matter has been treated as Information within the meaning of Rule 7 of the Chartered Accountants (Procedure of Investigations of Professional and Other Misconduct and Conduct of Cases) Rules, 2007 (hereinafter referred to as the "Rules"). As per the information letter, the allegations in brief are as under:-

- The Respondent has conducted the audit of a Group Housing Society (hereinafter referred to as Society) for the financial years 1996-97 and 1997-98 and submitted forged Audit Report on behalf of M/s. XXX & Co., Chartered Accountants. The Respondent neither was the Proprietor/Partner nor was authorised by M/s. XXX & Co., Chartered Accountants to carry out the said audit on its behalf.
- The Respondent has audited the accounts of the Society for the financial year 1998-99 on behalf of M/s. ZZZ & Co., Chartered Accountants and for the financial year 1999-2000 as a Proprietor of M/s. AAA & Associates, Chartered Accountants. Further, the Respondent has submitted his Audit Report to the office of Registrar Cooperative Societies under his signatures. But the names of these two firms were not registered with the ICAI.
- The investigation revealed that the Respondent also audited the accounts of the Society for the financial years 2000-01 to 2002-03 on

behalf of M/s. UUU & Associates, Chartered Accountants and submitted the Audit Report of the Society to the Office of Registrar Cooperative Societies. The Respondent neither was the Proprietor/Partner nor was authorised by M/s. UUU & Associates, Chartered Accountants to carry out the said audit on its behalf.

- Further, the Respondent had earlier worked as Administrative Officer in National Insurance Company from 1978 to July, 2007. Hence, he was not permitted to do any private business up to July, 2007 like audit of the Society. Due to this reason, he has conducted the audit of the Society in the name of above mentioned firms.

The matter was enquired by the Disciplinary Committee and the Committee, *inter alia*, gave its finding as under:-

The Committee noted allegation against the Respondent was that the Respondent as auditor of Group Housing Society submitted forged Audit Report on behalf of M/s. XXX & Co. and M/s UUU & Associates, Chartered Accountants for the financial years 1996-97, 1997-98 and 2001-01 to 2002-03 respectively. The Respondent was neither the Proprietor/Partner nor was authorised by the aforesaid Chartered Accountant firms to carry out the said audit. Besides, the Respondent submitted audit reports on behalf of M/s. ZZZ & Co., and M/s AAA & Associates, Chartered Accountants for the financial years 1998-99 and 1999-2000 and these two CA firm were not registered with ICAI.

In context of the above allegations, the Respondent stated that he was doing practice continuously from 01.05.1976 to 15.05.2001 under the name of M/s. ZZZ & Co. The Respondent admitted that he signed the audit report of the Society for the financial year 1998-1999 and submitted to the office of the Registrar. He, however, denied to carry out audit of the other financial years under question on behalf of M/s XXX & Co., M/s AAA & Associates, M/s UUU & Associates.

The Committee noted that the Respondent was partner in the following firms:-

(i) M/s ZZZ & Co. [FRN 0033760N] from 01.05.1976 to 01.07/1991, 01.11.1996 to 15.05.2001, 01.05.2003 to 28.07.03 and 28.08.2003 to till date.

(ii) M/s XXX & Co. [FRN/011/67W] from 15.05.2003 to 28.07.2003 and 28.08.2003 to 22.06.2010.

The Committee, on perusal of statement of the Respondent recorded u/s. 161 of Cr.P.C., noted that the Respondent stated that he was the Proprietor of M/s ZZZ & Associates and three other firms were Partnership firm in which he was one of the Partners. He further admitted that he was signing all the audit reports of the Society under the aforesaid audit firm. The Committee noted that the above statement u/s. 161 was not signed by the Respondent and the Respondent also raised question on the authenticity of the same. Hence, the Committee decided not to give much weightage to the same.

The Committee noted that during the course of investigation, the CBI has taken the specimen signature of the Respondent in the Court and sent those signatures to the Government examiner for verification. The Government examiner was of the opinion that the Respondent's signature matched with questioned signatures. The Respondent also admitted that his signatures were taken for verification by CBI. It was noted that the Respondent did not submit any documents to negate the opinion of handwriting experts.

The Committee noted that the handwriting report from the Government forensic expert had come out clearly that the signature of the Respondent is there in case of three firms. Though he was not partner in these firms, yet he signed the Financial Statement of the Society under the different firm name, namely M/s XXX & Co., M/s AAA & Associates and M/s UUU & Associates. Considering the material available on record, the Committee held that the Respondent is guilty of 'Other Misconduct falling within the meaning of Clause (2) of Part IV of the First Schedule and Clause (1) of Part II of the Second Schedule to the Chartered Accountants Act, 1949 [As Amended by the Chartered Accountants (Amendment) Act, 2006]. The Committee after affording an opportunity of hearing to the Respondent and after considering all the material on record is of the view that the Professional Misconduct on the part of Respondent does not qualify for a severe sentence, hence, ordered that the name of the Respondent be removed from the Registrar of Members for a period of one month. ■